

Office for
**Budget
Responsibility**

Welfare trends report

October 2014

Office for Budget Responsibility

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Foreword

The Office for Budget Responsibility (OBR) was created in 2010 to provide independent and authoritative analysis of the UK's public finances. Parliament has stated that it *"is the duty of the Office to examine and report on the sustainability of the public finances."*

In December 2013, the Chancellor of the Exchequer asked the OBR to take on additional responsibilities in relation to the Government's newly announced cap on a subset of welfare spending, which was then quantified in the March 2014 Budget. This request was in two parts – to assess the Government's performance against the welfare cap and, in order to facilitate open and constructive debate about welfare spending, to *"prepare and publish information on the trends in and drivers of welfare spending within the cap."*

This first *Welfare trends report (WTR)* represents our response to that request for greater transparency about welfare spending to facilitate debate. The approach we have taken is to:

- focus our analysis on welfare spending delivered through the benefits system (managed by the Department for Work and Pensions) and the tax credits and child benefit systems (managed by HM Revenue and Customs). We do not consider spending on benefits in kind, for example social housing, education and healthcare;
- consider spending both in cash terms – as the welfare cap is a cash ceiling – and as a share of GDP – which is more relevant for the sustainability of the public finances;
- look in detail at trends over the past 30 years and in the 5-year forecast period of our March 2014 *Economic and fiscal outlook (EFO)*, as well as providing a summary of long-term prospects contained in our July 2014 *Fiscal sustainability report*;
- provide greater detail about the judgements and assumptions that underpin our latest medium-term forecast and the risks and uncertainties to which they are subject; and
- draw out the broad themes that help explain fluctuations in welfare spending over the past and in our medium-term forecast and long-term projections.

At any one time around half the UK population receives income from at least one social security benefit – and over a lifetime most people will. This underlines the potential scope of a report that aims to explain trends in welfare spending. Inevitably, we have not been able to explore every avenue in as much detail as we would have liked. We will be able to return to other issues – UK spending in international perspective or the implications of the distribution of earnings growth, for example – in future reports. As with all our flagship reports, the *WTR* is a work in progress. We have refined and modified our other reports in response to feedback from users and we would be very keen to hear suggestions on the scope and format of this report.

Foreword

The analysis and projections in this report represent the collective view of the three independent members of the OBR's Budget Responsibility Committee. We take full responsibility for the judgements that underpin them and for the conclusions we have reached. We have, of course, been supported in this by the full-time staff of the OBR, to whom we are enormously grateful.

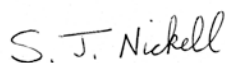
We have also drawn on the help and expertise of our advisory panel and of officials across government, including the Department for Work and Pensions (DWP), HM Revenue and Customs and HM Treasury. We are particularly grateful for the time and effort of forecasting officials at DWP, who were at the same time engaged in the early stages of work on our forthcoming December 2014 *EFO* forecast. We have been provided with all the information and analysis that we requested.

We are also grateful to a wide range of external stakeholders who gave of their time and shared their expertise in helping us to produce this first *WTR*. The Institute for Fiscal Studies (IFS) advised us in a number of areas and provided us with an early draft of their updated report *A survey of the UK benefits system*, on which Chapter 2 of our report draws heavily. Professor Sir John Hills at the London School of Economics and Carl Emmerson at the IFS (a member of our advisory panel) both reviewed an early draft of the report, providing very helpful advice and comments.

We provided the Chancellor of the Exchequer with a full and final copy of the report 24 hours in advance of publication.



Robert Chote



Steve Nickell



Graham Parker

The Budget Responsibility Committee

Executive summary

- 1 This is our first *Welfare trends report (WTR)*, a new annual publication that will examine trends in spending on different elements of the welfare system, including those items that will be subject to the Government's new 'welfare cap'. Reflecting the remit that we have been given by Parliament – to focus on the public finances – the report does not consider the impact of the welfare system on the distribution of income or on measures of poverty.
- 2 At any one time around half the UK population receives income from at least one social security benefit – and over the course of a lifetime most people will. So there is much that can be said about the way the welfare system operates and why it costs what it costs.
- 3 In this report we:
 - focus on spending delivered through the benefits system (managed by the Department for Work and Pensions across Great Britain) and the tax credits and child benefit systems (managed by HM Revenue and Customs across the whole of the UK). We do not consider benefits-in-kind, for example social housing, education and healthcare;
 - consider spending both in cash terms – as the welfare cap is a cash ceiling – and as a share of GDP – which is more relevant for the sustainability of the public finances. We say much less about real-terms spending and spending per head;
 - look in detail at trends over the past 30 years and in the five-year forecast period of our March 2014 *Economic and fiscal outlook (EFO)*, as well as providing a summary of long-term prospects contained in our July 2014 *Fiscal sustainability report (FSR)*;
 - provide greater detail about the judgements and assumptions that underpin our latest medium-term forecast and the risks and uncertainties to which they are subject; and
 - draw out the broad themes that help explain fluctuations in welfare spending over the past and in our medium-term forecast and long-term projections.
- 4 Even having narrowed our focus to spending on social security benefits and tax credits, there remains considerable variety in the types of spending we examine. In our discussion, we have been guided by the Institute for Fiscal Studies' approach in its report *A survey of the UK benefit system* in grouping spending by the type of recipient.
- 5 One important new feature of the welfare system relevant to this report is the welfare cap. The Government announced in Autumn Statement 2013 that it would introduce a cap on certain items of welfare spending, excluding state pensions – which it argued are "*better planned and controlled over a longer time period*" – and jobseeker's allowance and

associated housing benefit payments – which it identified as “the most cyclical elements of welfare” in order “to allow the automatic stabilisers to operate”.¹

- 6 The cap was formally defined and initially set by the Government in Budget 2014. It will apply from 2015-16 – when it covers £119.5 billion of spending, around 55 per cent of total welfare spending – to the end of the forecast period, which was 2018-19 in Budget 2014.

Drivers of welfare spending

- 7 Trends in the number or proportion of the population eligible for many benefits reflect developments in the underlying drivers of individuals’ circumstances. For example, the number of pensioners in part reflects trends in life expectancy at older ages, while the number of housing benefit recipients depends in part on the number of households renting rather than owning their home.
- 8 Some of the most important trends affecting welfare spending over the past 30 years and across our latest five-year forecast are related to demography, the labour market, inflation and earnings, and the housing market. In particular:
- **demographic trends:** the population has been ageing in recent decades, as fertility rates fell and life expectancy at older ages increased substantially. That led to a falling number of children until recently, while the size and proportion of the population aged over 65 has been rising steadily. Trends in family status and the availability of housing have meant the number of households has typically risen slightly faster than the population, reflecting a fall in the average household size;
 - **labour market trends:** eligibility for a number of benefits depends on people’s labour market status. Unemployment tends to follow a cyclical path, rising in recessions and falling in recoveries. It is expected to fall in our latest medium-term forecast. More people are inactive – neither working nor seeking work – than unemployed, and this can be for a variety of reasons. Among older people, labour market inactivity is generally due to retirement, so is influenced by demographic trends. Among working-age women, inactivity is most often due to family responsibilities. Inactivity in this group has been on a declining trend (with employment rates rising), which has implications for contributory benefits like state pensions. Among working-age men, inactivity increased from the 1970s until the mid-1990s, largely due to long-term sickness – a trend that subsequently reversed. For younger men and women, inactivity due to study has been rising. Self-employment and part-time work have also been on rising trends that accelerated through the late 2000s recession;
 - **inflation and earnings growth:** most benefits are uprated each year in line with an official measure of inflation. Over the past few years, uprating by inflation has caused welfare spending to rise as a share of GDP because earnings growth – and productivity growth – has been very weak. An issue that we have not explored in detail

¹ HM Treasury (2013)

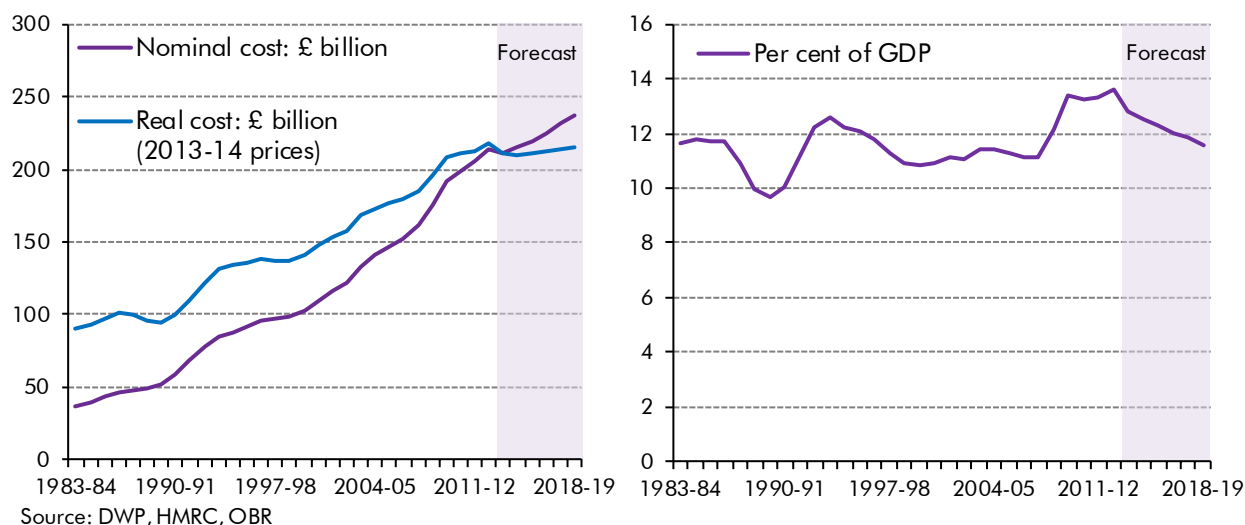
in this report – but to which we will return in the future – is differences in earnings developments across the income distribution. For example, in recent years it appears that much of the growth in self-employment has been at the lower end of the income distribution, which will have affected spending on tax credits; and

- **housing market trends:** housing benefit – support for people on low incomes who rent their homes – accounts for a significant share of welfare spending, so trends in the housing market are very important. The number of households living in the social-rented sector has been declining steadily for decades. Since the mid-2000s, the number of households living in the private-rented sector has been rising. That trend picked up in the late 2000s recession and in 2012-13 the number of private renters exceeded the number of social renters for the first time in almost 50 years. As private rents are on average higher than social rents, that shift puts upward pressure on welfare spending. Administrative data from the benefits system also suggests that rents have risen faster than earnings and inflation over the past decade.

Trends in welfare spending

- 9 At a high level, trends in welfare spending reflect the underlying economic and social drivers set out above, together with Government decisions about the scope of support that it will provide to people through the welfare system. That is apparent in the rising share of welfare spending devoted to pensioners – which reflects demographic trends and policy decisions (such as the ‘triple lock’ on uprating or the introduction of winter fuel payments) – and to children – due to the large expansion of tax credits focused on families with children.
- 10 Over the past 30 years, welfare spending has risen steadily in cash and real terms, but on average that increase has been broadly in line with growth in the economy. So the proportion of national income devoted to welfare spending has not shown a significant upward or downward trend over time.
- 11 Welfare spending has, however, fluctuated significantly with the economic cycle. That has reflected two important features:
 - first, the caseloads of small and highly counter-cyclical benefits (like jobseeker’s allowance) rise significantly in recessions and fall significantly in recoveries. These elements of spending are excluded from the welfare cap; and
 - second, the average awards of large and mildly counter-cyclical benefits (like state pensions or disability benefits) are more stable than GDP over the economic cycle, thereby fluctuating negatively with the cycle relative to GDP. With the exception of state pensions, these elements of spending are subject to the welfare cap.

Chart 1: Total welfare spending in the UK



Explaining trends in welfare spending in recent decades

12 We have looked at the factors that have explained the rises and falls in welfare spending as a share of GDP over the past 30 years. This report shows that:

- during the period of strong GDP growth **from 1983-84 to 1989-90**, spending fell by 2.0 per cent of GDP. The largest contributions to that fall were lower spending on unemployment benefits as the economy boomed and lower spending on state pensions as earnings growth outpaced uprating. The rising proportion of adults receiving incapacity benefits slightly offset those falls;
- **between 1989-90 and 1993-94**, a period that included the early 1990s recession, spending increased by 3.0 per cent of GDP. The largest contributions were caseload-driven increases in spending on unemployment and incapacity benefits, and average award-driven increases in spending on housing benefit, as the recession bit. Spending on state pensions was pushed up as a share of GDP thanks to the weakness of earnings growth relative to the amount by which they were uprated;
- **between 1993-94 and 2007-08**, a period of sustained economic growth, spending fell by 1.5 per cent of GDP. The largest contribution was the steady reduction in the unemployment rate. Spending on incapacity benefits also fell as uprating and other factors pulled average awards lower relative to earnings. This period also saw a big shift in spending from different parts of the benefits system to tax credits; and
- **between 2007-08 and 2012-13**, a period that spans the late 2000s recession and slow recovery that followed, spending increased by 2.5 per cent of GDP. The rise in the caseload for jobseeker's allowance made a surprisingly small contribution to the increase in spending. The largest contribution was from the uprating of state pensions as inflation outstripped growth in earnings and GDP. Spending on tax credits and housing benefit also increased significantly, the former reflecting generous

discretionary uprating (especially of the child element) and the latter reflecting growth in the number of renters and rent inflation outstripping earnings growth.

Future prospects for welfare spending

March 2014 *Economic and fiscal outlook* central forecast

- 13 Our latest medium-term forecast shows welfare spending rising by 12.5 per cent in cash terms between 2013-14 and 2018-19. We expect the cash size of the economy to grow significantly more quickly, so this reduces expected welfare spending by 1.2 per cent of GDP between 2013-14 and 2018-19, from 12.8 per cent to 11.6 per cent.

Table 1: Medium-term forecast of welfare spending

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
£ billion							
Total welfare spending	212.9	210.1	213.9	218.8	224.5	230.6	236.3
of which:							
Welfare spending subject to the welfare cap	116.5	116.4	117.8	119.5	122.0	124.6	126.7
Welfare spending outside the welfare cap	96.4	93.8	96.1	99.3	102.5	106.0	109.6
Per cent of GDP							
Total welfare spending	13.6	12.8	12.4	12.2	12.0	11.8	11.6
of which:							
Welfare spending subject to the welfare cap	7.4	7.1	6.8	6.7	6.5	6.4	6.2
Welfare spending outside the welfare cap	6.1	5.7	5.6	5.6	5.5	5.4	5.4

- 14 Spending that will be subject to the welfare cap is expected to fall by 0.9 per cent of GDP over the next five years. This is driven by:
- a 0.2 per cent of GDP drop in the cost of tax credits – the largest category of spending subject to the cap. This reflects a number of policy measures designed to cut spending, including uprating by 1 per cent for three years from 2013-14;
 - falls of 0.1 per cent of GDP in spending on both housing benefit and incapacity benefits – the next largest spending items. Housing benefit falls as caseloads linked to other benefits decline relative to the adult population, partly offset by growth in the ‘housing benefit only’² caseload of those in work. The expected fall in spending on incapacity benefits is partly driven by our assumption that the reassessment of employment and support allowance claims will reduce the overall caseload;
 - a substantial fall in spending on disability benefits (worth 0.2 per cent of GDP) that is driven by the assumed reduction in caseloads as people’s eligibility for support is reassessed when cases are migrated from the existing disability living allowance to the new personal independence payment; and

² This ‘housing benefit only’ caseload is described as ‘only’ in DWP data because recipients are not also in receipt of another DWP benefit. From the broader perspective of welfare spending, such claimants will typically receive some income from tax credits and, if they have children, will also receive income from child benefit.

- falls in spending on a number of other benefits, including pension credit (as the qualifying age is raised and the single tier pension is introduced), child benefit (due to uprating) and income support (as incapacity-related claims are migrated to employment and support allowance).

15 Spending outside the welfare cap is expected to fall by around a third as much – 0.3 per cent of GDP – as spending subject to the cap. That reflects:

- a 0.1 per cent of GDP decline in spending on state pensions, as the pressure from population ageing is more than offset by raising the state pension age, while the triple lock on uprating sees average awards rise broadly in line with earnings; and
- a 0.2 per cent of GDP fall in spending on the unemployed – comprising jobseeker's allowance and housing benefit paid to jobseekers. Spending on state pensions was around 12 times higher than spending on these benefits in 2013-14, so this represents a much larger proportional fall. Lower spending is driven both by lower cyclical caseloads and by average awards rising more slowly than earnings.

Key risks to the forecast

16 Our forecast for welfare spending is subject to a number of important risks and uncertainties. In particular:

- the three largest sources of uncertainty – and risks to the forecast – probably relate to housing benefit, incapacity benefits and disability benefits. In the case of housing benefit, this relates to the underlying economic drivers of both the caseload and the implied average award per claim. For incapacity and disability benefits, the major uncertainties are associated with ongoing policy reforms – the effect on caseloads and average awards as systems are changed, as existing caseloads are migrated from old to new benefits, and as savings are assumed to flow from the associated reassessment process. In both cases there have been delays to delivery of these reforms that have affected the timing and scale of expected savings. We will revisit our assumptions on these key areas ahead of our December 2014 forecast;
- the migration from six existing benefits to the single universal credit that is planned to take place over the coming years will pose many of the same problems, often to an even greater degree. But, quantitatively, this is not as large a risk to the forecast over the next five years as the reforms described above; and
- we have been surprised at the speed with which claimant count unemployment has fallen – not just because the broader survey measure of unemployment has fallen unexpectedly rapidly, but because the claimant count has fallen unexpectedly rapidly relative to that survey measure. The claimant count moved below 1 million in August 2014 – a level we not expect it to reach until 2017 in our latest forecast in March. It has fallen at a faster rate over the past year than at any time since 1973. This suggests that in our December 2014 forecast we will need to revise down our forecast of

spending on jobseeker's allowance significantly. Some of the fall may reflect claimants moving onto other benefits, such as employment and support allowance.

- 17 So how do these risks affect the Government's welfare cap? The cap was formally defined and initially set in line with our Budget 2014 forecasts (Table 2). It will apply from 2015-16 to the end of the forecast period, which was 2018-19 in Budget 2014. The Government has set a forecast margin above the cap of 2 per cent in each year. In our December EFO, we will have to assess whether spending is likely to exceed the cap for discretionary policy reasons or the cap-plus-forecast-margin due to changes in our forecast assumptions.

Table 2: The level of the welfare cap and the forecast margin

	£ billion			
	2015-16	2016-17	2017-18	2018-19
Welfare cap	119.5	122.0	124.6	126.7
2 per cent forecast margin	2.4	2.4	2.5	2.5

- 18 The downside risks we have identified to our forecasts for jobseeker's allowance and associated payments of housing benefit lie outside the cap, whereas the significant upside risks on incapacity and disability benefits lie within it. The 'housing benefit only' group that has been the source of recent upward revisions to spending also lies within the cap.
- 19 More generally, with the welfare cap having been set in cash terms, inflation surprises are a key risk – especially if there is an upside surprise that comes after the period over which the uprating of most working-age benefits is being capped at 1 per cent. (Our central forecast implies that this cap will be binding and we assume that throughout the report.) An upside inflation surprise that occurred during the period of 1 per cent uprating would reduce the real value of most working-age benefits, rather than feeding through to higher spending.

July 2014 Fiscal sustainability report projections

- 20 Our 2014 FSR contained long-term projections of welfare spending. These projections capture the effects of demographic change on spending, with neutral assumptions in most other areas. An important difference from our medium-term forecasts is that we assume that benefits are uprated in line with earnings rather than inflation, which means that we do not allow spending to fall in our projections due to an ever-widening divergence between the living standards of those in work and those receiving income from the welfare system.
- 21 Our long-term projections show total welfare spending rising by 2.5 per cent of GDP between 2018-19 – the end of our medium-term forecast – and 2063-64, with almost all of the rise accounted for by benefits paid to the elderly. This is largely driven by demographic trends, which are partly offset by further expected increases in the state pension age. (This is based on the principle set out by the Government that people should expect to spend a third of their adult life in receipt of the state pension.) 'Triple lock' uprating is assumed to put further upward pressure on state pensions spending as a share of GDP over the long term.
- 22 Among other benefits, the main projected changes over the long term are that:

- spending on incapacity and disability benefits rises, in large part due to the ageing of the population, because we assume constant age-specific shares of the population in receipt of incapacity benefits. Cohort effects raise the caseload as a share of the adult population as the population ages. For disability benefits, even though we assume increases in disability-free life expectancy, the significant rise in the population of very old people lifts spending overall. The number of people aged 85 and over is projected to rise from 2.3 per cent of the population in 2014 to 7.7 per cent in 2064; and
- spending on housing benefit falls, due in large part to assumed higher home-ownership rates for pensioners. This reflects cohort effects – newly-retired pensioners have higher home-ownership rates than the oldest pensioners, which all else equal means fewer newly-retired pensioners are eligible for housing benefit.

Table 3: Long-term projections of welfare spending

	Forecast		Projections				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP							
Total welfare spending	12.6	11.6	11.8	12.9	13.6	13.9	14.1
of which:							
State pensions ¹	5.8	5.5	5.7	6.7	7.4	7.6	7.9
Other welfare spending	6.8	6.1	6.1	6.1	6.2	6.3	6.2
Per cent of total welfare spending							
State pensions ¹	46.0	47.7	48.1	52.2	54.3	54.8	56.0
Other welfare spending	54.0	52.3	51.9	47.8	45.7	45.2	44.0

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis, consistent with our 2014 *Fiscal sustainability report* projections.

¹ Basic state pension, state earnings related pension scheme, state second pension, single-tier pension, other elements of state pension, pension credit and other pensioner benefits

1 Introduction

- 1.1 Around half the population receive income from at least one social security benefit at any given time, and almost everyone does so at some point in their lifetime. Furthermore, eligibility for different benefits is determined by a wide range of household or individual circumstances. The potential scope of a report on trends in welfare spending is therefore enormous, so we have had to decide how to make it manageable for a single report. This chapter sets out the approach we have taken.

Defining welfare spending

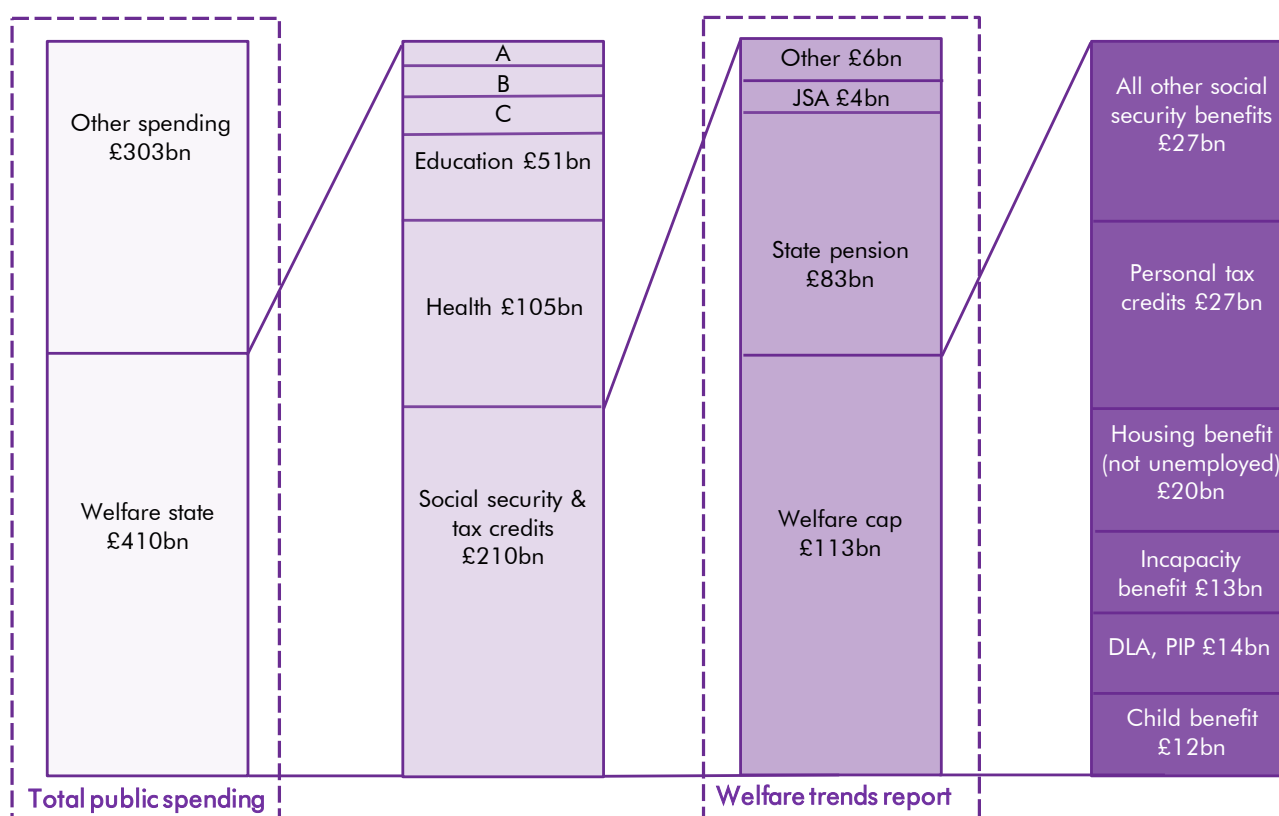
- 1.2 The term ‘welfare’ means different things to different people. At its broadest, welfare spending might be considered as any spending that plays a part in the provision of the welfare state – including spending on health, long-term care, education and social housing, as well as social security benefits and tax credits for children, people of working-age and pensioners. A narrower definition would focus just on the benefit and tax credits systems, which transfer cash from some parts of the population to others on the basis of eligibility. At a minimum, our report must satisfy the Government’s request that we look at spending subject to its welfare cap, a cash ceiling applied to a subset of benefits and tax credits.
- 1.3 For the purposes of this first *WTR*, we define welfare spending as all spending on benefits and tax credits as they appear in our medium-term forecasts. This definition covers all spending subject to the welfare cap and places that spending in the context of other spending on benefits, notably the largest element of the benefits system: state pensions.
- 1.4 The majority of the spending covered is administered by three separate organisations:¹
- the Department for Work and Pensions (DWP), which administers most benefits in Great Britain;
 - HM Revenue and Customs (HMRC), which administers the personal tax credits and child benefit systems across the United Kingdom; and
 - the Northern Ireland Social Security Agency, which administers most benefits in Northern Ireland.
- 1.5 Due to the administrative separation of the benefits system between Great Britain and Northern Ireland, which is replicated in the historical data and our forecasts, this report

¹ Some smaller benefits are administered by other departments – for example, paternity pay is administered by the Department for Business, Innovation and Skills and war pensions by the Ministry of Defence.

focuses largely on trends in spending in Great Britain. The exceptions are the sections on tax credits and child benefit, for which the administration and historical data are UK-wide.

- 1.6 Figure 1.1 shows how the definition of welfare spending used in this report relates to total public spending and to some other possible definitions of welfare spending. In future reports, we will look in more depth at the interactions between trends in spending on benefits and tax credits and trends in public spending more broadly.

Figure 1.1: Welfare spending in the UK



Note: A: Housing, £7bn; B: Public sector pensions, £10bn; C: Public and social services, £29bn

Deciding what period to consider

- 1.7 There have been forms of social protection in the UK for centuries, from the Elizabethan and Victorian poor laws to the workplace compensation schemes of the industrial revolution. The welfare system in its current form began to take shape under the Liberal Government of Herbert Asquith with the introduction of a state pension for the elderly – initially those aged over 70 – in the Old Age Pensions Act 1908. This was followed by the introduction of contributory insurance against sickness and unemployment in the National Insurance Act 1911. The creation of the ‘cradle to grave’ welfare state as we now know it came during the post-war Labour Government of Clement Attlee, following the Beveridge Report of 1942. This included the introduction of child benefit in the Family Allowances Act 1945, the

creation of the NHS in the National Health Service Act 1946 and the expansion of compulsory social insurance in the National Insurance Act 1946.²

- 1.8 A full history of trends in welfare spending – encompassing the evolution from basic social assistance through forms of social protection and social insurance to the full welfare state – is beyond the scope of this report. Instead, we focus on the three decades from 1983-84, a period that covers two recessions and a number of major reforms to the welfare system. This permits a reasonably full analysis of the drivers of trends in welfare spending from which we can draw out common themes and challenges that are relevant to fiscal sustainability and our forthcoming assessments of the Government’s performance against the welfare cap.
- 1.9 We also look forward to the future prospects for welfare spending, focusing on our latest medium-term forecast for the period to 2018-19 made in March 2014. We provide greater detail on the assumptions and judgements that are required to produce our central forecasts and the uncertainties and risks to which they are subject. Finally, we summarise our latest illustrative long-term projections from July 2014, which extend 50 years to 2063-64.

Identifying appropriate spending metrics

- 1.10 Having established which types of spending to analyse over what time period, the next decision is to choose which metrics to focus on. Different metrics are appropriate for different questions. The three most common measures of spending used are:
- **cash or nominal spending:** this is simply the cash amount spent in a given period. It is the metric most relevant to the Government’s welfare cap, which has been set in cash terms for the period from 2015-16 to 2018-19. But without putting the cash amount into context – by asking what the recipients could buy with it or how much national income is available to fund it – interpreting changes in cash spending is difficult, particularly over longer time periods;
 - **spending in real terms:** trends in cash spending can be adjusted for whole economy or consumer price inflation, to give a sense of the volume of goods and services that could be purchased with that spending – either across the whole economy or in the hands of the recipients; and
 - **spending as a share of national income:** trends in cash spending can be related to the cash value of the economic activity that can be taxed to finance it. This is the most relevant metric when considering the sustainability of the public finances.
- 1.11 There are other possible metrics that might be considered, including:
- as a share of total public spending – which would illustrate the trade-offs between welfare and other priorities within a given spending envelope;

² See for example Briggs (1961) or Gregg (2008).

- relative to revenues – a more direct measure of spending relative to the resources available to finance it; or
- in per capita terms – either cash or real – which could be related more directly to individual incomes or living standards.

1.12 In this report we focus on spending in cash terms – as the welfare cap is a cash ceiling – and as a share of GDP – given our focus on the sustainability of the public finances.

1.13 As noted above, the majority of welfare spending in the UK is administered at the Great Britain level by DWP, with benefits in Northern Ireland administered separately. For simplicity, we use UK GDP as the denominator in all of the analysis in this report. This is also consistent with our focus on comparing spending to the full UK national income that can be taxed to finance it.

An approach to analysing trends in welfare spending

1.14 When analysing trends in welfare spending there are a number of different drivers that need to be taken into account. The approach we take in this report is to split those drivers into those that affect the number of recipients of a benefit – the caseload – and those that affect the amount paid to each recipient – the average award.

1.15 Total spending on each benefit and the average caseload through each year are derived from administrative data, with the average award calculated from the relationship between the two. The average award is not the same as the statutory rate or rates for a given benefit. In some cases, an average annual award is a meaningful concept – for example, those receiving the basic state pension will claim throughout each year once they have started to receive payments. In other cases, it is less meaningful – for example, currently around 70 per cent of those claiming jobseeker's allowance have been doing so for less than 12 months. We have therefore focused on an implied average weekly award in the report, but even that measure can often be different from statutory rates of benefit.

1.16 When considering trends in cash spending, we are interested in absolute changes in the different drivers of the caseload and average award. Taking each in turn, changes in spending will reflect:

- changes in the caseload, which among other things can be affected by:
 - changes in the population eligible for a benefit, due to demographic or economic factors – such as growth in the number of people aged above the state pension age, changes in the number of people unemployed or rent inflation affecting the number of people renting their homes that are eligible to receive housing benefit;
 - the proportion of those that are eligible who choose to take up their entitlement – this may be affected by knowledge of the entitlement or stigma associated with making a claim; and

- policy changes that alter eligibility criteria – such as raising the state pension age.
- changes in the implied average award, which among other things can be affected by:
 - statutory or default uprating of benefits and the economic factors that affect the measures by which benefits are uprated – for example, the default setting for most benefits since the Coalition Government’s 2010 reforms is uprating by consumer price (CPI) inflation each year, which means the actual rate of CPI inflation is a key driver of changes in average awards;
 - policy choices to uprate benefits by an amount that differs from the default setting – for example, the basic state pension was uprated by substantially more than retail price (RPI) inflation in the years after 2000-01, when the Labour Government decided that uprating in line with the low rate of RPI inflation that year – 1.1 per cent – had been inadequate; and
 - changes in the composition of the caseload, which can change the average award when different groups receive different amounts. This is particularly true of housing benefit, where the amount paid to each recipient varies considerably across the country and in the social- and private-rented sectors, and the state pension, where a growing proportion of recipients are women entitled to the full state pension.

1.17 When considering trends in spending as a share of GDP, we also need to consider how all the factors affecting cash spending relate to GDP growth. In order to assess the relative importance of changes in caseload and average award drivers for the ratio of spending to GDP, we have to decompose GDP growth itself into relevant components. We do that by considering changes in caseloads relative to the population – in this report the adult population aged 16 and over – and changes in average awards relative to GDP per person – GDP per adult in this report. GDP per adult can be thought of as a proxy for average incomes, so the ratio of the average award to GDP-per-adult is a measure of the ‘generosity’ of a given benefit.

1.18 This approach allows us to analyse whether a rise (fall) in spending on any benefit is explained by a rise (fall) in the proportion of the adult population claiming or because the average award has risen faster (slower) than average incomes. Where sufficient data are available, we can further decompose these explanations into the factors identified above. For example, we can calculate the extent to which spending on state pensions is changing as a share of GDP due to the ageing of the population, recent changes in the state pension age, the effects of the triple lock on uprating and changes in the composition of the caseload.

Structure of the report

1.19 The report is structured as follows:

- Chapter 2 describes the welfare system that is being analysed;
- Chapter 3 discusses demographic and economic trends – in particular, the labour market, inflation and housing – that affect welfare spending;
- Chapter 4 draws on detailed analysis of individual benefits to describe trends in welfare spending over the past 30 years and prospects for spending in our latest 5-year forecast period and over the coming 50 years. This chapter assesses the implications for the Government's welfare cap of our analysis of backward-looking trends and of the risks and uncertainties surrounding our latest forecast; and
- Chapters 5 to 10 present detailed analysis of trends in spending on individual benefits and tax credits, grouped by the type of recipient – the elderly (Chapter 5), the sick and disabled (Chapter 6), families (Chapter 7), the unemployed (Chapter 8), those receiving support with housing costs (Chapter 9) and the bereaved (Chapter 10).

2 An overview of the welfare system

- 2.1 In this report, we focus on the benefits and tax credits elements of the broader welfare state. The system has evolved over time, expanding in some areas and withdrawing from others. This chapter briefly describes the system in its current form and uses survey data to provide a snapshot of how the population interacts with the system at any given time.

Features of the welfare system today

- 2.2 As set out in the Institute for Fiscal Studies' (IFS) *A survey of the UK benefit system*, published earlier this month, the welfare system as we define it is made up of a large number of benefits and tax credits – more than 40 are referenced in its report. These benefits and tax credits have different characteristics that provide support to different types of recipient. The IFS report provides further detail on all the features described in this section.¹

Eligibility characteristics

- 2.3 One way in which individual benefits and tax credits differ is in how eligibility to receive them is determined. For means-tested benefits, such as income support, eligibility usually depends on the claimant's family income, together with other family circumstances and personal characteristics. For contributory benefits, eligibility usually depends on the claimant having paid sufficient National Insurance contributions (NICs) during their lifetime. Some benefits, such as disability living allowance, are neither contributory nor means-tested and are universally available to all people who meet some qualification criteria.
- 2.4 Eligibility requirements to be resident (to have your home) and/or present (to be physically located) in Great Britain also vary between different benefits and tax credits. For example, entitlement to social security in Great Britain depends on how long applicants have been present in the country, their nationality, their immigration status, and whether they are covered by provisions of European Law.² The majority of benefits and tax credits have residency conditions. Contributory benefits typically only have presence requirements. Most retirement pensions are payable without time limit while the claimant is abroad. But there are some benefits – e.g. statutory maternity pay – for which there are no residence or presence conditions.

¹ We are grateful to the IFS for sight of an earlier draft of their latest survey, from which this section has drawn extensively.

² There is a reciprocal agreement between Great Britain and Northern Ireland such that, in general, individuals can satisfy residence conditions if they move between Great Britain and Northern Ireland.

The benefit cap and the welfare cap

2.5 There are two important ‘caps’ that currently feature in the welfare system – one that applies bottom up at the level of benefit recipients and another that applies top down to a subset of overall welfare spending:

- **the benefit cap:** since April 2013, a benefit cap has been in force in an attempt to ensure that no family receives more on benefits than the average family in work. The benefit cap only applies for households claiming housing benefit (or universal credit). If their total weekly income from specified benefits exceeds the cap, their housing benefit payments are reduced to bring them down to the cap. Households in receipt of certain benefits – such as disability benefits – are exempt from the cap. The current level of the cap is £500 a week for couples (with or without children living with them); £500 a week for single parents whose children live with them; and £350 a week for single adults who do not have children, or whose children do not live with them; and
- **the welfare cap:** the Government announced in Autumn Statement 2013 that it will introduce a cap on certain items of welfare spending, excluding state pensions – which it argues are “*better planned and controlled over a longer time period*” – and jobseeker’s allowance and associated housing benefit payments – which it identifies as “*the most cyclical elements of welfare*” in order “*to allow the automatic stabilisers to operate*”.³ The cap was formally defined and initially set by the Government in Budget 2014. It will apply from 2015-16 to the end of the forecast period.

The main groups supported by the welfare system

2.6 One way to think about the structure of the welfare system is to group together different benefits and tax credits based on the characteristics of their primary recipients. The IFS report organises benefits into the following categories: families with children; unemployed people; those on low incomes; older people; sick and disabled people; and bereaved people. It warns that the breakdown should be treated with caution as the categories correspond to the primary recipient of a given benefit, not the full amount spent on a particular group. For example, while spending on benefits targeted specifically at unemployed people is small, they also receive a significant proportion of housing benefit.

2.7 In this report we have largely followed the IFS approach, but we have treated housing benefit separately – in part because its recipients include those with a range of different characteristics and in part because it has been an area where our forecasts have been subject to significant errors in recent years. We have also grouped income support with other benefits paid largely to families with children, as lone parents are the largest remaining target group for income support. Historically, income support was the means of supporting those whose incomes were low for a number of other reasons.

³ HM Treasury (2013).

Benefits for the elderly

- 2.8 Benefits for the elderly are dominated by the basic state pension, which contains both contributory and non-contributory elements. An earnings-related element is available through additional pension schemes – notably the state second pension, which replaced the state earnings-related pension scheme in April 2002. Pension credit tops up the income of older people to a minimum level through the guarantee credit, while a savings credit aims to ensure that incentives to save for retirement are not blunted by the guaranteed minimum.
- 2.9 There are some benefits exclusively for older people, including winter fuel payments and free television licenses for the over-75s. The Christmas bonus is predominantly, though not exclusively, paid to pensioners. And the financial assistance scheme compensates certain people who lost their pension provision because their provider unexpectedly shut down.

Benefits for the sick and disabled

- 2.10 There is a wide range of welfare provision for sick and disabled people. During a short-term illness, people may be able to claim statutory sick pay. For longer-term issues, employment and support allowance (ESA) has replaced incapacity benefit as the main benefit for people unable to work due to disability. Disability living allowance (DLA) provides allowances for daily care and/or mobility needs, based on the extent of disability. DLA is currently being replaced by personal independence payments (PIP), which have different eligibility criteria. Attendance allowance (available only to pensioners) and carer's allowance provide support for those sick and disabled people that require substantial and regular care.
- 2.11 Support is also provided for sickness or injury resulting from accidents or work-related injuries. And there are specific schemes concerned with conditions resulting from service in the armed forces.

Benefits for families with children

- 2.12 There are a number of benefits targeted at families with children. Child benefit and guardian's allowance provide near-universal support for parents or guardians bringing up children. Child tax credit provides more generous support to low-income households with children. Statutory maternity, paternity and adoption pay, as well as maternity allowance, are paid out when there is a new addition to the family, for people who have worked and built up entitlement. In contrast, as part of the social fund, sure start maternity grants are one-off payments made to new mothers on the basis of need. Families may be able to receive additional help from benefits and credits that are also available to other groups – for example, lone parents are now the main recipients of income support. Tax credits and child benefit are the largest items of spending in this category.

Benefits for the unemployed

- 2.13 Jobseeker's allowance (JSA) provides a safety net for the unemployed on the condition that they take steps to find a job. There are several conditions linked to the payments. For instance, JSA claimants are required to take part in a work programme after claiming for a certain length of time. Meanwhile, the new enterprise allowance – not covered in this report

– aims to encourage more people to consider becoming self-employed and to start their own businesses as a way to get back into work. Unemployed people may also be able to claim many of the benefits aimed at other groups – notably housing benefit.

Benefits for those needing support with housing costs

- 2.14 Housing benefit is available to people on low incomes – from benefits or work – who rent their homes in the private- or social-rented sectors. Unlike many benefits, there is no set amount available to each claimant. This depends on an estimate of ‘eligible’ rent – local housing allowance rates in the private sector – and other household circumstances. These include family composition, the number of non-dependants, income, whether there is a spare room in the home, and the age and disability status of those in the household. Discretionary housing payments are payable at the discretion of local authorities to those entitled to housing benefit or universal credit who require additional financial assistance.

Benefits for the bereaved

- 2.15 Support is provided for the spouse and/or relatives of a person that dies, so long as the recipient is below pensionable age. Bereavement payments are a one-off lump sum payment to be claimed up to 12 months following a death. Bereavement allowance is a weekly payment that replaced the widow’s pension. If the bereaved person had children or was pregnant at the time of the death, then they may be able to claim widowed parent’s allowance, which replaced widowed mother’s allowance.

How the population interacts with the welfare system

- 2.16 Around half the population receive income from at least one social security benefit at any given time, and almost everyone does at some point in their life. Using survey data from the DWP family resources survey, which have been calibrated to actual benefit caseloads to adjust for under-reporting of claims for different benefits, we provide a snapshot of how different DWP benefits provided income to different types of family in Great Britain.
- 2.17 This should be treated as an approximation. It does not cover tax credits and child benefit administered by HMRC. And it does not tell us how many families are in receipt of income from more than one benefit or where more than one individual in the family is in receipt of income from the same benefit, though in some cases that can be inferred. The illustration is provided to help to frame the trends that are discussed in this report.
- 2.18 Table 2.1 shows that in 2012-13:
- among pensioner households – defined as families where at least one adult is above the state pension age – almost all pensioners were in receipt of the state pension, winter fuel payments and the Christmas bonus. Pensioner families typically contain one or two recipients of these benefits, so the caseload was around one and half times the number of pensioner families reported in the survey. Around half of pensioner families received a free television licence, which is available only to those aged over 75. The caseload for means-tested pension credit was equivalent to a quarter of pensioner

families and that for attendance allowance around a fifth of pensioner families. For those benefits not primarily focused on the elderly, caseloads for individuals living in pensioner households exceeded 1 million for disability living allowance – where eligibility is determined by health status of the individual (who may not be the pensioner in the household) – and for housing benefit and council tax benefit – which are income-related benefits for support with housing costs;

- among out-of-work working-age families – defined here as families where no one recorded working more than 16 hours a week – there were caseloads of more than 1 million for disability and incapacity benefits, and for jobseeker's allowance. But the largest caseloads were for housing benefit and council tax benefit. Recipients of some out-of-work benefits receive housing benefit automatically (through 'passporting'), but the income from other out-of-work benefits is typically low enough to make recipients eligible for it in any event. Child benefit and the child tax credit will also have been a source of income for many of these households; and
- among in-work working-age families – those where someone was recorded working more than 16 hours a week – there were also around a million recipients of housing benefit, a figure that has risen substantially in recent years. A significant number of in-work working-age households received winter fuel payments, where the qualifying age is linked to the female state pension age. As the pension ages of women and men are progressively equalised over the period to 2018, that figure will fall. Many of these working age households will have received child benefit, with many low income working families also receiving tax credits.

Table 2.1: Selected 2012-13 DWP benefit caseloads broken down by family type

	2012-13 spending (£ billion)	Estimated caseload					
		Millions of individuals			Per cent of families in each group		
		Working-age			Working-age		
		Above state pension age	Out of work (less than 16 hours)	In work (16+ hours)	Above state pension age	Out of work (less than 16 hours)	In work (16+ hours)
Elderly							
State pension	79.8	12.8	0.0	0.0	151	0	0
Pension credit	7.5	2.3	0.2	0.0	27	3	0
Winter fuel payments	2.1	11.6	0.4	0.7	136	6	4
Over-75s TV licences	0.6	4.3	0.0	0.0	51	0	0
Christmas bonus	0.2	12.1	2.4	1.1	143	36	6
Sick and disabled							
Disability benefits ¹	14.3	1.3	1.6	0.6	15	24	3
Incapacity benefits ²	10.1	0.1	1.5	0.2	1	23	1
Attendance allowance	5.5	1.6	0.0	0.0	18	0	0
Carer's allowance	1.9	0.1	0.4	0.2	1	5	1
Industrial injuries benefit	0.9	0.2	0.1	0.1	2	1	1
Families with children							
Income support	5.3	0.0	1.2	0.0	0	19	0
Maternity benefits ³	2.7	0.0	0.0	0.3	0	1	2
Unemployed							
Jobseeker's allowance	5.2	0.0	1.3	0.1	0	20	1
Housing costs							
Housing benefit	23.9	1.5	2.6	1.0	18	39	5
Council tax benefit	4.9	2.4	2.7	0.9	28	41	5
Bereaved							
Bereavement benefits	0.6	0.0	0.0	0.0	0	1	0

¹ Disability living allowance and severe disability living allowance.² Employment and support allowance and incapacity benefit.³ Statutory maternity pay (SMP) and maternity allowance (MA). Caseload breakdown only available for MA, so same proportions have been assumed for SMP caseload.

3 Drivers of welfare spending

Introduction

- 3.1 In Chapter 1, we explained that there are a variety of ways in which trends in welfare spending can be assessed – in cash terms, in real terms and as a share of national income. Whichever approach is taken, we need to understand how developments in the economy help drive those trends. These drivers can typically be split into those that affect the caseload – the number of people eligible for and claiming a benefit – and those that affect the average award – the average amount each claimant receives. In this first *Welfare trends report (WTR)*, we focus on spending in cash terms – as the welfare cap is a cash ceiling – and as a share of GDP – given our focus on the sustainability of the public finances.
- 3.2 When considering welfare spending in cash terms, we are interested in the absolute drivers of the caseload or average award. For example, population growth and ageing driving the state pension caseload, and inflation or earnings growth driving the average awards for benefits that are uprated in line with them.
- 3.3 When considering welfare spending as a share of GDP (i.e. relative to the economic activity that can be taxed to finance it), we are interested in the drivers of changes relative to GDP rather than in absolute terms, which means changes in the caseload relative to the population and changes in average awards relative to GDP per person. In this report we focus on the drivers of changes in caseloads relative to the adult population (aged 16 and over) and changes in average awards relative to GDP-per-adult.
- 3.4 With sufficient data, we can relate trends in the underlying drivers of welfare spending back to the ratio of welfare spending to GDP. For example:
- population ageing and increasing female labour market participation have increased the basic state pension caseload relative to the size of the adult population. The former has increased the proportion of adults eligible, while the latter has specifically increased the proportion of women eligible. And more of these women now qualify for the full payment, increasing the size of annual awards. Recently, the decision to uprate state pensions in line with the triple lock has also led to the average amount received rising faster than both earnings and GDP-per-adult (see Chapter 5); and
 - changes in housing tenure have been a key driver of spending on housing benefit in recent years, with the proportion of households owning their property falling and the proportion renting rising. The proportion of renters qualifying for support has also risen. Both raise the caseload relative to the population (see Chapter 9).

- 3.5 This chapter draws together the main economic trends that have affected welfare spending over the past three decades and which affect our forecasts for future spending. It focuses on four areas:
- demographic trends;
 - labour market trends;
 - inflation and earnings growth; and
 - housing market trends.
- 3.6 The forecasts used in this report are our central forecasts from the March 2014 *Economic and fiscal outlook*, on the basis of which the Government set the welfare cap in Budget 2014. Given that this was a median forecast, we would expect there to be a 50 per cent probability that spending will be higher and a 50 per cent probability that it will be lower. The trends described in this chapter are already embodied in the forecast. So, for example, it would need the proportion of households renting to rise *by more than expected*, not just in absolute terms, for us to expect housing benefit spending to be higher than forecast.
- 3.7 Chapter 4 presents ready reckoners for the impact of selected forecast changes on aspects of welfare spending to help quantify some of the risks to the forecast.

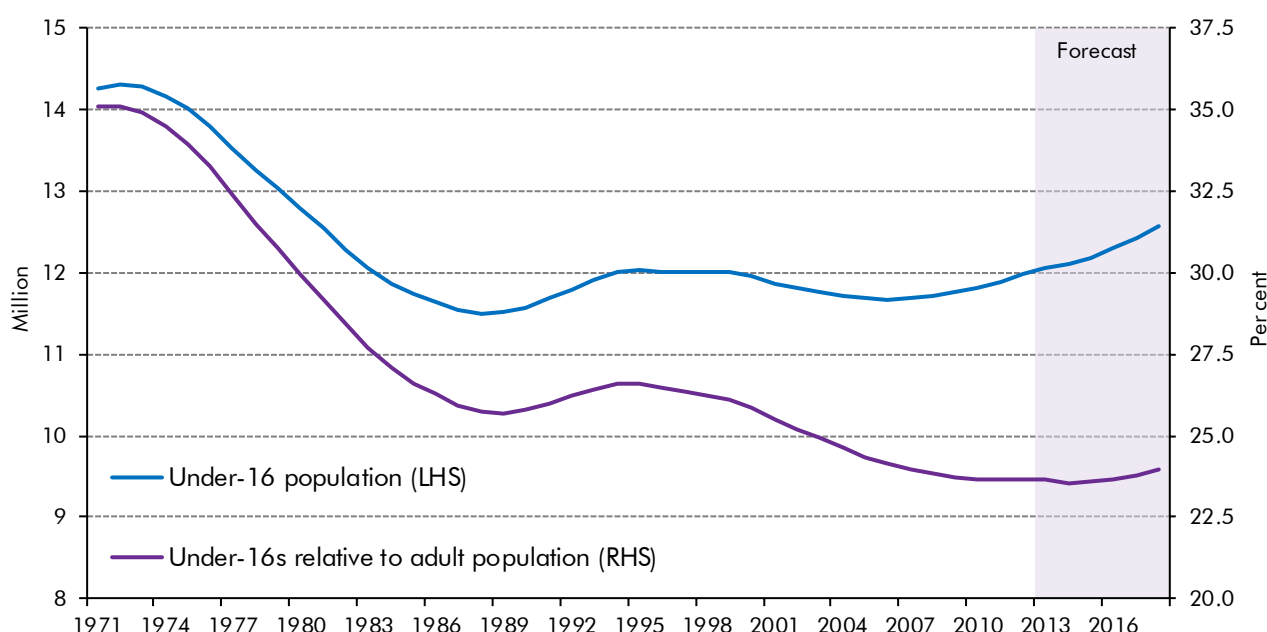
Demographic trends

Size and structure of the population

- 3.8 The size and structure of the population are important drivers of welfare spending. For example, spending on the basic state pension will be determined in part by the number of people over the state pension age (SPA), and spending on child benefit by the number of children in the population.
- 3.9 The size and structure of the population at any given time is determined by a number of factors:
- **fertility rates:** variations in the birth rate have an immediate effect on the number of children. Large fluctuations can also have long-lasting effects on the population as a cohort ages – the post-war baby-boom, for example, led to a demographic bulge that continues to affect the size and age structure of the population (see Box 3.1);
 - **life expectancy:** reductions in mortality rates at older ages tend to increase the proportion of older people in the population; and
 - **net migration:** changes in net migration affect not just the size of the population but also its age structure. In recent years, a higher proportion of immigrants to the UK have been of working age than in the native population.

3.10 Charts 3.1 and 3.2 show the evolution of two important age groups for welfare spending – those under 16 and those above the SPA. The absolute and relative size of the under-16 age group declined steadily in the 1970s and 1980s, reflecting a fall in the fertility rate from an average of 2.8 in the 1960s to an average of 1.7 in the 1990s.¹ More recently, the trend decline in the under-16 population has stabilised and reversed slightly, supported by the gradual increase in the fertility rate from 2002. All else equal, these trends would reduce the child benefit caseload relative to the adult population (see Chapter 7).

Chart 3.1: Under-16 population



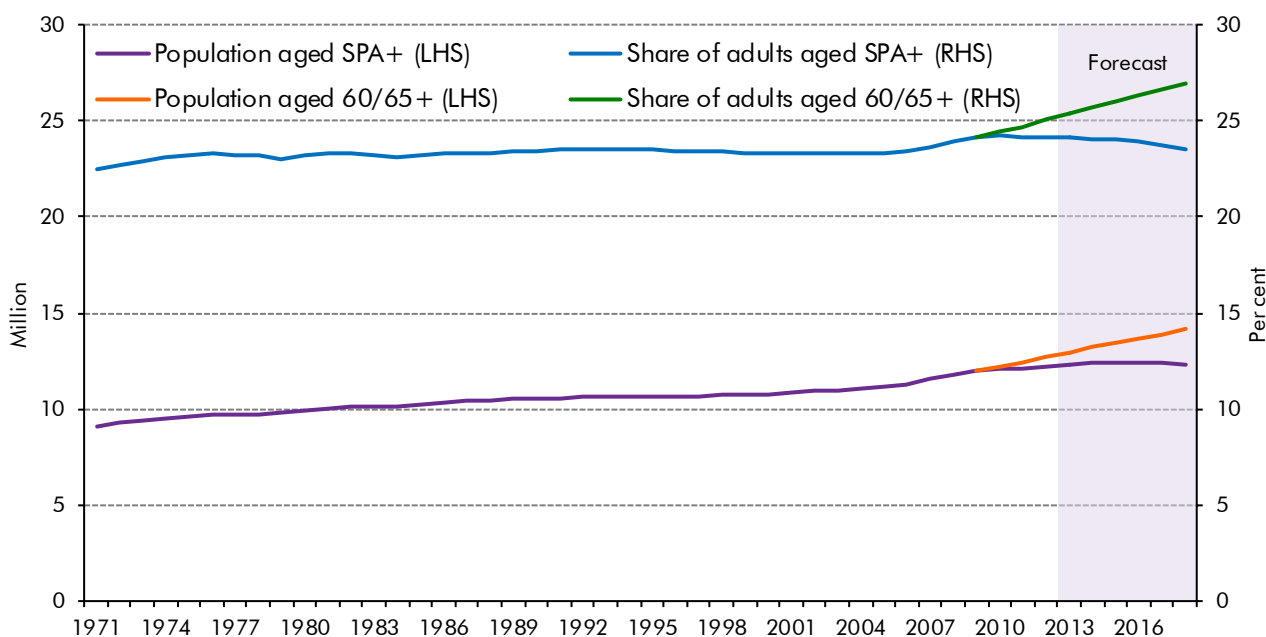
Source: ONS

- 3.11** Up to 2010, the SPA was 60 for women and 65 for men. Between April 2010 and November 2018, the SPA for women is being increased in stages from 60 to 65. From December 2018 to October 2020, the SPA for men and women will be increased from 65 to 66. So the age boundary defining the population above the SPA is moving higher.
- 3.12** Prior to these reforms, the population aged above the SPA increased steadily in absolute terms, but from the mid-1970s to the mid-2000s it was reasonably stable as a share of the adult population. In part, this reflects the gradual expansion of the working-age population, in turn reflecting past net migration and historical increases in the fertility rate. A growing working-age population leads to a growing population above the SPA as those cohorts age, but the share of the adult population aged below and above the SPA need not change.
- 3.13** More recently, the size of the population above the SPA has picked up sharply as the large post-World War II baby-boom generation has entered this age group. All else equal, this change in age structure has increased the number of people qualifying for the basic state pension. This demographic trend is being partly offset by the increases to the female SPA

¹ Total fertility rate (TFR) for the UK.

from 2010, which reduce the absolute and relative size of the population eligible for state pensions. As Chart 3.2 shows, were the female SPA not increasing to 65 by 2018, the population aged above the SPA would be 1.8 million higher and 3.5 per cent higher as a share of the adult population by that year.

Chart 3.2: Population above the state pension age

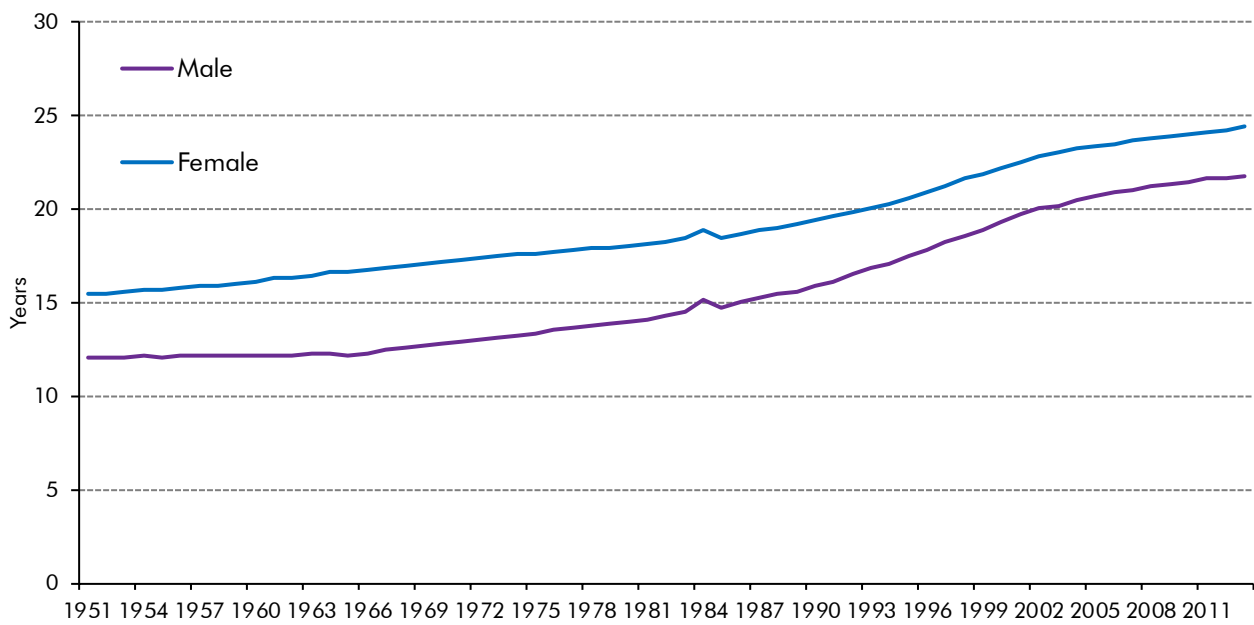


Source: ONS, OBR

3.14 Increases in life expectancy at older ages have pushed up the proportion of the adult population over the SPA. Cohort life expectancy at 65 was around 12 years for men and 16 years for women in the 1950s and 1960s. By 2011, it had increased to around 22 years and 24 years respectively (Chart 3.3).²

² Note that the bump in cohort life expectancy at 65 shown in 1984 in Chart 3.3 reflects the cohort born in 1919. Individuals born during the post-World War I influenza epidemic have subsequently experienced lower mortality rates than those born in neighbouring years.

Chart 3.3: Cohort life expectancy at age 65



Source: DWP

Box 3.1: Cohort effects in the age structure of the population

Chart A shows 'age pyramids' of the population structure in England and Wales over the sixty years from 1951 to 2011. (Detailed UK-wide data are only available from 1971.)

The 1951 census was the first after World War II. The total population in England and Wales was 43.8 million, of which 52.0 per cent were women. This reflected the greater longevity of women (visible at the top right of the 1951 pyramid), but also the direct effect of wars on several male cohorts. The pyramids are indented at certain cohorts due to lower fertility during the 1930s depression (individuals aged 12 to 20 in 1951) and the influenza pandemic of the late 1910s (the 32 to 33 year old cohort). The beginning of the post-war baby boom – when total fertility rates increased from 2.0 children per woman in 1946 to 2.6 in 1948 – is also visible, particularly for children aged 3 to 4 years by 1951. The old-age dependency ratio – the population over 65 relative to the working-age population – was 16.5 per cent in 1951.

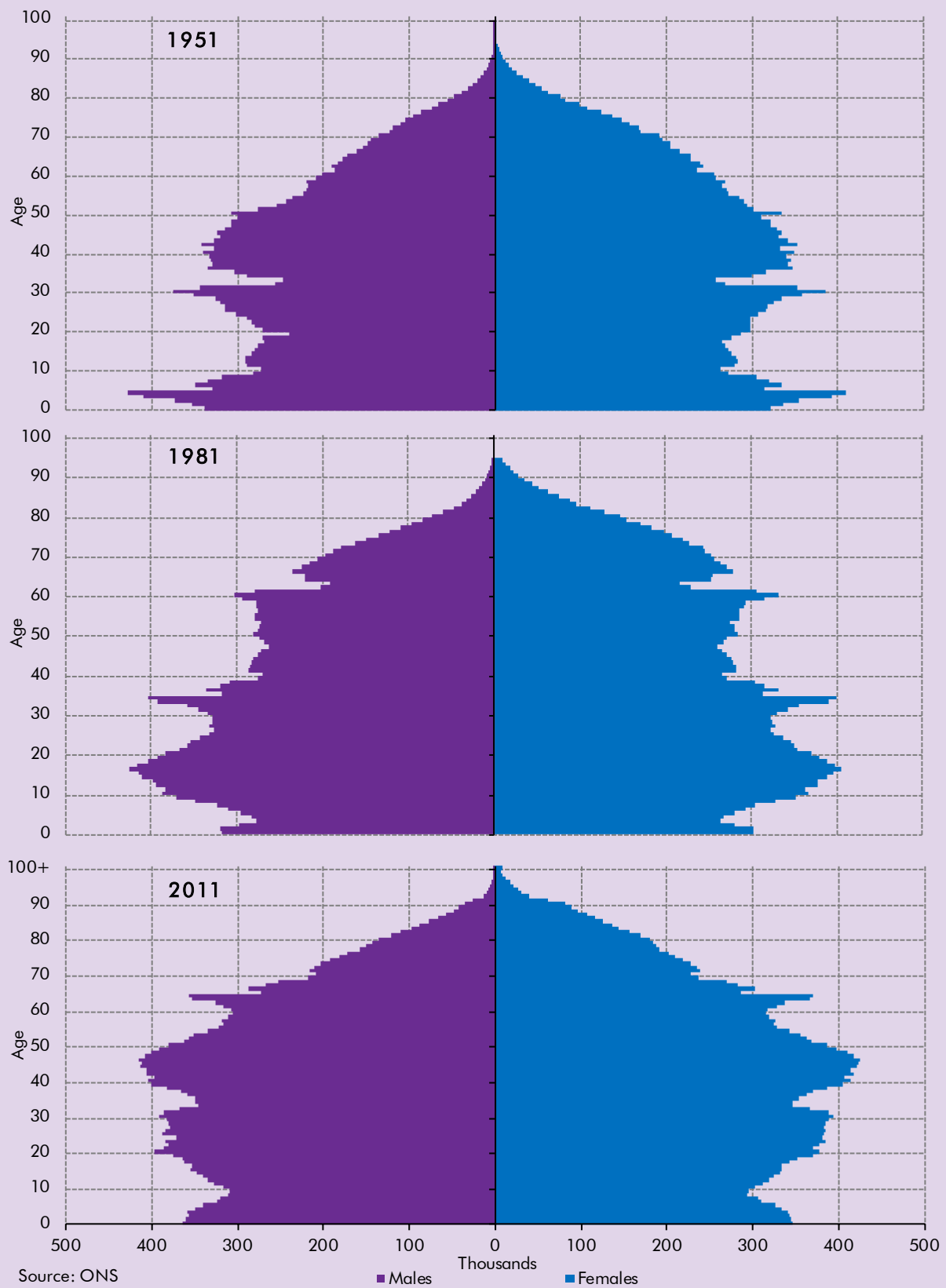
By 1981, the total population in England and Wales had reached 48.5 million. The gender composition was more balanced than in 1951, with women making up 51.3 per cent of the total. Life expectancy at birth had risen from 66 to 71 years for men and from 71 to 77 years for women, reflecting both lower rates of infant mortality and more people living past the age of 65. The first wave of baby boomers had now reached their early 30s, in the middle of their working lives. By this stage, the second baby-boom was also evident in the number of individuals aged 16 to 26, i.e. people born between 1955 and 1965. Towards the end of the 1960s, birth rates fell, which is reflected in fewer people aged 3 to 15. The old-age dependency ratio in 1981 was 23.2 per cent, an increase of 6.7 percentage points compared to 1951.

In the most recent 2011 census, the population in England and Wales had reached 56.1 million, up 7.6 million since 1981 and 12.3 million since 1951. Women represented 50.8 per cent of the population. The pyramid shows a bulge in the number of people above 60 years old – the post-war baby boom cohorts were 60 to 64 years old – and a lower proportion of people under 20 years old. The number of younger children has started to increase again, which is likely to reflect higher fertility rates of both UK-born women and immigrants arriving after the expansion of the European Union in 2004. The total fertility rate in the 2011 census was 1.93 for all women, up from the post-1930s low of 1.60 in 2001. Life expectancy at birth had risen to 79 years for men and 83 for women. The old-age dependency ratio had increased further to 25.0 per cent by 2011.

The 1960s baby-boom generation were by this stage 46 to 55 years old so – for the most part – they were still working. As they reach retirement, the shape of the population pyramid will continue to evolve and the old age dependency ratio will continue rising.

The trends depicted in these pyramids help us to understand trends in welfare spending and age-related spending more generally. For example, the post-war baby-boom generation will have affected spending on family allowance – the predecessor of child benefit – in the 1950s; working-age benefits from the 1960s to 2000s; and pensions and other benefits for the elderly from the 2010s. More generally, as we have shown in our *Fiscal sustainability reports (FSR)*, an ageing population raises the share of GDP spent on health, long-term care and pensions. As Chapter 6 discusses, spending on benefits for the sick and disabled are also likely to be affected.

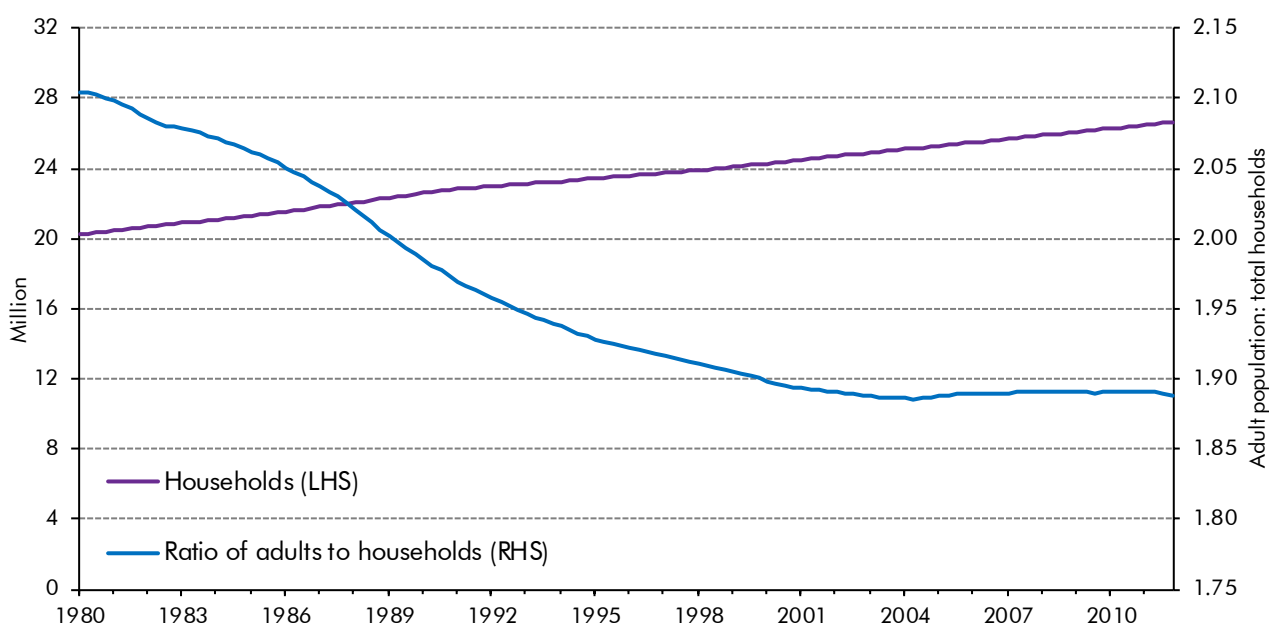
Chart A: Population pyramids for England and Wales: 1951, 1981 and 2011



Number and size of households

3.15 For some benefits – e.g. housing benefit – eligibility is linked to household rather than individual status.³ The number of households is closely linked to the size of the population, but is also affected by average household size, which in turn reflects family status and trends in the availability of housing. Chart 3.4 shows that the number of households has risen steadily but the average size of households – inferred from the ratio of the number of adults to the number of households – fell until the early 2000s and has recently been fairly stable.

Chart 3.4: The number and average size of households in the UK



Source: CLG, ONS

Labour market trends

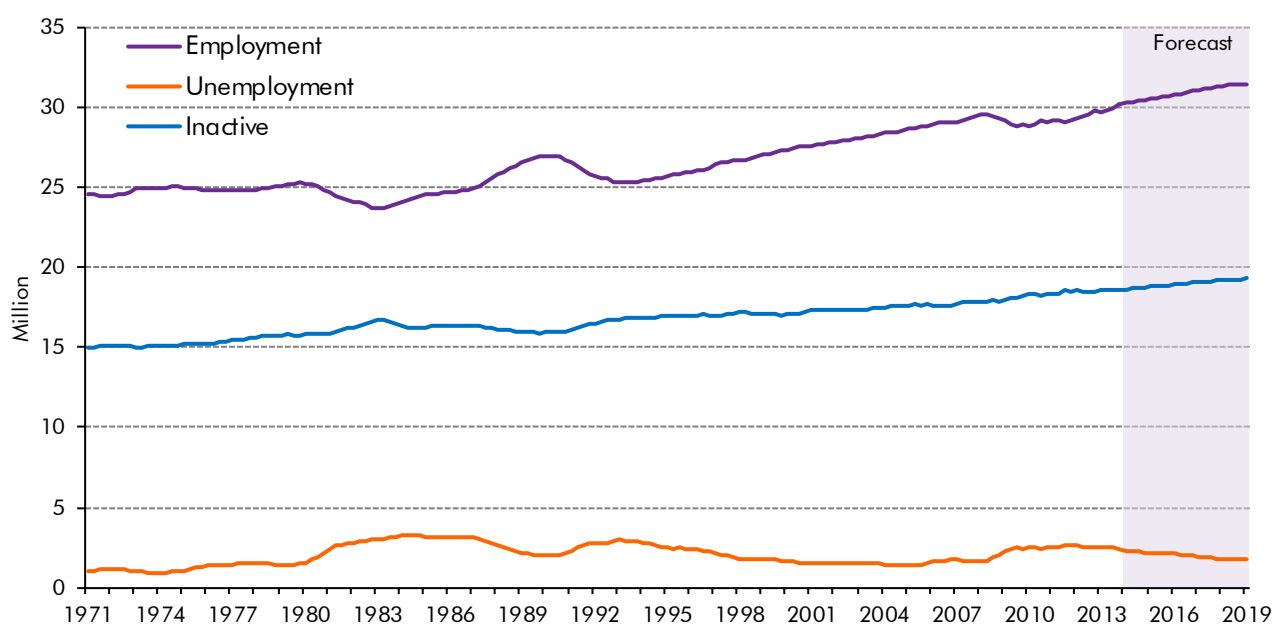
3.16 Developments in the labour market are an important driver of welfare spending. Eligibility for some benefits is associated with the labour market status of the recipient – whether a person is in paid work (employed), out of work but available for and seeking work (unemployed) or out of work but not available for and seeking work (inactive). For example, subject to certain conditions, the unemployed are eligible to claim jobseeker's allowance, while individuals inactive in the labour market may be eligible for other benefits depending on the reason for their inactivity.

3.17 Changes in employment, unemployment and inactivity can therefore have significant effects on cash welfare spending. Chart 3.5 shows the evolution of the labour force survey (LFS) measures of employment, unemployment and inactivity in absolute quantities since the 1970s. As the adult population has expanded, both employment and inactivity have trended upward. Unemployment is much smaller in absolute size than either employment or

³ In Chapter 9, we analyse changes in the housing benefit caseload relative to households rather than adults, and changes in average awards relative to GDP-per-household rather than GDP-per-adult.

inactivity. It fluctuates with the economic cycle around a slowly rising trend as the population grows. All else equal, increases in the absolute size of unemployment and inactivity will imply larger caseloads and hence greater spending on related benefits – such as jobseeker's allowance (see Chapter 8) or incapacity and disability benefits (see Chapter 6).

Chart 3.5: Labour market status of adults

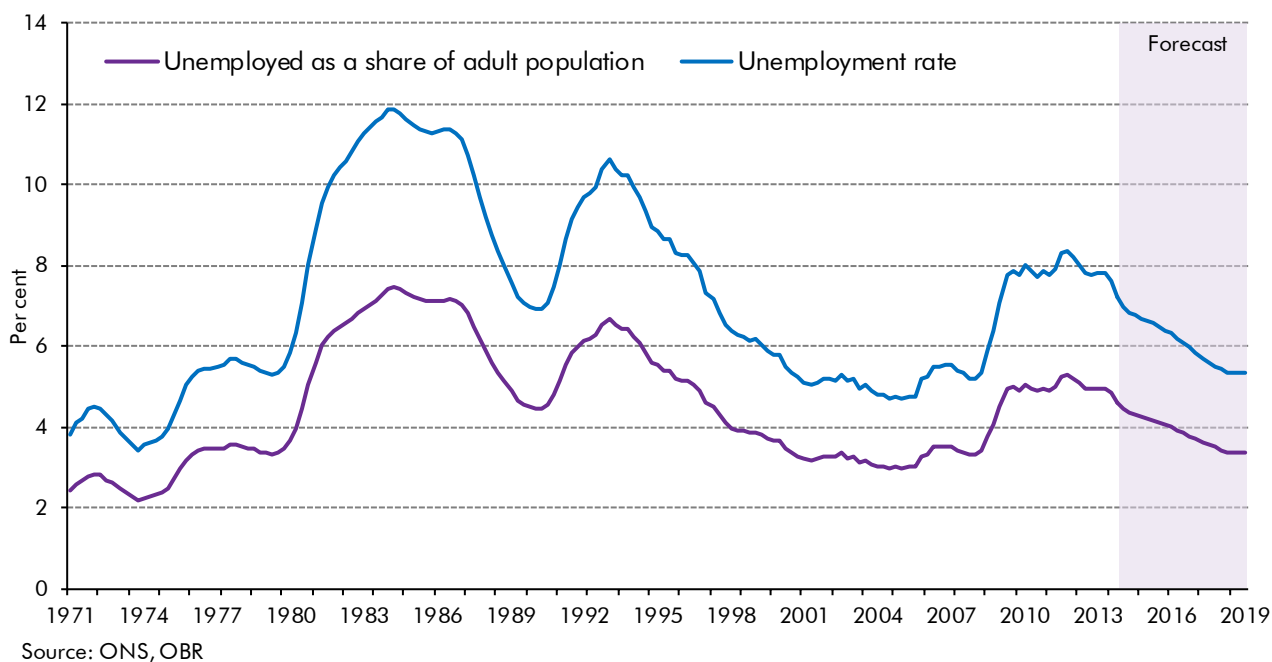


Source: ONS, OBR

- 3.18** Changes in the absolute numbers of people employed, unemployed and inactive over time largely reflect changes in the size of the population. These also affect the size of the economy. So when we look at what drives welfare spending as a share of GDP, it is more useful to consider how these quantities have evolved relative to the size of the adult population.
- 3.19** Charts 3.6 and 3.7 show the evolution of unemployment and inactivity as a share of the adult population. The share of unemployment in the adult population – a slightly different measure to the headline unemployment rate, which is measured relative to the active population – fluctuates inversely with the economic cycle. As might be expected, the rate rises during economic downturns and falls during subsequent recoveries.
- 3.20** The share of unemployed people in the adult population picked up sharply during the late 2000s recession. Since then, it has fallen back as the labour market has strengthened. Taken in isolation, this will have helped to reduce spending relative to GDP. In our latest forecast, we expect the share of unemployment in the adult population to continue to fall and thus spending on jobseeker's allowance to fall as a per cent of GDP.
- 3.21** It is worth noting that the measure of unemployment relevant for spending on unemployment benefits is the claimant count – an administrative measure that has been affected by changes to eligibility for and administration of unemployment benefits. The

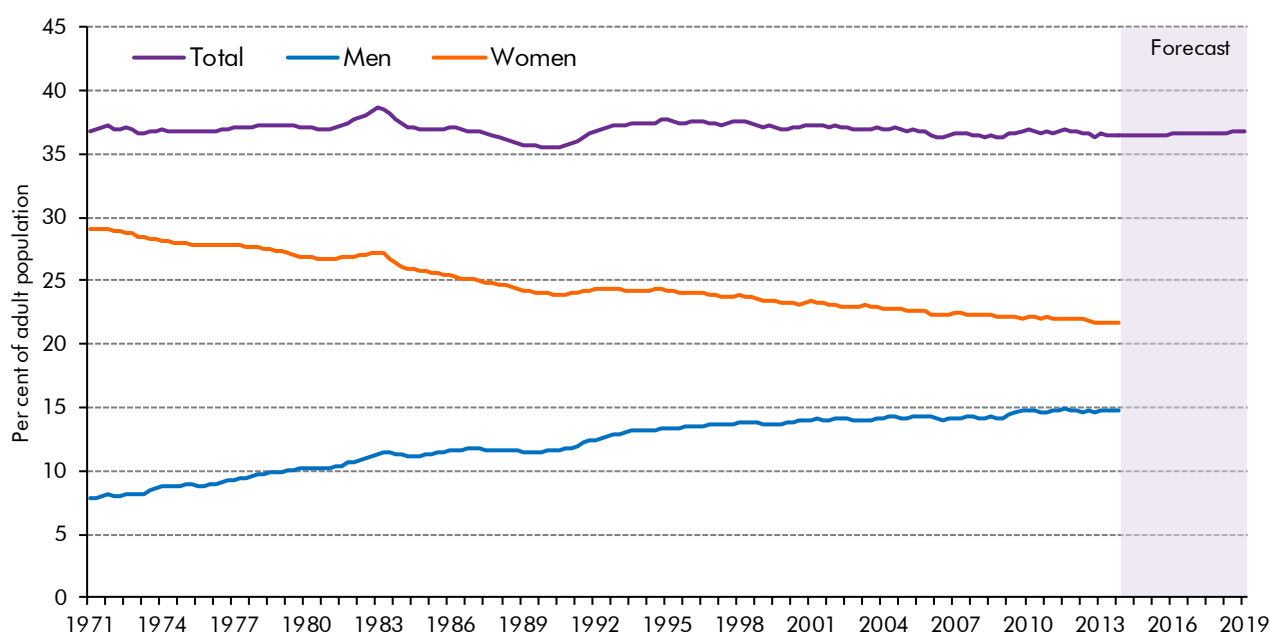
claimant count moves in a similar way to the LFS measure of unemployment, but there is typically a gap between the two that can vary over time. Box 8.1 shows that the claimant count has recently fallen even more sharply than LFS unemployment.

Chart 3.6: Unemployment relative to the adult population



3.22 A number of other benefits – such as incapacity and disability benefits – are linked more to inactivity. The share of inactive people in the adult population fluctuated with the economic cycle in the 1980s and early 1990s, but has remained relatively stable since the mid-1990s. This masks very different trends for men and women, with a rising share of inactive men offset by a steadily declining share of inactive women (Chart 3.7). The steady fall in the female inactivity rate has raised the proportion of women eligible for the full basic state pension and thereby increased the caseload as a share of the adult population. The inactive share picked up only slightly during the recent recession before falling back from 2011 as inactivity rates among older groups have fallen.

Chart 3.7: Inactivity relative to the adult population

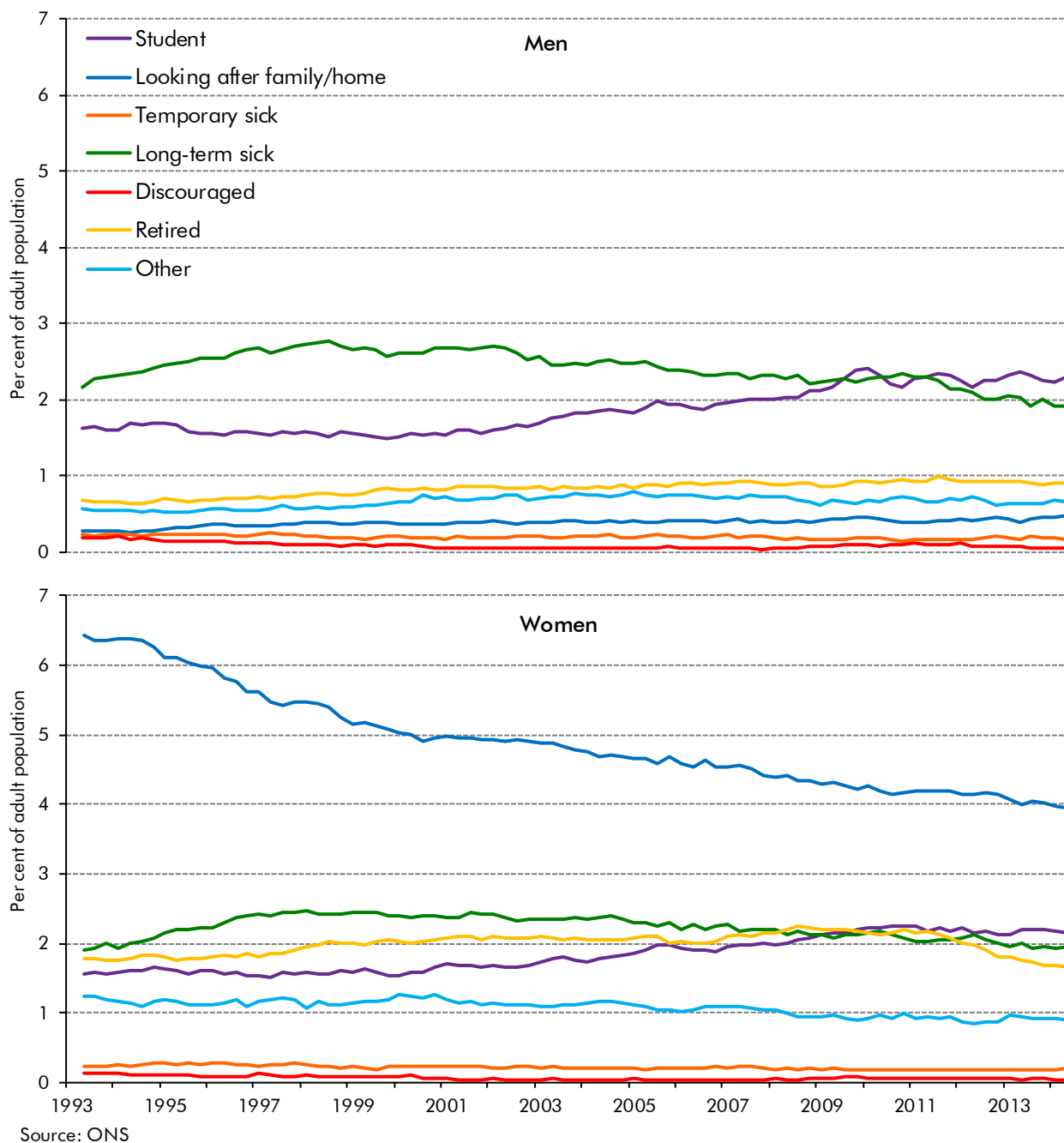


Source: ONS, OBR

3.23 For the period since 1993, LFS data allow changes in the inactive share of the population to be decomposed into the reasons given for inactivity. For those aged above the SPA, the vast majority of the inactive are retired. But among those of working age, there are a variety of different reasons reported. Chart 3.8 shows male and female working-age inactivity as a share of the adult population, decomposed into these different reasons for inactivity. The proportion of men that report being inactive due to long-term illness has gradually declined since the late 1990s – the implications of which are discussed in Chapter 6. The share of men retiring before the SPA increased steadily from the early 1990s, but has stabilised in recent years. The decline in the female inactivity rate is largely accounted for by a steady fall in the relative number of women that report being inactive due to looking after their homes and families. As with men, the relative number of retired working-age women increased slightly between the early 1990s and 2010, although the proportion has fallen more recently as the female SPA has gradually increased.⁴

⁴ Annex A to our 2014 *Fiscal sustainability report* discussed trends in activity among older people in more detail.

Chart 3.8: Labour market inactivity by reason (16 to 64 year olds)

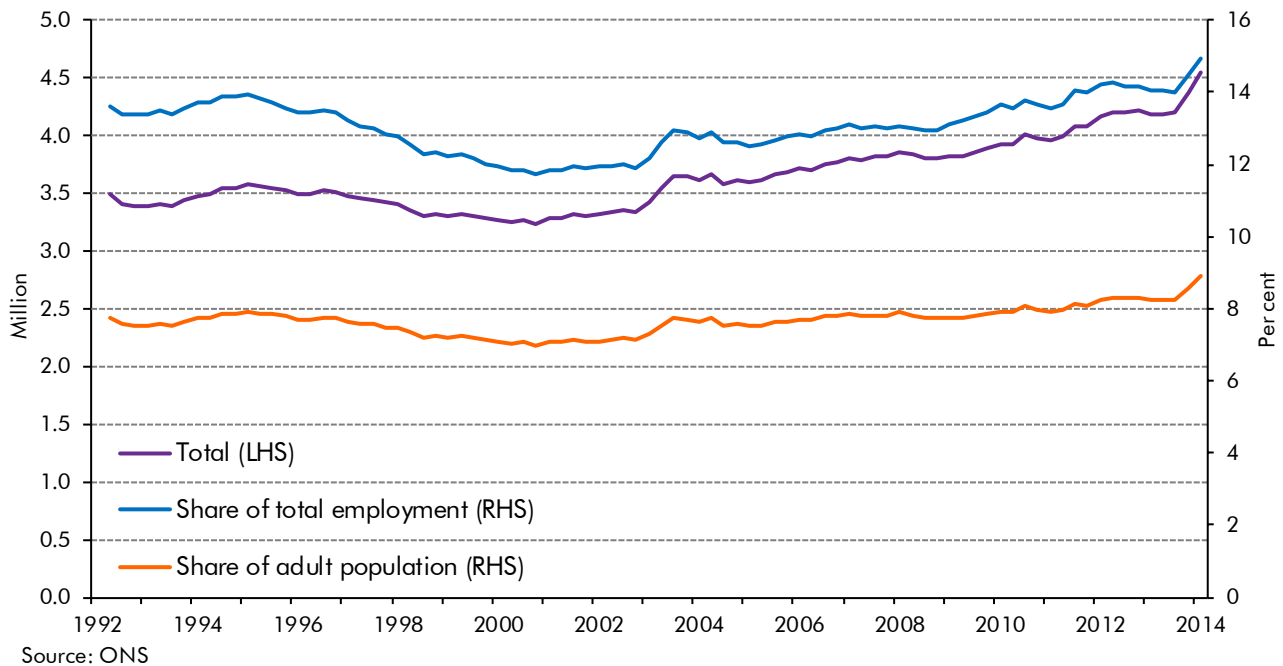


3.24 Trends in the labour market can affect welfare spending in other ways. For example, the number and relative size of self-employment may affect the tax credit caseload through eligibility for the working element of tax credits. Indeed, it is possible that this eligibility, coupled with the tougher jobseeker's allowance sanctions regime introduced in 2012, may have encouraged people to declare themselves self-employed on low income rather than unemployed. Many other factors will also have driven the recent rise in self-employment.⁵

⁵ See Annex A of our 2014 *Fiscal sustainability report*.

3.25 Chart 3.9 shows the number of self-employed people in absolute terms, as a share of the adult population and as a share of total employment. The number of self-employed has risen steadily since the 1990s in absolute terms and relative to both the adult population and total employment. These trends have accelerated since the recent recession, with self-employment accounting for much of the strength in employment in recent years.

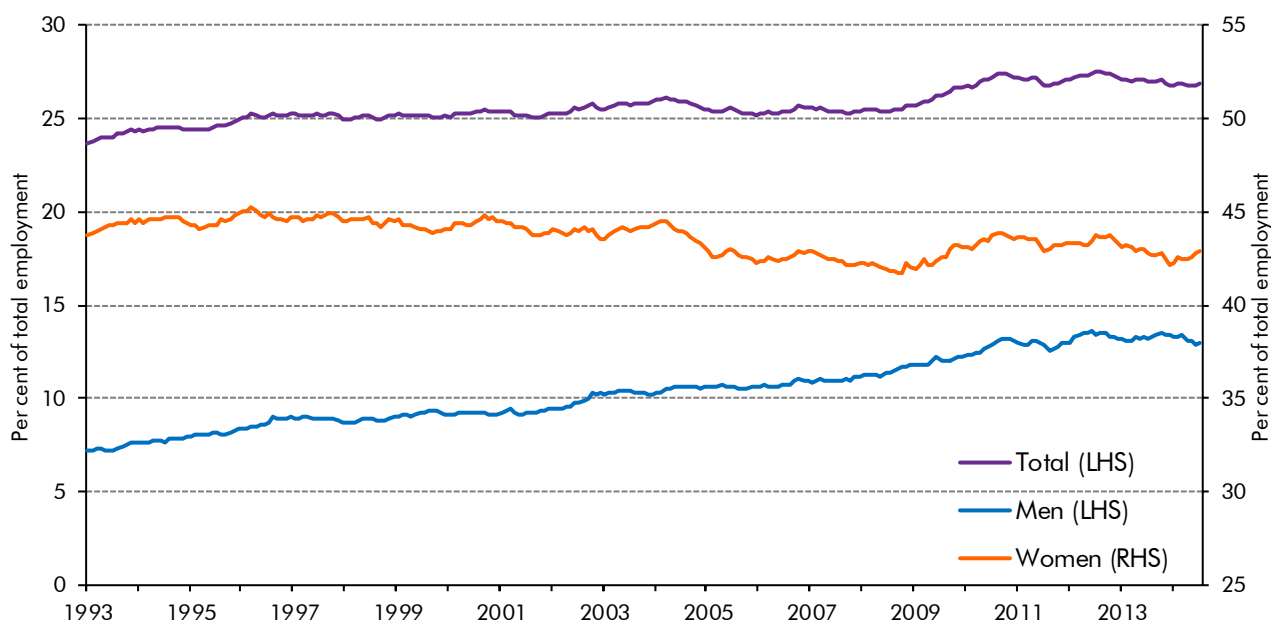
Chart 3.9: Self-employment



3.26 A number of elements of welfare spending – such as tax credits – are related to the number of hours worked. Trends in average hours worked – including the relative number of full-time and part-time workers – can therefore also affect welfare spending.

3.27 Chart 3.10 shows the trend in part-time employment over the past two decades, which has on average risen as a share of total employment. The rate of part-time working is higher among women – shown on the right-hand axis – than men, while the overall upward trend has been accounted for by a rising proportion of men working part-time. The overall share picked up during the early 1990s recession and again during the late 2000s recession, as firms adjusted to weaker demand during recessions by reducing hours worked.

Chart 3.10: Part-time employment



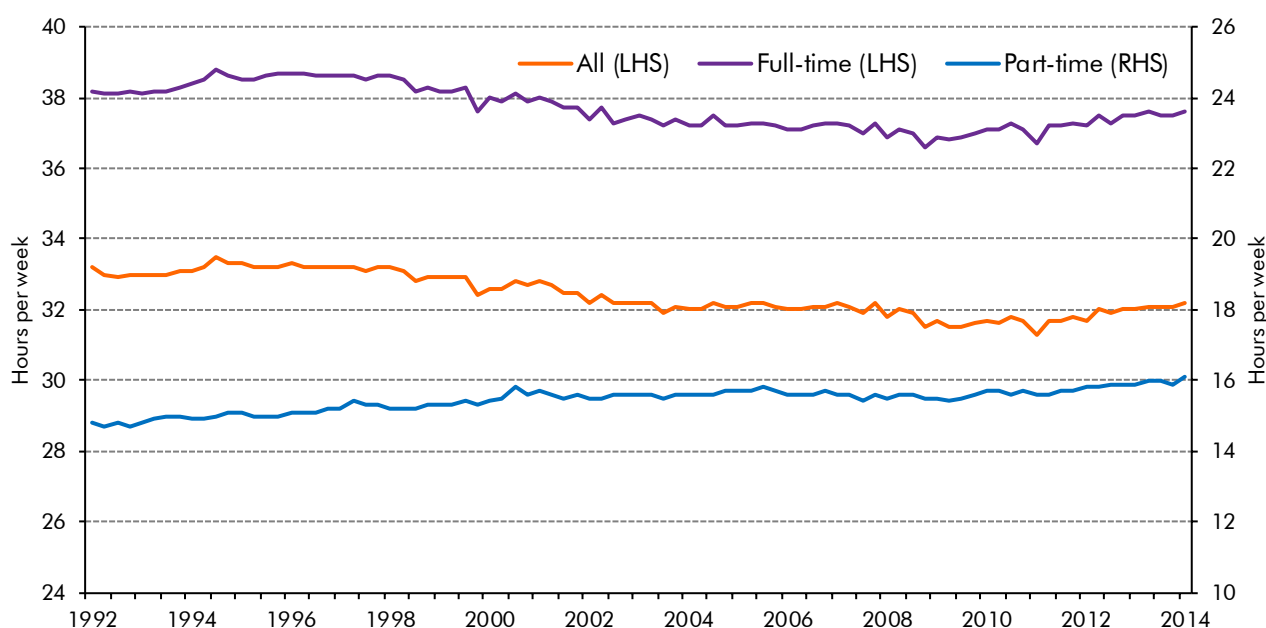
Source: ONS

3.28 Chart 3.11 shows average hours worked by those in full-time and part-time employment and the average across all employment, which is also affected by the composition of employment. Total average hours worked fell steadily between the early 1990s and 2008, continuing a downward trend in evidence for over a century. The decline over the past two decades largely reflects the trend in full-time average hours, partially offset by a gradual increase in the average hours of those working part-time. The share of those working part-time picked up sharply during the early 1990s, further reducing total average hours worked relative to full-time working hours. The share stabilised between the mid-1990s and 2008, before rising again in recent years. During the late 2000s recession, lower weekly earnings for those with reduced hours of work will have resulted in higher means-tested benefits and tax credits payments.

3.29 The downward trend in average hours over much of this period may be attributable to a number of factors, including the introduction of the 1998 working time regulations and changes in the industrial composition of employment. More recently the decline in average hours worked has reversed, despite the pick-up in the share of part-time employment. Both part-time and full-time average hours have risen steadily since 2009.⁶

⁶ See Annex A of our 2014 *Fiscal sustainability report* for further details on trends in average hours.

Chart 3.11: Average hours



Source: ONS

Inflation and earnings

Inflation rates and earnings growth

- 3.30** The rate at which benefits are uprated each year is typically tied to a measure of inflation or, less often, to a measure of earnings growth. Inflation or earnings growth are therefore important determinants of the average award for most benefits.
- 3.31** The extent to which benefits that are linked to price inflation change relative to overall earnings depends on the evolution of real earnings growth, since earnings growth in cash terms is the sum of two components – real earnings growth and price inflation. As such, if real earnings growth is positive, benefits linked to inflation will rise less quickly than overall earnings growth, and average awards will fall relative to earnings.
- 3.32** Over time, real earnings growth would be expected to grow broadly in line with productivity growth – the growth in real GDP per worker. Real GDP per worker is in turn closely linked to the GDP-per-adult measure we use in later chapters of this report to decompose the effect of average awards on welfare spending as a share of GDP. Changes in GDP-per-adult are equal to the sum of changes in GDP per worker and changes in the employment rate. This means that for benefits that are linked to price inflation:
- if productivity growth is positive, average awards will tend to fall relative to GDP-per-adult and average earnings. All else equal, the stronger the rate of productivity growth, the stronger the growth in GDP-per-adult and average earnings relative to price inflation and average awards – and vice versa; and

- if the employment rate rises, average awards would fall relative to GDP-per-adult, but not average earnings. All else equal, the more quickly the employment rate rises (for given productivity growth), the greater the margin by which GDP-per-adult rises relative to price inflation and average awards – and vice versa.

3.33 Different measures of inflation can also affect the relative growth of GDP-per-adult and average awards. For example, the whole economy measure of inflation used in GDP is the GDP deflator; the rate of inflation used to uprate benefits is generally a narrower measure of consumer prices. While consumer price inflation is an important component of the GDP deflator, the two measures typically diverge,⁷ implying that benefits are rarely uprated at the same pace as the GDP measure of inflation.

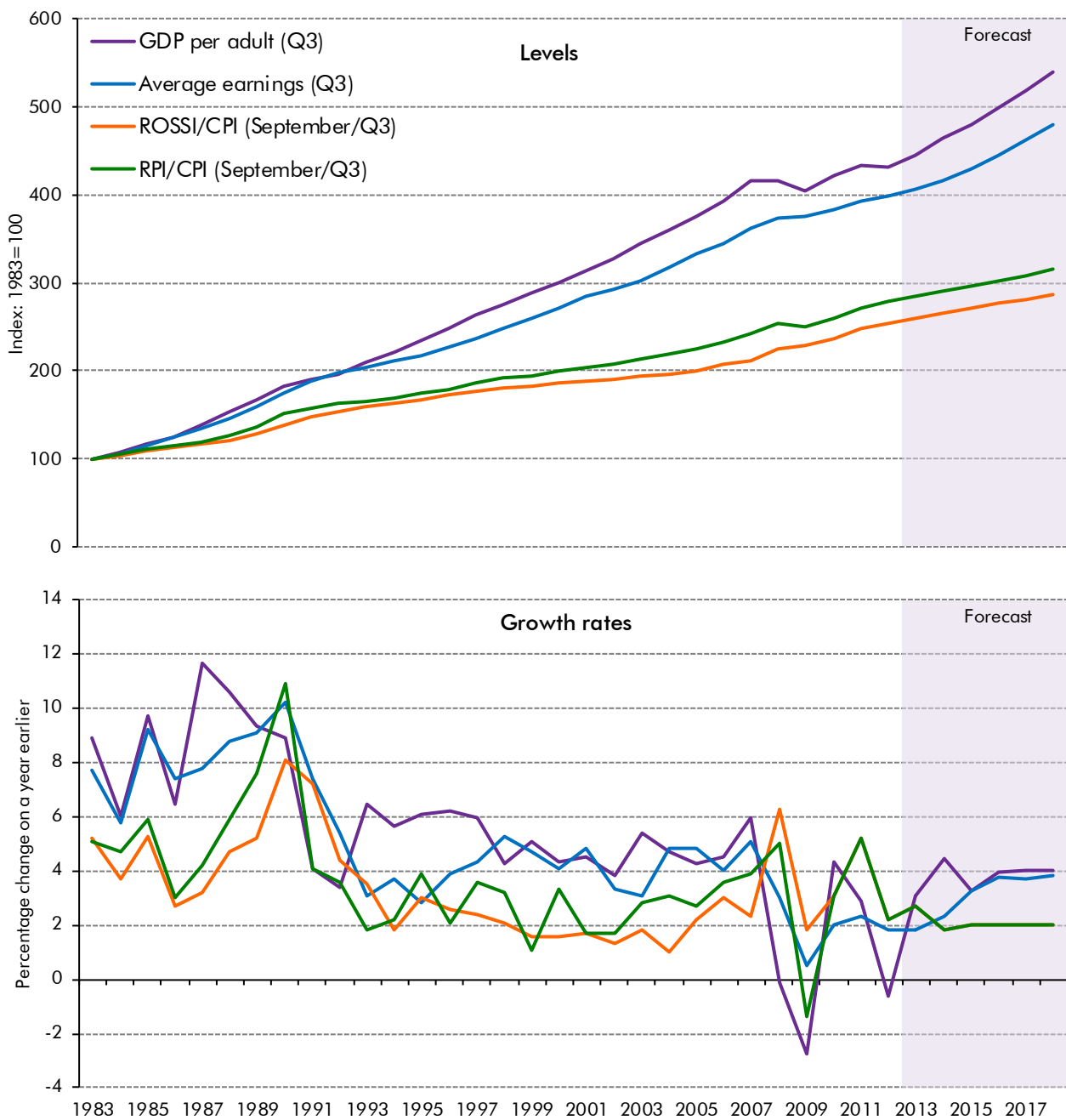
3.34 A number of different measures of price inflation have been used to uprate benefits. Prior to 2011-12, most benefits were uprated in line with the retail prices index (RPI) measure of inflation, while means-tested benefits were generally uprated in line with the ROSSI measure, which is RPI excluding a variety of housing costs. Since 2011-12, the baseline assumption has been to uprate most benefits in line with the consumer prices index (CPI), though policy measures have been introduced to uprate many working-age benefits by 1 per cent in certain years. (The Office for National Statistics concluded in 2013 that the RPI did not meet its required standards for designation as a 'national statistic'.)

3.35 Chart 3.12 compares the measures of price inflation with the growth of GDP-per-adult and average earnings. The two measures of inflation shown link either RPI or ROSSI inflation up to 2010 with CPI inflation from 2011, reflecting the default uprating for most benefits. Between the early 1990s and 2008, both GDP-per-adult and average earnings grew more quickly than ROSSI and RPI inflation – consistent with positive average productivity growth over this period. Taken in isolation, the typical uprating of benefits would have therefore implied falling average awards relative to GDP-per-adult and average earnings.

3.36 Since the start of the recession in 2008, productivity has fallen and price inflation has outpaced the growth of average earnings and GDP-per-adult, thereby boosting the relative generosity of average awards. The fall in the employment rate in 2008 and 2009 will have further reduced GDP-per-adult relative to price inflation, although this has been largely reversed by the subsequent recovery in employment.

⁷ This could either be because one of the other elements of the GDP deflator – the government consumption deflator, investment deflator, or terms of trade – is growing at a different rate to the consumer price index or because the specific consumer price index used to uprate a benefit differs to the one used in the construction of the GDP deflator.

Chart 3.12: Measures of inflation and earnings

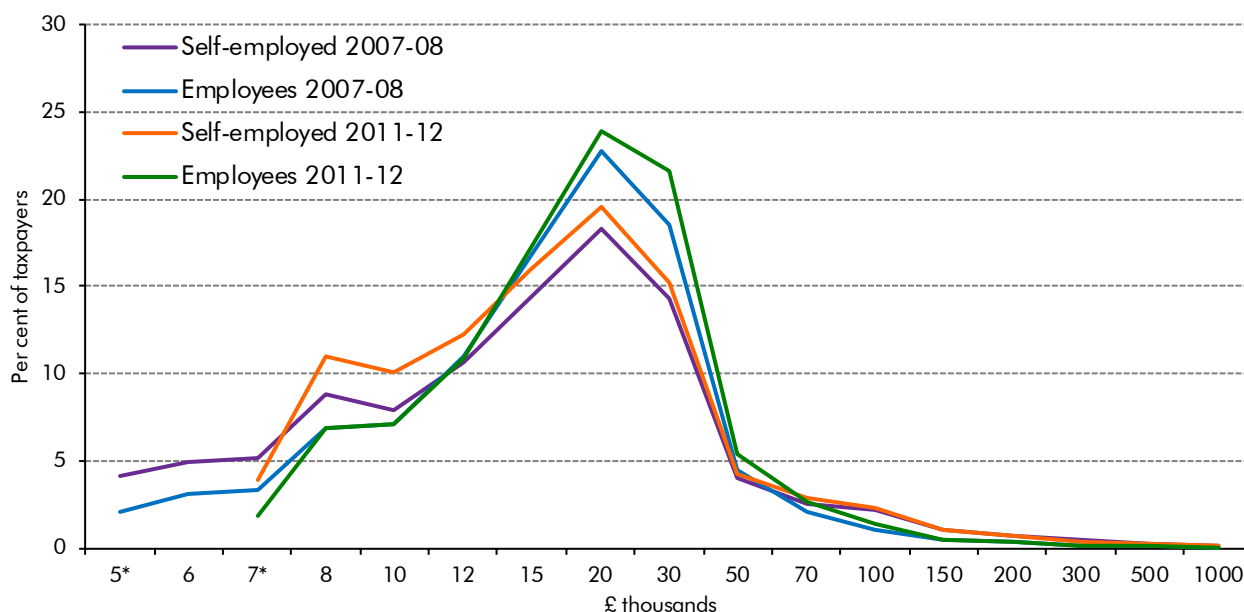


3.37 Not all benefits are uprated in line with price inflation. The basic state pension is uprated each April in line with the 'triple lock' – the highest of the previous September's average earnings growth, CPI inflation or 2.5 per cent. Partly because of the weakness of productivity growth and real earnings, this has led to the average amount received rising faster than earnings and GDP-per-adult in recent years.

Income distribution

- 3.38** Changes in the distribution of income – in particular those affecting the lower end of the distribution – can affect eligibility of means-tested benefits such as tax credits and housing benefit. Withdrawal rates on some benefits can be over 100 per cent, which means rises or falls in wage income can be offset pound-for-pound by changes in benefit entitlement.
- 3.39** The introduction of the national minimum wage in 1998 – followed by the substantial increases in the minimum wage in 2002 and 2003 – contributed to hourly earnings rising faster at the bottom of the income distribution than the median over the five years to 2003.⁸
- 3.40** More recently, there has been evidence that the strong growth in self-employment has been skewed towards the lower end of the income distribution. HMRC data indicate that the proportion of the self-employed reporting incomes below the personal allowance rose from 21 per cent in 2007-08 to 35 per cent in 2011-12 (Chart 3.13). For those subject to income tax, a higher proportion of the self-employed declared lower incomes in 2011-12 than in 2007-08.

Chart 3.13: Employee and self-employed income distribution (taxpayers only)



*Distributions start at personal allowances for 2007-08 (£5225) and 2011-12 (£7475)
Source: HMRC

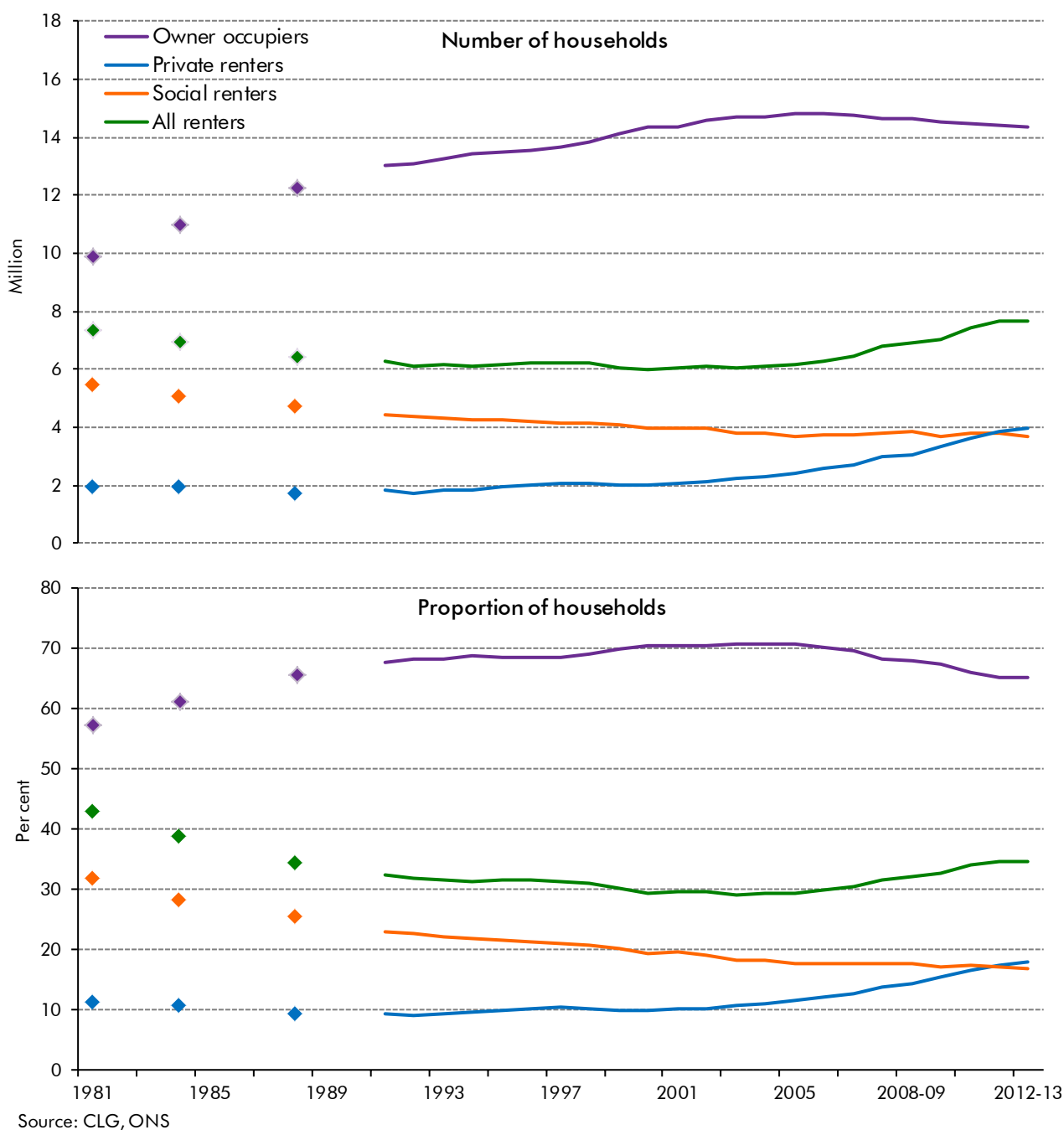
Housing market trends

- 3.41** Developments in the housing market are an important driver of spending on housing benefit. The housing benefit caseload is affected by trends in housing tenure – specifically, the number of households renting rather than owning their homes – and eligibility among renting households, which will reflect labour market status and rents.

⁸ See Gregg (2008).

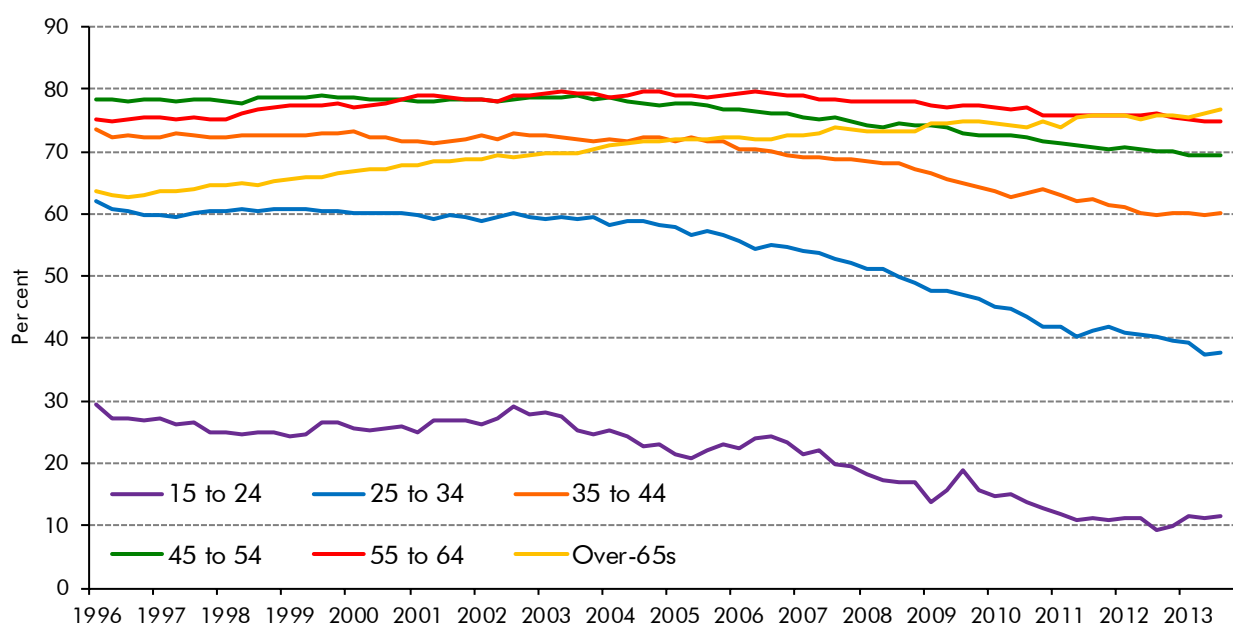
- 3.42 Chart 3.14 shows trends in housing tenure in England since the early 1980s. The absolute and relative numbers of those renting privately remained broadly flat through the 1980s and the 1990s. By contrast, the number of owner occupiers increased steadily over the period and the number of social renters gradually declined – trends at least partly explained by the introduction of ‘right to buy’ schemes in the 1980s.
- 3.43 More recently, the number of private renters has increased while the number of owner-occupiers has fallen – trends that pre-date the 2008-09 recession but that were exacerbated by it. Between 2007-08 and 2012-13, the combination of high house prices relative to average earnings and tougher mortgage requirements reduced the scope for people to move from renting to owning. With the number of social renters broadly stable in absolute terms, the increase in private renters has helped to increase the total number of renters, increasing the potential size of the housing benefit caseload. (In 2012-13, the number of private renters exceeded the number of social renters for the first time in almost 50 years.) Our March 2014 forecast assumed a continuation of these trends – at a more gradual rate than in recent years – with a fall in owner-occupancy among working-age households offsetting a rise in owner-occupancy among pensioner households.

Chart 3.14: Housing tenure in England



3.44 Chart 3.15 shows owner-occupancy rates by age group as reported in LFS microdata. The trend away from owner-occupancy over the past decade has been concentrated among younger age groups, with particularly significant falls among those aged under 44. The relative number of owner-occupiers aged over 44 has been more stable, although these groups have also seen owner-occupancy rates decline since the mid-2000s. The fall in working-age owner-occupancy has been partly offset by a steady upward trend among the over-65s.

Chart 3.15: Owner-occupancy rates by age group



Source: DWP analysis of LFS microdata

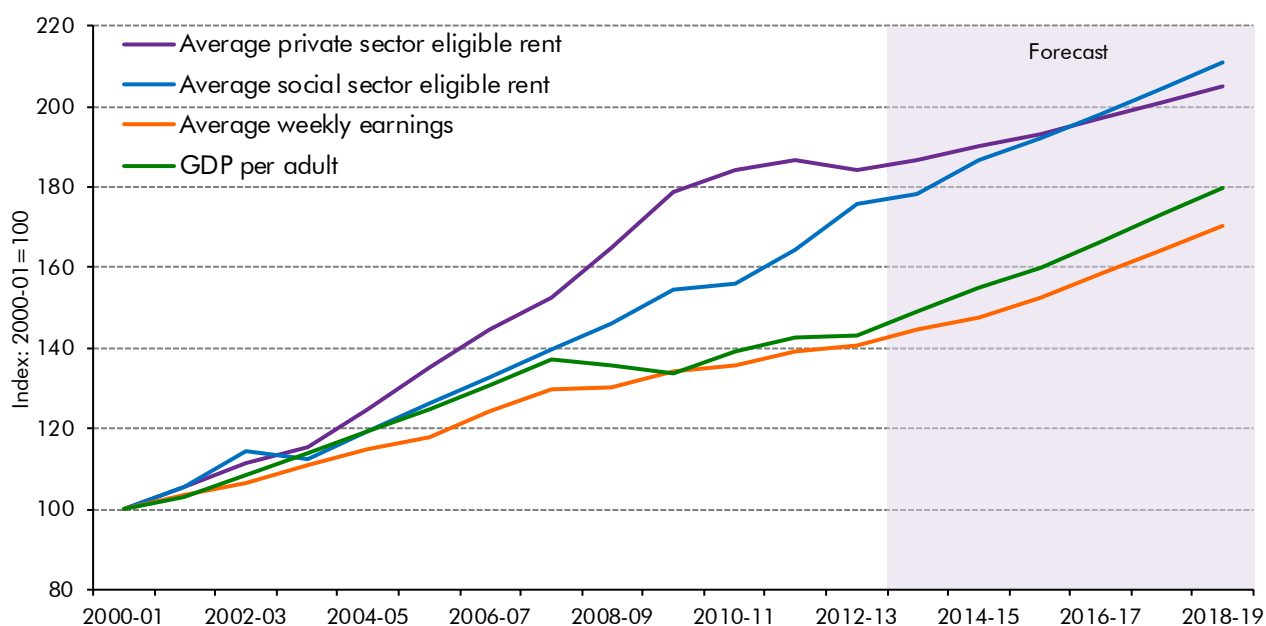
- 3.45** The proportion of renters eligible for housing benefit reflects economic developments relative to eligibility criteria. To claim housing benefit, a household's income and capital (for example, savings or property) must be below a certain level, so the size of the caseload will depend partly on the rate of earnings growth. The recent rise in the proportion of the renting population claiming housing benefit is likely to be related to the weakness of average wage growth relative to rent inflation. This explanation is supported by Department for Work and Pensions (DWP) administrative data, which suggest that the rise in the private-rented sector housing benefit caseload since the recession has been accounted for by people in employment.
- 3.46** As housing benefit provides assistance with the payment of rent, trends in the average award will – in the absence of policy effects – depend on movements in average rents. In relative terms, trends will depend on how average rents evolve relative to earnings and GDP-per-adult.
- 3.47** Chart 3.16 shows the evolution of average eligible rents in the private and social-rented sectors since 2000-01, and compares them with the trend in average earnings and GDP-per-adult. (Due to a number of problems with the measurement of private rents in the CPIH measure of inflation,⁹ we have based this comparison on DWP administrative data on eligible rents.) Since 2000-01, average eligible rents in the private sector have increased more quickly than average earnings or GDP-per-adult. This gap opened up further in the first two years of the recession as productivity fell, although it has since stabilised. Eligible rents in the social sector – which are in large part driven by policy – generally kept pace with

⁹ See ONS (2014).

GDP-per-adult between 2000-01 and 2007-08, before the fall in productivity led to a divergence between the two from 2008-09.

- 3.48 All else equal, the increase in average eligible rents in the private sector implies a rising average award relative to GDP-per-adult. In addition, the shift in the composition of the renting population toward the private sector – where average rents are generally higher – will also have increased the average award across housing benefit as a whole. Chapter 9 provides further analysis of housing benefit spending.

Chart 3.16: Rents and earnings growth



Source: DWP, ONS, OBR

Conclusion

- 3.49 In order to understand trends in welfare spending, it is necessary to consider developments in the underlying economic drivers of those trends. These drivers can typically be split into those that affect the caseload – the number of people eligible for and claiming a benefit – and those that affect the average award – the average amount each claimant receives.
- 3.50 Trends in the size and structure of the population, the labour market, inflation and the housing market are all important determinants of the size of the caseload and the average award. In Chapters 5 to 10 we examine trends in different types of welfare spending in more detail, and decompose these trends into the underlying drivers described in this chapter. Chapter 4 draws together the main themes from these analyses and the implications for our latest forecast and for the Government's welfare cap.

4 Overall trends in welfare spending

Introduction

4.1 In Chapters 5 to 10, we use the approach set out in Chapter 1 to analyse trends in spending on individual benefits and tax credits over the past three decades and in our latest medium-term forecasts and long-term projections. Before turning to that benefit-by-benefit analysis, this chapter:

- discusses overall trends in welfare spending and identifies the main themes;
- identifies some key risks to our latest forecasts for welfare spending; and
- considers the implications these trends and risks may have for our forthcoming assessment of the Government's performance against the welfare cap.

Historical trends in welfare spending

4.2 This section starts by describing the evolution of welfare spending since 1983-84, before looking at the main drivers of trends over that period. It concludes by decomposing the changes numerically to identify the most important factors driving them.

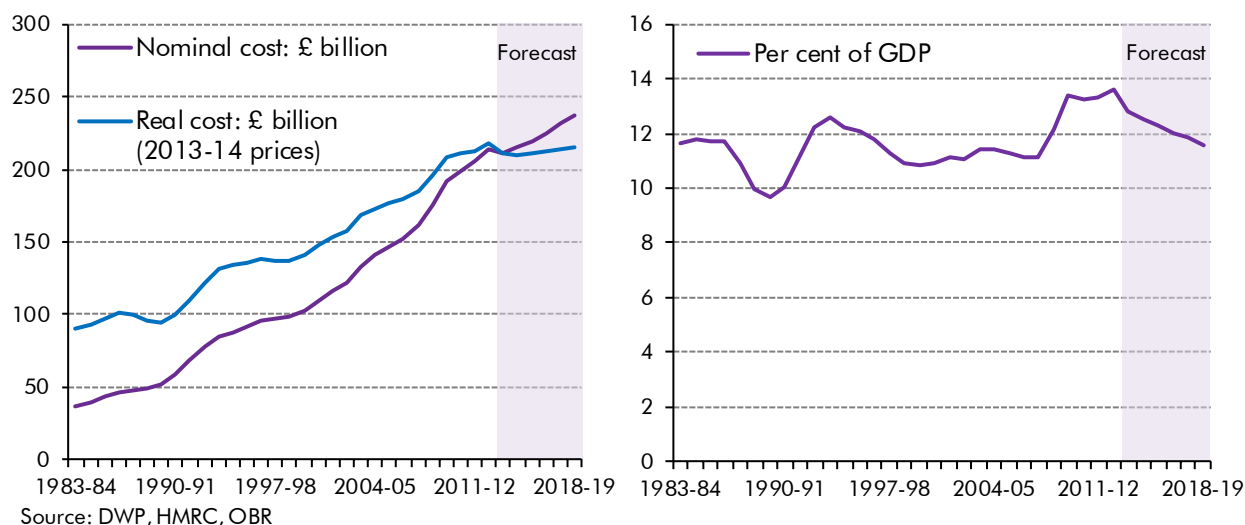
The size and composition of welfare spending

4.3 Chart 4.1 shows that between 1983-84 and 2013-14, overall spending on welfare increased around fourfold in cash terms (from £36½ billion to £211 billion) and more than doubled in real terms, adjusted for whole economy inflation. As a proportion of national income, there has been no clear upward or downward trend in spending over time, although there have been fluctuations from year to year. The ups and downs are counter-cyclical, with spending rising during recessions and falling as the economy recovers.

4.4 Between 1983-84 and 2007-08 – the brink of the last recession – welfare spending varied between 9.6 per cent of GDP in 1989-90 and 12.6 per cent of GDP in 1993-95, averaging 11.2 per cent over the period as a whole. It was much the same at the end of the period (11.1 per cent of GDP in 2007-08) as at the beginning (11.6 per cent of GDP in 1983-84).

4.5 Between 2007-08 and 2012-13, during the recent recession and weak recovery, higher spending and very weak nominal GDP growth pushed welfare spending up to a fresh peak of 13.6 per cent of GDP. This was a slightly smaller rise than that seen during the recession and recovery of the 1990s, even though the latest recession was much deeper.

Chart 4.1: Total welfare spending in the UK

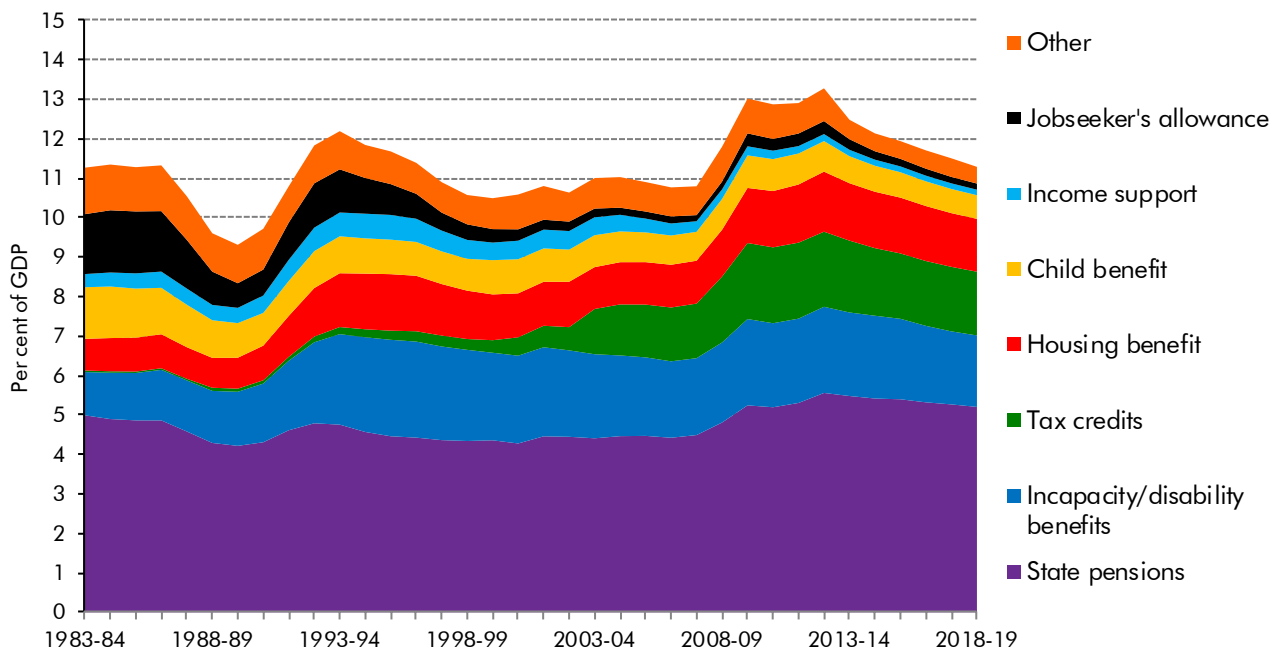


Trends in the composition of welfare spending by different benefits

- 4.6 Chart 4.2 shows the changing composition of welfare spending in recent decades and across our latest forecast period. One constant has been that state pensions have been the largest component, averaging 37 per cent of total welfare spending over the past 30 years and expected to rise to 44 per cent of the total by 2018-19.
- 4.7 Fluctuations in welfare spending as a share of GDP have reflected movements in the most counter-cyclical benefits – unemployment benefits and, more recently, housing benefit. Box 4.1 looks in more detail at the extent to which spending on different benefits moves with the cycle. In addition to these cyclical patterns, periods of stronger GDP growth – such as the late 1980s – often see all types of welfare spending falling as a share of GDP, reflecting default uprating by inflation rather than earnings for many benefits, and the effects of policy responses to increases in welfare spending in preceding periods of weaker GDP growth.
- 4.8 It is also apparent from Chart 4.2 that:
- spending on the main income-replacement benefits for people who are out of work has fallen over time. This is partly because ‘extra costs’ additions have been stripped out of unemployment benefits, incapacity benefits and income support. But it also reflects steady falls in caseloads (abstracting from the late 2000s recession) and the uprating of benefits in line with, and sometimes by less than, inflation; and
 - the largest rises in welfare spending have been on the ‘extra cost’ payments for housing, disability and children, which were created or extended in the 1970s and have since been substantially expanded in cost and scope:
 - spending on housing benefit has risen by 0.7 per cent of GDP over the past 30 years to 1.5 per cent in 2013-14;

- spending on disability living allowance has risen by 0.5 per cent of GDP since its introduction in 1992-93 to reach 0.8 per cent in 2013-14; and
- spending on cash benefits for families with children has risen by 1.2 per cent of GDP to reach 2.5 per cent in 2013-14 (with higher spending on tax credits offsetting falls in child benefit).

Chart 4.2: Welfare spending by type of benefit



Box 4.1: The cyclicalities of spending on benefits and tax credits

The economic cycle is one driver of trends in welfare spending. We can assess its importance by estimating the sensitivity of spending to changes in the output gap – the difference between actual GDP and an estimate of its potential or underlying level.

Table A reports the results of regressions estimating the cyclicalities of different benefits and tax credits. It shows that spending on most benefits is counter-cyclical, but typically not that strongly.

Table A: The elasticity of benefits and tax credits to the economic cycle, 1985-86 to 2012-13

	Spending as a per cent of GDP	Caseloads as a per cent of the adult population	Average awards as a per cent of GDP-per-adult
Unemployment benefits	-11.89 *** 2.02	-10.76 *** 2.59	-1.29 1.83
Housing benefit ¹ - outside the cap (1989-90 to 2012-13)	-9.82 *** 2.14	-6.93 *** 2.05	-2.61 *** 0.58
Housing benefit ¹ - inside the cap (1989-90 to 2012-13)	-2.41 *** 0.47	0.00 0.32	-2.42 *** 0.31
Tax credits	-3.62 ** 1.24		
Incapacity benefits	-2.62 *** 0.51	-0.86 ** 0.41	-1.78 0.58
Disability living allowance (1992-93 to 2012-13)	-2.52 0.90	-0.45 0.35	-1.38 0.50
Pension credit ²	-2.28 1.05	0.46 1.06	-2.72 1.19
Child benefit	-2.05 0.58	-0.21 0.06	-1.84 0.59
State pension	-1.85 ** 0.38	-0.12 0.09	-1.73 * 0.37
Attendance allowance	-1.73 0.74	-0.09 0.67	-1.71 *** 0.23
<i>Memo: Housing benefit¹ - total</i>	-2.31 *** 0.41	-0.41 0.28	-1.23 *** 0.29

Note: Bold figures represent elasticities with respect to the output gap, capturing both contemporaneous and lagged effects.

Significance is assessed against a coefficient of -1 for spending and average awards (to abstract from the denominator effect, as GDP moves with the output gap) and 0 for caseloads.

*** Significant at 1 per cent; ** significant at 5 per cent; * significant at 10 per cent. Figures in italics represent robust standard errors.

¹ Housing benefit caseloads represent caseloads as a per cent of total households, and average awards represent average awards as a per cent of GDP-per-household.

² Includes pension credit and its predecessors.

Table A also looks at whether it is the caseload or the average award that explains any counter-cyclical pattern in spending. It shows that the most counter-cyclical benefits have caseloads that are closely associated with the cycle, in particular jobseeker's allowance (JSA) and the element of the housing benefit caseload that is passported for those claiming JSA (both of which are outside the welfare cap). The caseload for these benefits is directly related to the output gap in the sense that one component of that gap is the difference between the actual unemployment rate and its

estimated structural or underlying rate. This is consistent with the Government's stated reason for not including these elements of spending in the welfare cap, due to their role as an automatic stabiliser helping to cushion the economy from the cycle.

For the mildly counter-cyclical benefits, their cyclicality appears to be due to the average award varying less than the output gap rather than the caseload being sensitive to the cycle. Counter-cyclical spending as a share of GDP on these benefits reflects a denominator effect – the cash value of GDP tends to fluctuate more over the cycle than the cash value of spending.

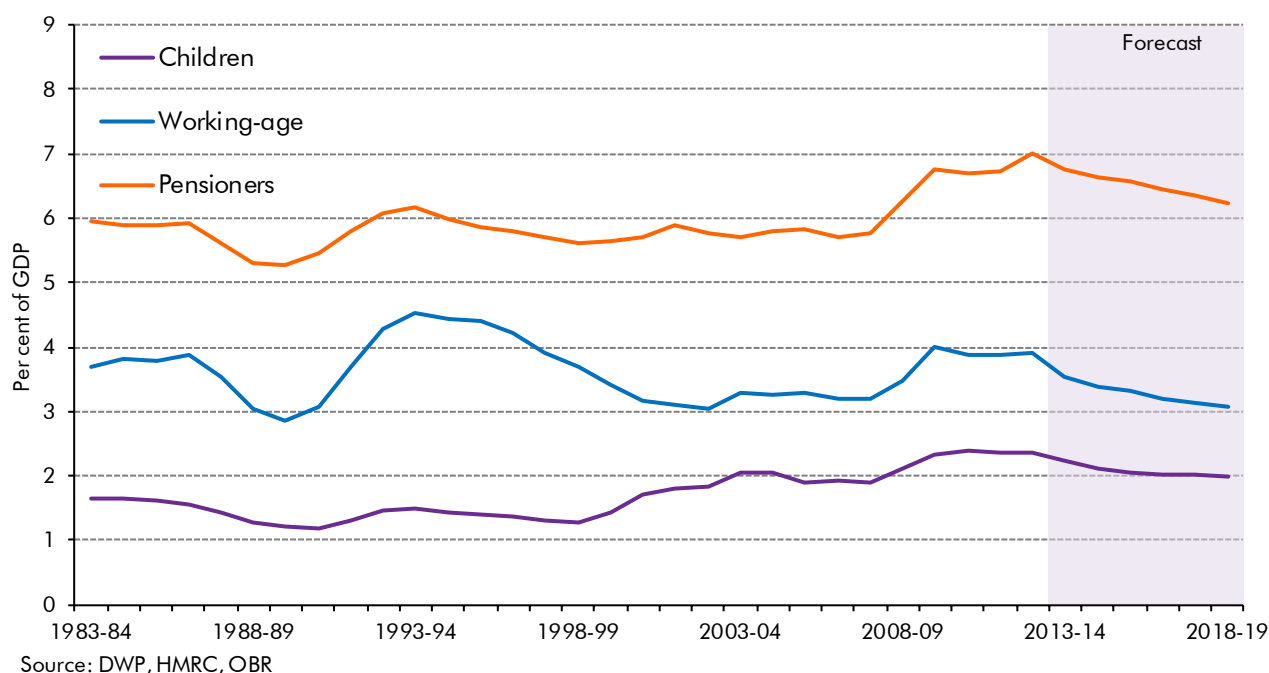
Trends in the composition of welfare spending by age group

4.9 Chart 4.3 shows trends in welfare spending on pensioners, the working-age and children. The distinction between spending focused on children and that on the working-age is less clear in the case of tax credits – which are awarded at the family level – but for the purpose of this illustration we have apportioned spending on the child tax credit to children and split spending on the working tax credit by the age of the main recipient.¹ The chart shows that:

- welfare spending on pensioners – of which state pensions are the largest component – accounted for roughly 55 per cent of welfare spending and were equal to almost 7 per cent of GDP in 2013-14. Despite the ageing of the population, spending on pensioners was fairly stable as a share of GDP until 2007-08, when the effect of the recession on GDP and relatively high inflation on uprating helped push it higher;
- welfare spending on children has risen gradually from 1.3 per cent of GDP in 1997-98 to 2.2 per cent of GDP in 2013-14 (increasing its share of welfare spending from 12 per cent to 18 per cent). This reflects greater spending on tax credits focused on families with children; and
- welfare spending on working-age claimants has fluctuated counter-cyclically over the past 30 years around an average of 3.6 per cent of GDP.

¹ On this basis, pensioners make up approximately 2 to 3 per cent of spending on the working tax credit. Prior to 2003-04, we have used the children/working-age/pensioner split published in DWP's outturn expenditure tables.

Chart 4.3: Welfare spending by age group



Drivers of changes in welfare spending

4.10 Potential drivers of changes in welfare spending can be split into those affecting caseloads and those affecting the amount each recipient is paid – the average award. For a given policy setting, caseloads can be driven by demographic and economic factors that change the number of people eligible for a benefit and by changes in the proportion of eligible people that choose to take up that benefit. Eligibility and take-up can in turn be affected by policy changes or other Government activity such as awareness campaigns. Average awards can be affected by economic factors (notably inflation, when benefit rates are automatically uprated by an official inflation measure), by changes in the composition of caseloads (if different groups receive different amounts) and by policy (particularly when rates are changed by more or less than the default uprating).

4.11 Considering the detailed benefit-by-benefit analysis contained in the later chapters of this report, the main themes that emerge include:

- **demographic and economic trends** can cause significant changes in the cost of different benefits. Most obviously, the ageing population has increased the state pensions caseload from 21.3 per cent of the adult population 30 years ago to 25.3 per cent in 2013-14, while cyclical fluctuations in the economy have caused the cost of unemployment benefits to rise and fall. Labour market and housing trends have had wider implications for welfare spending. Rising female labour market participation has lifted the proportion of women eligible for the full basic state pension and average awards.² Recent increases in the share of the population renting rather than owning their home has increased the housing benefit caseload, while the shift in renting from

² See, for example, Johnson and Stears (1996).

the social- to the private-rented sector has raised the cost per claimant. Most importantly for the system as a whole, changes in inflation feed through to the cost of most benefits and tax credits via uprating. When, as in recent years, inflation is higher than earnings growth, that causes the welfare bill to rise relative to GDP;

- major **reforms of the welfare system** often lead to unexpected changes in spending, in part as administrators and claimants adapt to the new system. The introduction and expansion of tax credits in the 2000s provides a recent example. The tax credits bill rose faster than expected as earnings grew more slowly in the tax credit population than in the wider economy and as childcare costs grew significantly. The system was also amended over time to address higher-than-expected levels of overpayments in the early years of operation. The introduction of disability living allowance in 1992 led to rapid growth in caseloads as a result of widening eligibility, the introduction of claimant self-assessment, and a rise in take-up. And reforms to unemployment benefits in the second half of the 1980s, which were designed to reduce the persistently high claimant count in the aftermath of the early 1980s recession, led to sharp increases in the incapacity benefits caseload. This in turn prompted major reform of the incapacity benefits system in 1995;
- while demographic and economic trends drive eligibility for benefits, trends in welfare spending are also affected by changes in **take-up rates**. The introduction of pension credit in 2003 was accompanied by a Government campaign to raise take-up. While the Government's target was not reached, the caseload did rise by more than 50 per cent between 2002-03 and 2005-06. In the case of tax credits, broadly comparable take up among low-income families on the highest awards increased from around 60 per cent for the family income supplement to around 80 per cent under family credit and the working families tax credit and then to 90 per cent for tax credits;³ and
- welfare spending is affected by **wider public policy decisions**. Spending on tax credits rose as rapidly as it did under the Labour Government from 2003-04 to 2010-11 in large part because the child element of child tax credits (indexed by earnings and often over-indexed) became its preferred policy tool to try to meet the child poverty targets that it had introduced early in government. Reduced spending on social housing may have had a significant impact on the housing benefit bill, by increasing the proportion of the caseload paying higher rents in the private-rented sector.⁴

Summary of changes in welfare spending

- 4.12** The changes in the size and composition of welfare spending can be decomposed in a way that allows us to identify the most important drivers of those changes. Table 4.1 draws on the benefit-by-benefit analysis in Chapters 5 to 10 to break down the changes in welfare spending as a share of GDP between its peaks and troughs over the past 30 years. (Table 4.4 later in this chapter shows the same decomposition for our latest forecast to 2018-19.)

³ HMRC (2013).

⁴ See, for example, National Housing Federation (2014).

4.13 Table 4.1 shows that:

- during the period of strong GDP growth **from 1983-84 to 1989-90**, welfare spending fell by 2.0 per cent of GDP. The largest contributions to that fall were lower spending on unemployment benefits as the economy boomed and lower spending on state pensions as earnings growth outpaced uprating. But the rising proportion of adults receiving incapacity benefits slightly offset those falls;
- **between 1989-90 and 1993-94**, a period that included the early 1990s recession, spending increased by 3.0 per cent of GDP. The largest contributions to that rise were caseload-driven increases in spending on unemployment and incapacity benefits, and average award-driven increases in spending on housing benefit, as the recession bit. Spending on state pensions was pushed up as a share of GDP due to the weakness of earnings growth relative to uprating;
- **between 1993-94 and 2007-08**, a period of sustained economic growth, spending fell by 1.5 per cent of GDP. The largest contribution was the steady reduction in the unemployment rate. Spending on incapacity benefits also fell as uprating and other factors pulled average awards lower relative to earnings. This period also saw a big shift in spending from different parts of the benefits system to tax credits; and
- **between 2007-08 and 2012-13**, a period that spans the late 2000s recession and the slow recovery that followed, spending increased by 2.5 per cent of GDP. The rise in the caseload for jobseeker's allowance made a surprisingly small contribution to the increase in spending. The largest contribution was from the uprating of state pensions as inflation outstripped growth in earnings and GDP. Spending on tax credits and housing benefit also increased significantly, the former reflecting generous discretionary uprating (especially of the child element) and the latter reflecting growth in the number of renters and rent inflation outstripping earnings growth.

4.14 With the exception of the early 1990s recession, average awards were the bigger driver of changes in welfare spending over these periods. That is consistent with the findings in Box 4.1, which show that only the small and highly cyclical benefits have caseloads that are particularly sensitive to the economic cycle. For the larger, mildly cyclical benefits spending it is average awards that explain the sensitivity of spending to the state of the economy.

Table 4.1: Breakdown of historical changes in welfare spending as a share of GDP

	Per cent of GDP			
	1983-84 to 1989-90	1989-90 to 1993-94	1993-94 to 2007-08	2007-08 to 2012-13
Spending at start of period	11.7	9.6	12.6	11.2
Spending at end of period	9.6	12.6	11.2	13.6
Change	-2.0	3.0	-1.5	2.5
<i>of which changes by caseload and average award:</i>				
Caseload changes	-0.5	1.2	-0.4	0.3
Average award changes	-1.5	1.0	-2.1	1.4
Other changes ¹	0.0	0.7	1.0	0.7
<i>of which changes by type of benefit:</i>				
State pensions	-0.8	0.3	-0.2	1.1
Caseloads	0.1	0.1	0.4	0.1
Average awards	-1.0	0.2	-0.6	1.0
Incapacity benefits	0.1	0.6	-0.7	0.0
Caseloads	0.2	0.5	-0.1	-0.1
Average awards	-0.1	0.1	-0.6	0.1
Disability benefits	0.1	0.3	0.3	0.2
Tax credits	0.0	0.1	1.2	0.5
Child benefit	-0.4	0.1	-0.2	0.0
Income support	0.1	0.2	-0.3	-0.1
Unemployment benefits	-0.9	0.5	-0.9	0.2
Caseloads	-0.6	0.5	-0.5	0.1
Average awards	-0.3	0.0	-0.4	0.0
Housing benefit	0.0	0.6	-0.3	0.4
Caseloads	-0.2	0.1	-0.3	0.2
Average awards	0.2	0.4	0.0	0.2
Other benefits	-0.2	0.3	-0.3	0.1

¹ Denotes changes for which a breakdown between caseloads and awards has not been undertaken (notably tax credits).

Future prospects for welfare spending

Our latest medium-term forecasts and long-term projections

March 2014 *Economic and fiscal outlook* forecast

4.15 Our latest medium-term forecast shows welfare spending rising by 12.5 per cent in cash terms between 2013-14 and 2018-19 (Table 4.2). That is a significantly slower increase than the growth in nominal GDP over the forecast period, reducing welfare spending from 12.8 per cent of GDP in 2013-14 to 11.6 per cent of GDP in 2018-19 (Table 4.3). The main drivers of this fall are explained more fully below, but can be summarised thus:

- economic factors reduce spending as a share of GDP, mostly as the expected pick-up in productivity leads to earnings and GDP-per-adult rising faster than inflation, and as lower unemployment reduces cyclical caseloads;

Overall trends in welfare spending

- policy measures reduce spending further as a share of GDP, notably raising the female state pension age to 65. This offsets the effect of demographic trends on spending on benefits for the elderly, but increases the proportion of the population eligible for working-age benefits;
- uprating of most working-age benefits is capped at 1 per cent in 2014-15 and 2015-16 – a cap that applies in both years in our central forecast, which also reduces spending as a share of GDP; and
- the assumed savings associated with ongoing reforms to incapacity and disability benefits.

Table 4.2: Welfare spending forecast in cash terms

	£ billion						
	Outturn	Forecast					
		2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Welfare cap							
DWP social security	71.2	71.5	73.3	74.3	75.0	76.0	76.8
of which:							
Incapacity benefits ¹	13.3	13.3	13.4	13.5	13.7	14.0	14.3
Statutory maternity pay	2.3	2.3	2.4	2.4	2.5	2.6	2.7
Income support (non-incapacity)	2.7	2.6	2.6	2.5	2.6	2.7	2.8
Pension credit	7.4	7.0	6.6	6.5	6.3	6.1	5.9
Winter fuel payments	2.1	2.2	2.1	2.1	2.1	2.1	2.0
Disability living allowance and personal independence payments	13.4	13.9	14.8	14.7	14.1	13.5	13.6
Attendance allowance	5.4	5.4	5.5	5.6	5.7	5.8	6.0
Carer's allowance	1.9	2.1	2.3	2.4	2.6	2.7	2.8
Universal credit ²	0.0	0.0	0.0	0.0	0.1	0.5	-0.2
Housing benefit (not unemployed)	19.9	20.3	21.3	22.1	22.9	23.5	24.2
Other DWP in welfare cap	2.6	2.4	2.4	2.4	2.4	2.5	2.5
Personal tax credits (AME spending)	26.8	27.2	26.8	27.1	29.3	31.7	33.0
Tax free childcare	0.0	0.0	0.0	0.2	0.7	0.8	0.9
NI social security in welfare cap	3.2	3.2	3.2	3.3	3.3	3.3	3.3
Child benefit	12.2	11.6	11.7	11.9	12.1	12.4	12.6
Paternity pay	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Welfare cap in AME	113.5	113.6	115.1	116.9	120.4	124.2	126.7
Personal tax credits (negative tax element)	3.0	2.7	2.7	2.5	1.6	0.3	0.0
Total welfare cap	116.5	116.4	117.8	119.5	122.0	124.6	126.7
Welfare spending outside the welfare cap							
DWP social security	93.3	90.7	93.0	96.1	99.2	102.6	106.1
of which:							
Jobseeker's allowance	5.1	4.3	3.6	3.4	3.3	3.2	3.1
State pension	79.8	83.0	86.5	90.0	93.1	96.8	100.3
Council tax benefit ³	4.8	-	-	-	-	-	-
Housing benefit (unemployed)	3.6	3.2	2.9	2.8	2.8	2.7	2.7
Discretionary housing payments ³	0.1	0.2	-	-	-	-	-
NI social security outside welfare cap	2.2	2.2	2.3	2.4	2.5	2.6	2.7
War pensions	0.9	0.9	0.9	0.8	0.8	0.8	0.8
Total welfare outside the welfare cap	96.4	93.8	96.1	99.3	102.5	106.0	109.6
Total welfare⁴	212.9	210.1	213.9	218.8	224.5	230.6	236.3
Memo: welfare cap as proportion of total welfare	54.7	55.4	55.1	54.6	54.4	54.0	53.6

Note: Figures as presented in Table 4.28 of our March 2014 *Economic and fiscal outlook*.

¹ Incapacity benefits includes incapacity benefit, employment and support allowance, severe disablement allowance and income support (incapacity part).

² Universal credit additional costs not already included against other benefits (i.e. UC payments that don't exist under current benefit structure).

³ Transferred to departmental expenditure limits.

⁴ Total welfare includes welfare spending in AME and the negative tax element of personal tax credits, which will move into spending under ESA10.

Table 4.3: Welfare spending forecast as a share of GDP

	Per cent of GDP						
	Outturn	Forecast					
		2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Welfare cap							
DWP social security	4.5	4.3	4.3	4.2	4.0	3.9	3.8
of which:							
Incapacity benefits ¹	0.8	0.8	0.8	0.8	0.7	0.7	0.7
Statutory maternity pay	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Income support (non-incapacity)	0.2	0.2	0.1	0.1	0.1	0.1	0.1
Pension credit	0.5	0.4	0.4	0.4	0.3	0.3	0.3
Winter fuel payments	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Disability living allowance and personal independence payments	0.9	0.8	0.9	0.8	0.8	0.7	0.7
Attendance allowance	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Carer's allowance	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Universal credit ²	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Housing benefit (not unemployed)	1.3	1.2	1.2	1.2	1.2	1.2	1.2
Other DWP in welfare cap	0.2	0.1	0.1	0.1	0.1	0.1	0.1
Personal tax credits (AME spending)	1.7	1.7	1.6	1.5	1.6	1.6	1.6
Tax free childcare	0.0	0.0	0.0	0.0	0.0	0.0	0.0
NI social security in welfare cap	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Child benefit	0.8	0.7	0.7	0.7	0.6	0.6	0.6
Paternity pay	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Welfare cap in AME	7.2	6.9	6.7	6.5	6.4	6.4	6.2
Personal tax credits (negative tax element)	0.2	0.2	0.2	0.1	0.1	0.0	0.0
Total welfare cap	7.4	7.1	6.8	6.7	6.5	6.4	6.2
Welfare spending outside the welfare cap							
DWP social security	5.9	5.5	5.4	5.4	5.3	5.2	5.2
of which:							
Jobseeker's allowance	0.3	0.3	0.2	0.2	0.2	0.2	0.2
State pension	5.1	5.0	5.0	5.0	5.0	4.9	4.9
Council tax benefit ³	0.3	-	-	-	-	-	-
Housing benefit (unemployed)	0.2	0.2	0.2	0.2	0.1	0.1	0.1
Discretionary housing payments ³	0.0	0.0	-	-	-	-	-
NI social security outside welfare cap	0.1	0.1	0.1	0.1	0.1	0.1	0.1
War pensions	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Total welfare outside the welfare cap	6.1	5.7	5.6	5.6	5.5	5.4	5.4
Total welfare⁴	13.6	12.8	12.4	12.2	12.0	11.8	11.6

Note: Figures as presented in Table 4.29 of our March 2014 *Economic and fiscal outlook*.

¹ Incapacity benefits includes incapacity benefit, employment and support allowance, severe disablement allowance and income support (incapacity part).

² Universal credit additional costs not already included against other benefits (i.e. UC payments that don't exist under current benefit structure).

³ Transferred to departmental expenditure limits.

⁴ Total welfare includes welfare spending in AME and the negative tax element of personal tax credits, which will move into spending under ESA10.

- 4.16 Table 4.4 decomposes the 1.2 per cent of GDP fall in welfare spending expected between 2013-14 and 2018-19 into contributions from different benefits inside and outside the welfare cap. This decomposition is based on our central forecast. The risks and uncertainties to which the forecast is subject are discussed later in the chapter.
- 4.17 For spending that will be subject to the welfare cap, the expected fall of 0.9 per cent of GDP over the next five years is driven by:
- a 0.2 per cent of GDP drop in the cost of tax credits – the largest category of spending subject to the cap. This reflects a number of policy measures designed to cut spending, including uprating by 1 per cent for three years from 2013-14;
 - smaller falls in housing benefit (0.1 per cent of GDP) and incapacity benefits (0.1 per cent of GDP) – the next largest spending lines. Housing benefit falls as caseloads linked to other benefits decline relative to the adult population, partly offset by growth in the ‘housing benefit only’⁵ caseload of those in work. The expected fall in spending on incapacity benefits is partly driven by our assumption that the reassessment of employment and support allowance claims will reduce the overall caseload;
 - a substantial fall in spending on disability benefits (worth 0.2 per cent of GDP) that is driven by the assumed reduction in caseloads as people’s eligibility for support is reassessed when cases are migrated from the existing disability living allowance to the new personal independence payment; and
 - falls in spending on a number of other benefits, including pension credit (as the qualifying age is raised and the single tier pension is introduced), child benefit (due to uprating) and income support (as incapacity-related claims are migrated to employment and support allowance).
- 4.18 Spending outside the welfare cap is expected to fall by around a third as much – 0.3 per cent of GDP – as spending subject to the cap. That reflects:
- a 0.1 per cent of GDP decline in spending on state pensions, as the pressure from population ageing is more than offset by raising the state pension age, while the triple lock on uprating sees average awards rise broadly in line with earnings; and
 - a 0.2 per cent of GDP fall in spending on the unemployed – comprising jobseeker’s allowance and housing benefit paid to jobseekers. Since spending on state pensions was around 12 times higher than spending on these benefits in 2013-14, this represents a much larger proportional fall. Lower spending is driven both by lower cyclical caseloads and by average awards rising more slowly than earnings.

⁵ This ‘housing benefit only’ caseload is described as ‘only’ in DWP data because recipients are not also in receipt of another DWP benefit. From the broader perspective of welfare spending, such claimants will typically receive some income from tax credits and, if they have children, will also receive income from child benefit.

Table 4.4: Breakdown of expected changes in welfare spending as a share of GDP

	Per cent of GDP				
	2014-15	2015-16	2016-17	2017-18	2018-19
Change from 2013-14	-0.35	-0.55	-0.78	-0.99	-1.21
of which:					
Welfare spending subject to the welfare cap					
Tax credits	-0.11	-0.16	-0.18	-0.19	-0.21
Housing benefit (inside cap)	-0.03	-0.04	-0.05	-0.06	-0.06
Caseloads	-0.03	-0.04	-0.04	-0.05	-0.05
Average awards	0.00	0.00	0.00	-0.01	-0.01
Incapacity benefits	-0.03	-0.05	-0.08	-0.10	-0.11
Caseloads	-0.01	-0.02	-0.03	-0.04	-0.04
Average awards	-0.03	-0.03	-0.05	-0.06	-0.07
Disability benefits	0.02	-0.02	-0.09	-0.15	-0.18
Caseloads	-0.01	-0.03	-0.10	-0.15	-0.13
Average awards	0.03	0.01	0.01	0.00	-0.05
Other benefits	-0.08	-0.12	-0.17	-0.22	-0.32
Total	-0.23	-0.40	-0.56	-0.71	-0.87
Welfare spending outside the welfare cap					
State pension	-0.02	-0.02	-0.07	-0.10	-0.13
Caseloads	-0.01	-0.02	-0.04	-0.07	-0.12
Average awards	-0.01	0.00	-0.03	-0.02	-0.02
Unemployment benefits ¹	-0.05	-0.08	-0.10	-0.14	-0.16
Caseloads	-0.02	0.01	-0.03	-0.05	-0.05
Average awards	-0.03	-0.08	-0.07	-0.09	-0.11
Other benefits	-0.04	-0.06	-0.05	-0.05	-0.04
Total	-0.12	-0.15	-0.23	-0.28	-0.34

¹ Jobseeker's allowance and housing benefit for jobseeker's.

July 2014 Fiscal sustainability report projections

- 4.19** Our 2014 *Fiscal sustainability report (FSR)* contained long-term projections of welfare spending. These capture the effects of demographic change with neutral assumptions made in most other areas. An important difference from our medium-term forecasts is that we assume benefits are uprated in line with earnings rather than inflation, which in effect switches off the fiscal drag effect of average awards rising more slowly than GDP-per-adult.
- 4.20** Our projections show total welfare spending rising by 2.5 per cent of GDP between 2018-19 – the end of our medium-term forecast – and 2063-64, with almost all of the rise accounted for by benefits paid to the elderly. These include state pensions, plus other pensioner-related benefits, including pension credit, winter fuel allowance, free TV licences and the Christmas bonus. The projections show this spending on the elderly rising from 5.5 per cent of GDP at the end of our medium-term forecast to 7.9 per cent of GDP in 2063-64. This is largely driven by demographic trends, partly offset by further expected increases in the SPA – based on the principle set out by the Government that people should expect to spend a third of their adult life in receipt of the state pension. Triple lock uprating is assumed to put further upward pressure on state pensions spending over the long term.

4.21 Among other benefits, the main projected changes over the long term are:

- spending on incapacity and disability benefits rises in large part due to the ageing of the population, because we assume constant age-specific shares of the population in receipt of incapacity benefits. Cohort effects raise the caseload as a share of the adult population as the population ages. For disability benefits, even though we assume increases in disability-free life expectancy, the significant rise in the population of very old people lifts spending overall. The number of people aged 85 and over is projected to rise from 2.3 per cent of the population in 2014 to 7.7 per cent in 2064; and
- spending on housing benefit falls, due in large part to assumed higher home-ownership rates for pensioners. This reflects cohort effects – newly-retired pensioners have higher home-ownership rates than the oldest pensioners, which all else equal means fewer newly-retired pensioners are eligible for housing benefit.

Table 4.5: Long-term projections of welfare spending

	Per cent of GDP						
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
State pensions ¹	5.8	5.5	5.7	6.7	7.4	7.6	7.9
Housing benefit	1.5	1.4	1.3	1.3	1.3	1.3	1.2
Personal tax credits	1.7	1.6	1.7	1.6	1.6	1.6	1.6
Disability benefits ²	1.2	1.0	1.0	1.1	1.2	1.2	1.3
Incapacity benefits ³	0.7	0.7	0.8	0.8	0.8	0.8	0.9
Income support	0.2	0.1	0.1	0.2	0.2	0.2	0.2
Unemployment benefits ⁴	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Child benefits	0.7	0.6	0.6	0.6	0.6	0.6	0.6
Other welfare benefits	0.5	0.4	0.4	0.4	0.4	0.4	0.4
Total welfare spending	12.6	11.6	11.8	12.9	13.6	13.9	14.1

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis, consistent with our 2014 *Fiscal sustainability report* projections.

¹ Basic state pension, state earnings related pension scheme, state second pension, single-tier pension, other elements of state pension, pension credit and other pensioner benefits.

² Disability living allowance, personal independence payments and attendance allowance.

³ Employment and support allowance and severe disablement allowance.

⁴ Jobseeker's allowance.

Key risks to the medium-term forecast

4.22 As we stress in every *Economic and fiscal outlook (EFO)*, all fiscal forecasts are subject to considerable uncertainty. The demographic and economic developments that underpin the fiscal forecast are unlikely to turn out precisely as expected. Even if they did, there would still be uncertainty over how fiscal variables would evolve in a given economic environment. For example, the composition of household incomes or employment may affect eligibility for certain benefits, even if the totals were as expected. The March 2014 *EFO* forecast for the benefits and tax credits covered in this report are therefore subject to all the usual risks and uncertainties associated with fiscal forecasting. But it is possible to identify some of the major or more complex judgements that we have had to make and that we consider to be

subject to greater uncertainty. These issues are likely to be particularly relevant to the Government's performance against the welfare cap.

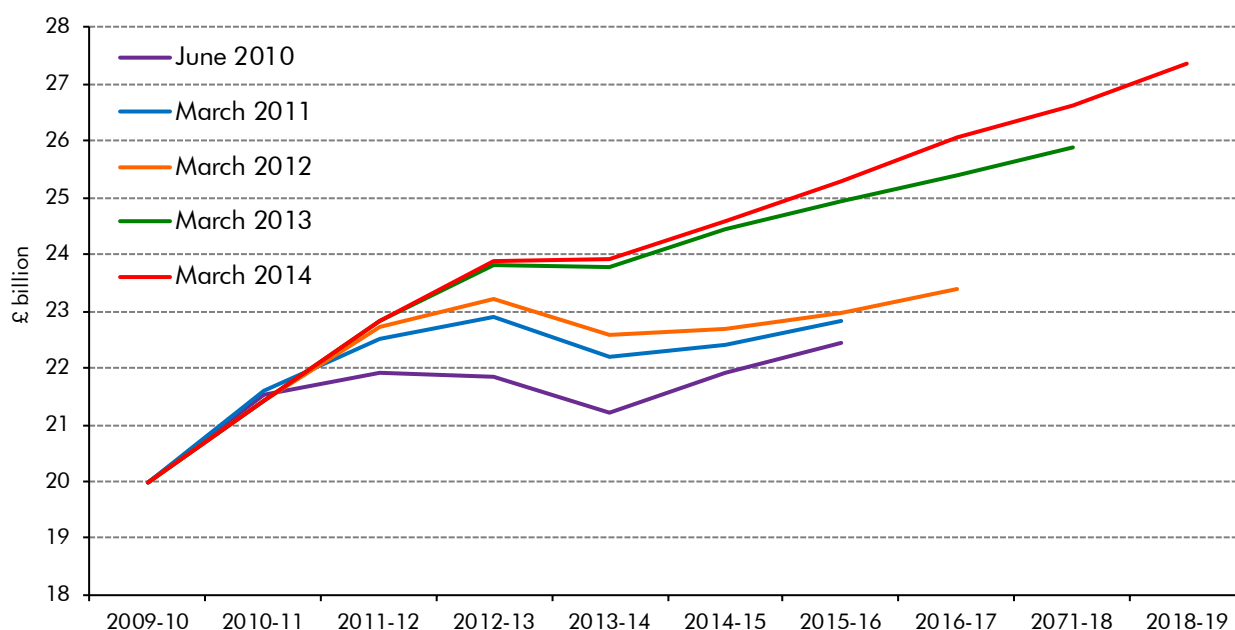
- 4.23 The three largest sources of uncertainty – and therefore risks to the forecast – relate to housing benefit, incapacity benefits and disability benefits. In the case of housing benefit, the major uncertainties relate to the underlying economic drivers of both the caseload and the implied average award per claim. For incapacity and disability benefits, the major uncertainties are associated with the impact of policy reforms – the effect on caseloads and average awards as the systems are changed, as existing caseloads are migrated from old to new benefits, and as savings are assumed to flow from the associated reassessment process. Our forecasting performance in these areas⁶ and the continuing risks they present are considered in more detail below.
- 4.24 The migration from six existing benefits to the single universal credit that is planned to take place over the coming years will pose many of the same problems, often to an even greater degree (see Box 4.2). But this is not a major factor in our latest forecast, because of the way in which the potential impact of universal credit has been incorporated in the figures.
- 4.25 More recently, we have been repeatedly surprised at the speed with which unemployment has fallen. The claimant count has fallen by 17.5 per cent relative to the level known when we completed our March 2014 forecast. It moved below 1 million in August 2014 – a level we had not expected it to reach until 2017 – having fallen at a faster rate over the past year than at any time since 1973. This suggests that in our December 2014 forecast, we will need to revise down our forecast of spending on jobseeker's allowance significantly.
- 4.26 An overarching uncertainty across the benefits and tax credits systems is the degree to which spending will be affected by fraud and error – the latest estimates and the risks posed to our forecast are discussed in more detail below.

Housing benefit

- 4.27 Our forecasts for housing benefit have, on average, underestimated spending. In the four Budget forecasts we made for spending in 2012-13, the average forecast error was a £1.0 billion or 4.3 per cent underestimate. These errors have reflected both higher-than-expected caseloads – particularly among the 'housing benefit only' group and among those also receiving incapacity benefits – and higher-than-expected average awards.

⁶ For a full discussion of how our forecasts have performed relative to the latest outturns, see our 2014 *Forecast evaluation report*, which is published alongside this report.

Chart 4.4: Successive OBR housing benefit forecasts since June 2010



Source: DWP, OBR

4.28 The most substantial errors have been associated with the 'housing benefit only' caseload group, for whom eligibility is not associated with the receipt of other benefits. This caseload has risen by 44 per cent between 2010-11 and 2013-14 and we expect it to rise by another 39 per cent by 2018-19. The errors here have been associated with three inter-related developments in the economy:

- the rise in the share of the population renting has continued at a faster pace than expected. This may be associated with house prices remaining high relative to incomes and reduced post-crisis supply of high loan-to-value and loan-to-income mortgages;
- employment growth has been much stronger than expected, but earnings growth has been much weaker. So the number of people in-work but earning sums that would leave them eligible for housing benefit has been higher than expected; and
- rent inflation, as measured in administrative data, has been higher than expected. Together with subdued earnings growth, this increases the eligible population further.

4.29 We have revised our forecasts to reflect this evidence, but significant uncertainties remain. The relevant judgements underpinning our latest forecast are:

- that the proportion of households renting will rise more slowly and eventually stabilise. There are risks in both directions. The prevalence of renting might continue to rise as house price inflation outstrips earnings growth and as the Mortgage Market Review affects mortgage availability at higher loan-to-value or loan-to-income ratios. Conversely, as the financial system continues to heal and Government schemes like

Help to Buy support borrowing at higher loan-to-value ratios, the decline in homeownership of recent years could begin to reverse;

- that productivity growth will start to pick up, leading to stronger earnings growth and slower employment growth. Based on recent trends, we assume that renters will account for 100 per cent of net employment growth and that 38 per cent of those employed renters will receive housing benefit. As a result, in-work 'housing benefit only' claimants are expected to rise by 0.4 million over the five years to 2018-19, more than accounting for the total rise in the housing benefit caseload. Relative to our March 2014 forecast, employment growth has continued to surprise on the upside and earnings growth to the downside; and
- that measures of rent inflation relevant to the housing benefit forecast will remain higher than average earnings growth until 2014-15, and lower thereafter. The average awards used in this report reflect variations in rents across regions and housing benefit tenures, with the difference between the highest and lowest average award being more than 350 per cent.⁷ As such, there is considerable scope for regional variations and changes in the composition of the caseload to push average rents above or below forecast. Moreover, data on rent inflation at the whole economy level are currently being reviewed,⁸ adding further uncertainty to the forecast.

Incapacity benefits

4.30 Our forecasts for incapacity benefits have, on average, underestimated spending. In the three comparable Budget forecasts that we made for spending in 2012-13, the average forecast error was a £0.9 billion or 7.9 per cent underestimate.⁹ These errors have reflected a number of factors, including a higher-than-expected caseload, slightly slower-than-expected migration from incapacity benefit to employment and support allowance (ESA), differences in the assumed proportions of claims being assessed as fit for work or assigned to the work-related activity and support groups of ESA in the work capability assessments, and differences in appeal success rates.

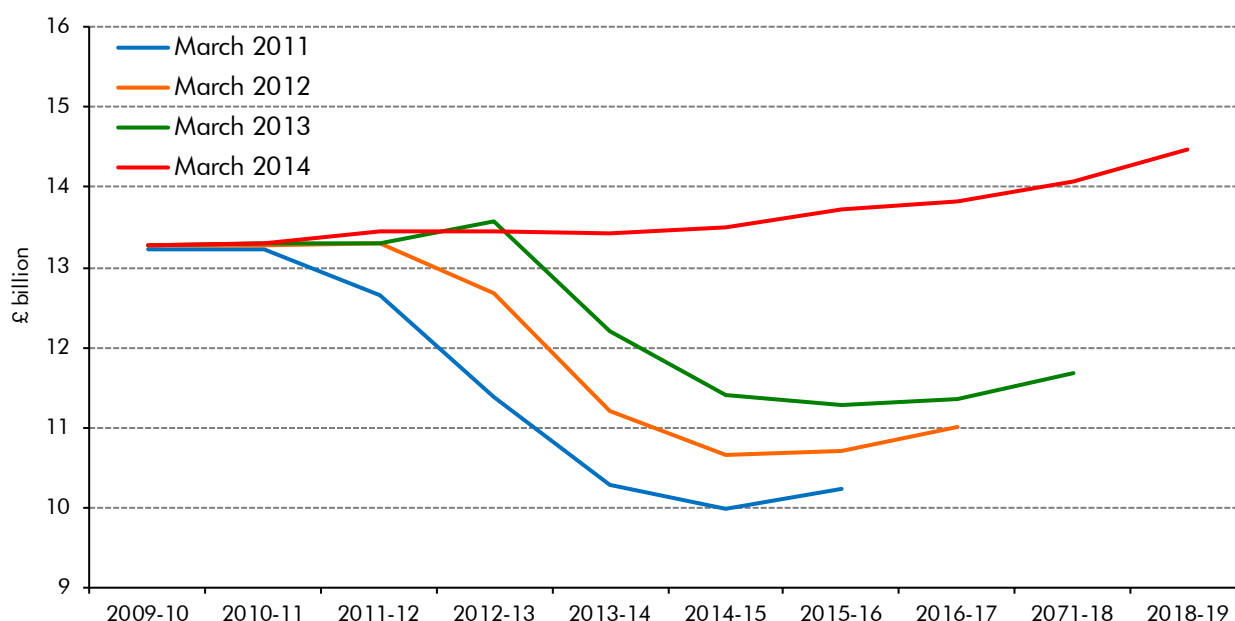
4.31 As Chart 4.5 shows, we have significantly altered the shape of our incapacity benefits forecast since Budget 2013, as we expect ESA to produce a much smaller reduction in spending on incapacity benefits. In our December 2013 forecast, we revised ESA spending up by £2.1 billion at the 2017-18 forecast horizon due to evidence from work capability assessments that the proportion of those assessed moving into the support group would be higher than previously assumed and the proportion declared fit for work lower. In addition, we judged that spending would remain higher in subsequent years because of delays to the work capability assessment programme. We reduced the assumed number of work capability assessments to reflect lower volumes then passing through the system and our updated view on prospects for clearing the backlog of assessments that had built up.

⁷ Based on DWP Stat-Xplore data on average weekly awards by local authority and tenure in May 2014. These ranged from a low of £51 a week in the social-rented sector in Moray to a high of £233 a week in Westminster.

⁸ See ONS (2014).

⁹ The June 2010 budget forecast for total incapacity benefits was not on the same basis as the subsequent forecasts as the 'incapacity element' of income support (part of total incapacity benefits spending) is not split out from income support spending in that forecast.

Chart 4.5: Successive OBR incapacity benefits forecasts since March 2011



Source: DWP, OBR

4.32 The key assumptions underpinning our March 2014 forecast – and the risks to which they are subject – include:

- that migration from incapacity benefit to ESA will be largely complete by 2015-16. We adjusted our March 2014 forecast to reflect the problems dealing with the backlog of assessments, but significant risks remain – especially until the Department for Work and Pensions finds a delivery partner to replace ATOS Healthcare;
- the outcomes of reassessments save more money over time and appeal rates settle in the medium term. Again, the performance of the new contractor is crucial – we are implicitly assuming improved performance relative to the present system;
- flows off ESA largely result in reduced welfare spending overall. Early evidence suggests there may be some recycling of those found fit for work into jobseeker's allowance and then back onto ESA. The design of ESA means that more people are moved around the benefit system, while the backlog of applications encourages claimants previously not found eligible for ESA simply to reapply;
- a stable rate of inflows going forward. There is a risk that inflows associated with the rising state pension age – which increases the number of older working-age people for whom risks of illness are higher – are more or less than assumed. Even absent changes to the state pension age, cohort effects could see greater bunching of the population at the pre-retirement stage when illness is more likely to prevent work; and

Overall trends in welfare spending

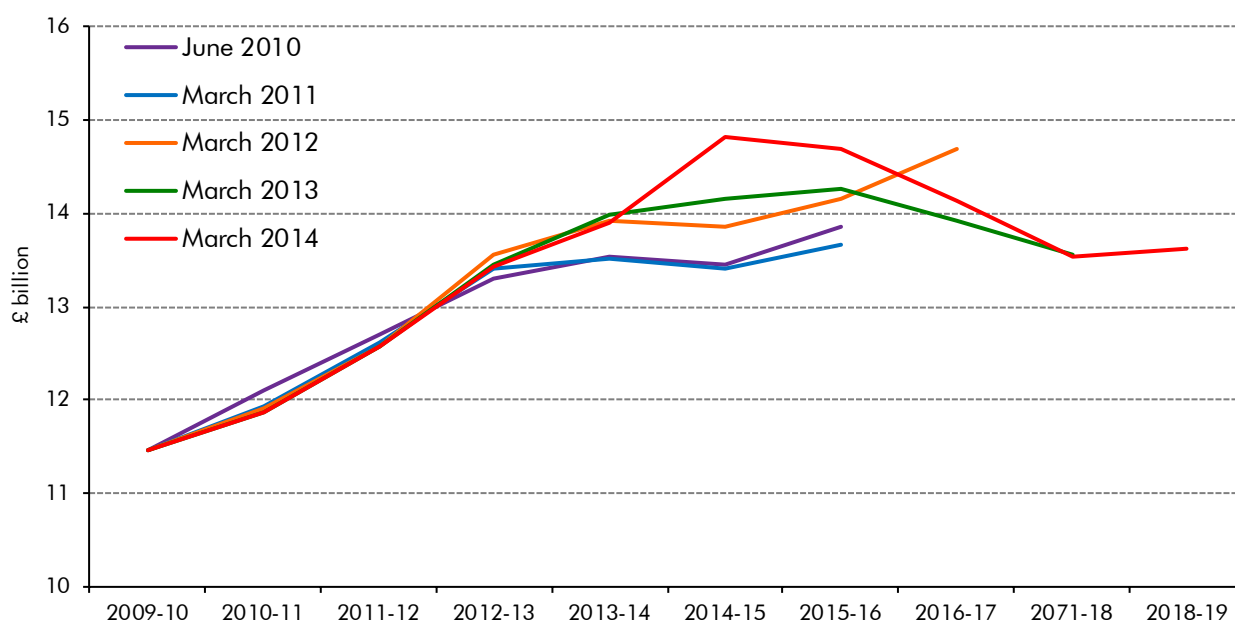
- finally, a recent Work and Pensions Committee review of ESA¹⁰ recommended a complete redesign of ESA processes. Moving to a new system could resolve or reduce these risks. But the history of major benefit reforms suggests caution before reaching any judgement on assumed gains.

4.33 Merely listing the judgements that need to be taken in order to forecast spending on incapacity benefits, as the transition to ESA is completed, illustrates the challenges involved. We aim to deliver a central forecast that reflects the tendency for major reforms to be rolled out more slowly and with greater difficulty than governments initially believe will be the case. In each forecast we have to judge the extent to which the latest delivery problems are temporary or will persist. As demonstrated by our recent forecast errors on incapacity benefits, we had not made sufficient allowance for such slippage. We will be reviewing these assumptions – and the implications of the Government’s new contractual arrangements, when they have been awarded – in future forecasts. It is clear that this will remain an area of significant uncertainty in our welfare spending forecast for some time.

Disability benefits

4.34 Our forecasts for disability benefits have so far not underestimated spending by the same substantial margins seen for housing and incapacity benefits. As Chart 4.6 shows, outturn spending in 2012-13 – as shown by the March 2014 forecast line – was very close to all of our previous forecasts, with an average error of zero. But the disability benefits regime is starting a period of major reform, with the migration of claimants from disability living allowance (DLA) to personal independence payments (PIP). This involves challenges very similar to those that have already prompted us to raise our forecasts for incapacity benefits.

Chart 4.6: Successive OBR disability benefits forecasts since June 2010



Source: DWP, OBR

¹⁰ House of Commons Work and Pensions Committee (2014).

4.35 The key assumptions underpinning our March 2014 forecast – and the risks to which they are subject – include:

- that 16 per cent of the DLA/PIP caseload will be on PIP by 2015-16, rising to 63 per cent by 2018-19. With comparatively little outturn data and a delayed rollout, we adjusted our forecast upward in March 2014 to reflect the emerging outturn data on the pace of the rollout. But it is too early to tell whether that was sufficient. We will return to this assumption in our December 2014 *EFO*;
- the process of reassessing DLA claims during the migration of PIP will deliver a 25 per cent reduction in the caseload, reducing spending by £2.8 billion a year by 2017-18. This saving is sensitive to the speed with which the caseload is migrated to PIP and the outcomes of reassessments and any subsequent appeals; and
- the proportion of PIP claims that are successful for the claimant averages around 60 per cent in 2014-15, falling to 35 per cent from 2016-17 as the system beds down and medical assessors improve the quality of their reports. Success rates appear to be falling in line with our assumptions for the first two years of the forecast – but there is little evidence available to inform the further reduction in success rates assumed thereafter. If success rates did not continue to fall as expected, our spending forecasts would be affected accordingly. Assumptions on the rate of appeals – and the proportion that are successful – pose further risks to the PIP forecast.

4.36 In summary, as with ESA the key judgements are to what extent delivery challenges are likely to be temporary or persistent. As the rollout to PIP is at a much earlier stage than that for ESA, this judgement is subject to even greater uncertainty. We will be reviewing all of these assumptions for our December 2014 forecast.

Fraud and error in the benefits and tax credits systems

4.37 Fraud and error are commonly cited as significant risks to welfare spending in the UK. When most people think of fraud and error they equate it to intentional manipulation of the system by individuals for personal gain – i.e. ‘fraud’¹¹ rather than ‘error’. But error – whether it be on the part of the claimant or the department administering the benefit – is an inevitable part of any system that aims to target spending on need by responding to changes in family circumstances that have to be reported to the administrators and acted upon. The birth of a child or the start of a new job, for example, would need to be reported and processed on the same day by departments in order to avoid generating any over- or underpayments. This unintentional error – though nonetheless undesirable – is less malign than deliberate attacks on the system.

4.38 It is difficult to determine the extent to which overpayments¹² are the result of fraud or of error. The administering departments produce estimates by getting officials that are expert in identifying fraud and error to assess a random sample of existing claims. Results are

¹¹ Departmental estimates of fraud use a wider definition than this.

¹² HMRC do not classify overpayments that are identified as part of the finalisation process as fraud or error.

published by DWP and HMRC every year. In terms of the welfare spending we cover in this report¹³, the latest results show that fraud and error in 2012-13 was estimated to account for net overpayments of £3.7 billion:

- around 2.1 per cent (£3.5 billion) of the £167 billion of benefits spending administered by DWP in 2012-13 is estimated to have been paid out in error and fraud favouring the claimant, compared to around 0.9 per cent (£1.6 billion) in underpayments favouring the department. Of that which favoured the claimant, roughly two-thirds is thought to have been error and a third to have been fraud; and
- around 7 per cent (£2.0 billion) of the roughly £30 billion tax credits spending administered by HMRC in 2012-13 is estimated to have been paid out in error and fraud favouring the claimant against, compared to around 0.7 per cent (£0.2 billion) in underpayments favouring the department. Of this 7 per cent favouring the claimant, a little under half is thought to have been error and a little over half fraud.

4.39 The ultimate impact on the public finances will reflect that part of the £3.7 billion net overpayment that is not subsequently recovered.

4.40 In our forecasts, we typically assume that the rate of fraud and error remains constant through our forecast at its latest estimated level. As a result, any increase or decrease in those rates would represent risks to the forecast. But at less than 1.5 per cent of welfare spending and less than 0.2 per cent of GDP across all benefits and tax credits, it would require large changes in rates of fraud and error to present material risks to spending.

Box 4.2: Universal credit

In our latest forecast, universal credit (UC) is assumed to roll out slowly during 2014-15 and 2015-16, with the pace increasing in 2016-17 and 2017-18 – by which time 5.8 million people are assumed to be on UC. But the forecast is based on a continuation of the legacy benefits regime, with UC added into the forecast as a marginal cost relative to the legacy system. This top-down approach is the best we can do until there are sufficient data to allow us to construct a bottom-up forecast of the rise of UC and the fall in the legacy benefits.

The rollout of UC has been subject to significant delays, related to well-documented challenges in developing an effective IT system. Designing a single IT system that can cope with the complex and frequently changing circumstances of widely differing households across different benefits is a significant challenge. The early experience with tax credits and the recent reforms to incapacity benefit/ESA and DLA/PIP illustrate the potential impact of such delivery challenges.

Using a top-down approach reduces some of the UC-related uncertainties in the forecast, since the marginal cost of UC relative to legacy benefits is estimated to be relatively small – less than £½ billion in any year. So the forecast is relatively insensitive to changes in the speed at which UC rolls out. It is, though, important to note that the estimated marginal cost of UC is the net effect of much larger gross costs and savings.

¹³ HMRC does not publish estimates of fraud and error for child benefit.

Increased generosity and assumed increased take-up under UC act to increase expected welfare spending in 2018-19 by around £3.5 billion. These increased costs are offset by:

- error and fraud savings worth an estimated £1.4 billion in 2018-19 (relating mainly to the use of real-time information tax data);
- the introduction of a minimum income floor for self-employed claimants, estimated to save around £1.1 billion in 2018-19;
- abolition of the income disregards currently in tax credits, worth an estimated £1.2 billion in 2018-19; and
- a number of other smaller policy changes, which together result in around £0.8 billion of estimated savings in 2018-19.

Transitional protection of claimants' awards temporarily increases the net cost of UC by around £0.6 billion in 2018-19 ahead of the system being assumed to reach steady-state in the 2020s.

To the extent that delays in rolling out UC and problems in developing effective IT solutions affect these estimated costs and savings by different amounts, the estimated marginal cost of UC could be significantly higher or lower than we currently estimate. We will revisit the assumptions underpinning our estimates of the marginal cost of UC ahead of our December 2014 *EFO*, which will have to continue to be based on a top-down approach for the time being.

Key sensitivities in the long-term projections

4.41 Our long-term projections are based on a number of simplifying assumptions. In general, these ensure that spending is not projected to rise or fall indefinitely for reasons that would likely not be sustainable over longer horizons – for example, we assume that most benefits and tax credits are uprated with earnings rather than inflation so that their value does not shrink steadily relative to the living standards of the bulk of the population. Varying these assumptions illustrates the sensitivity of different types of spending to different drivers.

4.42 The key sensitivities in our long-term projections include:

- demographic and employment trends. These can have significant implications for spending, depending on the policy regime. With the SPA now more closely linked to demographic trends, the sensitivity of spending to changes in longevity is less than was previously the case. But spending as a share of GDP remains sensitive to changes in the number of workers relative to the number of pensioners. For example, higher net migration¹⁴ or greater than projected labour market participation among older age groups would reduce spending as a share of GDP by increasing GDP proportionally more than spending on pensions. Similarly, higher or lower birth rates would affect spending on child benefit. And changes in the amount or age structure of net migration could affect spending on a wide range of benefits, as well as affecting GDP;

¹⁴ All else equal, net migration increases the working-age population and GDP. See Box 3.4 of the 2014 *Fiscal sustainability report* for a discussion of why all else might not be equal.

- uprating working-age benefits in line with inflation rather than earnings over the next 30 years would reduce spending on those benefits by 1.3 per cent of GDP. Our long-term projection of pension spending is also sensitive to the assumption we make about the cost of the triple lock on uprating, which ratchets up average pension awards every time earnings growth drops below inflation or 2.5 per cent;
- long-term projections of housing benefit spending are sensitive to assumptions about housing tenure and the rate of rent inflation relative to earnings. Our central projections are based on neutral assumptions that the proportion of the population renting is flat beyond the medium term and that rents rise in line with earnings. If either of these were to rise (or fall), spending on housing benefit would be expected to rise (or fall) as a share of GDP; and
- changes in the age-specific prevalence of incapacity and disability – related to changes in the number of disability-free years that average person can expect to enjoy after retirement – as the population continues to age.

Implications for the welfare cap

The welfare cap

- 4.43 The Government announced in Autumn Statement 2013 that it would introduce a cap on certain items of welfare spending, excluding state pensions – which it argued are “*better planned and controlled over a longer time period*” – and jobseeker’s allowance and associated housing benefit payments – which it identified as “*the most cyclical elements of welfare*” in order “*to allow the automatic stabilisers to operate*”.¹⁵
- 4.44 The cap was formally defined and initially set by the Government in Budget 2014. It will apply from 2015-16 to the end of the forecast period, which was 2018-19 in Budget 2014. The Government has set a forecast margin above the cap of 2 per cent in each year. Table 4.6 shows the welfare cap and additional forecast margin that were set at Budget 2014.
- 4.45 How the cap will operate – including the actions required if the cap is exceeded – was outlined in the March 2014 update of the *Charter for budget responsibility*. In our December 2014 *EFO*, we will formally assess whether relevant spending exceeds the welfare cap for discretionary policy reasons or the cap-plus-forecast-margin due to changes in forecast assumptions.

Table 4.6: The level of the welfare cap and the forecast margin

	£ billion			
	2015-16	2016-17	2017-18	2018-19
Welfare cap	119.5	122.0	124.6	126.7
2 per cent forecast margin	2.4	2.4	2.5	2.5

¹⁵ HM Treasury (2013).

- 4.46 Given the distinction between spending exceeding the cap due to changes in forecasting assumptions and due to discretionary policy changes, the classification of movements in the forecast is clearly crucial to our assessment. Some changes are obviously forecasting changes (for example, updated economic determinants) while others are clearly policy changes (appearing on the Treasury's scorecard of measures at each Budget or Autumn Statement). But there are grey areas, notably operational changes resulting from Ministerial decisions or responses to legal challenges. These will require careful consideration.

Forecast risks

- 4.47 As discussed above, there are risks on both sides of our central forecast of overall welfare spending. However, in terms of the welfare cap specifically, downside risks to jobseeker's allowance and associated payments of housing benefit lie outside the cap, whereas the significant upside risks on incapacity and disability benefits lie within it. The 'housing benefit only' group that has seen recent upward revisions also lies within the cap.
- 4.48 These risks are in addition to the general forecast risks that stem from our need to predict inherently complex demographic and economic determinants. Table 4.7 presents some illustrative ready reckoners of the effect on welfare spending of different changes in some of the main economic determinants. It shows that:
- a 1 percentage point upside inflation surprise in September 2014, affecting uprating in 2015-16, would raise spending by around £1 billion. This comes about primarily through higher uprating of pensioner benefits. Relative to our March 2014 forecast, triple lock uprating of the basic state pension would move from the 2.5 per cent floor to CPI inflation, while other pensioner benefits uprated by CPI would be affected in full. Disability benefits would also be affected;
 - the same surprise in September 2015, affecting uprating in 2016-17, would have a slightly larger effect, as most benefits and tax credits are uprated by CPI inflation in that year. But, in this instance, around three quarters of the increase in spending would come from items that lie within the welfare cap, because the triple lock would continue to to uprate the basic state pension in line with earnings;
 - a 5 per cent increase in the claimant count would raise spending on jobseeker's allowance and associated housing benefit – which are both outside the welfare cap – by around £0.3 billion;
 - a 5 per cent rise in the number of private renters – around half the size of the increase between 2007-08 and 2009-10 – would add more than £1 billion a year to housing benefit spending. A 1 per cent rise in the level of eligible rents would cost around £0.3 billion; and
 - a 1 per cent rise in the number of children would add around £0.1 billion to child benefit spending. A 1 per cent rise in the number of pensioners would add over £1 billion to spending, assuming that they had the same entitlements as current

pensioners, with the majority of the effect coming from higher spending on state pensions that are outside the welfare cap.

- 4.49 Inflation surprises therefore represent a key risk to the welfare cap – especially an upside surprise that came beyond the period during which most working-age benefits are being uprated by 1 per cent. An upside inflation surprise that occurred during the period of the 1 per cent uprating cap would reduce the real value of most working-age benefits rather than feeding through to higher welfare spending.

Table 4.7: Ready reckoners for the sensitivity of welfare spending

	Impact on spending (£ billion)			
	2015-16	2016-17	2017-18	2018-19
Change in 2015-16 (unless otherwise stated)				
Inflation¹				
1 percentage point increase in CPI inflation affecting 2015-16 (1% uprating cap for some benefits)	0.9	1.0	1.0	1.0
1 percentage point increase in CPI inflation affecting 2016-17 (uprating of CPI for most benefits)	0.0	1.7	1.7	1.7
Labour market				
5 per cent increase in claimant count ²	0.3	0.3	0.3	0.4
Housing market				
5 per cent increase in number of private renters ³	1.3	1.3	1.3	1.3
1 per cent increase in housing benefit eligible rents ³	0.3	0.3	0.3	0.3
Demographics				
1 per cent increase in child benefit caseload	0.1	0.1	0.1	0.1
1 per cent increase rise in pensioner caseloads ⁴	1.2	1.2	1.2	1.3

¹ Impact of an increase in the preceding September that affects uprating in the following fiscal year.

² Impact on jobseeker's allowance and passported housing benefit.

³ Impact on housing benefit only.

⁴ Impact on all benefits for which pensioner caseloads are available.

- 4.50 There are a number of potential operational and legal risks to the forecast, including:

- problems with the programmes of reassessment associated with reforms to incapacity and reassessment could lead to differences relative to forecast in the number of cases being assessed and the outcomes from those that are assessed;
- similar problems with the roll-out of universal credit could present more significant risks to our forecasts in the future, once sufficient data are available to switch our forecasting approach from top-down to bottom-up. (Such a change of forecasting approach might itself have implications for the cap if it led to significant changes in the overall welfare spending forecast or the split between spending inside and outside the cap); and
- the Government's welfare reforms have already been subject to a number of legal challenges, and it is clearly possible that there could be further challenges in the future.

Policy risks

4.51 In setting the OBR's remit, Parliament has required that we only consider the current policies of the current Government. We do not, therefore, quantify any policy risks to our forecasts. But it is clear that future policy decisions could affect our forecasts in a number of ways. For example, with the welfare cap set in cash terms, it is possible that inflation surprises might lead to offsetting uprating decisions. And decisions about the delivery of major ongoing reforms to incapacity benefits, disability benefits and universal credit could have material effects on our spending forecasts.

Conclusion

4.52 The assessment of trends in welfare spending described in this chapter and detailed further in Chapters 5 to 10 lead us to draw a number of over-arching conclusions:

- spending on benefits and tax credits fluctuates with the economic cycle – due in part to the sensitivity of unemployment to the state of the economy, but also because the value of benefits tends to be more stable than the economy from year to year;
- the share of welfare spending directed to pensioners and children has tended to rise relative to that directed to people of working age;
- among the working-age, means-tested benefits like tax credits and housing benefit have become increasingly important;
- by 2018-19, welfare spending as a share of GDP is forecast to fall back to its pre-crisis level thanks to reductions in the generosity of working-age benefits relative to average earnings, reduced caseloads in cyclically-sensitive benefits such as jobseeker's allowance and the assumed savings associated with reforms to incapacity and disability benefits. Spending on state pensions falls slightly as a share of GDP as the female state pension age is raised to 65 by 2018;
- within total welfare spending, that covered by the welfare cap is forecast to fall from 55.4 per cent of the total in 2013-14 to 53.6 per cent in 2018-19, reflecting in part the more generous uprating of state pensions relative to working-age benefits; and
- there are significant risks to our forecasts for welfare spending. Specific risks include: the downside risks to spending on jobseeker's allowance from the continued sharp falls in unemployment; uncertainties about housing benefit from trends in housing tenure and rents; and upside risks from delivery challenges in incapacity and disability benefits. More generally, with the welfare cap having been set in cash terms, inflation surprises that feed through to welfare spending via uprating represent a key risk.

5 Spending on elderly people

5.1 Around 55 per cent of welfare spending as defined in this report is paid to pensioners, with state pensions the largest component. The current state pension system has a two-tier structure. The first provides a basic level of retirement income through the basic state pension. The second is based on prior earnings and consists of the state second pension and its predecessors. A means-tested safety net is provided through pension credit. Other benefits paid to pensioners include winter fuel payments and the Christmas bonus, while some pensioners are entitled to free television licences for the over-75s or payments from the financial assistance scheme.

5.2 This chapter covers the following benefits and payments:¹

- state pensions;
- pension credit;
- winter fuel payments;
- free television licences for over-75s;
- the financial assistance scheme; and
- Christmas bonus.

State pensions

5.3 The basic state pension is a contributory benefit, with eligibility related to National Insurance contributions or credits. The level of an individual's basic state pension award depends on the number of years of contributions/credits accrued during his or her working life, with 30 years required to receive the full rate and entitlement reduced pro rata for those with less than 30 qualifying years. Its value is currently uprated in line with the triple lock – the highest of CPI inflation, average earnings growth and 2.5 per cent – each year. The amount received for additional state pensions depends on earnings.² State pensions are payable from the state pension age (SPA).

¹ The main figures on welfare spending and its drivers used in this report are consistent with data available at the time of our March 2014 *Economic and fiscal outlook*. Spending data cover Great Britain and are drawn from DWP expenditure tables produced at the time of our March EFO.

² At present, the state second pension has a flat rate amount for earnings up to £15,100 and for people credited into the system, and an earnings-related band for earnings between £15,100 and £40,040.

- 5.4 Under the current system, members of defined benefit occupational pension schemes that meet some minimum requirements have the choice to contract out of additional state pensions. Contracted out employees and employers pay reduced National Insurance contributions via a contracted out rebate. The conditions under which schemes and individuals could contract out have varied with changes in additional state pensions but, in general, they could contract out if:
- from 1961, an employer provided an occupational pension that paid benefits that were at least as good as those payable under the graduated retirement benefit scheme – a second-tier additional pension that was in operation between 1961 and 1975;
 - from 1978, their employer provided a contracted out occupational pension scheme that committed to pay a guaranteed minimum pension;
 - from 1988, by joining an appropriate personal pension or contracted out money purchase scheme with protected rights; and
 - from 1997, the scheme satisfied the reference scheme test.³
- 5.5 Under the Pensions Act 2014, the current two-tier pension system will be replaced by a single-tier pension, open to newly-retired pensioners, from April 2016. This will combine the basic state pension and state second pension into a flat-rate pension set above the basic level of means-tested support. It is expected to be uprated in line with the triple lock.⁴ The number of qualifying years required to claim the full single-tier pension will rise to 35 years, with a minimum qualifying period of 10 years. The effect of single-tier on our medium-term forecast is limited since it only affects new claims from April 2016, but its longer-term effects are more substantial and have been described in our *Fiscal sustainability reports*.
- 5.6 As the introduction of single-tier will mean the closure of the state second pension for new retirees, members of defined benefit occupational pension schemes will no longer be able to contract out and receive a National Insurance contributions rebate from 2016-17.
- 5.7 Other recent policy changes to the pension system include:
- introducing the 'triple lock' on uprating in the June 2010 Budget;
 - raising the SPA for women to equalise it with that for men at age 65 by 2018 (Pensions Act 2011);
 - raising the SPA for both men and women to 66 between 2018 and 2020 (Pensions Act 2011); and
 - legislating for a review of the SPA at least once every six years – based on a technical assessment by the Government Actuary and an additional report considering other

³ Bozio et al (2010).

⁴ The standard minimum guarantee is £148.35 in 2014-15.

relevant factors. The reviews will be guided by the core principle that people should expect to spend on average a third of their adult life (from age 20) in receipt of the state pension, with at least ten years' notice provided and changes being phased in over two years.⁵

- 5.8 Spending on state pensions was estimated at £83.0 billion in 2013-14, around 40 per cent of total welfare spending.⁶ Across all public spending, only the NHS total departmental expenditure limit of £109.7 billion in 2013-14 was larger than spending on state pensions.⁷ State pensions spending is not subject to the welfare cap. The Government argues that spending on pensions *"is better planned and controlled over a longer time period, for example by using the state pension age to account for rising longevity."*⁸

Trends in spending on state pensions

- 5.9 Spending on state pensions is by far the largest single item of welfare spending. As Figure 5.1 shows, spending on state pensions has risen steadily in cash terms – and also in real terms, adjusted for whole economy inflation – over the past three decades. Spending fell as a share of GDP in the mid-1980s, then moved in a fairly narrow range of 3.8 to 4.2 per cent of GDP in the two decades to 2007-08. This stability reflected a rising caseload as a share of the adult population that was broadly offset by the average award rising more slowly than GDP-per-adult.
- 5.10 State pensions spending then increased to more than 5 per cent of GDP through the late 2000s recession and remained at that level through the subsequent slow recovery. That reflected the continuing rise in the caseload, plus the combination of a sharp fall in nominal GDP and relatively generous uprating.

⁵ For further detail on the Government's announcement, see DWP (2013a).

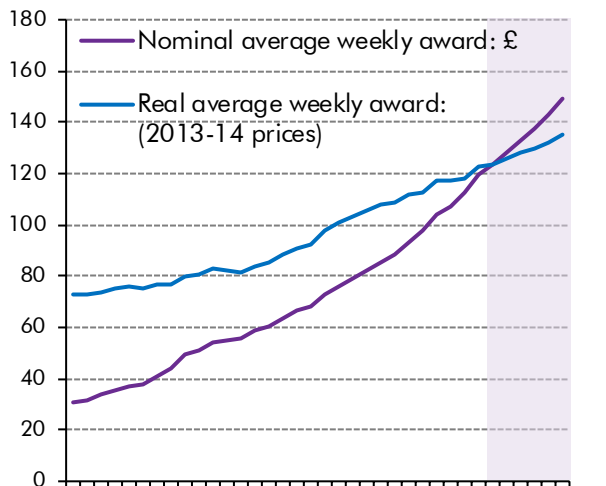
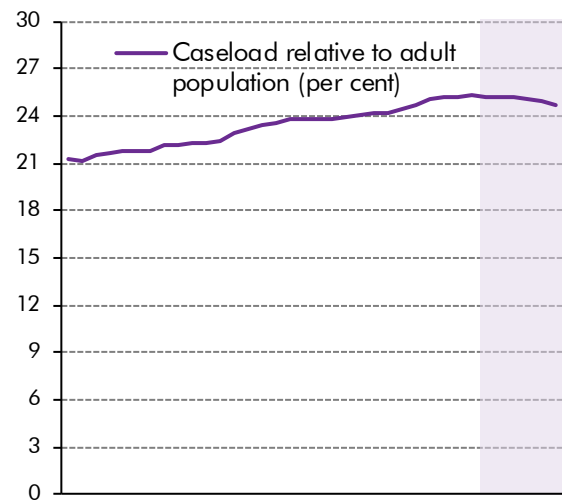
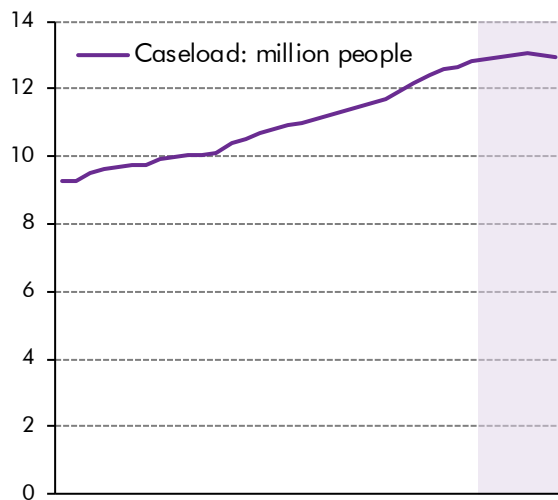
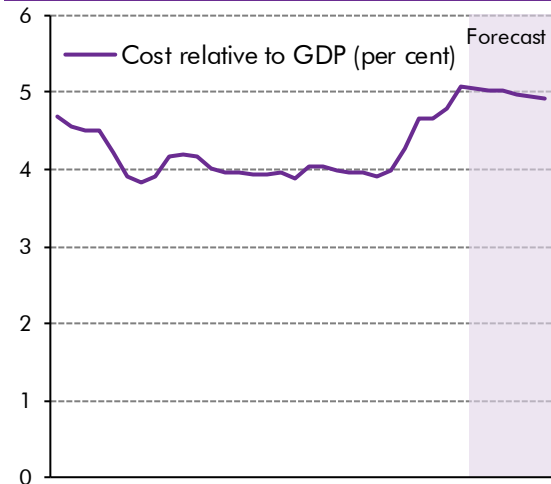
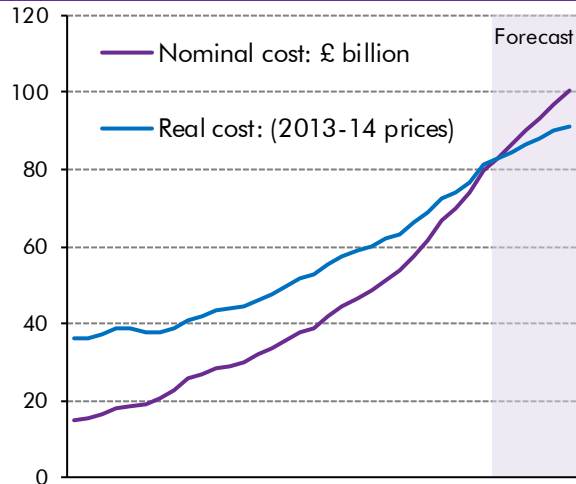
⁶ State pensions here includes the basic state pension, graduated retirement benefit, additional state pensions and deferral amounts (increments and lump sum payments).

⁷ HM Treasury (2014).

⁸ HM Treasury (2013).

Figure 5.1: State pensions: key facts

Current main rates (2014-15)		£ per week		Total cost (2013-14)	
Full basic state pension for full entitlement		113.10		£ billion	83.0
Average weekly award, including additional state pensions		128.33		Per cent of GDP	5.1
				Per cent of total welfare spending	39.5
				Per cent of welfare cap	n/a



Source: DWP, ONS, OBR

5.11 Table 5.1 decomposes changes in spending on state pensions into contributions from different drivers of changes in caseloads and average awards over selected periods from 1983-84 to 2018-19. The table shows that:

- **between 1983-84 and 1988-89**, spending on state pensions fell relative to GDP. The average award and RPI uprating increased more slowly than GDP-per-adult;
- **from 1988-89 to 2007-08**, spending was on average stable as a share of GDP. The rising caseload (largely resulting from non-demographic factors such as growth in the number of women entitled to a state pension in their own right)⁹ and the rising average additional state pension award were offset by GDP-per-adult rising faster than inflation. The early 1990s recession and recovery on GDP also led to fluctuations in spending as a share of GDP;
- **between 2007-08 and 2012-13**, spending increased by over 1 per cent of GDP. The value of the basic state pension increased by 28 per cent over these five years, while GDP-per-adult grew by just 4½ per cent. This reflected uprating in line with relatively high inflation rates in each year – except 2010-11, when it was increased by 2.5 per cent, which was higher than both inflation and average earnings growth. The caseload also continued to rise, mainly driven by an ageing population; and
- **between 2012-13 and 2018-19**, spending on state pensions is forecast to fall slightly, relative to GDP. The rising SPA for women reduces the state pension caseload relative to the adult population, offsetting the pressures that an ageing population would otherwise have exerted. Other things being equal, the triple lock would see average awards fall slightly relative to GDP-per-adult over the forecast period (as a rising employment rate lifts GDP growth relative to average earnings growth). But average awards are actually forecast to be stable relative to GDP-per-adult. This reflects higher average awards relative to existing pensioners for new retirees with generous additional state pension entitlements and growth in the number of women who will have accrued the minimum qualifying years for a full award.

⁹ See, for example, Johnson and Stears (1996).

Table 5.1: Drivers of changes in state pensions spending

	Per cent of GDP			
	1983-84 to 1988-89	1988-89 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	4.68	3.92	3.98	5.08
Spending at end of period	3.92	3.98	5.08	4.92
Change	-0.76	0.06	1.10	-0.17
of which:				
Caseloads	0.13	0.45	0.14	-0.12
Demography ¹	0.03	0.04	0.24	0.38
State pension age changes ²	0.00	0.00	-0.14	-0.52
Other	0.09	0.40	0.04	0.02
Average awards	-0.89	-0.38	0.97	-0.04
Fiscal drag ³	-1.03	-1.19	0.60	-0.20
Additional uprating ⁴	0.00	0.29	0.16	-0.04
Additional state pensions ⁵	0.07	0.65	0.13	-0.05
Other	0.08	-0.13	0.08	0.24

¹ Changes in the share of the population aged over 65 for men and 60 for women.

² Raising the state pension age for women to 65 by 2018 and for men and women to 66 by 2020.

³ Differences between RPI inflation and earnings growth.

⁴ Uprating beyond RPI inflation.

⁵ Effect on the average award from additional state pensions, including the state earnings related pension and state second pension.

Changes in caseloads

5.12 The state pension caseload increased by 39 per cent over the three decades to 2013-14 (from 9.2 million to 12.9 million), rising from 21.3 per cent of the adult population to 25.3 per cent. Women account for a larger share of the state pension caseload than their population share, reflecting their lower SPA (for the time being) and higher life expectancy than for men. Changes in the state pension caseload were largely driven by demographic trends, overlaid by changes in eligibility.

Demographic effects

5.13 Between 1983-84 and 2013-14, the UK resident population aged above the SPA rose from 10.1 million to 12.3 million people, largely reflecting increasing life expectancy at older ages and the post-war baby boom cohort moving above state pension age (see Chapter 3). Rising life expectancy at age 65 has meant that – prior to the SPA reforms currently in progress – over time pensioners have on average been claiming state pensions for longer.

5.14 In our medium-term forecast, the impact of ageing on the caseload is more than offset by the rise in the SPA for women to 65 by 2018. As Table 5.1 shows, without the rising SPA, spending on pensions would be around 0.5 per cent of GDP higher in 2018-19. Raising the male and female SPA to 66 between 2018 and 2020 has little effect on our latest medium-term forecast, but will have a greater effect when our forecast horizon rolls on to 2019-20 in this December's *Economic and fiscal outlook*.

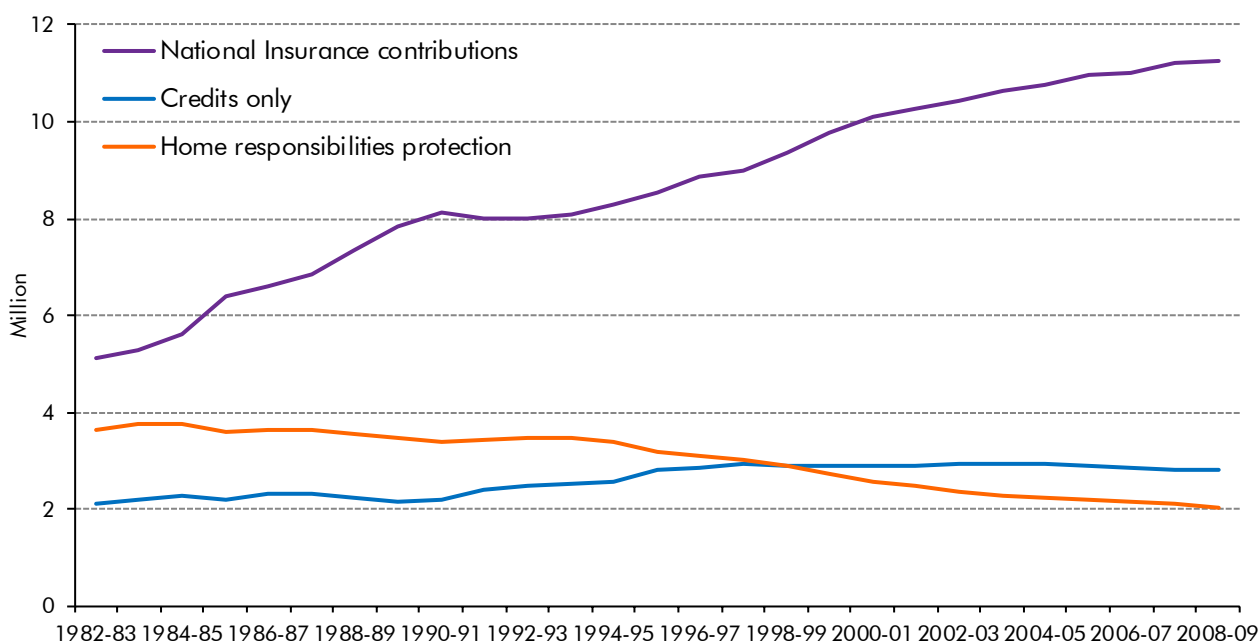
Female eligibility

5.15 Alongside growth in the pension age population, the state pension caseload has increased in part due to the growing number of women entitled to state pensions. This reflects:

- more women accruing basic state pension qualifying years through increased labour market participation (see Chapter 3); and
- the abolition of the 'married woman's reduced rate election' option and the 'half test' (Social Security Act 1975), as a result of which all employed women earning above the lower-earnings limit had to pay full National Insurance contributions.¹⁰

5.16 Chart 5.1 shows the number of women accruing a qualifying year for the basic state pension by different methods since the late 1970s. This shows the significant increase in those entitled to some basic state pension due to National Insurance contributions.

Chart 5.1: Number of women who have accrued a qualifying year for state pension by method of accrual



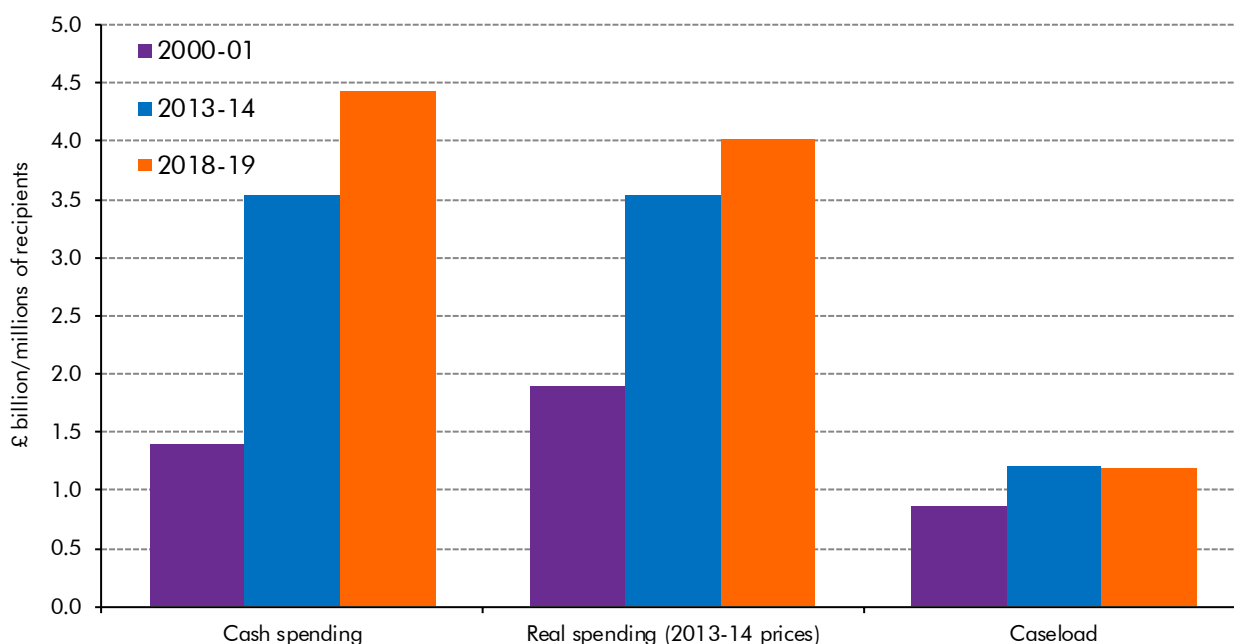
Source: DWP

State pensions paid overseas

5.17 The state pension caseload includes pensioners qualifying for a UK state pension who live overseas and is therefore higher than the resident UK pensioner population. State pensions paid outside the UK have risen from £1.4 billion in 2000-01 to £3.5 billion in 2013-14. Over the same period, the caseload has risen by almost half to 1.2 million.

¹⁰ See Meyer and Pfau-Effinger (2006).

Chart 5.2: State pensions spending overseas



Changes in average awards

5.18 The main drivers of the average state pension award relative to GDP-per-adult are:

- uprating policy – both the fiscal drag effect of inflation typically lagging earnings growth and additional effects from uprating by more or less than inflation; and
- changes in the composition of the caseload – particularly increases in the number of pensioners also entitled to an additional state pension.

Inflation and uprating

5.19 State pensions were generally indexed to RPI inflation until 2010-11, with the addition of a 2.5 per cent floor that was announced in the 2001 Pre-Budget Report.¹¹ On occasion, the Government chose to override the default uprating. For example, the basic state pension was uprated by substantially more than RPI inflation in the years after 2000-01, when the Labour Government decided that uprating in line with the low rate of RPI inflation that had been applied that year – 1.1 per cent – had been inadequate.

5.20 In June 2010, the Coalition Government announced the triple lock, which has meant that the basic state pension is now uprated by the highest of CPI inflation, average earnings and 2.5 per cent each year. In 2011-12, RPI inflation was used for uprating, which was higher than all three elements of the new triple lock. As Table 5.2 shows, the triple lock has delivered uprating higher than earnings growth in every year since its introduction and is expected to do so again in 2015-16.

¹¹ This floor was used twice: first, in 2003-04, then again in 2010-11 when the previous September's RPI inflation rate had been negative.

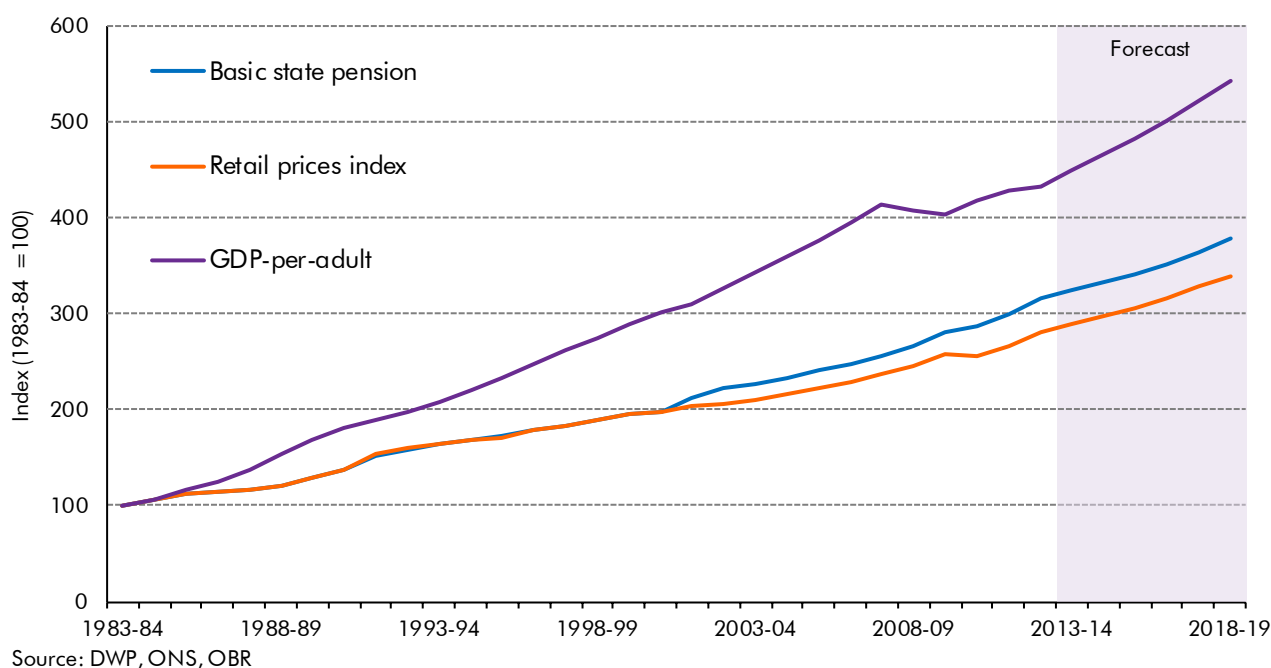
Table 5.2: Basic state pension uprating between 2007-08 and 2018-19

	Cash rise in basic state pension	Uprating	Previous year's average earnings	Uprating in line with
2007-08	£3.05	3.6%	4.4%	Previous September's RPI inflation
2008-09	£3.40	3.9%	3.5%	Previous September's RPI inflation
2009-10	£4.55	5.0%	3.5%	Previous September's RPI inflation
2010-11	£2.40	2.5%	1.8%	2.5 per cent
2011-12	£4.50	4.6%	1.3%	Previous September's RPI inflation
2012-13	£5.30	5.2%	2.9%	Previous September's CPI inflation
2013-14	£2.70	2.5%	1.6%	2.5 per cent minimum
2014-15	£2.95	2.7%	1.2%	Previous September's CPI inflation
2015-16	£2.85	2.5%	2.1%	2.5 per cent minimum
2016-17	£3.85	3.3%	3.3%	Previous year's average earnings
2017-18	£4.30	3.6%	3.6%	Previous year's average earnings
2018-19	£4.60	3.7%	3.7%	Previous year's average earnings

Note: Forecasts based on March 2014 *Economic and fiscal outlook*.

5.21 The average state pension award fell relative to GDP-per-adult between 1983-84 and 2007-08 as productivity growth meant GDP-per-adult increased faster than RPI inflation uprating (Chart 5.3). In recent years, as inflation – and more recently triple lock uprating – has outstripped earnings growth, the average award has risen relative to GDP-per-adult.

Chart 5.3: Basic state pension uprating relative to inflation and incomes



Composition of the caseload

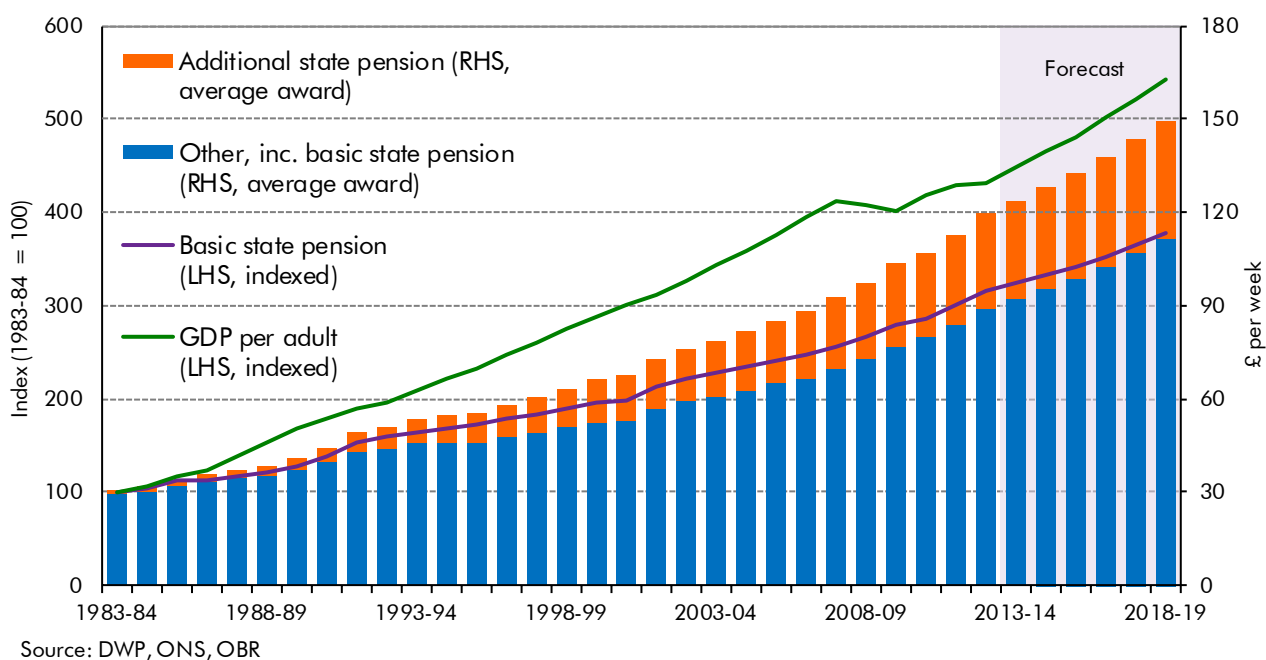
5.22 The most important compositional change driving changes in average awards has been the rising number of pensioners entitled to an additional state pension.¹² The caseload for such

¹² See Banks et al (2006).

pensions has risen more than tenfold, from around 0.9 million in 1983-84 – or around 8 per cent of pensioners – to just under 10 million in 2013-14 – around 70 per cent of pensioners. The more general increase in eligibility for women described above is echoed here too. Moreover, as the state earnings related pension scheme and state second pension have been more generous than the graduated retirement benefit that preceded them, the average award for pensioners in receipt of additional state pensions has risen faster than that for the basic state pension.

5.23 Chart 5.4 shows how the overall state pension average award has risen since 1983-84 and how that breaks down into the basic state pension and additional state pensions. Overall, the average award increased around fourfold between 1983-84 and 2013-14 in cash terms. The implied basic state pension average award almost trebled – broadly in line with the effect of uprating – while the additional state pension average award rose by more than 20 times – due to the tenfold increase in the number of pensioners receiving such payments, plus the composition of the caseload shifting towards those with more generous awards.

Chart 5.4: Basic and additional state pension awards



State pension spending in the medium-term forecast

Spending, caseloads and average awards

5.24 In our latest medium-term forecast, spending on state pensions is forecast to rise from £83.0 billion in 2013-14 to £100.4 billion in 2018-19. With nominal GDP forecast to grow slightly faster, spending on state pensions is expected to fall from 5.1 per cent of GDP in 2013-14 to 4.9 per cent in 2018-19. Over this period, the increases in the SPA, particularly equalising the male and female SPA at 65 by 2018, more than offset the pressures from an ageing population on the caseload.

- 5.25 Average awards are expected to rise by 3.8 per cent a year on average over the period, remaining broadly flat relative to GDP-per-adult. Triple lock uprating is expected to be slightly lower than growth in GDP-per-adult. This reflects the fact that the employment rate is expected to rise, which means that GDP-per-adult grows slightly faster than average earnings. But this effect is broadly offset by changes in the composition of the caseload, with higher average awards relative to existing pensioners for new retirees with generous additional state pension entitlements and growth in the number of women that will have accrued the minimum qualifying years for a full award.

Table 5.3: State pensions spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	79.8	83.0	86.5	90.0	93.2	96.9	100.4
Caseload (million)	12.8	12.9	13.0	13.0	13.0	13.0	12.9
Average annual award (£ thousand)	6.2	6.4	6.7	6.9	7.4	7.4	7.8
Forecast in the context of welfare spending							
Per cent of total welfare spending	37.5	39.5	40.5	41.1	41.5	42.0	42.5
Forecast relative to the economy							
Spending (% of GDP)	5.1	5.1	5.0	5.0	5.0	5.0	4.9
Caseload (% of adults)	25.3	25.3	25.2	25.2	25.1	24.9	24.7
Average award (% of GDP-per-adult)	20.1	20.0	19.9	20.0	19.9	19.9	19.9

Key risks to the forecast

- 5.26 The caseload for state pensions is largely driven by demographic factors interacting with policy changes to the SPA. These effects are relatively certain over a five-year horizon. This is overlaid by changes in the composition of the caseload and the effect of the triple lock on uprating. These determinants of the forecast are subject to greater uncertainty, with the main risk coming from our economic forecast of average earnings and inflation, which feeds through to the triple lock on uprating.
- 5.27 In terms of cash spending, the risk is simply that higher or lower earnings growth would lead to higher or lower uprating and spending due to the triple lock. In terms of spending relative to GDP, if inflation exceeds earnings growth, the average state pension award would tend to rise relative to GDP-per-adult, pushing spending higher as a share of GDP. This has been very evident in recent years.
- 5.28 The introduction of the single-tier pension from April 2016 could present risks to the forecast given the historical evidence that major changes to the benefit system can lead to unexpected outcomes.

Long-term projection of state pensions spending

- 5.29 Our 2014 *Fiscal sustainability report (FSR)* contained long-term projections for UK state pensions spending to 2063-64. In our long-term projections, we combine state pensions with other pensioner-related benefits covered in this chapter, including pension credit, winter fuel allowance, free television licences and the Christmas bonus. The projections

show state pensions spending on this basis rising from 5.5 per cent of GDP at the end of our medium-term forecast in 2018-19 to 7.9 per cent of GDP in 2063-64.

- 5.30** The rise in spending is largely driven by demographic trends – for example, the proportion of the population aged over 65 is projected to rise from 17.6 per cent in 2014 to 27.1 per cent in 2064. Our projection of further increases in the SPA – based on the principle set out by the Government that people should expect to spend a third of their adult life in receipt of the state pension – reduces the effect of ageing on state pensions spending. Our estimate of the long-term effect of the triple lock on uprating works in the opposite direction – it assumes that, on average, state pensions will be uprated by earnings plus 0.3 per cent a year, based on analysis of past developments in inflation and earnings growth.
- 5.31** The main sensitivities around our state pensions projections were explored in the *FSR*. With the SPA now more closely linked to demographic change, spending is less sensitive to changes in longevity is less than was previously the case. But spending as a share of GDP remains sensitive to changes in the number of workers relative to the number of pensioners. For example, higher net migration¹³ or greater-than-projected labour market participation among older age groups would reduce spending as a share of GDP by increasing GDP proportionally more than spending on pensions.

Table 5.4: State pensions long-term spending projection

	Forecast		Projections				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP ¹	5.8	5.5	5.7	6.7	7.4	7.6	7.9
Per cent of welfare spending ¹	46.0	47.7	48.1	52.2	54.3	54.8	56.0

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis, consistent with our 2014 *Fiscal sustainability report* projections.

¹ State pensions covers basic state pension, state earnings related pension scheme, state second pension, single-tier pension, other elements of state pension, pension credit and other pensioner benefits.

Pension credit

- 5.32** Pension credit was introduced in October 2003, replacing the minimum income guarantee – previously income support for the over 60s – as the main means-tested benefit for pensioners. Pension credit is designed to provide pensioners with a guaranteed minimum level of income through means-tested benefits, and to encourage workers to make provision for their own retirement. To do this, it comprises two components:
- **guarantee credit:** the direct replacement for the minimum income guarantee, which provides qualifying pensioners with a minimum level of income for which anyone aged above the female SPA is eligible. The qualifying age is rising from 60 to 65 in line with the female SPA – described in the first section of this chapter – and from December 2018 onwards in line with SPA for both men and women from 65 to 66; and

¹³ All else equal, net migration increases the working-age population and GDP. See Box 3.4 of the 2014 *Fiscal sustainability report* for a discussion of why all else might not be equal.

- **savings credit:** which is designed to reduce the disincentive to save created by the means-tested guarantee credit. It provides extra financial support to people aged over 65 (or whose partners are aged over 65) who have made some provision for their retirement such as savings or a second pension.

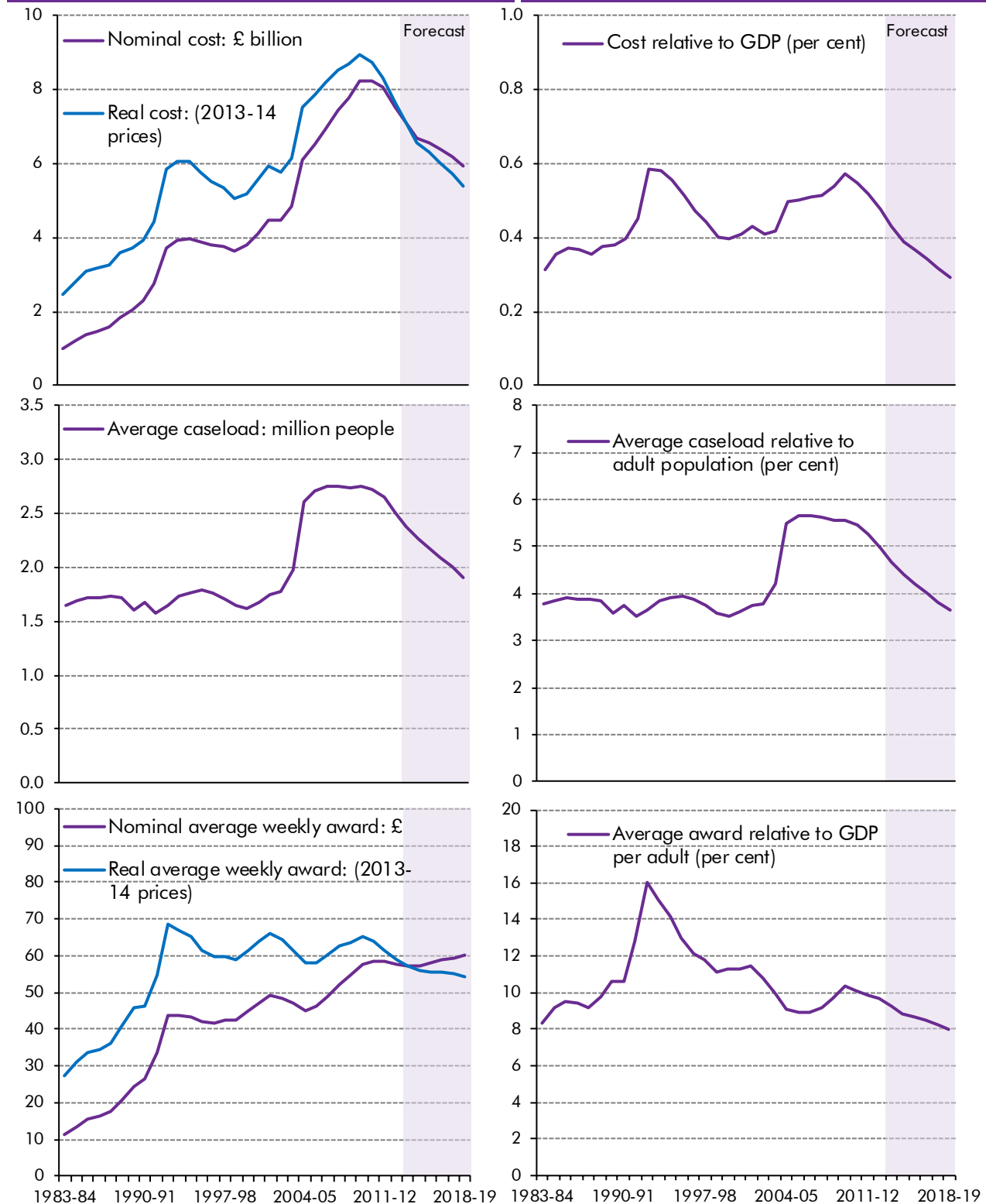
- 5.33 Claimants may be entitled to one or both elements of pension credit. In 2013-14, of the 2.4 million people receiving pension credit, around 40 per cent received both guarantee credit and savings credit, 40 per cent the guarantee credit only and 20 per cent the savings credit only. Women account for around 60 per cent of the pension credit caseload.
- 5.34 From April 2016, the new single-tier pension will be set above the level of the basic means test – the pension credit standard minimum guarantee. At the same time, eligibility for the savings credit element will be removed for most individuals reaching the SPA after April 2016, so the caseload will only be made up of existing claims and will decline over time.
- 5.35 Spending on pension credit is subject to the welfare cap. In 2013-14, spending on pension credit is estimated at £7.1 billion, accounting for 3.4 per cent of total welfare spending and 6.1 per cent of spending that will be subject to the welfare cap from 2015-16.

Trends in spending on pension credit

- 5.36 Spending on pension credit and its predecessors has fluctuated between 0.3 per cent of GDP and 0.6 per cent of GDP over the past 30 years (Figure 5.2). It increased from the late 1980s to the early 1990s, peaking at 0.59 per cent of GDP in 1992-93. It then fell back by the early 2000s, before rising again to a recent peak of 0.57 per cent of GDP in 2009-10.
- 5.37 The early 1990s rise reflected a rise in average awards that outstripped growth in GDP-per-adult, while the late 2000s rise reflected a jump in the share of the adult population claiming after the introduction of pension credit in 2003. Spending on pension credit is forecast to fall sharply relative to GDP due largely to the effect on the caseload of raising the female SPA and the introduction of the single-tier pension.

Figure 5.2: Pension credit: key facts

Current main rates (2014-15)	£ per week	Total cost (2013-14)	
		£ billion	7.1
Single person guarantee credit	148.35	Per cent of GDP	0.43
Single person savings credit	16.80	Per cent of total welfare spending	3.4
Average weekly award	57.13	Per cent of welfare cap	6.1



Source: DWP, ONS, OBR

- 5.38 Table 5.5 decomposes changes in spending on pension credit and its predecessors over selected periods into contributions from different drivers of changes in caseloads and average awards. It shows how the rise and fall of spending on the predecessors to pension credit (pre-2003-04) was driven almost entirely by changes in average awards relative to GDP-per-adult. Changes in pension credit spending (2003-04 onwards) have been driven by the caseload: a rise after its introduction, followed by a fall that initially reflected falling take-up from 2007-08 and then the effects of the rising female SPA from 2010.

Table 5.5: Drivers of changes in pension credit spending

	Per cent of GDP					
	1983-84 to 1987-88	1987-88 to 1992-93	1992-93 to 2002-03	2002-03 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	0.31	0.36	0.59	0.41	0.51	0.48
Spending at end of period	0.36	0.59	0.41	0.51	0.48	0.29
Change	0.04	0.23	-0.18	0.11	-0.04	-0.19
of which:						
Caseloads	0.01	-0.02	0.02	0.17	-0.06	-0.11
Demography ¹	0.00	0.00	-0.01	0.01	0.03	0.03
Other	0.01	-0.02	0.03	0.16	-0.09	-0.15
Average awards	0.03	0.25	-0.20	-0.07	0.03	-0.07

¹ Changes in the share of the population aged 60 and over.

Changes in caseloads

- 5.39 Trends in the caseload for pension credit and its predecessors are driven by demographic factors (the number of people above the qualifying age), economic factors and policy decisions affecting eligibility (the proportion of people that would pass the means test for additional support) and take-up (the proportion of eligible people that claim the benefit).
- 5.40 The introduction of pension credit in 2003-04 was followed by a drive to increase take-up between 2004-05 and 2007-08. The pension credit caseload increased from 4.2 per cent of the adult population in 2003-04 to a peak of 5.7 per cent in 2006-07. In absolute terms, the caseload increased from 1.8 million for the minimum income guarantee in 2002-03 to 2.7 million for pension credit in 2007-08 (although this did not meet the Spending Review 2002 goal to be “paying pension credit to at least 3 million pensioner households by 2006, by ensuring that claiming is simplified and less intrusive so that pensioners are encouraged to take up their full entitlement.”).¹⁴ The effect can be seen in Table 5.5, where non-demographic effects on the caseload more than account for the increase in spending as a share of GDP between 2002-03 and 2007-08.
- 5.41 The caseload was stable at around 2.7 million between 2006-07 and 2010-11 – and therefore declined slightly as a share of the adult population – as awareness campaigns ended and take-up fell.

¹⁴ HM Treasury (2002).

- 5.42 Between 2012-13 and 2018-19, the caseload is expected to fall by 24 per cent from 2.5 million to 1.9 million – declining by 1.3 per cent of the adult population. The main driver of this fall is the higher qualifying age, with the introduction of the single-tier pension having a small effect from 2016-17 that will increase beyond the forecast horizon.

Changes in average awards

- 5.43 Average awards for pension credit and its predecessors have fluctuated significantly over the past 30 years, both in cash terms and relative to GDP-per-adult. Awards increased sharply from the late 1980s to the early 1990s. They were then relatively stable in cash terms through to the late 1990s, thus falling in real terms and relative to GDP-per-adult. These changes were driven by a combination of default uprating overlaid by policy decisions.
- 5.44 Focusing on the periods of greatest change in average awards relative to GDP-per-adult – when these changes contributed materially to the overall trend in spending on pension credit and its predecessors as a share of GDP – the main drivers have been:
- the switch from supplementary benefit to income support in 1988-89, which increased the generosity of the support. The introduction of the enhanced pensioner premium in the early 1990s, which delivered additional support for older pensioners, also increased generosity. At the same time, inflation increased faster than GDP-per-adult during the early 1990s recession; and
 - during the rest of the 1990s, uprating in line with ROSSI inflation during a period of strong GDP growth led to a fall in the average award relative to GDP-per-adult.
- 5.45 More recently, policy decisions on uprating have typically increased generosity:
- from 2001, the minimum income guarantee was simplified into one rate – effectively the highest, over-80s rate – for all those over 60;
 - in 2003-04, guarantee credit uprating was switched from ROSSI inflation to average earnings growth;
 - in 2007-08 and 2008-09, guarantee credit was uprated by more than the increase in average earnings; and
 - since 2010, guarantee credit has been uprated in line with the cash increase in the basic state pension, in order to maintain its value relative to the basic state pension. This has increased its value relative to average earnings and GDP-per-adult. But at the same time, the savings credit maximum award was reduced.

Pension credit spending in the medium-term forecast

Spending, caseloads and average awards

- 5.46** We forecast spending on pension credit to fall from £7.1 billion in 2013-14 to £5.9 billion by 2018-19, dropping to 0.3 per cent of GDP. This mainly reflects the reduction in the caseload due to raising the female SPA – and thus the pension credit qualifying age – and, to a much lesser extent, the introduction of the single-tier pension, which will remove eligibility for many individuals reaching the SPA after April 2016.
- 5.47** The higher SPA has a proportionately larger impact on the pension credit caseload than for state pensions, as the female SPA sets the qualifying age for both men and women for pension credit. The caseload is forecast to fall from 4.7 per cent of the adult population in 2013-14 (or 2.4 million) to 3.6 per cent (1.9 million) in 2018-19. Average awards rise only slightly in cash terms over the forecast period, and fall relative to GDP-per-adult.

Table 5.6: Pension credit spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	7.5	7.1	6.7	6.6	6.4	6.2	5.9
Caseload (million)	2.5	2.4	2.3	2.2	2.1	2.0	1.9
Average annual award (£ thousand)	3.0	3.0	3.0	3.0	3.0	3.1	3.1
Forecast relative to welfare spending							
Per cent of total welfare spending	3.5	3.4	3.1	3.0	2.8	2.7	2.5
Per cent of welfare cap spending	6.4	6.1	5.7	5.5	5.2	5.0	4.7
Forecast relative to the economy							
Spending (% of GDP)	0.48	0.43	0.39	0.37	0.34	0.32	0.29
Caseload (% of adults)	4.9	4.7	4.4	4.2	4.0	3.8	3.6
Average award (% of GDP-per-adult)	9.7	9.3	8.9	8.7	8.5	8.3	8.0

Winter fuel payments

- 5.48** Winter fuel payments were introduced in 1997-98. They provide a flat rate benefit for all individuals over the age of 60, the claimed purpose of which is to support them with their winter fuel bills, although the use to which the money is put is entirely at the discretion of the recipient. The qualifying age for winter fuel payments is linked to the SPA for women and is therefore currently rising.
- 5.49** Spending on winter fuel payments is subject to the welfare cap. In 2013-14, £2.2 billion was spent on winter fuel payments – equivalent to a little under half the amount spent on jobseeker's allowance for the unemployed. That was 1.0 per cent of total welfare spending and 1.9 per cent of spending that will be subject to the welfare cap.
- 5.50** In 2014-15, the 'standard' winter fuel payment rates are £200 per eligible household where the oldest person is under 80 and £300 for households containing a person aged 80 or over. Lower rates apply for the second qualifying individual in a household. The rate

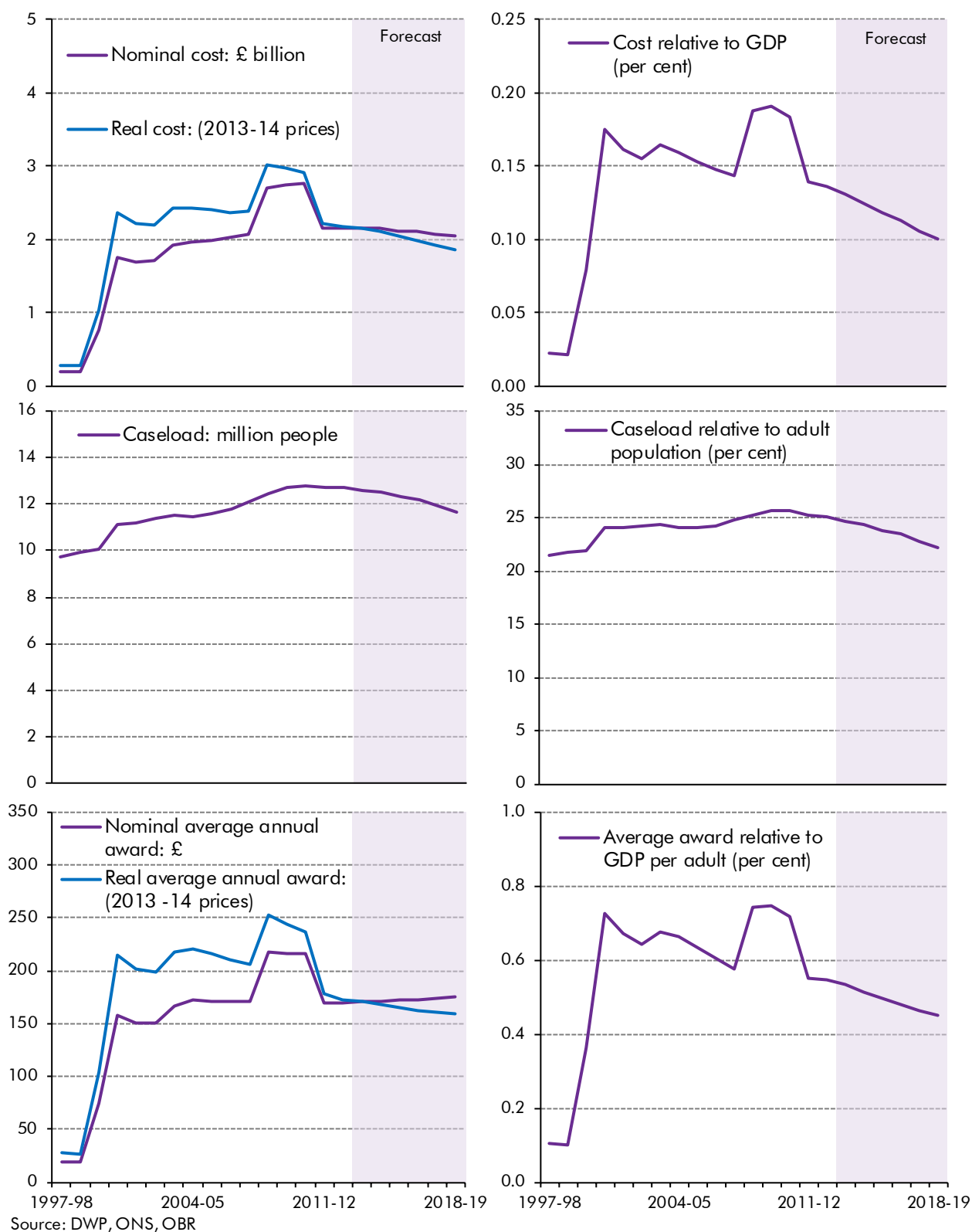
received depends on a person's circumstances during the qualifying week, which for 2014-15 was the penultimate week of September 2014.

Trends in spending on winter fuel payments

- 5.51 Spending on winter fuel payments has increased from £0.2 billion (0.02 per cent of GDP) on their introduction in 1997-98 to £2.2 billion (0.13 per cent of GDP) in 2013-14 (Figure 5.3). The main drivers have been demographic trends and policy decisions affecting the caseload and average award. In terms of their contribution to changes in spending, policy decisions affecting average awards have been by far the most important.

Figure 5.3: Winter fuel payments: key facts

Current main rates	£ annual	Total cost (2013-14)	
Under/over 80 years - only eligible person in household	200/300	£ billion	2.2
Multiple person household not getting pension credit or income related JSA	100	Per cent of GDP	0.1
Average annual award	172	Per cent of welfare spending	1.0
		Per cent of welfare cap	1.9



- 5.52** The winter fuel payments caseload increased by 29 per cent between 1997-98 and 2013-14, rising from 9.8 million to 12.6 million. This was mainly explained by the decision in 2000-01 to lower the qualifying age for men from the male SPA of 65 to align it with the female SPA of 60. In addition, the same demographic trends that have affected the caseload for other benefits for the elderly have been relevant for winter fuel payments too.
- 5.53** The main rate paid was increased from £20 when it was introduced to £100 in 1999-00 and then £200 in 2000-01. Additional 'one-off' payments of £100 for households containing someone aged over 80 and £50 for all other eligible households were made in 2008-09, during the late 2000s recession, and were repeated up to 2010-11.

Winter fuel payments spending in the medium-term forecast

Spending, caseloads and average awards

- 5.54** Spending is forecast to be roughly flat in cash terms over the forecast period, thereby falling from 0.13 per cent of GDP in 2013-14 to 0.10 per cent of GDP in 2018-19. Both the caseload and the average award contribute to the fall. The caseload falls as a share of the adult population because the qualifying age is being raised in line with the female SPA. The average award is relatively flat in cash terms – small changes reflect the composition of the caseload – so falls relative to GDP-per-adult.
- 5.55** Over the forecast period, the Government's policy to remove entitlement to winter fuel payments from pensioners overseas "*in warm countries*" – introduced in response to a 2011 European Court of Justice ruling that increased eligibility overseas¹⁵ – is expected to reduce the caseload by around 1 per cent when it comes into operation in 2015-16.

Table 5.7: Winter fuel payments forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	2.1	2.2	2.1	2.1	2.1	2.1	2.0
Caseload (million)	12.7	12.6	12.5	12.3	12.2	11.9	11.6
Average annual award (£ thousand)	0.17	0.17	0.17	0.17	0.17	0.17	0.18
Forecast relative to welfare spending							
Per cent of total welfare spending	1.0	1.0	1.0	1.0	0.9	0.9	0.9
Per cent of welfare cap spending	1.8	1.9	1.8	1.8	1.7	1.7	1.6
Forecast relative to the economy							
Spending (% of GDP)	0.14	0.13	0.12	0.12	0.11	0.11	0.10
Caseload (% of adults)	25.0	24.7	24.4	23.8	23.4	22.8	22.2
Average award (% of GDP-per-adult)	0.55	0.53	0.51	0.50	0.48	0.46	0.45

¹⁵ Following a 2011 European Court of Justice judgment in the 'Stewart case' (relating to short-term incapacity benefit in youth), DWP could no longer require that – where the claimant is subject to the EU social security co-ordination legislation and has a genuine and sufficient link with the UK – claimants of winter fuel payments and other non-contributory benefits must acquire the benefit in the UK. DWP began to operate the extended eligibility policy in the European Economic Area and Switzerland, along with a genuine and sufficient link test, in winter 2012-13.

Key risks to the forecast

- 5.56** With the caseload driven largely by demographics, and a cash amount paid that is not automatically uprated, the main risks to the forecast are policy related – particularly the amounts paid per beneficiary. One uncertainty related to the caseload is the extent to which newly-eligible pensioners in European countries take up their entitlement, which could be more or less than assumed. A related uncertainty stems from the announced withdrawal of winter fuel payments from pensioners in warmer countries from 2015-16, which may also affect take-up. It is possible, for example, that take-up in European countries that have not been defined as ‘warm’ by the policy could be affected by greater awareness of entitlement as the policy is applied in countries that have been defined as ‘warm’.

Free television licences for the over-75s

- 5.57** Free television licences for the over 75s were introduced in 2000-01. The policy currently saves over 4 million recipients the £145.50 cost of an annual television licence at a cost of £0.6 billion in 2013-14 – approximately half the cost of the Department of Culture, Media and Sport’s current departmental spending in that year.¹⁶

Trends in spending on television licences for the over-75s

- 5.58** Spending on television licences for the over 75s is a very small part of total welfare spending. It is not subject to the welfare cap. The caseload has increased substantially since the policy was introduced, reflecting the rising share of the population aged 75 and over. Spending is forecast to rise broadly in line with GDP as the effect of the ongoing rise in the eligible population is partly offset by the licence fee being fixed in cash terms until 2016. From 2016, we assume the licence fee rises in line with CPI inflation.

Table 5.8: Free television licences for the over-75s forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	0.60	0.62	0.63	0.64	0.65	0.70	0.76
Caseload (million)	4.3	4.4	4.6	4.6	4.7	4.8	5.0
Average annual award (£ thousand)	0.14	0.14	0.14	0.14	0.14	0.14	0.15

Financial assistance scheme

- 5.59** The financial assistance scheme offers help to some people who have lost out on their pension, because they belonged to pension schemes where the employer failed and the schemes contained insufficient funds to pay members’ benefits. It is generally only applicable to those schemes that closed between 1 January 1997 and 5 April 2005. The scheme is administered by the Pension Protection Fund on behalf of the Department for Work and Pensions (DWP). Until Budget 2014, payments associated with the scheme were made from DWP’s departmental expenditure limit (DEL) budget. In Budget 2014, financial

¹⁶ HM Treasury (2014).

assistance scheme spending was reclassified to annually managed expenditure (AME) and will be subject to the welfare cap.

- 5.60 We forecast that spending associated with the financial assistance scheme will rise from £0.17 billion in 2013-14 to £0.31 billion in 2018-19. While this is small relative to total welfare spending, this forecast is subject to significant uncertainty because of the judgements that need to be made about the scale and timing of payments – including lump sum payments – to a small number of beneficiaries.

Christmas bonus

- 5.61 The Christmas bonus is a one-off annual tax-free payment of £10 that is paid to anyone receiving an eligible benefit. This extends beyond the elderly, though pensioners make up the largest single recipient group. With the cash award fixed, spending is driven by growth in the caseload, which stood at around 15.5 million in 2013-14 (spending of £155 million) and is forecast to fall by 3.5 per cent to 14.9 million in 2018-19 (spending of £149 million), with the non-pensioner caseload driving the fall. In 2008-09, the Christmas bonus was used by the Labour Government to deliver additional payments of £60 to people during the recession,¹⁷ with spending reaching £1.0 billion in that year. Spending on the Christmas bonus is subject to the welfare cap.

¹⁷ In HM Treasury (2008), this was described as the Government making “a payment of £60 to each pensioner, equivalent to bringing forward uprating of the basic State Pension from April to January. Around 12.5 million pensioners will benefit. A £60 payment will also be made to 2.5 million individuals who are in receipt of certain other benefits.”

6 Spending on sick and disabled people

6.1 Welfare spending on sick and disabled people consists of a number of different benefits, the caseloads for which are often closely related. For example, the latest data suggest that over 70 per cent of working-age claimants in receipt of incapacity benefits were also in receipt of disability living allowance,¹ while eligibility for carer's allowance is explicitly linked to caring for someone in receipt of certain other disability benefits. In this chapter, trends in each benefit are discussed in turn, but these interactions are important to bear in mind.

6.2 The chapter covers the following benefits:

- employment and support allowance and other incapacity benefits;
- disability living allowance and personal independence payment;
- attendance allowance;
- carer's allowance;
- a number of smaller benefits for sick and disabled people; and
- war pensions and the armed forces compensation scheme.

Incapacity benefits

6.3 Incapacity benefits are income-replacement benefits available to people who are unable to work as a result of sickness or disability. Currently, incapacity benefits include employment and support allowance (ESA) – the replacement for incapacity benefit² – plus the incapacity element of income support and severe disablement allowance. ESA was introduced in 2008-09 for new claims alongside a staged migration of existing cases from incapacity benefit, income support and severe disablement allowance. By 2013-14, almost 80 per cent of the total incapacity benefits caseload was made up of ESA claimants.

6.4 All spending on incapacity benefits will be subject to the welfare cap from 2015-16. Spending on incapacity benefits in 2013-14 was estimated at £13.4 billion, some 6.4 per cent of total welfare spending and 11.5 per cent of spending subject to the welfare cap.

¹ DWP (2014a).

² Incapacity benefit was itself a replacement for invalidity benefit and sickness benefit.

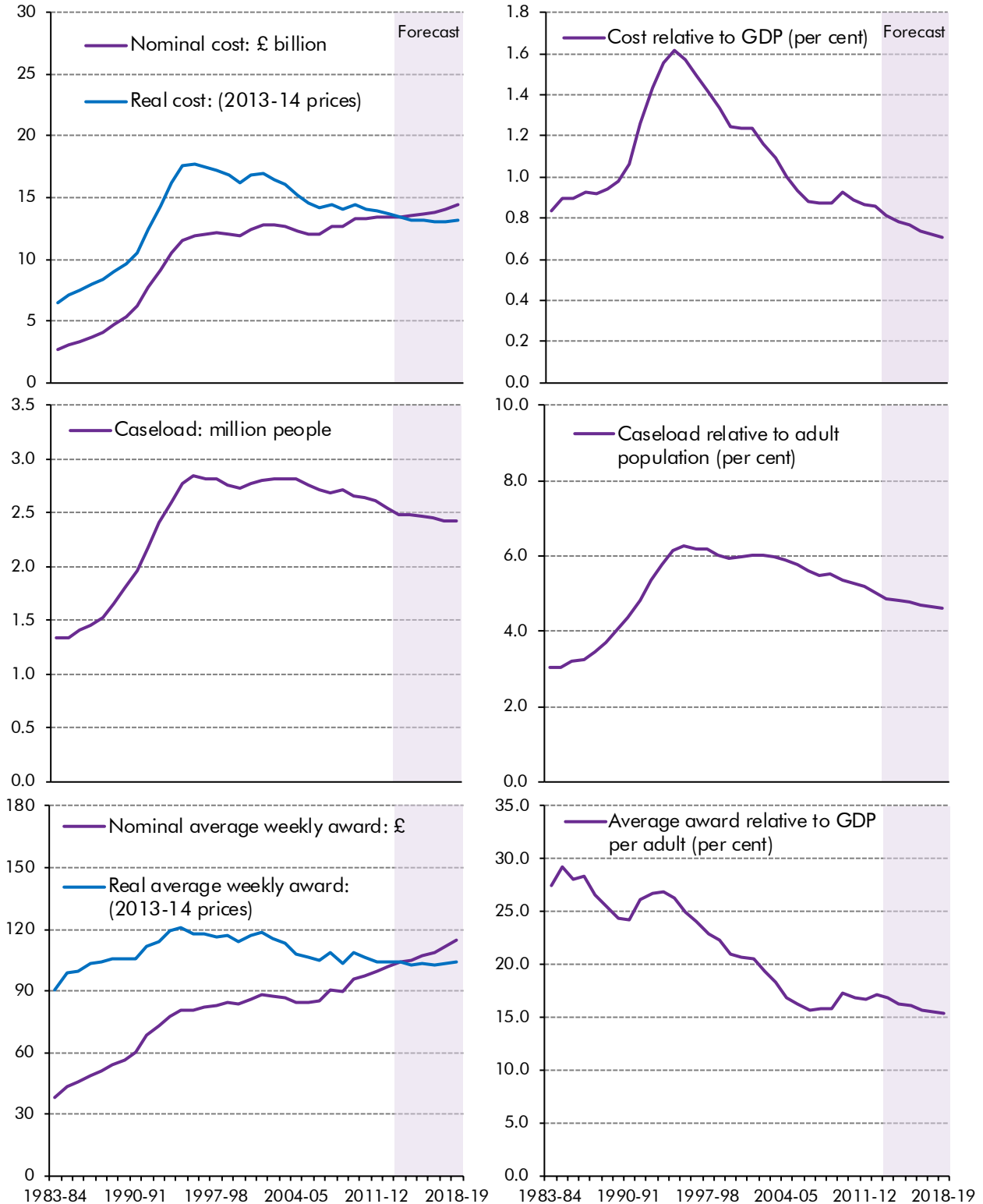
Trends in spending on incapacity benefits

6.5 Figure 6.1 shows trends in spending on incapacity benefits between 1983-84 and 2012-13 and in our latest medium-term forecast. These can be split into four discrete time periods:

- the rise in spending from **the mid-1980s to the mid-1990s**. This was largely the legacy of high unemployment and the effects of industrial restructuring through the 1980s and early 1990s. Higher spending prompted the Government to tighten the conditionality for unemployment benefits and to make them less generous relative to incapacity benefits. This duly encouraged out-of-work people to move to incapacity benefits;
- the fall in spending as a share of GDP **between 1995-96 and 2007-08**. This followed wide-ranging incapacity benefit reforms in 1995 and also reflected the strength of the wider economy;
- the relative stability of spending as a share of GDP during and after the late 2000s recession **from 2007-08 to 2012-13**; and
- our forecast **to 2018-19**, during which spending is expected to fall as a share of GDP.

Figure 6.1: Incapacity benefits: key facts

Current main rates - ESA (2014-15)	£ per week	Total cost (2013-14)	
Work related activity group	101.15	£ billion	13.4
Support group	108.15	Per cent of GDP	0.8
Enhanced disability premium - single	15.55	Per cent of total welfare spending	6.4
Average weekly award	104.70	Per cent of welfare cap	11.5



Source: DWP, ONS, OBR

- 6.6** Table 6.1 breaks down the changes in spending as a share of GDP in each time period into those driven by caseloads and average awards. For each, the changes are further broken down into those related to changes in the economy – proxied by the labour market inactivity rate for caseloads and inflation uprating for average awards – and other factors such as policy changes, or differences in take-up rates and the composition of the caseload.
- 6.7** This decomposition illustrates how the rise in spending through to the mid-1990s was driven by a sharp increase in the caseload relative to the adult population and relative to the number of people inactive in the labour market. Over subsequent periods, the caseload has fallen relative to the adult population, while average awards have typically risen more slowly than GDP-per-adult. The main exception has been the late 2000s recession, as uprating outpaced the sustained weakness of real earnings growth and growth in GDP-per-adult.

Table 6.1: Drivers of changes in incapacity benefit spending

	Per cent of GDP			
	1983-84 to 1995-96	1995-96 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	0.84	1.57	0.87	0.86
Spending at end of period	1.57	0.87	0.86	0.71
Change	0.74	-0.70	-0.01	-0.15
<i>of which:</i>				
Caseload	0.82	-0.18	-0.08	-0.06
Inactivity ¹	-0.07	-0.05	-0.02	-0.01
Other	0.89	-0.13	-0.05	-0.05
Average award	-0.08	-0.52	0.06	-0.08
Fiscal drag ²	-0.25	-0.23	0.07	-0.03
Other	0.17	-0.29	0.00	-0.05

¹ Effect of changes in labour market inactivity

² Effect of differences between inflation and earnings growth

Changes in caseloads

- 6.8** Incapacity benefits caseloads increased significantly between 1983-84 and 1995-96. The caseload rose from 1.3 to 2.8 million over that period, doubling to a peak of 6.3 per cent of the adult population in 1995-96. The caseload then fell gradually to 5.5 per cent of the adult population by 2008-09, and is expected to fall further to 4.6 per cent by 2018-19.
- 6.9** These changes in caseloads were primarily driven by policy decisions. The labour market inactivity rate was relatively stable on average over this period – particularly post-1995. Falls in female inactivity rates were offset by rises in male inactivity rates (see Chapter 3).

Policy changes

- 6.10** The rise in the caseload between 1983-84 and 1995-96 can be explained largely by a sustained rise in the number of mainly older working-age men claiming incapacity benefits. The combined effect of the following factors encouraged flows onto incapacity benefits:

- the early 1980s recession, which led to a large increase in the number of unemployed men, particularly older men. Industrial restructuring continued throughout the decade;
- the increased generosity of incapacity benefits relative to benefits paid to the unemployed;³
- the tightening of the unemployment benefit regime from the mid-1980s (see Chapter 8), which made the incapacity benefit regime comparatively more attractive; and
- the relatively passive administration of the incapacity benefits system, with only a small proportion of claims being subjected to medical tests.

6.11 In response to this marked rise in spending, the Government reformed incapacity benefits in 1995. The main features of the reforms were:

- cutting the generosity of incapacity benefit, with the introduction of three different rates linked to the duration of incapacity;⁴
- reduced generosity of age-related additions, with claimants no longer able to claim invalidity pension if their period of incapacity began after age 45;⁵
- incapacity benefit was made taxable in line with unemployment benefits and pensions;
- the removal of incapacity benefit from anyone over the state pension age;⁶ and
- tighter eligibility requirements, through the introduction of the 'all work test' as a replacement for the 'suitable work test' that applied to invalidity benefit after 28 weeks.

6.12 The immediate impact of the 1995 reforms was to reduce inflows into the long-term incapacity benefit caseload, through tighter testing and the allocation of recipients to more short-term groups. The main group affected were older men, for some of whom incapacity benefits had been used as a stepping stone from work to retirement.⁷ This is illustrated in Chart 6.1, which shows age-specific rates of invalidity benefit and incapacity benefit claims. The proportion of 55 to 59 year old men claiming invalidity benefit nearly doubled to 20 per cent between 1985-86 and 1995-96, but it had fallen back to around 12 per cent by 2012-13. By contrast, the proportion of younger men claiming incapacity benefit has remained well above its early 1980s level.

³ Banks et al. (2011).

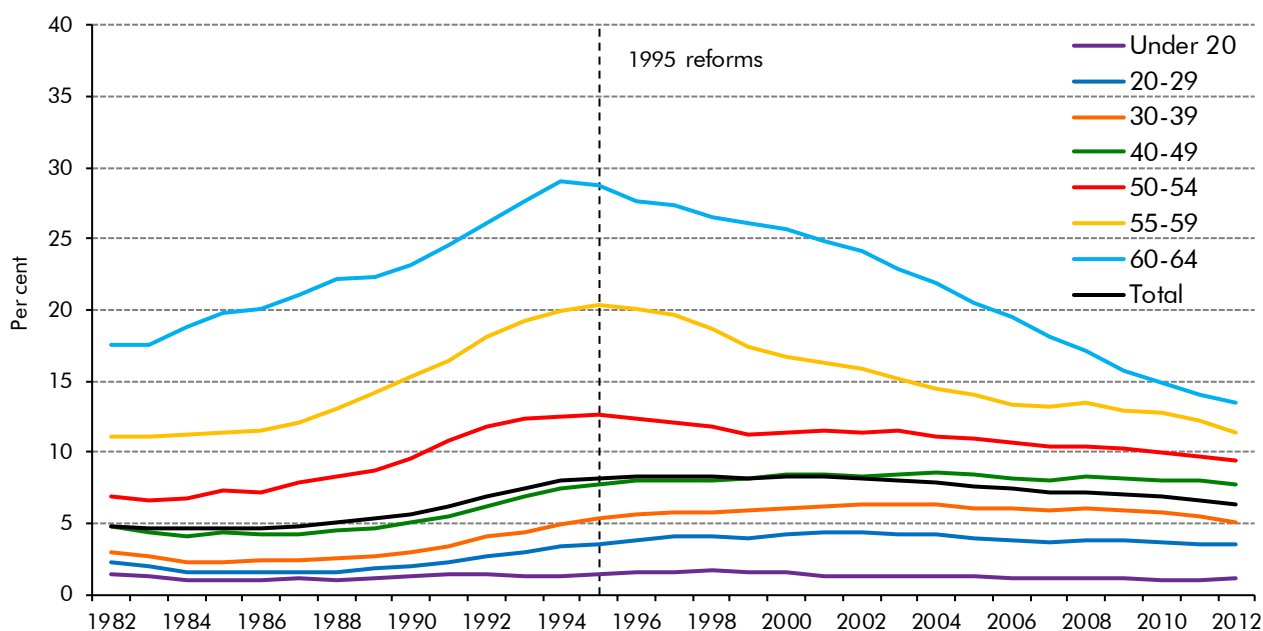
⁴ The rates were (i) a short-term lower rate for incapacity benefit replacing sickness benefit for people not eligible for statutory sick pay; (ii) a short-term higher rate payable from week 29 to week 52, which was less generous than the invalidity benefit rate; and (iii) long-term incapacity benefit rate that was as generous as invalidity benefit and only payable from 52 weeks onwards.

⁵ Prior to the reforms, claimants were eligible for age additions payments to their invalidity pension if their period of incapacity began before age 59.

⁶ Although people receiving short-term incapacity benefit could continue to do so for the full 52 weeks.

⁷ Banks et al. (2011).

Chart 6.1: Proportion of men claiming invalidity and incapacity benefit by age group



Source: DWP

- 6.13 The gradual fall in the caseload from 1995-96 to 2008-09 also reflects further changes subsequent to the 1995 reforms,⁸ but the slow pace of the decline underlines the difficulty in moving people off incapacity benefits.

Compositional effects

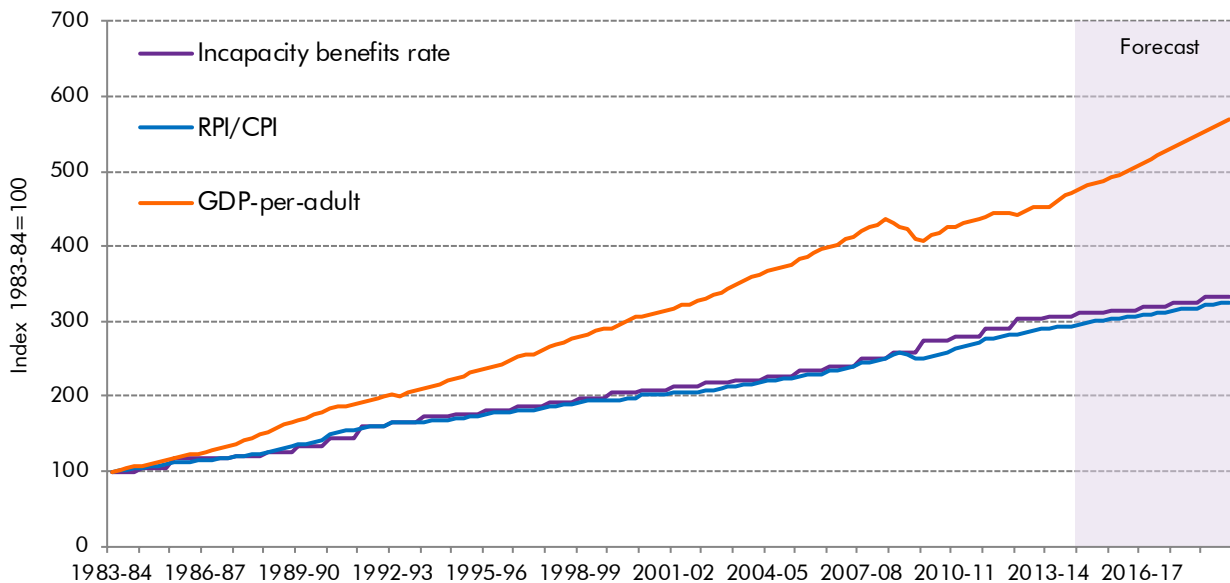
- 6.14 The pattern of incapacity benefits receipt has been different for men and women, with men more likely to receive contributory benefits (such as incapacity benefit) and women more likely to claim non-contributory benefits (such as severe disablement allowance). These gender differences used to reflect the fact that fewer women met the contribution conditions required to receive incapacity benefit. This pattern has changed over time as more women participate in the labour market for longer (see Chapter 3).

Changes in average awards

- 6.15 For much of the period between 1983-84 and 2013-14, average awards for incapacity benefits have risen more slowly than GDP-per-adult (Chart 6.2). In part this reflects uprating in line with different measures of inflation that have on average been lower than growth in GDP-per-adult. The rise in average awards relative to GDP-per-adult in the late 2000s also reflects very weak nominal GDP growth. Compositional effects (such as the changing proportion of older men on incapacity benefits) and policy effects (such as the payment of age additions) will also have affected the average award.

⁸ In 2001, the Government increased the contribution requirement to qualify for incapacity benefit and started to means-test claimants with regard to pension income. (Banks *et al*, 2011)

Chart 6.2: Relative generosity of incapacity benefits



Source: DWP, ONS, OBR

Note: The incapacity benefits rate represents the invalidity personal benefit rate between 1983-84 and 1995-96 and the standard long term incapacity benefit rate from 1996-97 onwards.

Incapacity benefits spending in the medium-term forecast

Spending, caseloads and average awards

6.16 In our latest medium-term forecast, spending on incapacity benefits is forecast to rise from £13.4 billion in 2013-14 to £14.5 billion in 2018-19. GDP is forecast to grow faster than that in cash terms, so spending is expected to fall from 0.8 per cent to 0.7 per cent of GDP over that period. This is driven by both caseloads and average awards. The reassessment of existing ESA claims and scrutiny of new claims are expected to reduce the overall incapacity benefits caseload. These are the main drivers of the lower caseload. Uprating of most incapacity benefits by 1 per cent up to 2015-16, and by CPI thereafter, also plays a part.

Table 6.2: Incapacity benefits spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	13.5	13.4	13.5	13.7	13.8	14.1	14.5
Caseload (million)	2.5	2.5	2.5	2.5	2.4	2.4	2.4
Average annual award (£ thousand)	5.3	5.4	5.4	5.6	5.7	5.8	6.0
Forecast in the context of the welfare cap							
Per cent of total welfare spending	6.3	6.4	6.3	6.3	6.2	6.1	6.1
Per cent of welfare cap spending	11.6	11.5	11.5	11.5	11.3	11.3	11.4
Forecast relative to the economy							
Spending (% of GDP)	0.9	0.8	0.8	0.8	0.7	0.7	0.7
Caseload (% of adults)	5.0	4.9	4.8	4.8	4.7	4.6	4.6
Average award (% of GDP-per-adult)	17.1	16.8	16.3	16.1	15.7	15.5	15.3

Key risks to the forecast

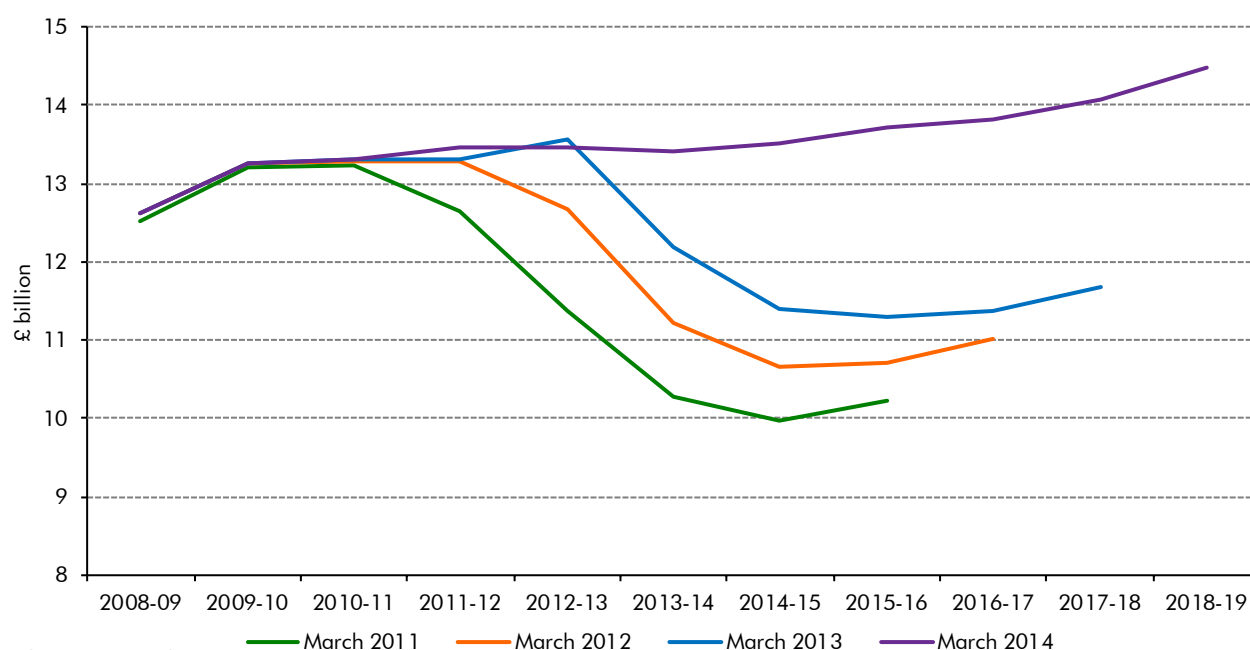
6.17 Our forecasts for incapacity benefits have, on average, underestimated spending. In the three comparable Budget forecasts we made for spending in 2012-13, the average forecast error was a £0.9 billion or 7.9 per cent underestimate.⁹ The main sources of higher than expected spending to date have been:

- slow rates of claim processing, reducing the number of exits;
- more cases going into the support group of ESA;
- more cases being entitled to income-related rather than contributory ESA;
- more successful appeals; and
- fewer exits from ESA due to time-limiting.

6.18 As Chart 6.3 shows, we have significantly altered the shape of our incapacity benefits forecast since Budget 2013, as we expect ESA to produce a much smaller reduction in spending on incapacity benefits. In our December 2013 forecast, we revised ESA spending up by £2.1 billion at the forecast horizon (2017-18) due to evidence from work capability assessments that the proportion of those assessed moving into the support group would be higher than previously assumed and the proportion declared fit for work lower. In addition, we judged that spending would remain higher in subsequent years, because of delays to the work capability assessment programme. We reduced the assumed number of work capability assessments to reflect the lower volumes then passing through the system and the reduced prospects for clearing the backlog of assessments that had built up.

⁹ The June 2010 budget forecast for total incapacity benefits was not on the same basis as the subsequent forecasts as the 'incapacity element' of income support (part of total incapacity benefits spending) is not split out from income support spending in that forecast.

Chart 6.3: Successive forecasts and outturns for incapacity benefits



- 6.19 The substantial risks and uncertainties associated with this forecast cover the same factors that have already caused us to increase our forecasts. For each factor, we need to judge the extent to which current issues are temporary or will persist.
- 6.20 The timing of the reassessment of the stock of ESA claims – which has fallen significantly behind original plans – is a major area of uncertainty in our forecast, as is the resulting composition of the caseload after assessments have taken place. This is subject to even greater uncertainty while the Department for Work and Pensions finds a delivery partner to replace ATOS Healthcare. Even when the new contractual arrangements have been put in place, uncertainty will continue until the assessment backlog has been cleared and the process reaches a steady state, providing firmer evidence on which to base our forecasts.
- 6.21 The rates at which claimants flow onto each group of ESA are another key uncertainty. Claimants applying for ESA initially go into the assessment group, during which time they receive a basic rate of ESA and must undergo a work capability assessment. There are three possible outcomes from this assessment. An individual can be:
- found to be fit for work, in which case they will cease to be eligible for ESA;
 - judged to have limited capability for work, in which case they are placed in the work related activity group. This group is able to claim up to £101.15 a week – for a period of up to one year on contributory ESA, but with no time limit on income-based ESA. Those in the work related activity group must attend regular interviews with an advisor, with failure to attend triggering a sanction process; or

- judged to have limited capability for work related activity, in which case they are placed in the support group. This group is able to claim up to £108.15 a week with no time limit on contributory ESA and £123.70 without time limit on income-based ESA.

6.22 This process is subject to a number of reviews, appeals and reassessments, each potentially resulting in extensions in eligibility. We have to make assumptions about these to forecast ESA spending. On the basis of the assumptions we made in our latest forecast, the support group caseload is expected to rise from 41 per cent of the total in 2013-14 to 52 per cent by 2018-19. This increase is offset by a lower proportion of assessment group cases, as the assessment backlog is assumed to clear and processing times to speed up. Outturns continue to challenge even these revised assumptions.

6.23 The introduction of ESA – and our ability to forecast it – was also complicated by the decision at the Spending Review 2010 to limit receipt of contributory ESA for those in the work related activity group to one year. This was assumed to lead to a fall in eligibility for a group for whom limited evidence was available. It also increased the sensitivity of the forecast to our assumptions about the outcomes of work capability assessments.

6.24 Our forecast assumes that ESA claimants found fit for work move off ESA, reducing welfare spending overall. But there may be some recycling of those found fit for work into jobseeker's allowance and then back onto ESA. One consequence of the design of ESA is that more people move around the benefit system. Moreover, the backlog of applications encourages claimants previously not found eligible for ESA simply to reapply.

6.25 The rising state pension age increases the number of older working-age people, for whom the probability of illness is higher than for younger people. This should generate greater inflows onto ESA, but the flow could be larger or smaller than we have assumed.

6.26 A recent parliamentary review recommended a redesign of ESA processes.¹⁰ There would be risks associated with any further changes to the system. Reform could mitigate some of the risks described here, but past experience recommends caution when assuming any gains.

Long-term projection of incapacity benefits spending

6.27 Our 2014 *Fiscal sustainability report* contained long-term projections for incapacity benefits spending to 2063-64. They show spending rising as a per cent of GDP beyond our medium-term forecast.

6.28 Our long-term projections largely reflect the impact of demographic changes on caseloads, with the age-specific probability of claiming held constant. We assume that awards rise in line with earnings rather than prices. The ageing of the population is expected to push spending on incapacity benefits higher as a share of GDP, because older people have a greater probability of claiming. But spending on incapacity benefits is nonetheless expected

¹⁰ House of Commons Work and Pensions Committee (2014).

to be relatively stable as a per cent of total welfare spending, as demographics exert stronger upward pressure on state pension costs.

- 6.29 Assuming no policy changes, the key sensitivities for spending on incapacity benefits would be to changes in demographic trends, age-specific probabilities of eligibility and the rate at which awards are uprated. If awards are uprated by less than earnings growth, other things equal, spending would be expected to fall as a share of GDP.

Table 6.3: Incapacity benefits long-term spending projection

	Forecast		Projection				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP ¹	0.7	0.7	0.8	0.8	0.8	0.8	0.9
Per cent of welfare spending ¹	5.7	6.5	6.4	6.1	6.1	6.1	6.1

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis, consistent with our 2014 *Fiscal sustainability report* projections.

¹ Incapacity benefits covers employment and support allowance and severe disablement allowance.

Disability benefits

- 6.30 For the purposes of this report, disability benefits are those that provide help towards the additional costs incurred as a result of disability, rather than replacing income. They currently consist of disability living allowance (DLA), personal independence payment (PIP) and attendance allowance. Mobility allowance was an earlier equivalent. PIP is being rolled out gradually over the next few years, replacing DLA for working-age claimants. Disability benefits are non means-tested and are made up of two components: care/daily living and mobility. There is some interaction between these benefits. For example, a person claiming DLA as a pensioner cannot claim attendance allowance.¹¹
- 6.31 In the sections that follow, DLA and its successor PIP are discussed separately from attendance allowance, with the analysis focusing on the period from 1992-93 when DLA was introduced.

Disability living allowance and personal independence payment

- 6.32 Spending on DLA and PIP will be subject to the welfare cap from 2015-16. In 2013-14, total spending on DLA/PIP was estimated at £13.9 billion, or 6.6 per cent of total welfare spending and 11.9 per cent of spending that will be subject to the welfare cap.
- 6.33 DLA is a benefit for disabled people who have personal care or mobility needs. It is designed to contribute towards the additional costs faced by people with disabilities. It was introduced in 1992, incorporating mobility allowance and attendance allowance payments for children and working-age claimants. PIP was introduced in April 2013 and is gradually being rolled out over the next few years, replacing DLA for working-age claimants. Children

¹¹ Age UK (2011).

and existing pensioner claimants will remain on DLA. Reassessment of claims as they are migrated from DLA to PIP is expected to reduce the number of people eligible.¹²

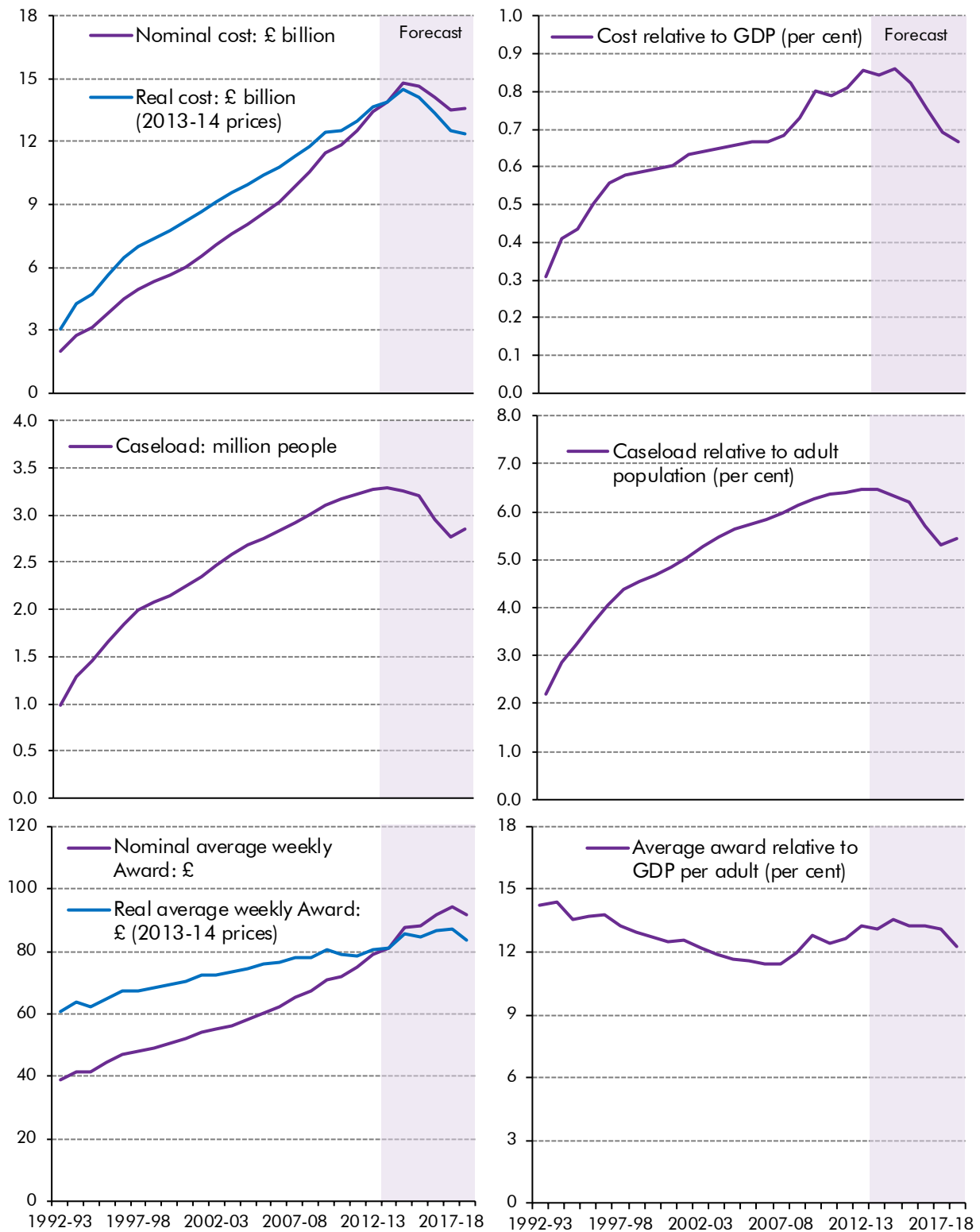
Trends in spending on DLA and PIP

6.34 Figure 6.2 shows that spending on DLA increased from 0.3 per cent of GDP in 1992-93 to 0.9 per cent of GDP by 2012-13, predominantly driven by caseload growth. Spending on DLA and PIP combined is forecast to fall to 0.7 per cent of GDP by 2018-19, as reassessments associated with the introduction of PIP are assumed to reverse the past upward trend in the proportion of adults claiming DLA.

¹² Eligible DLA/PIP claimants can receive the mobility and care components at the same time.

Figure 6.2: DLA and PIP: key facts

Current main rates (2014-15)	£ per week	Total cost (2013-14)	
		£ billion	13.9
DLA/PIP mobility highest rate	56.75	Per cent of GDP	0.8
DLA care middle/PIP daily living standard rate	54.45	Per cent of total welfare spending	6.6
Average weekly award	87.49	Per cent of welfare cap	11.9



Source: DWP, ONS, OBR

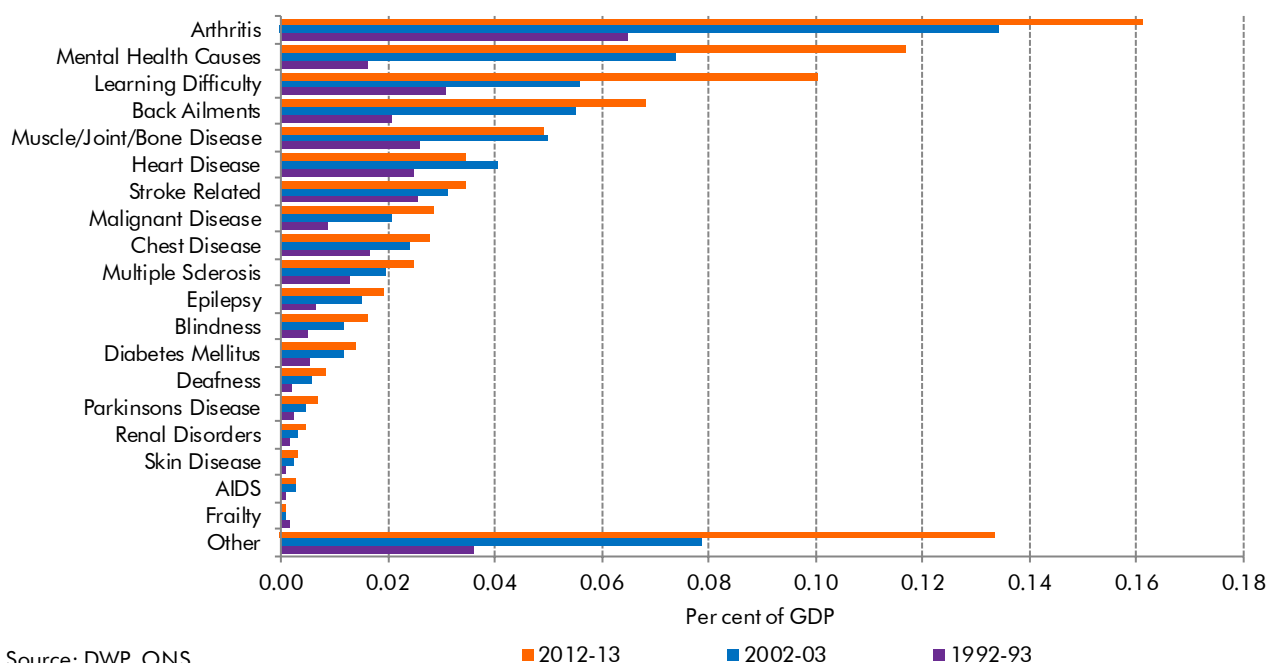
6.35 Table 6.4 shows that the working-age caseload has been the main source of changes in the overall caseload relative to the adult population.

Table 6.4: Drivers of changes in DLA/PIP spending

	Per cent of GDP			
	1992-93 to 1997-98	1997-98 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	0.31	0.58	0.68	0.86
Spending at end of period	0.58	0.68	0.86	0.67
Change	0.27	0.10	0.17	-0.19
of which:				
Caseload	0.29	0.19	0.06	-0.13
Children	0.03	0.02	0.01	0.00
Working age	0.19	0.08	0.03	-0.08
Pensioners	0.07	0.09	0.02	-0.05
Average awards	-0.02	-0.09	0.11	-0.06

6.36 While total spending on DLA has more than doubled since its introduction, there have been even larger increases for spending on some disabling conditions. By far the largest has been for spending on mental health conditions, which has increased six-fold from 0.02 per cent of GDP in 1992-93 to 0.12 per cent in 2012-13. This has taken it from 5 to 14 per cent of total DLA spending. Caseload growth among children and younger working-age people largely reflects the increase in claims among those with mental health problems and learning difficulties (Chart 6.4).¹³

Chart 6.4: DLA spending by main disabling condition



¹³ In 2008, there was a change in the recording of different disabling conditions. For instance, elements that were previously classified under 'mental health causes' were moved to be classified under 'learning difficulties' and 'others' (for example, obesity was transferred from 'mental health causes' to 'other').

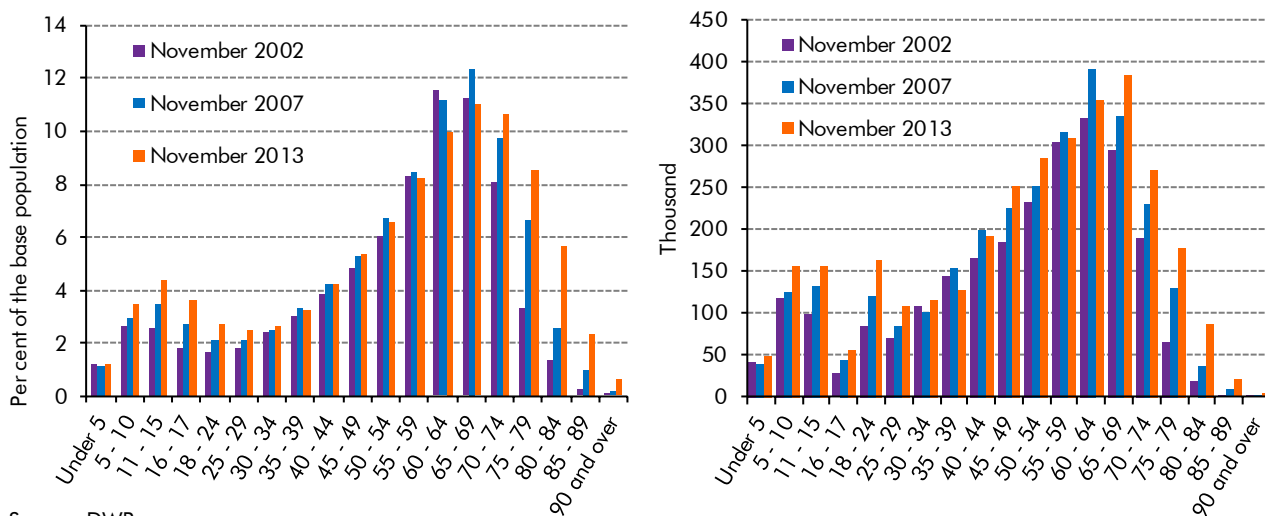
Changes in caseloads

- 6.37 As noted above, increased spending on DLA has mainly been driven by caseload growth. This was due to increased eligibility and take-up, alongside operational changes – such as substituting medical assessment for mainly self-assessment. The same factors driving the rise in the incapacity benefits caseload through to the mid-1990s will have also affected the DLA caseload, given the interaction between these benefits. There is also a maturation effect on DLA caseloads. A claimant must claim DLA before the age of 65, which means that there were no claimants aged 65 or over when DLA was introduced in 1992.¹⁴ But a claimant can continue to receive DLA as they move from working age to pension age, so a high proportion of the caseload will stay on DLA until they die. This has meant that the maximum age of claimants has been increasing each year, and that a growing proportion of pensioners receive DLA. This will continue until such time as inflows and outflows balance.
- 6.38 The introduction of DLA, which followed a major review of social security in the mid-1980s, introduced two lower rates of DLA and increased the number of people eligible to receive it. Within the overall total, there was also considerable growth in the numbers receiving the middle and higher rates compared to the predecessor benefits. This was due in part to new claims procedures (which eased the burden of proof through self-assessment of qualifying disability) and in part to increased take-up from 1992-93 onwards.¹⁵
- 6.39 From 1997-98, caseloads increased at a slower rate, because of a reduction in the number of new awards. This reflected the 1996 ‘safeguarding project’, which reversed the move to self-assessment by requiring additional corroborative evidence for claims for the higher mobility rate. Reduced inflows to incapacity benefits since the mid-1990s are also likely to have resulted in reduced DLA inflows.
- 6.40 Chart 6.5 shows that growth in the caseload since 2002 has been concentrated among the young and the old. The growing number of children and younger working-age people claiming reflects more claims by people with mental health and learning difficulties, while growth in the pensioner population reflects the maturation effect. Furthermore the large disability benefit inflows in the 1980s are now passing through to the pensioner population.

¹⁴ With a few exceptions (some people who had received mobility allowance before 1992).

¹⁵ DSS (2002).

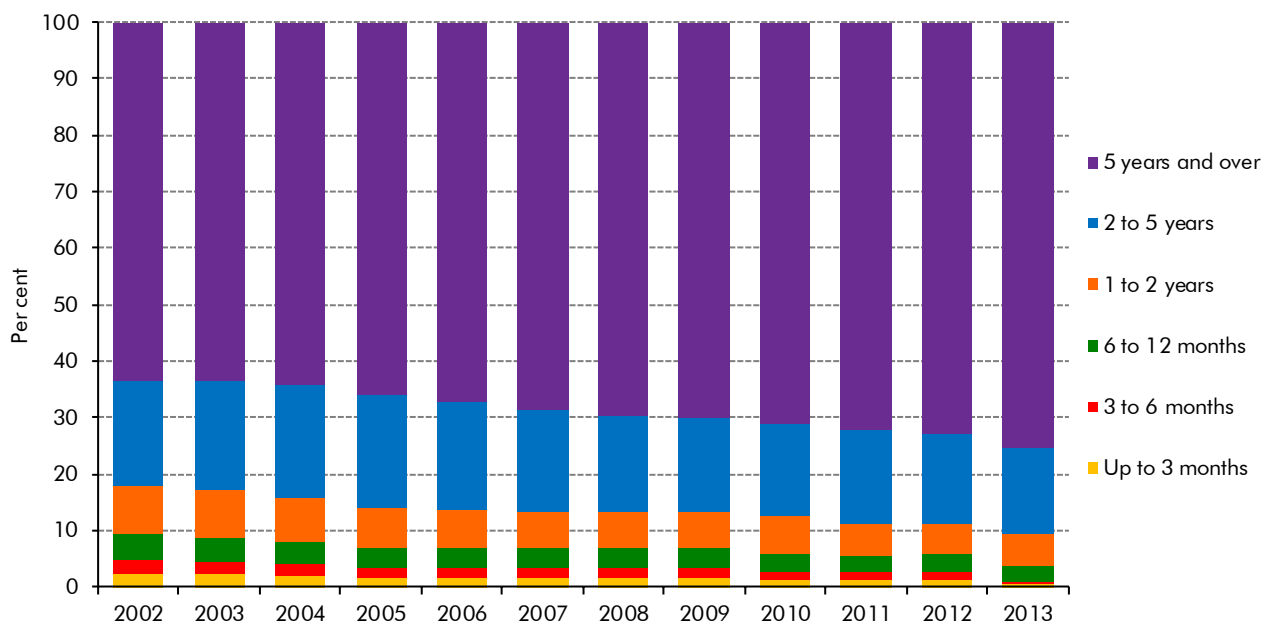
Chart 6.5: DLA caseloads by age group



Source: DWP

6.41 The low exit rates from DLA are partly explained by the fact that the majority of claimants – around two thirds – are on indefinite awards, so that they only exit when the claimant actively reports a change in circumstances or dies. Chart 6.6 shows that currently around three quarters of claimants have been claiming for more than five years.

Chart 6.6: DLA claimants by duration of claim



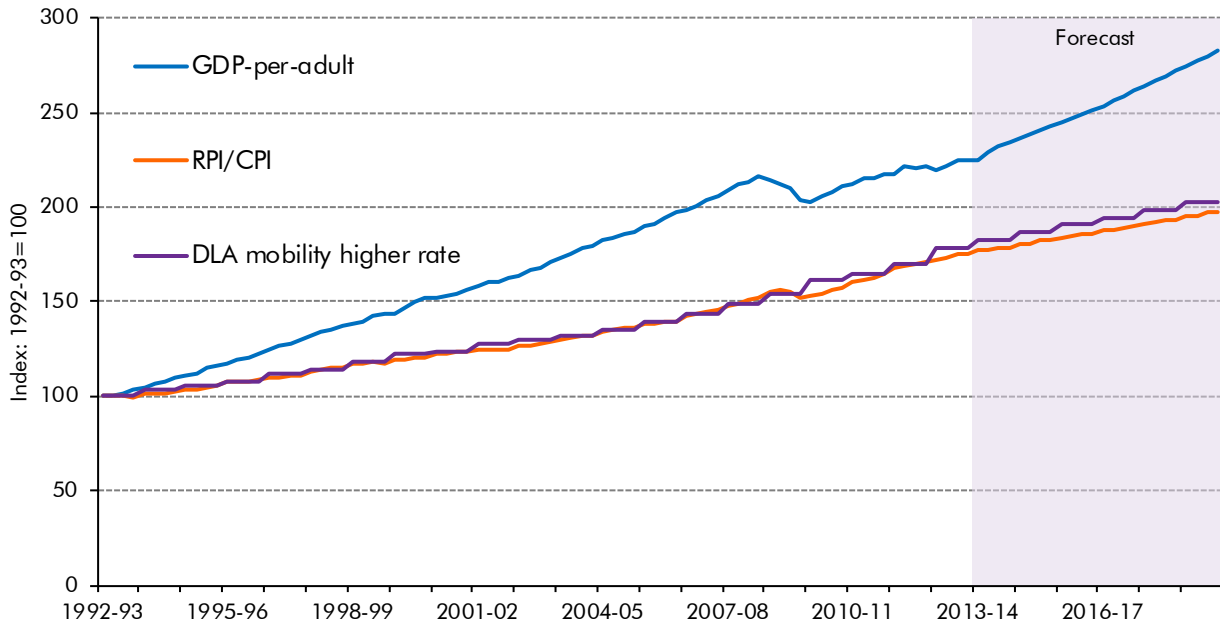
Source: DWP

Changes in average awards

6.42 For most of the period covered by this report, DLA average awards have risen more slowly than GDP-per-adult, as shown for one of the main rates in Chart 6.7. This reflects uprating in line with different measures of inflation, which have on average been lower than growth in GDP-per-adult, and compositional changes within the caseload. Between 1983-84 and

2010-11, DLA was linked to RPI inflation. Since 2011-12 it has been linked to CPI inflation, which is typically lower than RPI inflation. Average awards increased relative to GDP-per-adult during the late 2000s recession due to very weak nominal GDP growth.

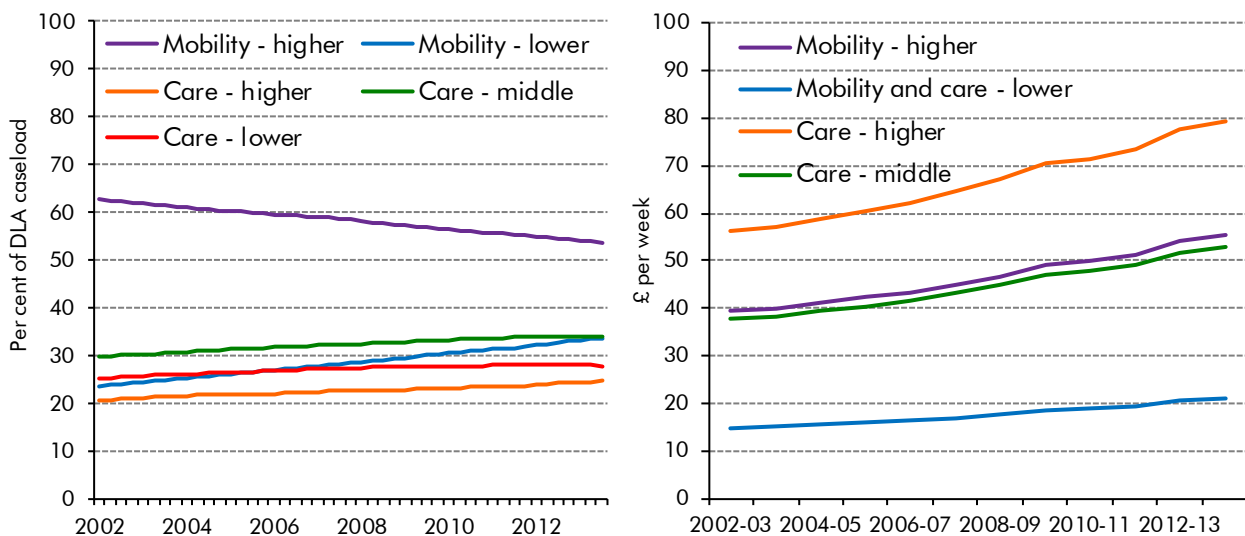
Chart 6.7: Relative generosity of DLA



Source: DWP, IFS, ONS, OBR

6.43 Compositional changes within the DLA caseload affecting average awards include a fall in the proportion of DLA mobility higher rate claimants and an increase in the proportion of lower rate claimants (Chart 6.8). This has reduced growth in average awards.

Chart 6.8: DLA caseload by component and rate



Source: DWP

DLA and PIP spending in the medium-term forecast

Forecasting disability benefits

- 6.44 The key assumptions underpinning the DLA/PIP forecast are similar to those needed to forecast ESA. We need to make assumptions about flows onto the benefit, the composition of claims once assessment has been made, and the duration of claims. Again, like ESA, the pace of dealing with new claims and assessments of existing cases, alongside the success rates of those making claims, are critical to producing a central forecast.
- 6.45 The disability test for PIP involves an assessment of the ability of an individual to ‘participate fully in society’ rather than the severity of impairment. This means that, unlike in DLA, there will be no medical conditions that lead to automatic entitlement to PIP. The PIP process will also involve continuing assessment of claimants’ needs. The assumption is that it will be awarded for a fixed term of between one and ten years. Claimants will be reassessed automatically at the end of their term, as well as during that term if circumstances change.
- 6.46 In our latest forecast, a key judgement was that success rates for new claims start in line with the latest outturns (around 55 per cent) and fall to around 35 per cent within three years. That assumption rests on the backlog of assessments being cleared, medical assessors improving the quality of their reports, and the assessment criteria being fine-tuned by DWP. For reassessments of existing claims we assume a higher success rate of 74 per cent – consistent with outturns – and that the success rate will not fall over the forecast period.

Spending, caseloads and average awards

- 6.47 In our latest medium-term forecast, spending on DLA/PIP is forecast to fall from a peak of £14.8 billion (0.9 per cent of GDP) in 2014-15 to £13.6 billion (0.7 per cent of GDP) in 2018-19. This is largely driven by the reassessments as cases migrate from DLA to PIP.
- 6.48 While the overall caseload for DLA and PIP combined is forecast to fall by 13 per cent between 2013-14 and 2018-19, the caseload for children on DLA is forecast to rise by 7 per cent. Working-age caseloads – affected by the PIP migration – fall by 16 per cent.

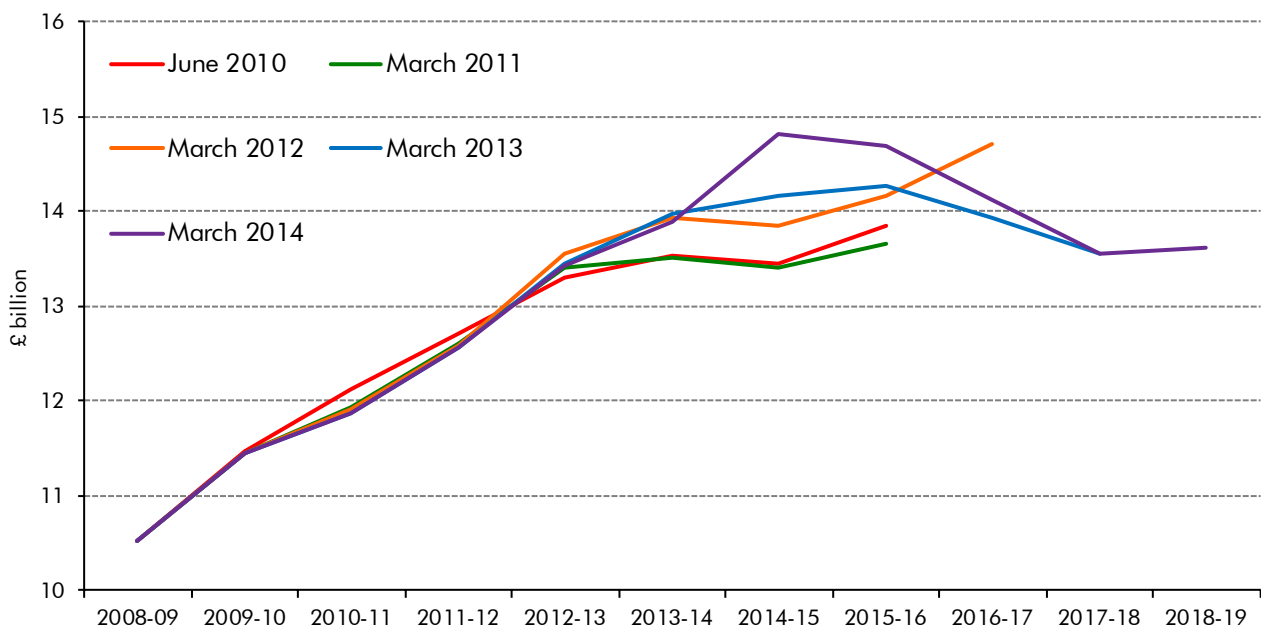
Table 6.5: DLA/PIP spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	13.4	13.9	14.8	14.7	14.1	13.5	13.6
Caseload (million)	3.28	3.29	3.26	3.21	2.96	2.77	2.85
Average annual award (£ thousand)	4.1	4.2	4.5	4.6	4.8	4.9	4.8
Forecast in the context of the welfare cap							
Per cent of total welfare spending	6.3	6.6	6.9	6.7	6.3	5.9	5.8
Per cent of the welfare cap	11.5	11.9	12.6	12.3	11.6	10.9	10.7
Forecast relative to the economy							
Spending (% of GDP)	0.86	0.84	0.86	0.82	0.75	0.69	0.67
Caseload (% of adults)	6.5	6.4	6.3	6.2	5.7	5.3	5.4
Average award (% of GDP-per-adult)	13.2	13.1	13.6	13.2	13.3	13.1	12.3

Key risks to the forecast

- 6.49 Our forecasts for disability benefits have not underestimated spending by the same substantial margin as our forecasts for incapacity benefits. As Chart 6.9 shows, outturn spending in 2012-13 – as shown by the March 2014 forecast line – was very close to all of our previous forecasts, with an average error of zero. But the migration of claimants from DLA to PIP involves challenges very similar to those that have already prompted us to raise our forecasts for incapacity benefits.

Chart 6.9: Successive forecasts and outturns for DLA/PIP



Source: DWP

- 6.50 When the Government announced in the June 2010 Budget that medical assessments would be used to “ensure payments are only made for as long as a claimant needs them”, this was estimated to save £360 million in 2013-14 and around £1 billion in 2014-15. We now expect any savings to come later and have revised up our spending forecasts from 2013-14 onwards. The process of reassessing claims during the migration of PIP is now assumed to deliver a 25 per cent reduction in the caseload, reducing spending by £2.8 billion a year by 2017-18. This saving is sensitive to the speed with which the caseload is migrated to PIP and the outcomes of reassessments and any subsequent appeals.
- 6.51 With comparatively little outturn data and a delayed rollout, it is not yet clear whether we have taken on board the lessons from IB/ESA sufficiently to be confident in the assumed savings from the DLA/PIP transition. In our March 2014 EFO, we adjusted the forecast upward to reflect the emerging outturn data on the pace of the PIP rollout, but it is too early to tell whether that was sufficient. We will return to this assumption in our December 2014 EFO.
- 6.52 The medium-term assumption of 35 per cent success rates for new claims is based on emerging evidence that we judged to be central at the time of our March 2014 EFO.

Success rates appear to be falling in line with our assumptions for the first two years of the forecast, but there is little evidence available to inform the further reduction in success rates assumed thereafter. If success rates did not continue to fall as expected, our spending forecasts would be affected accordingly. Assumptions on the rate of appeals – and the proportion that are successful – pose further risks to the PIP forecast.

- 6.53 As with incapacity benefits, there are also demographic uncertainties relating to increasing numbers of older working-age people who are most at risk of developing a long-term illness or disability. Similarly, the number of children that are flowing onto DLA for reasons of mental health or learning difficulties also represents a risk to the forecast.
- 6.54 As with our incapacity benefits forecast, we need to judge the extent to which the challenges in delivery are likely to be temporary or persistent. As the rollout to PIP is at a much earlier stage than that for ESA, this judgement is subject to even greater uncertainty.

Attendance allowance

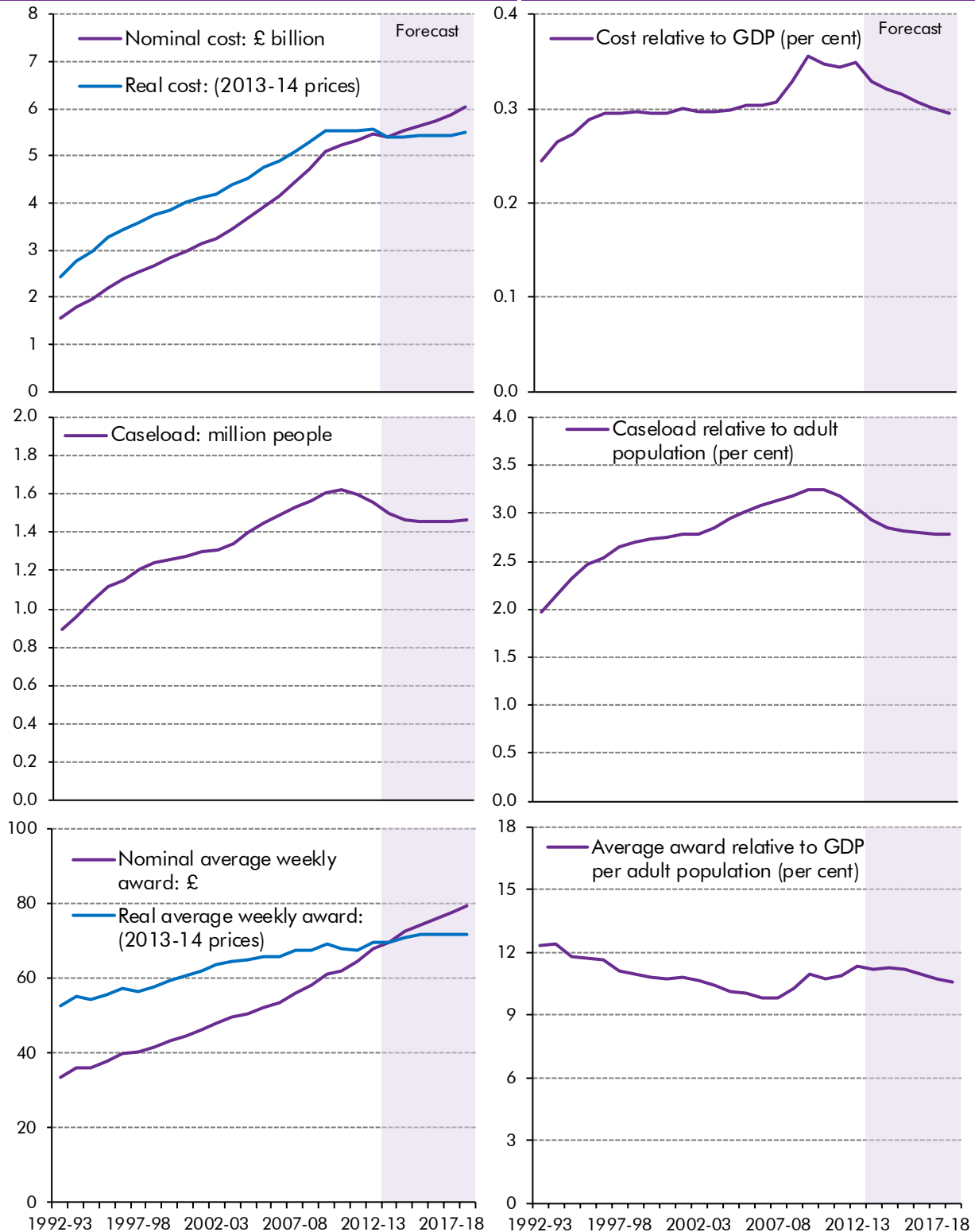
- 6.55 Attendance allowance is paid to people aged 65 or over who are ill or disabled and who need someone to help with their personal care. It is designed to help with the additional costs faced by people with disabilities. It is paid at two rates, equivalent to the middle and higher rates of DLA the care component. It has similar entitlement conditions to DLA.
- 6.56 Attendance allowance will be subject to the welfare cap from 2015-16. In 2013-14, spending on attendance allowance was estimated at £5.4 billion, around 3 per cent of total welfare spending and 5 per cent of spending that will be subject to the welfare cap.

Trends in spending on attendance allowance

- 6.57 The introduction of DLA in 1992 transferred children and working-age claimants from attendance allowance. But even prior to 1992, spending on attendance allowance was predominantly on pensioners. Spending on attendance allowance has increased from 0.24 per cent of GDP in 1992-93 to 0.35 per cent of GDP in 2012-13 (Figure 6.3). Over the medium-term forecast, it is forecast to fall to 0.30 per cent of GDP.
- 6.58 One of the main factors behind the moderate rise in attendance allowance spending has been average awards rising more slowly than GDP-per-adult, broadly offsetting the gradual increase in caseloads relative to the adult population. In addition, administrative changes since 2008 – such as the introduction of customer case management and increases in the number of fixed-term awards – have contributed to a decline in caseloads relative to the adult population since then.

Figure 6.3: Attendance allowance: key facts

Current main rates (2014-15)		Total cost (2013-14)	
	£ per week	£ billion	
Higher rate	81.30	5.4	Per cent of GDP
Lower rate	54.45	0.3	Per cent of total welfare spending
Average weekly award	72.34	2.6	Per cent of welfare cap
		4.7	



Source: DWP, ONS, OBR

6.59 Table 6.6 decomposes the relatively small changes in attendance allowance spending as a share of GDP into those driven by changes in caseloads and average awards. Most of the changes are not material, with the most noteworthy being the increased caseload from 1992-93 to 2007-08 (which follows the trend in disability benefits more broadly) and the subsequent decline expected over the forecast period. Average awards relative to GDP-per-adult also rose through the late 2000s recession and the subsequent slow recovery.

Table 6.6: Drivers of changes in attendance allowance spending

	Per cent of GDP				
	1992-93 to 1996-97	1996-97 to 2002-03	2002-03 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	0.24	0.30	0.30	0.31	0.35
Spending at end of period	0.30	0.30	0.31	0.35	0.30
Change	0.05	0.00	0.01	0.04	-0.05
of which:					
Caseloads	0.07	0.03	0.04	-0.01	-0.03
of which:					
Demography ¹	0.00	0.00	0.00	0.02	0.03
Increased incidence ²	0.07	0.03	0.03	-0.02	-0.06
Average awards	-0.01	-0.03	-0.02	0.05	-0.02

¹ Changes in the number of pensioners relative to the adult population.

² Changes in the number of claimants relative to the number of pensioners.

Changes in caseloads

6.60 The attendance allowance caseload increased during the early years after the introduction of DLA, perhaps reflecting greater awareness among potential recipients following the 1992 reforms. As there is an overlap between those claiming attendance allowance and pension credit, the take-up campaign associated with the introduction of pension credit in 2003-04 may also have affected take up of attendance allowance.

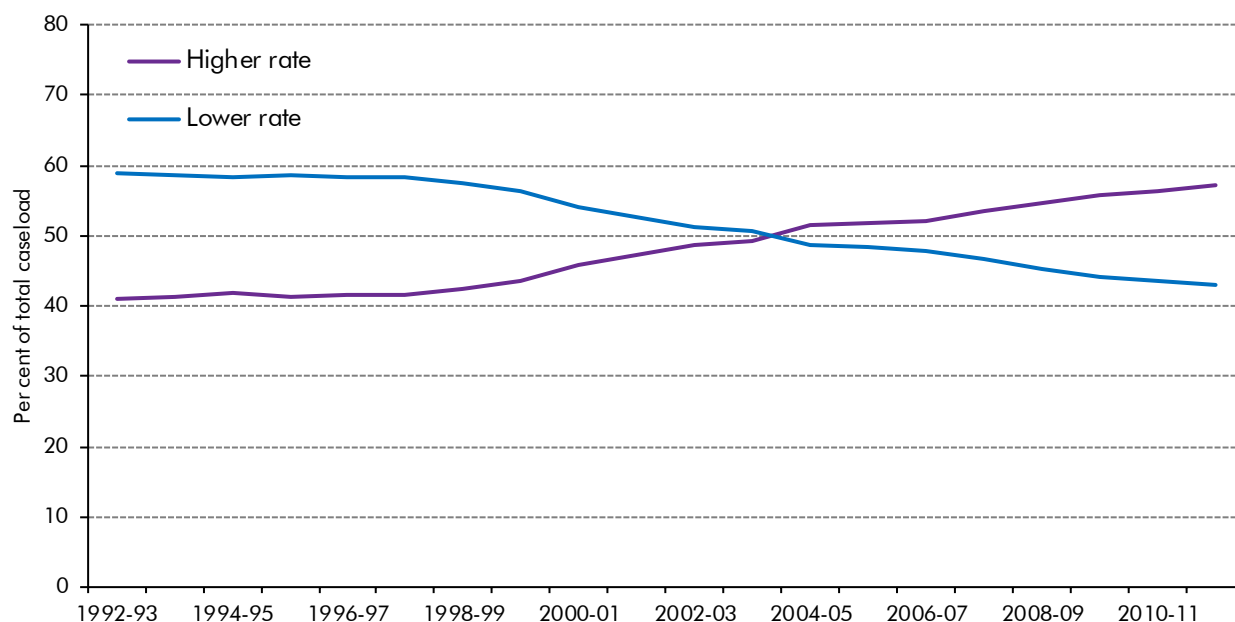
6.61 Since 2009-10, the caseload has fallen for both men and women and across different age groups. Administrative changes have been a key driver, as was a fall in claims in late 2008 coinciding with the end of the pension credit take-up campaign. The introduction of customer case management at roughly the same time introduced a more rigorous application of entitlement criteria, reducing the claim success rate. There have also been more fixed-term awards, and more individuals leaving benefit at time of renewal. This has resulted in reduced new claims and more claimants moving off the benefit.

Changes in average awards

6.62 For most of the period covered in this report, attendance allowance average awards have risen more slowly than GDP-per-adult. This reflects uprating in line with different measures of inflation, which have on average been lower than growth in GDP-per-adult. Between 1983-84 and 2010-11, DLA was linked to RPI inflation. Since 2011-12, it has been linked to CPI inflation, which is typically lower than RPI inflation. Average awards increased relative to GDP-per-adult during the late 2000s recession due to very weak nominal GDP growth.

6.63 There has also been a compositional shift in the caseload, with a higher proportion claiming the higher rate since 2004-05 (Chart 6.10). This has increased the average award.

Chart 6.10: Higher and lower rate attendance allowance caseloads



Source: DWP, IFS

Attendance allowance spending in the medium-term forecast

Spending, caseloads and average awards

6.64 In our latest medium-term forecast, spending on attendance allowance is forecast to rise from £5.4 billion in 2013-14 to £6.0 billion in 2018-19. As GDP is forecast to grow more quickly than that in cash terms, spending falls from 0.35 to 0.30 per cent of GDP. This is partly the result of the reforms to the renewal of claims, which are expected to keep the caseload broadly flat in absolute terms and therefore reduce it relative to the adult population. Up-rating in line with CPI inflation means that average awards are expected to rise less than GDP-per-adult, which also reduces spending as a share of GDP.

Table 6.7: Attendance allowance spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	5.5	5.4	5.5	5.6	5.7	5.9	6.0
Caseload (million)	1.55	1.50	1.47	1.46	1.46	1.46	1.46
Average annual award (£ thousand)	3.5	3.6	3.8	3.9	3.9	4.0	4.1
Forecast in the context of the welfare cap							
Per cent of total welfare spending	2.6	2.6	2.6	2.6	2.6	2.5	2.6
Per cent of the welfare cap	4.7	4.7	4.7	4.7	4.7	4.7	4.8
Forecast relative to the economy							
Spending (% of GDP)	0.35	0.33	0.32	0.32	0.31	0.30	0.30
Caseload (% of adults)	3.1	2.9	2.9	2.8	2.8	2.8	2.8
Average award (% of GDP-per-adult)	11.4	11.2	11.2	11.2	11.0	10.8	10.6

Key risks to the forecast

- 6.65 Take-up of attendance allowance has varied over the past, which suggests that it may remain a risk to the forecast. Spending could also be affected by social care policies being undertaken by other parts of central and local government. In addition, underlying eligibility will be affected by the increasing number of older working-age people, who are most at risk of developing a long-term illness or disability. This effect could be more or less pronounced than implied by our forecast.

Long-term projection of disability benefits spending

- 6.66 Our 2014 *Fiscal sustainability report* contained long-term projections for disability benefits spending to 2063-64. The projections show spending increasing slightly as a share of GDP beyond our medium-term forecast. This largely reflects the ageing of the population. Even though we assume increases in disability-free life expectancy, the looming rise in the very old population lifts spending on disability benefits overall. The proportion of the population aged 85 and over is projected to rise from 2.3 per cent in 2014 to 7.7 per cent in 2064.

Table 6.8: Disability benefits long-term spending projection

	Forecast		Projection				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP ¹	1.2	1.0	1.0	1.1	1.2	1.2	1.3
Per cent of welfare spending ¹	9.8	8.8	8.8	8.7	8.7	8.9	8.9

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis, consistent with our 2014 *Fiscal sustainability report* projections.

¹ Disability benefits covers disability living allowance, personal independence payments and attendance allowance.

Carer's allowance

- 6.67 Carer's allowance is, with some exceptions,¹⁶ a non-means-tested benefit paid to carers looking after chronically sick and disabled people. It is intended to act as an income replacement benefit. Carer's allowance replaced invalid care allowance in 2003-04. To be eligible for carer's allowance, claimants must provide at least 35 hours of unpaid care to a person receiving a qualifying disability benefit.¹⁷
- 6.68 Carer's allowance spending will be subject to the welfare cap. Spending is estimated at £2.1 billion in 2013-14, accounting for less than 1 per cent of total welfare spending and 2 per cent of spending that will be subject to the welfare cap.

Trends in spending on carer's allowance

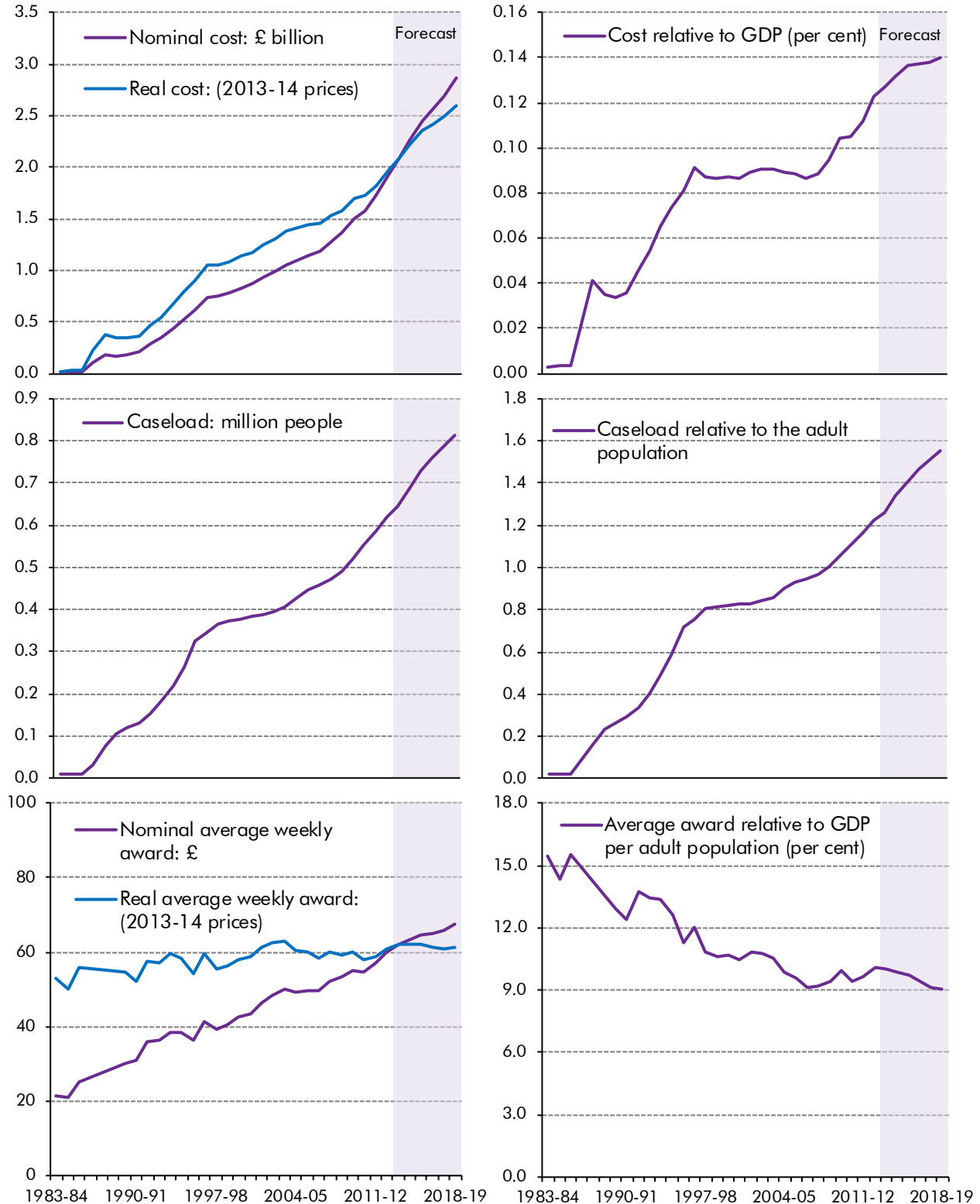
- 6.69 In the early years of invalid care allowance, spending was relatively low, not reaching £100 million a year in cash terms until 1986-87 and not topping 0.1 per cent of GDP until 1986-87. As Figure 6.4 shows, the rise in spending between 1983-84 and 2013-14 and through the forecast period is driven by the caseload rising as a share of the adult population.

¹⁶ Claimants who are in paid work earning more than £102 a week after deductions cannot claim carers allowance.

¹⁷ Eligibility for carer's allowance is based on the person cared for being in receipt of a number of benefits including personal independence payment (PIP) daily living component, disability living allowance (DLA) middle or higher care rate, attendance allowance and the armed forces independence payment.

Figure 6.4: Carer's allowance: key facts

Current main rates (2014-15)		Total cost (2013-14)	
	£ per week	£ billion	2.1
		Per cent of GDP	0.13
Main rate	61.35	Per cent of total welfare spending	1.0
Average weekly award	62.22	Per cent of welfare cap	1.8



Source: DWP, ONS, OBR

Changes in caseloads

- 6.70** As the caseload for carer's allowance is explicitly linked to caring for a person in receipt of certain forms of DLA or attendance allowance, trends in the caseload to some extent reflect trends in those benefits, overlaid by the widening of eligibility for carer's allowance itself.
- 6.71** The carer's allowance caseload was just 0.02 per cent of the adult population in 1983-84, but has since risen to 1.2 per cent in 2012-13. Growth in the caseload in the mid-1980s reflected increased take-up and the extension of eligibility for invalid care allowance to married women in 1986. Growth in the 1990s was linked to qualifying benefits, such as DLA and attendance allowance, and the introduction of the carer premium in income support in the early 1990s, which made the benefit more attractive to claimants.

Changes in average awards

- 6.72** The average award has generally risen more slowly than GDP-per-adult over the past 30 years, as uprating has on average been lower than the growth in GDP-per-adult. The standard rate of carer's allowance has increased by 4 per cent a year on average over the period whereas GDP-per-adult has grown by 5 per cent a year on average.

Carer's allowance spending in the medium-term forecast

Spending, caseloads and average awards

- 6.73** In our latest medium-term forecast, spending on carer's allowance is forecast to rise from £2.1 billion in 2013-14 to £2.8 billion in 2018-19, rising slightly as a share of GDP. This is in part driven by an increase in the caseload related to the rising state pension age, as new carer's allowance claims can only be made by people below the state pension age.

Table 6.9: Carer's allowance spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	1.9	2.1	2.3	2.4	2.6	2.7	2.9
Caseload (million)	0.6	0.6	0.7	0.7	0.8	0.8	0.8
Average annual award (£ thousand)	3.1	3.2	3.3	3.4	3.4	3.4	3.5
Forecast in the context of the welfare cap							
Per cent of total welfare spending	0.9	1.0	1.1	1.1	1.1	1.2	1.2
Per cent of welfare cap spending	1.7	1.8	1.9	2.0	2.1	2.2	2.3
Forecast relative to the economy							
Spending (% of GDP)	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Caseload (% of adults)	1.2	1.3	1.3	1.4	1.5	1.5	1.6
Average award (% of GDP-per-adult)	10.1	10.0	9.8	9.7	9.4	9.1	9.0

Industrial injuries benefit

- 6.74** Benefits for those who suffer industrial accidents have one of the longest histories of any part of the welfare system, with workmen's compensation schemes in existence in the

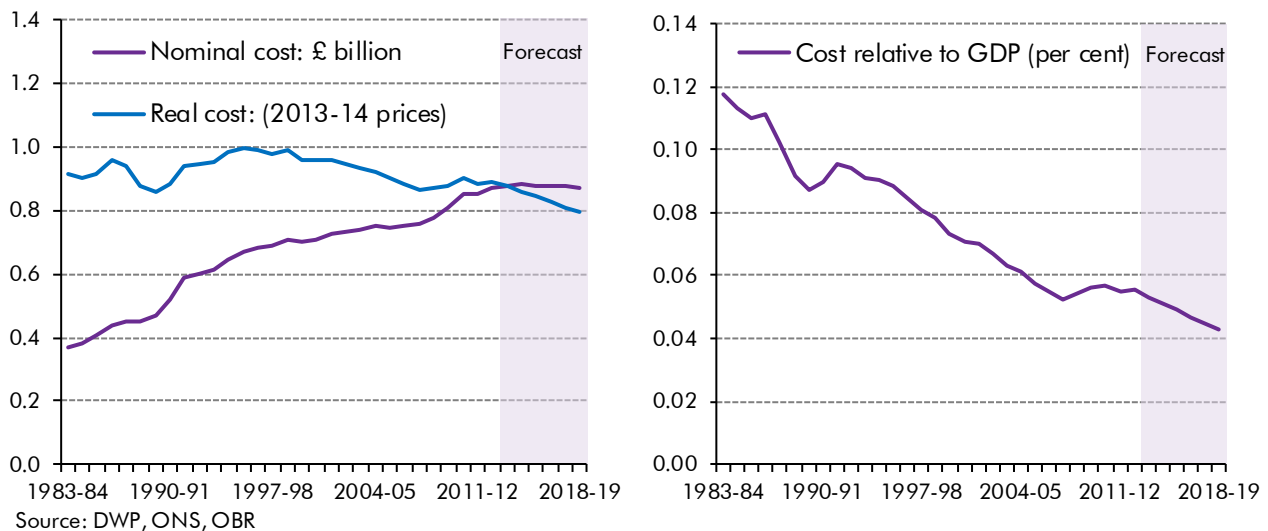
nineteenth century. Today, industrial injuries benefits – the largest of which is the industrial injuries disablement benefit – are payable to individuals who are ill or disabled as a result of an accident or disease caused by work. For industrial injuries disablement benefit, the amount paid is related to the level of disablement as assessed by a medical advisor, with amounts varying significantly from the lowest to the highest possible awards.

- 6.75 In 2013-14, just under £1 billion was spent on industrial injuries benefits, of which around 90 per cent was spent on industrial injuries disablement benefit. All industrial injuries benefits that are part of AME spending are subject to the welfare cap.

Trends in spending on industrial injuries benefit

- 6.76 Chart 6.11 shows the trend in spending on industrial injuries disablement benefit over the past three decades. It has generally fallen as a share of GDP. Between 1983-84 and 2013-14, the spending to GDP ratio fell by a little over half, broadly in line with the fall in the share of jobs in the manufacturing and construction sectors. This trend can also be seen in the available caseload data, with the caseload relatively stable at between 6 and 7 per cent of the number of jobs in the manufacturing and construction sectors, but falling as a share of the adult population. Average awards have fluctuated over the past decade, which will reflect both uprating and the composition of the caseload.

Chart 6.11: Industrial injuries benefit spending



Industrial injuries benefit spending in the medium-term forecast

- 6.77 In our latest medium term forecast, we expect the caseload to continue to fall in absolute terms and relative to the adult population, and the average award to increase more slowly than GDP-per-adult. As a result, spending is forecast to fall as a share of GDP.
- 6.78 The key risks to the forecast relate to the caseload. The extent to which the recovery in employment is concentrated in jobs that are more prone to industrial injuries may be

important.¹⁸ In the case of prescribed diseases, the emergence of new evidence on conditions and links to past employment represent key uncertainties. For the average award, the composition of the caseload is important given the substantial differences in weekly awards at different degrees of assessed disablement.

Independent living fund

- 6.79 The independent living fund provides money to help disabled people live an independent life in the community, rather than in residential care. From 2014-15 onwards the scheme will no longer exist when funding will be transferred to local government DEL. In 2013-14, spending on the independent living fund is estimated to have been £0.3 billion.

Statutory sick pay

- 6.80 Statutory sick pay is a benefit paid by employers for a maximum of 28 weeks to employees who are incapable of work. It is a legal minimum, and many employers will pay more than this amount. Statutory sick pay will be subject to the welfare cap from 2015-16. In 2013-14, spending on statutory sick pay is estimated to have been £51 million.

Motability scheme

- 6.81 The motability scheme was set up as a partnership between government, charities and the private sector. It enables disabled people to use their higher-rate DLA (mobility) allowances or war pensioners' mobility supplement to hire or for hire-purchase facilities on cars, electric wheelchairs and electric scooters. Extra money is available to help finance the adaptation of vehicles to suit particular types of disabilities through the specialised vehicle fund, administered by the charity.
- 6.82 Motability grants will not be subject to the welfare cap. In 2013-14, spending was estimated to have been £17 million, primarily through the specialised vehicles fund.

War pensions and armed forces compensation scheme

- 6.83 In its current form, the main benefits of this type are war pensions, the armed forces compensation scheme, and the armed forces independence payment. From 2005, the war pensions scheme has been replaced by the armed forces compensation scheme for injuries and death suffered as a result of service in the armed forces. Pensions are also available to widows, widowers and dependents of those killed in service.
- 6.84 War pensions are outside the welfare cap. In 2013-14, spending on them was estimated at £0.9 billion.¹⁹

¹⁸ Davies *et al* (2009) find positive and significant effects of the business cycle on the prevalence of major injuries in the manufacturing and construction sectors, suggesting that in the construction sector in particular the prevalence of small firms and chains of subcontractors may explain relatively high and cyclical hazard rates.

¹⁹ Includes both war disablement and war widow(er)'s pensions, but does not include armed forces compensation scheme or armed forces independence payment spending.

7 Spending on families

7.1 Around 23 per cent of welfare spending in 2013-14 (as defined in this report) and 41 per cent of spending that will be subject to the welfare cap from 2015-16 is paid primarily to families with children. This chapter covers the following benefits:¹

- tax credits;
- child benefit;
- statutory maternity pay, maternity allowance and statutory paternity pay;
- tax-free childcare;
- income support, which is now predominantly paid to lone parents and carers, but in the past supported a wider range of recipients; and
- the social fund.

Tax credits

7.2 Tax credits make up a significant proportion of welfare spending as defined in this report and they will be subject to the welfare cap from 2015-16. In 2013-14, total spending (including the negative tax element) was estimated to be £30.1 billion,² accounting for 14.3 per cent of total welfare spending and 25.9 per cent of spending on items that will be subject to the welfare cap. Tax credits are therefore one of the largest items of welfare spending, with a cost broadly similar to income tax relief on registered pension schemes (£34.8 billion in 2012-13)³ or the Ministry of Defence (£34.5 billion in 2013-14).⁴

7.3 Tax credits are a cash benefit paid at the household level. They comprise the working tax credit – payable to families in work (typically defined as working 16 hours or more) – and the child tax credit – payable to families with children. There is a childcare element of working tax credit, which subsidises working families' childcare costs. Tax credit awards are based on family circumstances and tapered with income beyond a relevant threshold, as

¹ The main figures on welfare spending and its drivers used in this report are consistent with data available at the time of our March 2014 *Economic and fiscal outlook (EFO)*. Spending data on the benefits administered by DWP cover Great Britain and are drawn from DWP expenditure tables produced at the time of our March 2014 *EFO*. Spending data on the tax credits and child benefit administered by HMRC are drawn from their equivalent data, covering the UK.

² This is our March 2014 forecast for 2013-14. It includes £180 million of spending on the child additions to income support and jobseeker's allowance paid to families that is yet to be migrated to tax credits.

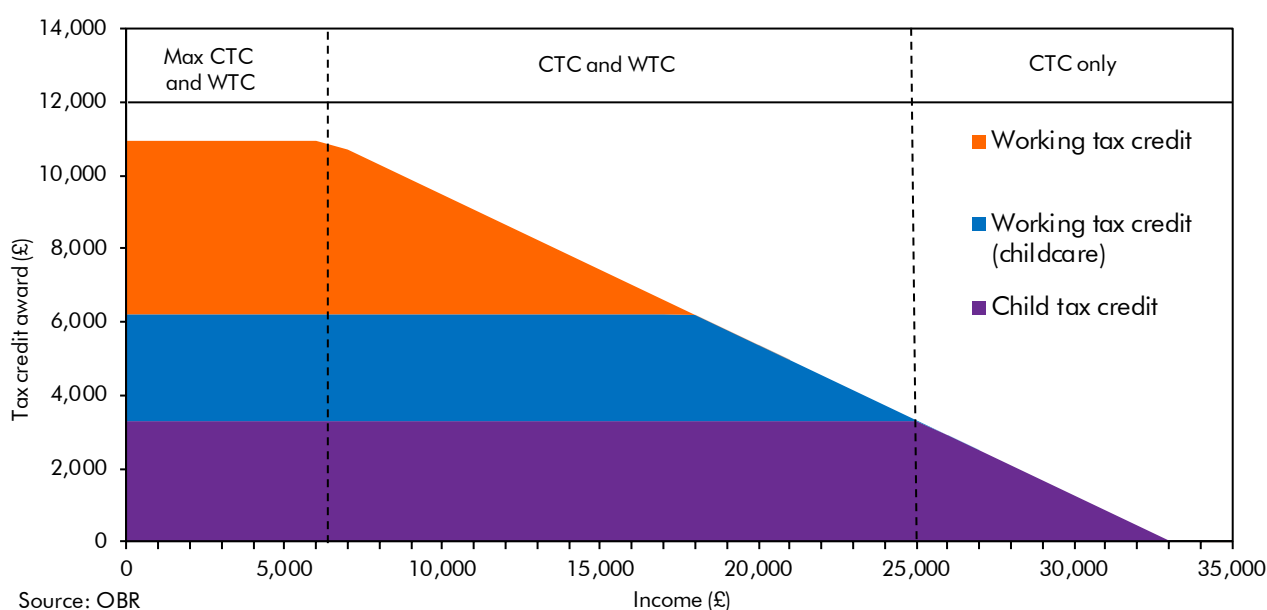
³ HMRC (2014). It is important to note that this is a 'static' estimate of the tax foregone due to this relief, not an estimate of the tax that would be raised by its removal, which would need to take into account any behavioural effects that were induced.

⁴ Total departmental expenditure limit (DEL). HM Treasury (2014).

illustrated in Figure 7.1. The tapering is designed so that the child tax credit award for families that are out of work begins to taper from the same point as for those in work.

- 7.4** The cost of tax credits is currently treated in the public finances statistics partly as spending and partly as negative tax revenue (for that element which notionally offsets an individual's income tax liability). The Government set the welfare cap such that the full cost of tax credits was covered. From 2015-16, the full cost of tax credits is expected to be treated as spending in the public finances data. We follow that treatment in this section.

Figure 7.1: Tapering of a tax credits award for a family in work and paying for childcare (2014-15)



Source: OBR

Note: This chart is illustrative for a family working full-time, with one child and average childcare costs. Changes to any of these circumstances will result in a different award profile.

- 7.5** Tax credits were introduced in their current form in 2003-04, replacing working families tax credit, disabled person's tax credit and the children's tax credit, as well as the child additions payable through income support and jobseeker's allowance. Working families tax credit was itself a replacement for family credit, which had been phased out by 2000-01. Chart 7.1 shows the evolution of spending on these different forms of tax credits over the past 30 years. The period can broadly be split into three:

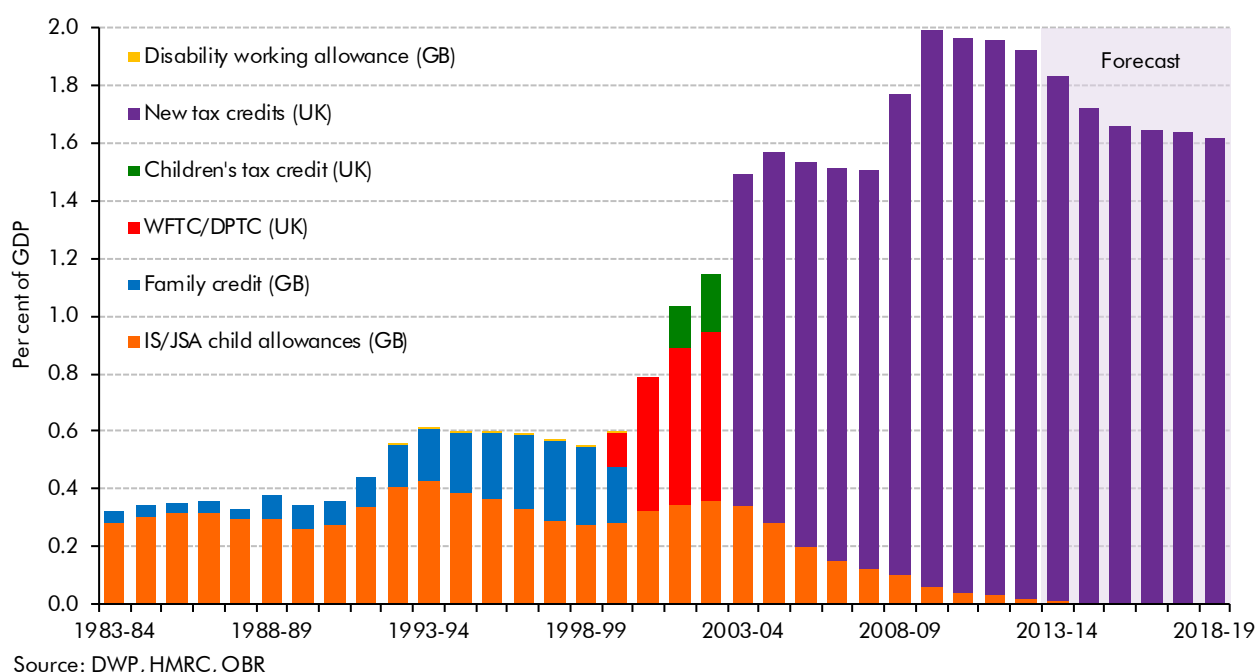
- **1983-84 to 1998-99:** family income supplement, family credit and the child additions for income support and jobseeker's allowance;
- **1999-00 to 2002-03:** working families tax credit (and the disabled person's tax credit), the child additions for income support and jobseeker's allowance, and the children's tax credit (which was provided as a 'tax reducer' rather than spending⁵); and

⁵ Not included in our analyses of welfare spending in this chapter.

- **2003-04 to 2018-19:** tax credits in their current form.

7.6 The analysis presented here includes all of the welfare spending above in the historical series. As described later, part of the changes in spending on tax credits are the result of transfers from other parts of the benefit system (for example, the child additions to income support and jobseeker's allowance) and from other parts of the tax system (for example, the children's tax credit,⁶ itself funded by the abolition of the married couple's allowance).⁷

Chart 7.1: Spending on tax credits: evolution of different systems



Trends in spending on tax credits

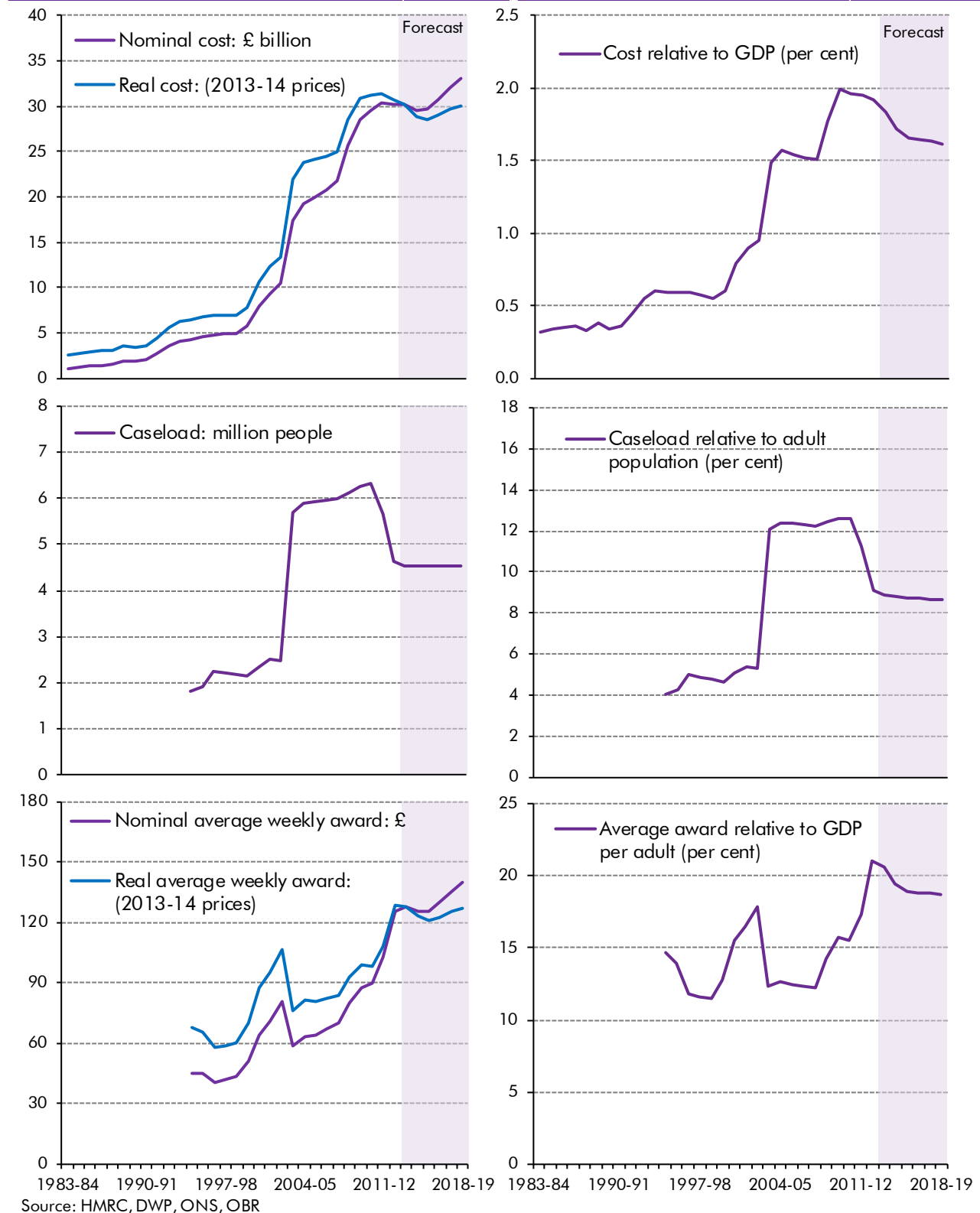
- 7.7** Spending on tax credits and their predecessors has risen from £1 billion to £30 billion in cash terms over the past 30 years, rising around tenfold in real terms (Figure 7.2). This in part reflects reforms that have moved other forms of support into the tax credits system.
- 7.8** Spending rose from 0.3 per cent of GDP in 1983-84 to 0.6 per cent by 1999-00. It then increased further to 0.9 per cent of GDP by 2002-03, with the introduction of working families tax credit and children's tax credit. The shift to tax credits in their current form in 2003-04 saw spending rise again to 1.5 per cent of GDP, before plateauing until the late 2000s recession saw a sharp rise to 2.0 per cent of GDP. Spending then started falling from 2011-12 and is forecast to continue doing so, reaching 1.6 per cent of GDP by 2018-19.

⁶ Technically this was a credit, but it only reduced tax up to the tax liability, but not beyond (i.e., it was a 'tax reducer').

⁷ We have included the spending on the children's tax credit in Chart 7.1 as it was explicitly linked to the reform in 2003-04. But since it was a tax reducer, we do not include it in further detailed analyses that follow. The married couple's allowance and children's tax credit each cost as much as 0.2 per cent of GDP.

Figure 7.2: Tax credits and predecessors: key facts

Current main rates (2014-15)	£ per week	Total cost (2013-14)	
		£ billion	30.1
Basic element of working tax credit	37.3	Per cent of GDP	1.8
Child element (per child)	52.9	Per cent of total welfare spending	14.3
Average award	125.4	Per cent of welfare cap	25.9



7.9 Table 7.1 decomposes changes in spending on tax credits into contributions from different drivers of changes in caseloads and average awards over selected periods from 1994-95 to 2018-19. A full decomposition prior to 1994-95 has not been possible on available data. During that period, spending on tax credits was stable as a share of GDP before rising during the early 1990s recession, driven by increases in spending on both family credit and the child additions of income support and jobseeker's allowance. The table shows that:

- **between 1994-95 and 1999-00**, spending on tax credits' predecessors was stable at around 0.6 per cent of GDP. Overall caseloads rose a little, offsetting a slight fall in average awards relative to GDP-per-adult;
- **from 1999-00 to 2002-03**, spending on tax credits and their predecessors increased by 0.35 per cent of GDP to 0.95 per cent of GDP. This was driven by higher average awards, following the introduction of the working families tax credit, disabled person's tax credit and the children's tax credit;
- **from 2002-03 to 2003-04**, spending rose further to 1.5 per cent of GDP, with the introduction of tax credits in their current form in 2003-04. Caseloads increased significantly, more than offsetting a fall in average awards relative to GDP-per-adult;
- spending levelled off between **2003-04 and 2007-08**;
- **between 2007-08 and 2012-13**, spending increased by 0.4 per cent of GDP to 1.9 per cent of GDP in 2012-13, having peaked at 2.0 per cent of GDP in 2009-10. That reflected generous discretionary uprating, particularly for the child element of the child tax credit. This outweighed a fall in caseloads relative to the adult population over the period as a whole, with an initial increase as a result of the recession followed by a fall as a result of policy changes; and
- **between 2012-13 and 2018-19**, spending is forecast to fall by 0.3 per cent of GDP. This is primarily because uprating is expected to be lower than earnings growth.

Table 7.1: Drivers of changes in tax credits spending

	Per cent of GDP					
	1994-95 to 1999-00	1999-00 to 2002-03	2002-03 to 2003-04	2003-04 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	0.59	0.60	0.95	1.49	1.50	1.92
Spending at end of period	0.60	0.95	1.49	1.50	1.92	1.62
Change	0.01	0.35	0.54	0.01	0.42	-0.31
of which:						
Caseloads	0.09	0.09	0.91	0.02	-0.46	-0.10
Average awards	-0.08	0.26	-0.37	-0.01	0.87	-0.20

7.10 As the evolution of spending on tax credits is largely driven by a series of significant policy changes, we examine the changes in caseloads and average awards quantified in Table 7.1 in more detail as part of the different systems that have operated over time.

Family income supplement, family credit and child additions to income support and jobseeker's allowance

- 7.11 From 1983-84 to 1998-99, support for families in work was provided through the family income supplement, subsequently replaced by family credit. Support for families out of work was provided through the child additions to income support and jobseeker's allowance (although predominantly through income support).⁸
- 7.12 Family income supplement and family credit were both means-tested benefits for working families with children. Caseloads for family income supplement were low initially, but increased significantly through the 1980s as generous uprating – averaging 8 per cent a year from 1983-84 to 1987-88 – led to higher take-up.
- 7.13 The restructuring of family income supplement into family credit in 1988-89 was coupled with a 60 per cent jump in the cash value of the average award. That was followed by seven years during which average awards rose by an average of 12 per cent a year. Caseloads continued to rise as take-up responded to greater generosity and as eligibility was widened further.⁹ Caseloads reached 1.7 per cent of the adult population in 1998-99, up from 0.5 per cent in 1983-84.
- 7.14 During this period, spending on families out of work, through the child additions of income support and jobseeker's allowance, fluctuated with the economic cycle. As spending on family income supplement then family credit increased, spending on the child additions was flat at around 0.3 per cent of GDP from 1983-84 to 1990-91. It increased sharply in the early 1990s recession to peak at 0.4 per cent of GDP in 1993-94, and then fell back as the economy recovered.

Working families tax credit, disabled person's tax credit, children's tax credit and the child additions to income support and jobseeker's allowance

- 7.15 In October 1999, family credit was replaced with a more generous working families tax credit. It was marketed as a tax credit rather than a benefit, administered by the Inland Revenue – now HM Revenue and Customs – and payable through employers.
- 7.16 Working families tax credit provided wider support and higher average awards than family credit due to a higher earnings threshold, a gentler taper and more generous help with childcare costs. So average awards rose sharply.¹⁰ Caseloads also increased, although more modestly, from 4.8 per cent of the adult population pre-reform to 5.3 per cent by 2002-03. Taken together, these developments saw spending on tax credits and their predecessors rise from 0.55 per cent of GDP pre-reform to 0.95 per cent by 2002-03, mostly driven by average award growth.

⁸ Support was also available through child additions for older people in receipt of the minimum income guarantee.

⁹ In the first half of the 1990s, the hours requirement was cut to 16 hours a week, and a childcare disregard was introduced to encourage higher participation, especially among mothers of young children, see Dilnot and Duncan (1992).

¹⁰ Including spending on the child additions of income support and jobseeker's allowance.

7.17 In 2001-02, additional support was provided for families with children, with the children's tax credit introduced outside the welfare system. This reduced tax paid for around 5 million income tax-paying families with children and was originally worth up to £520 per year.¹¹ In April 2002, the credit was increased in line with inflation and an additional 'baby' rate was paid for the first year of a child's life – equivalent to a further credit of £10 a week. This report does not consider in detail the impacts of changes outside the welfare system, so this element does not feature in our detailed analysis of welfare spending.

Tax credits

7.18 The introduction of tax credits in their current form in 2003-04 extended entitlement to welfare spending to families on higher incomes than had traditionally been covered by the benefit system. The new system brought together a number of different items:

- the working families tax credit was subsumed within the child tax credit and the working tax credit;
- the childcare tax credit within working families tax credit was subsumed within the working tax credit;
- child additions to income support and jobseeker's allowance were subsumed within the child element of the child tax credit; and
- the children's tax credit was subsumed within the child tax credit as the family element (along with the additional payment for the first year of a baby's life – re-labelled the 'baby element').

7.19 Subsuming the child additions to income support and jobseeker's allowance into the child tax credit for new claims was accompanied by a large discretionary uprating of the child additions as their value was pegged to the higher value child element of child tax credits.

7.20 Tax credits were designed to increase the responsiveness of the system to changes in family circumstances. The entitlement period reduced from a week to a day, so that in principle a family could move out of work and inform Inland Revenue one day, and the tax credits award would change accordingly the next day. A consequence of this shorter entitlement period was that accurate payments required all-but-instant reporting (and administrative processing) of changes of circumstances. At that time, it was part of the design of the system to reconcile the award at the end of the year – 'finalisation'. But complex, frequently changing circumstances and low awareness among claimants of their reporting responsibilities, combined with administrative difficulties, caused a large number of over- and under-payments in the early years. The Government subsequently expanded the original £2,500 income disregard to £25,000 so that changes in income up to this level were ignored for the tax credits calculation for the rest of that year. This reduced the level of overpayments by around one-third, but increased the cost of the system.

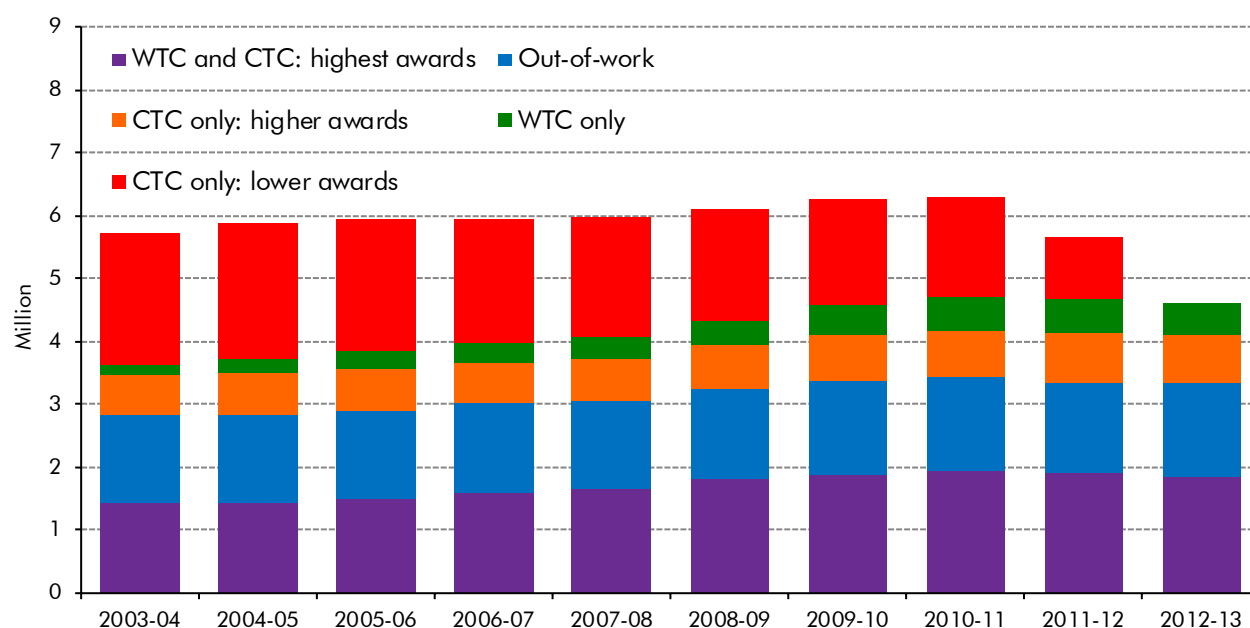
¹¹ The credit took the form of an allowance – set at £5,200 for 2001-02 – for which relief was given at 10 per cent: families could cut their annual income tax bill by up to £520. See House of Commons library (2014).

- 7.21 This wider overhaul of support for families with children was partly funded by switching support out of the tax system. Abolishing the children's tax credit was estimated to have raised around £1.5 billion in 2001-02 and £2.2 billion in 2002-03.
- 7.22 Abstracting from such effects, spending on tax credits still represented a step-change in support in comparison to the previous system with spending as a share of GDP rising by around half to 1.5 per cent of GDP in the year of introduction (2003-04). This jump was driven by a more than doubling of the proportion of the adult population claiming (from around 5 per cent to just over 12 per cent) as a result of extending eligibility higher up the income distribution. Most of the increase in spending came from this source, with around 2 million higher-income families taking up the relatively modest £545 family element – leading to a compositional effect that resulted in a fall in the overall average award.
- 7.23 At the same time, eligibility for the working tax credit was also extended to those without children. These families were entitled to working tax credit only, meaning that maximum awards were on average significantly lower. Further, since the family element plateau did not apply, awards were reduced at the taper rate all the way to zero (much like the current system for all families). Together this meant that – despite the lower take-up rate within this group¹² – caseloads increased alongside relatively lower average awards.
- 7.24 After these reforms, spending remained relatively stable at around 1.5 per cent of GDP between 2003-04 and 2007-08. Caseloads fell slightly relative to the adult population as the growing economy lifted higher-income families above the fixed income threshold – a fiscal drag effect – but average awards increased slightly faster than GDP-per-adult. This reflected the changing composition of the tax credits caseload, with families on higher awards gradually making up a higher proportion of awards (Chart 7.2).¹³

¹² Around 30 per cent for these families relative to around 90 per cent for working tax credit for families with children with higher awards in 2010-11.

¹³ By higher awards, we mean families receiving both working tax credit and child tax credit. By lower awards we mean families receiving child tax credit only tapered closer to zero and also families claiming working tax credit only.

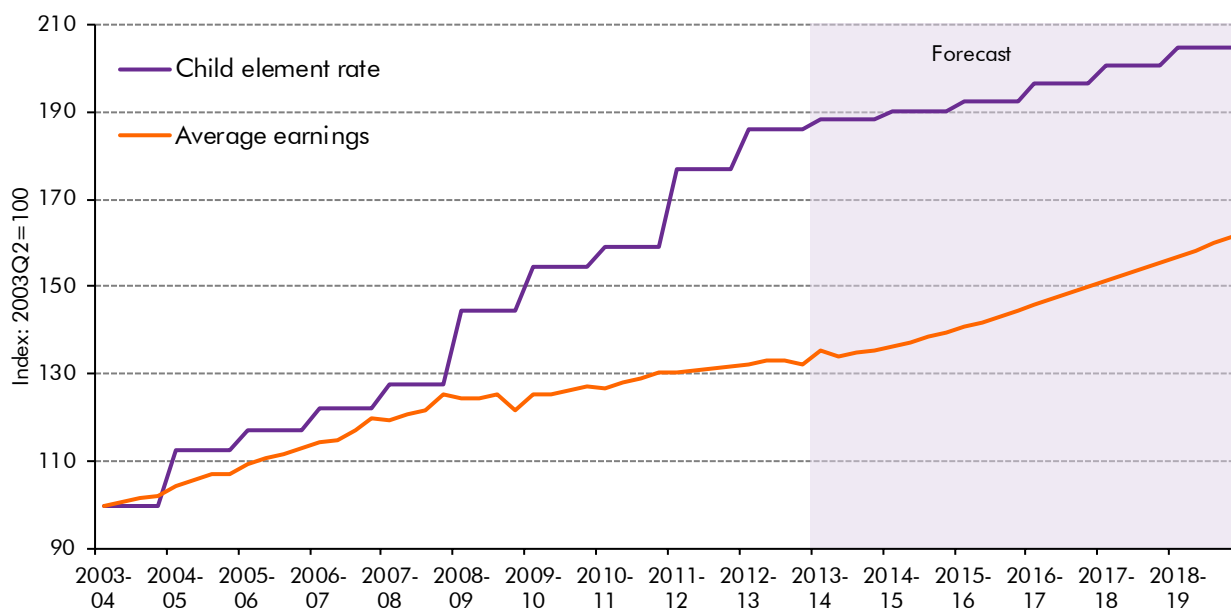
Chart 7.2: Composition of tax credits caseload



Source: HMRC, OBR

7.25 Chart 7.2 also shows a marked rise in the number of low-income high-award families during the late 2000s recession. Between 2007-08 and 2010-11, the Labour Government uprated the principal component of tax credits spending – the child element payable for each child – at least by earnings (Chart 7.3). This was part of the Government’s effort to meet its targets to reduce relative income poverty among families with children. Increasing the childcare element in 2005-06 and 2006-07 fed through to above-earnings increases in childcare costs. These factors raised average awards relative to GDP-per-adult. At the same time, caseloads continued to fall slowly relative to the adult population due to fiscal drag at the top end of the income distribution.

Chart 7.3: Relative generosity of child tax credit



Source: HMRC, ONS, OBR

7.26 In the June 2010 Budget, the Government took steps to reduce spending on tax credits, primarily by reversing the expansion of support higher up the income distribution. It reduced the second income threshold from £50,000 to £40,000 in 2011-12.¹⁴ It then removed the family element plateau entirely in 2012-13. As Chart 7.2 showed, this removed over a million higher-income families on low awards from entitlement. As higher-income families with low awards lost eligibility as a result of these changes, the average award increased due to the consequent change in the composition of the caseload.

7.27 The Government took a number of further steps to reduce spending:

- the uprating of various tax credits elements was moved from RPI to CPI inflation from 2011-12, followed by a one-year freeze in most rates in 2012-13;¹⁵
- reducing support for childcare costs from 80 per cent to 70 per cent;
- abolishing the baby element of child tax credit, the supplement for babies aged one and two, and the 50+ element of working tax credit;
- increasing the withdrawal rate from 39 per cent to 41 per cent;
- reducing the disregard for income rises from £25,000 to £10,000 in 2011-12 and then to £5,000 in 2012-13; and
- introducing a disregard of £2,500 for income falls.

¹⁴ Thereby reducing the number of families on incomes just above £40,000 that would otherwise have received tax credits.

¹⁵ Disability elements were among those not subject to the freeze.

- 7.28 The changes to income disregards will reduce spending, but they reintroduce some of the sensitivity of spending to changing family circumstances that was evident in earlier years.
- 7.29 Partly offsetting the measures that reduce spending, the child element of child tax credit was again uprated above earnings in 2011-12.

Tax credits spending in the medium-term forecast

Spending, caseloads and average awards

- 7.30 In our latest medium-term forecast, the cost of tax credits is expected to rise from £30.1 billion in 2013-14 to £33.0 billion in 2018-19. As GDP in cash terms is forecast to grow at a faster rate than that, spending falls from 1.8 per cent of GDP to 1.6 per cent over the forecast period. A key driver of this fall is the three-year cap of 1 per cent on uprating from 2013-14 to 2015-16, in line with uprating policy across a number of working-age benefits. This helps to keep the caseload broadly flat in absolute terms (and therefore falling relative to the adult population) and the average award rising more slowly than GDP-per-adult.

Table 7.2: Tax credits spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	30.2	30.1	29.6	29.6	30.7	32.0	33.0
Caseload (million)	4.6	4.5	4.5	4.5	4.5	4.5	4.5
Average award (£ thousand)	6.5	6.7	6.5	6.5	6.8	7.1	7.3
Forecast in the context of welfare spending							
Per cent of total welfare spending	14.2	14.3	13.8	13.5	13.7	13.9	14.0
Per cent of cap spending	26.6	26.5	25.7	25.3	25.5	25.7	26.0
Forecast in the context of the economy							
Spending (% of GDP)	1.9	1.8	1.7	1.7	1.6	1.6	1.6
Caseload (% of adults)	9.1	8.9	8.8	8.8	8.7	8.7	8.6
Average award (% of GDP-per-adult)	21.1	20.7	19.5	18.9	18.8	18.8	18.7

Key risks to the forecast

- 7.31 Forecasting tax credits spending has been relatively difficult, largely because of the high volume of policy changes since their introduction. Beyond the standard risks associated with policy costings, there are a number of other risks:
- whole economy earnings growth affects eligibility and awards. Any differences from the whole economy average at the lower end of the income distribution would disproportionately affect low-income, in-work families (on higher awards);
 - the forecast for the number of out-of-work families is linked to the jobseeker's allowance forecast, but the two have followed different paths in the past. We assume that the jobseeker's allowance caseload falls faster than the out-of-work tax credits caseload in our latest forecast, but this is uncertain;¹⁶ and

¹⁶ Definitions of 'out of work' are different under jobseeker's allowance and tax credits so these are not automatically comparable.

- an increasing number of operational measures that are designed to achieve savings that are difficult to evaluate – for example, reducing error and fraud.

Long-term projection of tax credits spending

- 7.32** Our 2014 *Fiscal sustainability report* contained long-term projections for tax credits spending to 2063-64. These show spending flat as a per cent of GDP beyond our medium-term forecast.
- 7.33** Our long-term projections largely reflect the impact of demographic changes on caseloads. We assume that awards rise in line with earnings rather than prices. The projections therefore show that the ageing of the population is expected to leave spending on tax credits flat as a share of GDP. But due to the upward pressure from demographics on state pension costs, spending on tax credits is expected to fall as share of total welfare spending.

Table 7.3: Tax credits long-term spending projection

	Forecast		Projections				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP	1.7	1.6	1.7	1.6	1.6	1.6	1.6
Per cent of welfare spending	13.1	14.0	14.1	12.6	11.7	11.6	11.3

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis excluding the negative tax element of tax credits, consistent with our 2014 *Fiscal sustainability report* projections.

Child benefit

- 7.34** Child benefit is a cash benefit paid to the parents or guardians of children under the age of 16 and of anyone aged between 16 and 19 who is in full-time non-advanced education at a school or college or undertaking approved training not provided via a contract of employment. Child benefit, introduced in the late 1970s to replace both family allowances and child tax allowances, was until very recently a universal benefit. However, the introduction of a tax charge for parents on individual annual incomes over £50,000 from January 2013 in effect introduces an element of means testing to child benefit. Spending on child benefit will be subject to the welfare cap from 2015-16. In 2013-14, child benefit spending was estimated at £11.6 billion, accounting for 5.5 per cent of total welfare spending and 10.0 per cent of spending on items that will be subject to the welfare cap.¹⁷

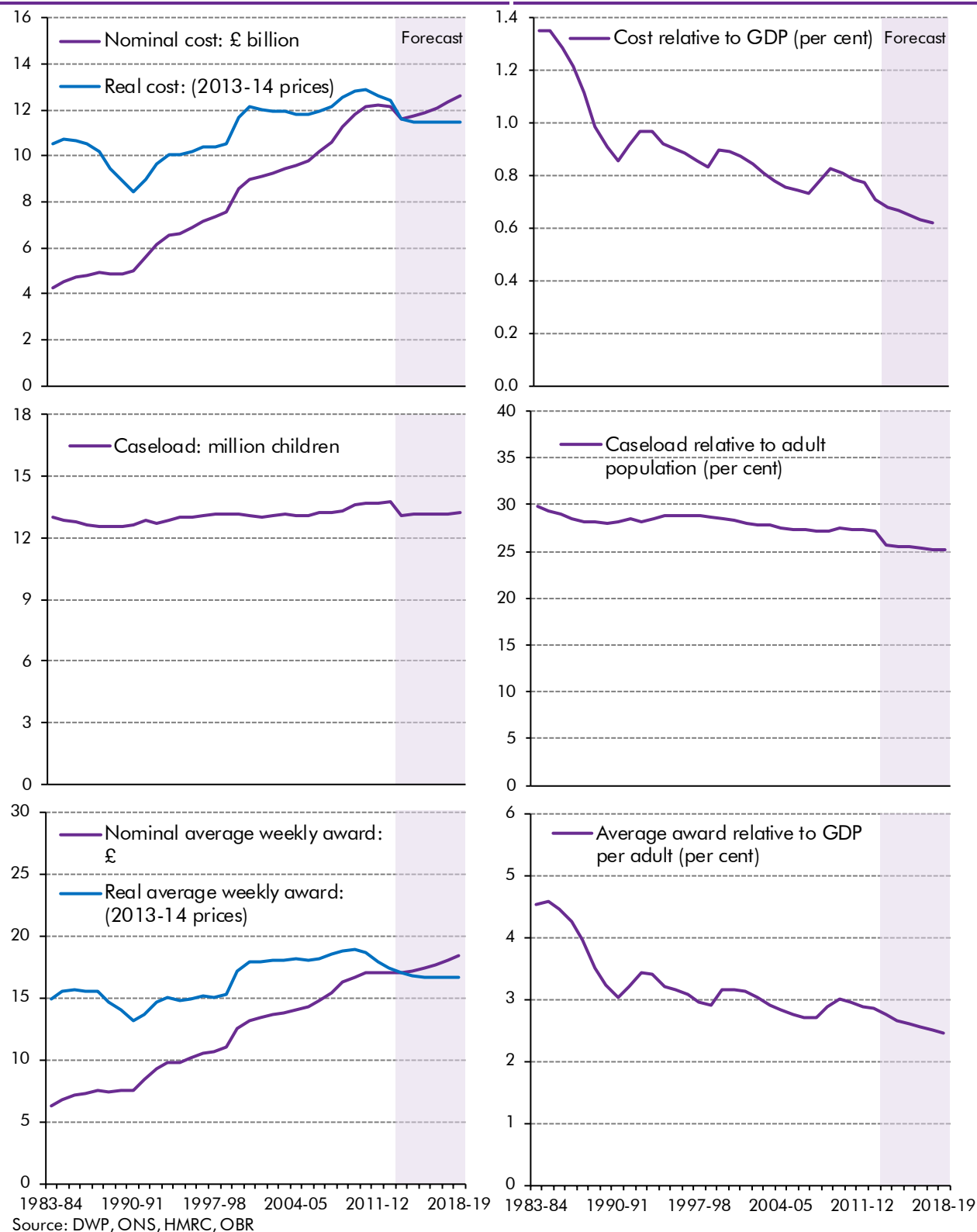
Trends in spending on child benefit

- 7.35** Over the past 30 years, spending on child benefit has increased from £4.2 billion to £11.6 billion, an 11 per cent rise in real terms. As a share of GDP, spending has been on a declining trend for most of that period, punctuated by occasional rises related to policy decisions to uprate child benefit by more than inflation and earnings growth.

¹⁷ Child benefit spending for this section covers spending on a range of smaller related benefits, including the one parent benefit, guardian's allowance and child special allowance.

Figure 7.3: Child benefit: key facts

Current main rates (2014-15)	£ per week	Total cost (2013-14)	
		£ billion	11.6
First child rate	20.50	Per cent of GDP	0.7
Subsequent child rate	13.55	Per cent of total welfare spending	5.5
Average weekly award	17.15	Per cent of welfare cap	10.0



7.36 Table 7.4 decomposes changes in child benefit spending into those driven by changes in caseloads (here, the number of children) and average awards. It shows that the fall in spending as a per cent of GDP has largely been driven by average awards tending to grow more slowly than GDP-per-adult, with changes in caseload typically less important.

Table 7.4: Drivers of changes in child benefit spending

	Per cent of GDP				
	1983 -84 to 1990-91	1990-91 to 1992-93	1992-93 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	1.35	0.86	0.97	0.73	0.77
Spending at end of period	0.86	0.97	0.73	0.77	0.62
Change	-0.49	0.11	-0.24	0.04	-0.16
of which:					
Caseload	-0.07	0.00	-0.03	0.00	-0.06
Demography	-0.13	-0.01	-0.06	-0.01	-0.01
Other	0.06	0.01	0.03	0.01	-0.05
Average award	-0.42	0.11	-0.20	0.04	-0.10

Changes in caseloads

7.37 Over the past 30 years, the child benefit caseload has been relatively stable in absolute terms and has fallen relative to the adult population. This largely reflects demographic factors – in particular changes in fertility rates – described in Chapter 3.

7.38 The fall in caseload from 2013-14 reflects the Government's policy decision to remove child benefit from families with at least one parent with an income of more than £60,000 and to taper awards for those with an income between £50,000 and £60,000, referred to as the 'high income child benefit charge'. Families affected can either opt out of receiving child benefit, reducing spending, or continue to receive child benefit and subsequently pay an income tax charge, which would increase income tax receipts. To date, around a third of affected families have chosen to opt out from receiving child benefit, reducing spending.

Changes in average awards

7.39 Child benefit average awards have risen more slowly than GDP-per-adult over much of the past 30 years. Policy decisions on uprating were the main driver of these changes. For example, freezing the cash award between 1987-88 and 1990-91 meant that average awards fell in real terms and fell more steeply relative to GDP-per-adult.

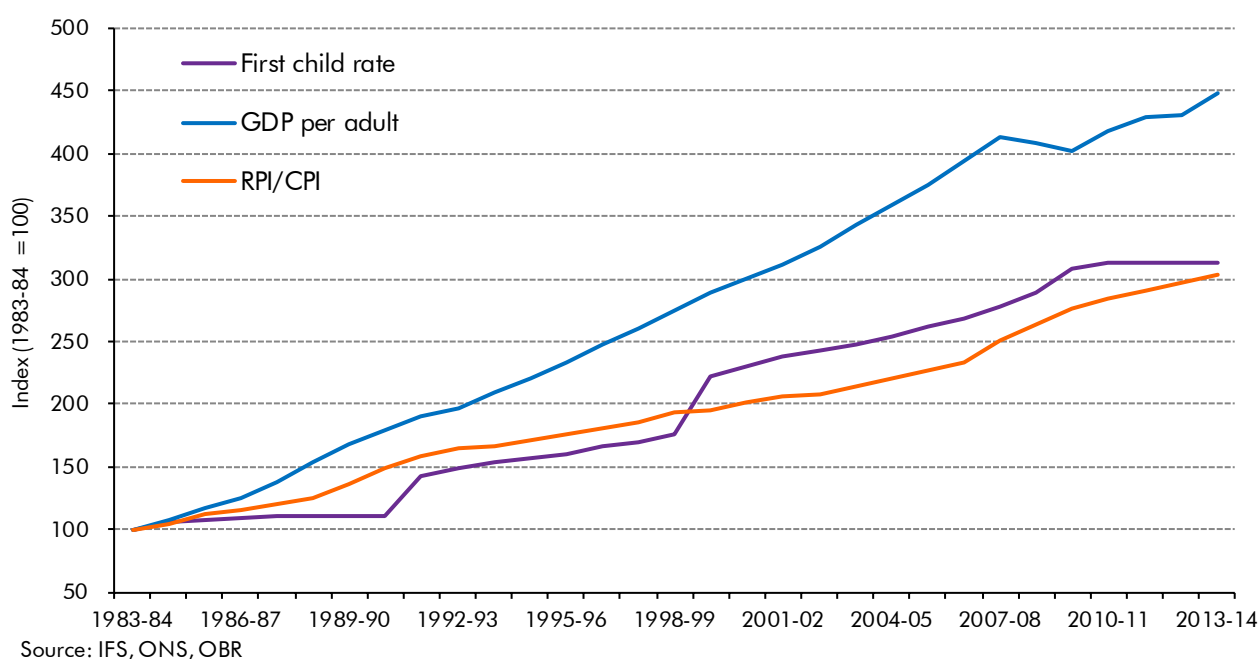
7.40 There have been three periods during which average awards have risen relative to GDP-per-adult, temporarily breaking the overall downward trend:

- in 1991-92, a higher rate for the first/eldest child was introduced. The higher rate was set £1 a week higher and then raised by a further £1 a week, with smaller increases introduced for subsequent children;

- between 1997-98 and 1999-00, the first/eldest child rate rose by around a third in cash terms due to uprating decisions (the subsequent child rate rose by 7 per cent over the same period). Over this period, GDP-per-adult increased by 10 per cent; and
- between 2007-08 and 2009-10, rates increased by 10 per cent in cash terms, but GDP-per-adult fell by 1 per cent, pushing the average award up relative to incomes.

7.41 In the June Budget 2010, the Government froze child benefit for three years from 2011-12.

Chart 7.4: Relative generosity of child benefit rates



Child benefit spending in the medium-term forecast

Spending, caseloads and average awards

7.42 In our latest medium-term forecast, spending on child benefit rises in cash terms from £11.6 billion in 2013-14 to £12.6 billion in 2018-19. As GDP in cash terms is forecast to grow faster than that, spending is expected to fall from 0.7 to 0.6 per cent of GDP over the forecast period. The fall is driven mainly by changes in average awards, with child benefit rates frozen in cash terms in 2013-14, and subject to a 1 per cent cap in uprating in 2014-15 and 2015-16 before reverting to CPI uprating from 2016-17 onwards. Opt-outs resulting from the high income child benefit charge are expected to reduce spending by £0.8 billion in 2015-16, rising thereafter in line with projections for the numbers of taxpayers crossing the £50,000 threshold.

Table 7.5: Child benefit spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	12.2	11.6	11.7	11.9	12.1	12.4	12.6
Caseload (million)	13.8	13.1	13.1	13.2	13.2	13.2	13.2
Average annual award (£ thousand)	0.88	0.89	0.89	0.90	0.92	0.94	0.96
Forecast in the context of welfare spending							
Per cent of total welfare spending	5.7	5.5	5.5	5.4	5.4	5.4	5.4
Per cent of welfare cap spending	10.4	10.0	9.9	10.0	9.9	9.9	10.0
Forecast in the context of the economy							
Spending (% of GDP)	0.77	0.71	0.68	0.67	0.65	0.63	0.62
Caseload (% of adults)	27.2	25.7	25.5	25.5	25.3	25.3	25.2
Average award (% of GDP-per-adult)	2.85	2.75	2.66	2.61	2.55	2.51	2.46

Key risks to the forecast

- 7.43 The main driver of spending on child benefit is the number of families with children. Since child benefit is payable from birth, changes in birth rates can affect the forecast over relatively short time horizons. Changes can also affect the other end of the relevant age distribution, for example if the number of 17-year olds staying on in full-time education is more or less than expected.
- 7.44 The main policy-related risk relates to the estimated impact of the high income child benefit charge. Higher or lower rates of earnings growth – or changes in income distribution at the top end – could lead to a larger or smaller number of families being affected by the policy.

Long-term projection of child benefit spending

- 7.45 Our 2014 *Fiscal sustainability report* contained long-term projections for child benefit spending to 2063-64. The projections show spending as a per cent of GDP flat beyond our medium-term forecast.
- 7.46 Our long-term projections largely reflect the impact of demographic changes on caseloads. We assume that awards rise with earnings rather than prices. The projections show that changes in the age structure of the population are expected to leave spending on child benefit flat as a share of GDP. But due to the upward pressure from demographics on state pension costs, spending on tax credits is expected to fall as share of total welfare spending.
- 7.47 The main sensitivity in our long-term projection would be to the proportion of the population made up of children. That could be affected by changes in fertility rates or by differences in the age structure of migrants to and from the UK.

Table 7.6: Child benefit long-term spending projection

	Forecast		Projections				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP	0.7	0.6	0.6	0.6	0.6	0.6	0.6
Per cent of welfare spending	5.6	5.4	5.4	4.9	4.5	4.5	4.4

Note: Figures for 2013-14 and 2018-19 consistent with our 2014 *Fiscal sustainability report* projections.

Statutory maternity pay and maternity allowance

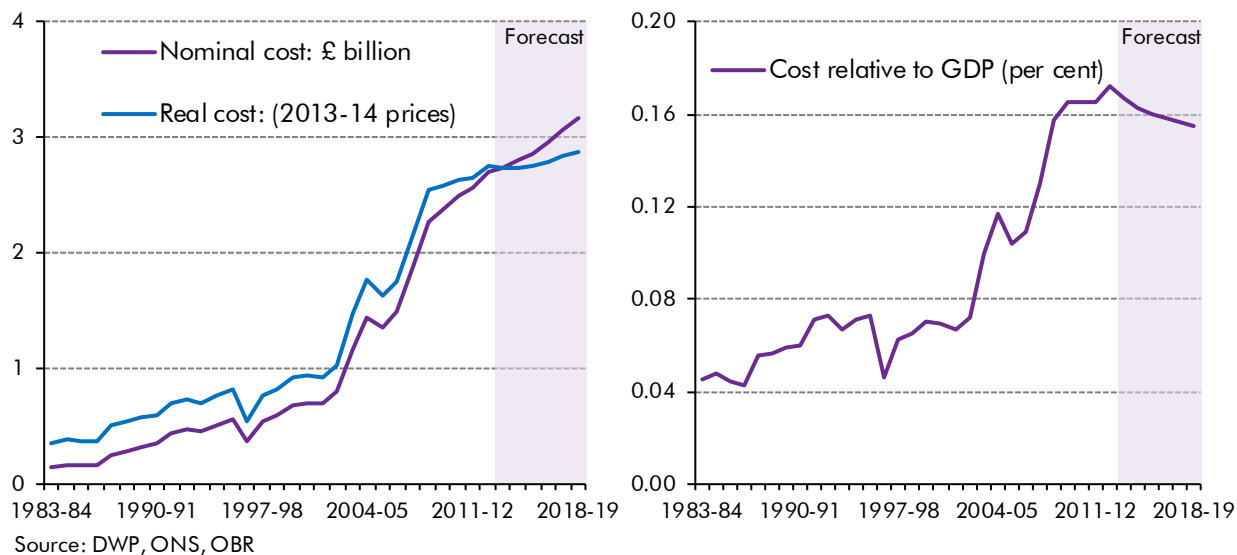
- 7.48 Statutory maternity pay is a legal minimum amount that employers must pay to their qualifying employees during maternity leave. It was introduced in 1987, although it existed in some form under the previous system of maternity allowance. Statutory maternity pay is also contingent on mothers being in employment and satisfying qualifying conditions. Since the introduction of statutory maternity pay, maternity allowance is only payable to those who do not qualify for statutory maternity pay, low income earners or the self-employed.
- 7.49 Spending on these maternity benefits is subject to the welfare cap, but makes up a relatively small proportion of welfare spending. In 2013-14, spending on these two benefits was estimated at £2.7 billion, mostly statutory maternity pay. They accounted for 1.3 per cent of total welfare spending and 2.4 per cent of spending on items that will be subject to the welfare cap from 2015-16.

Trends in spending on maternity benefits

- 7.50 Figure 7.4 shows that spending has increased from £0.1 billion in 1983-84 to £2.7 billion in 2013-14 in cash terms, an eight-fold rise in real terms and from 0.05 per cent of GDP to 0.17 per cent of GDP. Much of the rise has taken place since 2002-03.
- 7.51 The rise in spending has been driven by successive policy changes that have extended both the payment period for which maternity benefits can be received and the standard rate paid to the recipient. One trend affecting the underlying caseload is rising employment rates for women (see Chapter 3), which increases the number of women potentially eligible. Increases in fertility rates since the early 2000s have also increased the caseload.
- 7.52 Between 2001-02 and 2003-04, the standard rate for statutory maternity pay and maternity allowance was increased from £62.20 to £100 a week. The payment period was increased from 18 to 26 weeks and further to 39 weeks in 2007-08.

Figure 7.4: Maternity benefits: key facts

Current main rates	£ per week	Total cost (2013-14)	
Statutory maternity pay/maternity allowance	138.18 (or 90% of the employee's average weekly earnings)	£ billion	2.7
		Per cent of GDP	0.2
		Per cent of total welfare spending	1.3
		Per cent of welfare cap	2.4



Maternity benefits spending in the medium-term forecast

- 7.53** In our latest medium-term forecast, spending on maternity benefits is forecast to fall slightly from 0.17 per cent of GDP to 0.15 per cent of GDP. This reflects the 1 per cent cap on uprating from 2013-14 to 2015-16, which means that average awards rise more slowly than GDP-per-adult.
- 7.54** The key risks to the spending forecast for maternity benefits are changes in the fertility rate and female employment. From 2015, women will also be able to end their maternity benefits earlier than the current 39 weeks, with unused weeks then available as statutory shared parental pay to eligible couples. The extent to which this is taken up is subject to considerable uncertainty, though the impact on overall spending is likely to be small.

Table 7.7: Maternity benefits spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	2.7	2.7	2.8	2.9	3.0	3.1	3.2
Caseload (million)	0.34	0.34	0.34	0.34	0.35	0.35	0.35
Average award (£ thousand)	8.0	8.1	8.2	8.4	8.6	8.8	9.0
Forecast in the context of welfare spending							
Per cent of total welfare spending	1.27	1.30	1.31	1.31	1.32	1.33	1.34
Per cent of cap spending	2.32	2.36	2.38	2.39	2.42	2.45	2.50
Forecast in the context of the economy							
Spending (% of GDP)	1.27	1.30	1.31	1.31	1.32	1.33	1.34
Caseload (% of adults)	2.32	2.36	2.38	2.39	2.42	2.45	2.50
Average award (% of GDP-per-adult)	0.17	0.17	0.16	0.16	0.16	0.16	0.15

Paternity pay

- 7.55** Ordinary statutory paternity pay is paid for a period of one or two weeks to partners following the birth or adoption of a child. It is paid by employer to employee and the employer can recover some or all of the payments from government. The amount reclaimed depends on National Insurance contributions paid in the appropriate tax year.
- 7.56** Claimants may also be entitled to up to 26 weeks' additional statutory paternity pay, depending on whether the other parent returns to work. Spending on paternity pay will be subject to the welfare cap from 2015-16.
- 7.57** In 2012 -13, spending on paternity pay reported to HMRC amounted to £56 million, but some employers do not claim statutory payments back.¹⁸
- 7.58** As noted above, from 2015-16 parents may be entitled to shared parental leave and statutory shared parental pay (to be taken in the first year).¹⁹ Eligible parents ending maternity or adoption leave or pay (or maternity allowance) early will be able to transfer the remaining leave as shared parental leave, payable as statutory shared parental pay.

Tax-free childcare

- 7.59** In Budget 2013, the Government announced a new tax-free childcare scheme, which will support around 1.9 million working families with 20 per cent of their childcare costs up to £2,000 per child per year. The new system will be phased in from autumn 2015, over time replacing the existing system of employer supported childcare. Unlike the existing system where the support is provided via the tax system, the new scheme will score as spending.
- 7.60** Households in which all parents work but do not receive support through tax credits (or universal credit in the future) will be eligible, so long as neither parent earns over £150,000

¹⁸ This is especially true when the employer pays occupational paternity pay above the statutory rate because the leave and pay is only available for 2 weeks at a flat rate (currently £136.78).

¹⁹ In England, Scotland, and Wales.

a year. The scheme will be rolled out to all eligible families with children under 12 within the first year of the scheme's operation. Disabled children up to age 17 will also be eligible. Spending on tax-free childcare will be subject to the welfare cap from 2015-16 and is forecast to cost almost £1 billion by 2018-19.

Income support

- 7.61 Historically, income support has been used to support a number of different groups, including the elderly and the unemployed. Over time, most elements have been transferred to other parts of the welfare system. The main beneficiaries of the remaining income support system are lone parents and carers, hence its inclusion in this chapter.
- 7.62 Income support is a means-tested benefit paid to people on low incomes that is intended to provide for basic living needs. Income support will be subject to the welfare cap from 2015-16. In 2013-14, total spending on income support was estimated at £3.6 billion. It accounted for 1.7 per cent of total welfare spending and 3.1 per cent of spending that will be subject to the welfare cap. The main claimant groups currently receiving income support are lone parents (£1.8 billion in 2013-14), carers (£0.5 billion), incapacity claimants (£0.9 billion),²⁰ and other claimant groups (£0.3 billion).

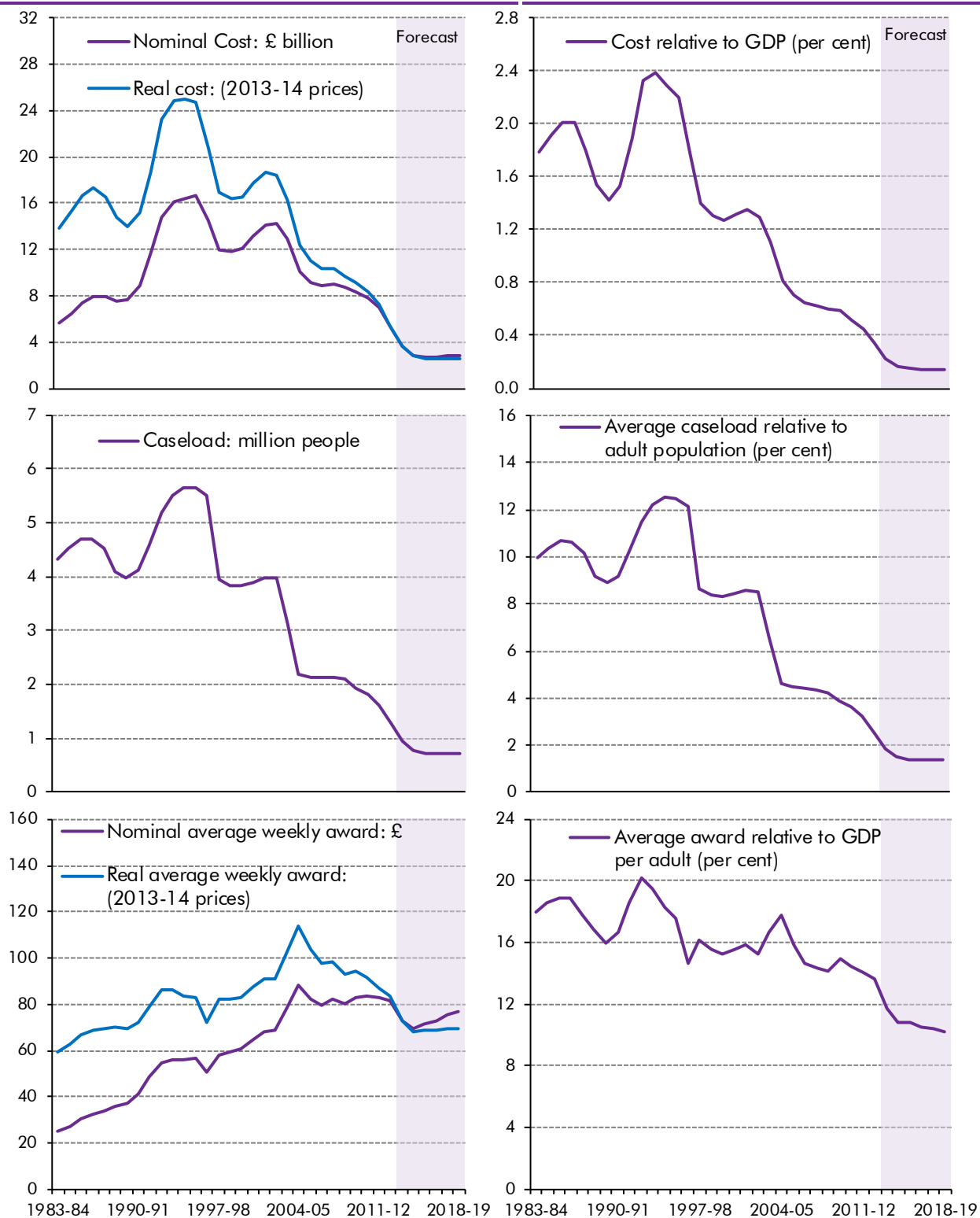
Trends in income support spending

- 7.63 As shown in Figure 7.4, spending on income support increased from £5.6 billion in 1983-84 to a peak of £16.7 billion in 1995-96, before falling to £3.6 billion in 2013-14. As a share of GDP, spending peaked earlier in 1993-94 at 2.4 per cent, before falling steadily over the following two decades to 0.2 per cent of GDP in 2013-14. Increases in the early 1990s reflected the impact of the recession at that time on caseloads, while the reduction since can largely be explained by support delivered through income support being shifted to other benefits (as described elsewhere). These effects can be seen in Table 7.8, which shows that changes in caseloads have been the main drivers of fluctuations in spending.

²⁰ 'Incapacity' claimants on income are gradually being transferred over to employment and support allowance (ESA). By 2015-16 migration over to ESA is expected to be complete.

Figure 7.5: Income support: key facts

Current main rates (2014-15)		£ per week		Total cost (2013-14)	
				£ billion	3.6
				Per cent of GDP	0.2
Lone parent/ single claimant, aged 18 or over		72.40		Per cent of total welfare spending	1.7
Average weekly award		69.52		Per cent of welfare cap	3.1



Source: DWP, ONS, OBR

Table 7.8: Drivers of changes in income support spending

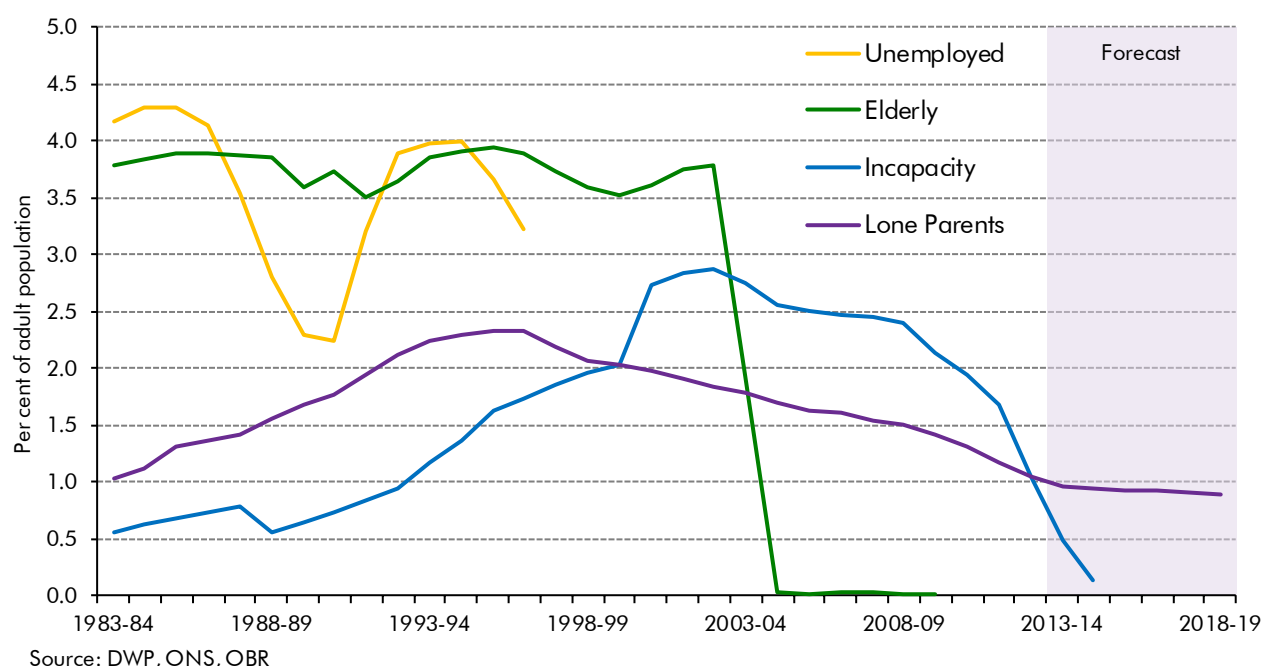
	Per cent of GDP					
	1983-84 to 1989-90	1989-90 to 1992-93	1992-93 to 1996-97	1996-97 to 2002-03	2002-03 to 2007-08	2007-08 to 2012-13
Spending at start of period	1.79	1.42	2.33	1.78	1.30	0.62
Spending at end of period	1.42	2.33	1.78	1.30	0.62	0.34
Change	-0.36	0.90	-0.54	-0.49	-0.67	-0.29
of which:						
Caseload	-0.18	0.48	0.12	-0.55	-0.60	-0.26
Average award	-0.18	0.42	-0.66	0.06	-0.07	-0.03

Changes in caseloads

7.64 The significant fall in the caseload is dominated by changes that moved people off income support to other parts of the system. These include:

- in October 1996, jobseeker's allowance replaced income support for the unemployed (Chapter 8). Until then, the unemployed were the second largest claimant group;
- in 2003-04, income support for those aged 60 and over was replaced by pension credit (Chapter 5);
- in 2003, payments of the child addition for new income support claimants were transferred to child tax credit. By 2015-16, all child additions are expected to be paid through child tax credit; and
- from October 2008, it was no longer possible to claim income support on incapacity grounds. Instead, new claimants were required to claim employment support allowance (ESA). Migration of claims began nationally in April 2011 and is ongoing.

Chart 7.5: Income support caseloads by claimant groups



7.65 The number of lone parents eligible for income support has fallen due to a tightening in conditionality. Between November 2008 and May 2012, under the lone parent obligation, the age of the youngest child enabling income support eligibility solely on the grounds of being a lone parent was reduced from under 14 to under five. Those losing entitlement to income support are able to claim another out-of-work benefit, such as jobseeker's allowance or ESA. As discussed in Chapter 8, the number of lone parents on jobseeker's allowance has risen substantially since the lone parent obligation was introduced.

7.66 Spending on lone parents was falling prior to the introduction of the obligation, due to the transfer of child elements to tax credits, an increase in the number of lone parents in work and some growth in lone parents on the income support incapacity element.

Changes in average awards

7.67 Average awards relative to GDP-per-adult have fluctuated around an overall declining trend. Movements mainly relate to changes in the relative generosity of the benefit, as well as the substantial changes in the composition of claimants described above.²¹

Income support spending in the medium-term forecast

Spending, caseloads and average awards

7.68 In our latest medium-term forecast, spending on income support is forecast to fall from 0.22 per cent of GDP in 2013-14 to 0.14 per cent of GDP in 2018-19. This is largely driven by

²¹ Incapacity and lone parent claimants which, up until recent years, have made up the majority of spending, typically receive higher awards than groups such as the elderly (which were transferred onto pension credit after its introduction). This compositional shift will push up average awards, all else being equal.

the migration of income support for incapacity onto ESA up to the end of 2014-15, further reducing caseloads. Our forecast also shows average awards rising more slowly than GDP-per-adult, reflecting uprating by 1 per cent up until 2015-16 and then CPI post-2015-16.

Table 7.9: Income support spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	5.3	3.6	2.8	2.6	2.7	2.8	2.9
Caseload (million)	1.25	0.96	0.78	0.71	0.71	0.72	0.72
Average award (£ thousand)	4.2	3.8	3.6	3.7	3.8	3.9	4.0
Forecast in the context of welfare spending							
Per cent of total welfare spending	2.49	1.73	1.32	1.21	1.20	1.21	1.21
Per cent of cap spending	4.56	3.12	2.40	2.22	2.21	2.25	2.26
Forecast in the context of the economy							
Spending (% of GDP)	0.34	0.22	0.16	0.15	0.14	0.14	0.14
Caseload (% of adults)	2.48	1.88	1.52	1.37	1.37	1.37	1.37
Average award (% of GDP-per-adult)	13.65	11.76	10.79	10.78	10.53	10.45	10.25

Key risks to the forecast

- 7.69** The transfer of the remaining claimants from income support to ESA is expected to be completed by the end of 2014-15, but the schedule remains a risk due to the current backlog of reassessment cases involved in the overall migration to ESA (see Chapter 6).

Long-term projection of income support spending

- 7.70** Our 2014 *Fiscal sustainability report* contained long-term projections for income support spending to 2063-64. The projections show spending staying broadly flat as a per cent of GDP beyond our medium-term forecast.
- 7.71** Our long-term projections largely reflect the impact of demographic changes on caseloads, and we assume that awards rise in line with earnings rather than prices. The projections therefore show that demographic factors are not expected to drive changes in spending on income support as a share of GDP. But due to the effect of demographics on state pensions, spending on income support is expected to fall as a per cent of total welfare spending.

Table 7.10: Income support long-term spending projection

	Forecast		Projections				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP	0.23	0.15	0.15	0.15	0.15	0.15	0.15
Per cent of welfare spending	1.9	1.3	1.3	1.2	1.1	1.1	1.1

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis, consistent with our 2014 *Fiscal sustainability report* projections.

Social fund

- 7.72 The social fund was introduced from 1987 to provide more short-term financial assistance to people in need. While some elements of the fund have been replaced by local provision, the Government still provides funeral payments, sure start maternity grants, cold weather payments and budgeting loans. In 2013-14, social fund spending – the majority of which was on cold weather payments – was estimated to be £219 million.²² Spending on the social fund will be subject to the welfare cap from 2015-16.

²² Net social fund expenditure, excluding winter fuel payments.

8 Spending on unemployed people

8.1 This chapter covers jobseeker's allowance and its predecessors.¹

Unemployment benefits

8.2 Jobseeker's allowance (JSA) replaced unemployment benefit and income support for unemployed people in October 1996. In this chapter, 'unemployment benefits' refers to JSA and its predecessors. There are two types of JSA:

- **contribution-based JSA:** which is paid to individuals who have satisfied the National Insurance contribution conditions – it accounted for 12 per cent of total spending on JSA in 2013-14; and
- **income-based JSA:** which is paid to claimants who satisfy a family income-based means test – it accounted for 88 per cent of JSA spending in 2013-14.

8.3 Spending on unemployment benefits is small relative to total welfare spending, accounting for just 2.1 per cent of total welfare spending in 2013-14. The Government announced in Autumn Statement 2013 that JSA spending – and associated housing benefit spending (see Chapter 9) – would not be subject to the welfare cap, as they were identified as *"the most cyclical elements of welfare"* that *"allow the automatic stabilisers to operate"*.²

Trends in spending on unemployment benefits

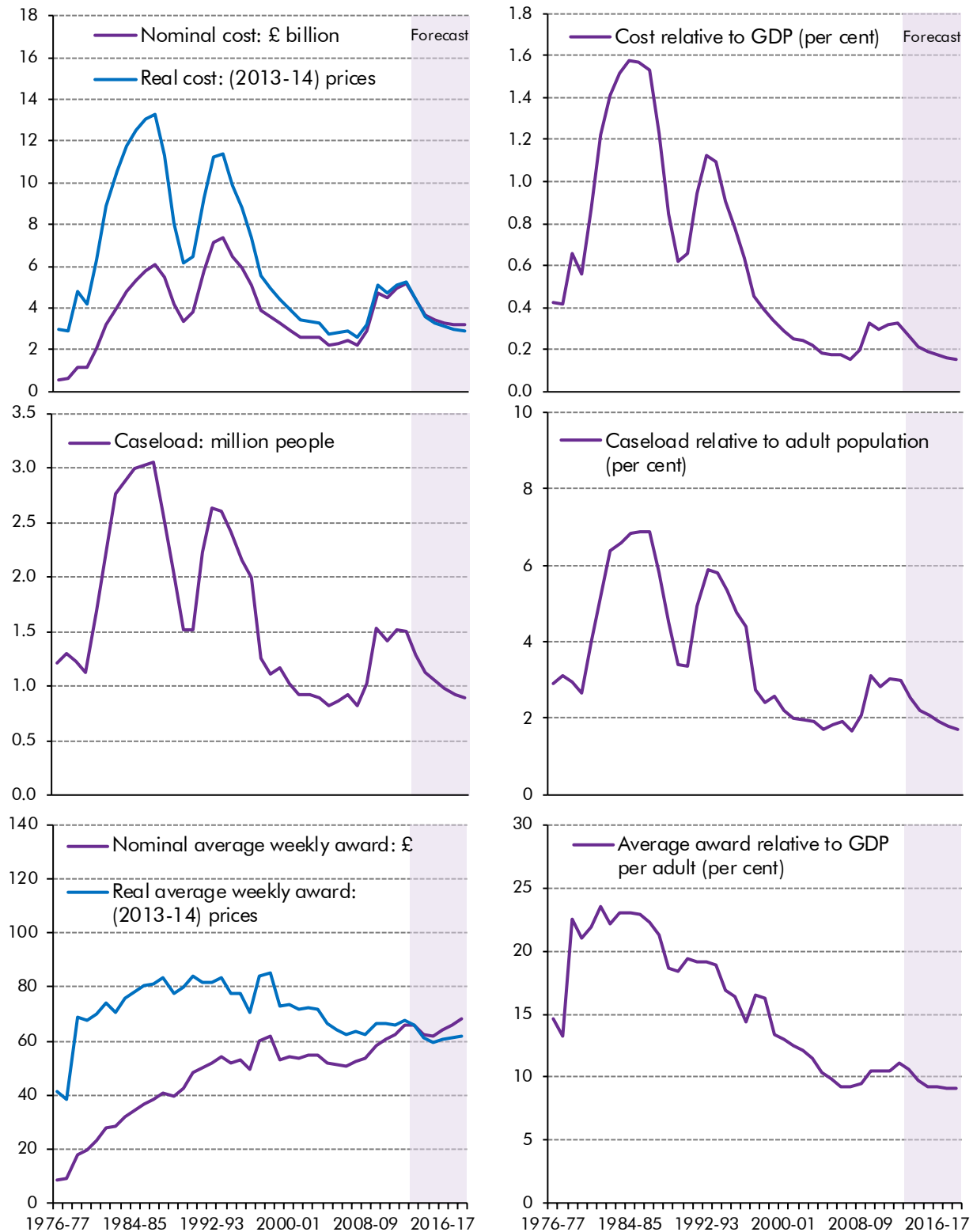
8.4 Spending on unemployment benefits is relatively volatile, as the unemployment caseload fluctuates with the economic cycle. Figure 8.1 shows that spending increased substantially in cash terms and as a share of GDP as a result of the early 1980s recession, reaching a peak in 1984-85 when the caseload topped three million people. Spending has followed a downward trend since then, but with further cyclical peaks after the early 1990s recession and, much smaller, after the late 2000s recession.

¹ The main figures on welfare spending and its drivers used in this report are consistent with data available at the time of our March 2014 *Economic and fiscal outlook*. Spending data cover Great Britain and are drawn from DWP expenditure tables produced at the time of our March EFO.

² HM Treasury (2013).

Figure 8.1: Unemployment benefits: key facts

Current main rates (2014-15)	£ per week	Total cost (2013-14)	
Single, under 25	57.35	£ billion	4.4
Single, 25 or over	72.40	Per cent of GDP	0.3
Income-based JSA (couples, both aged 18+)	113.70	Per cent of total welfare spending	2.1
Average weekly award	62.55	Per cent of welfare cap	n/a



Source: DWP, ONS, OBR

- 8.5 Table 8.1 breaks down the sources of changes in spending as a share of GDP between the peaks and troughs since 1983-84. From 1.5 per cent of GDP in that year, it fell to a low of 0.15 per cent in 2007-08. That reflected both the declining generosity of unemployment benefits and the fall in caseloads relative to the adult population. The latter contained both cyclical and structural elements. Having risen during the late 2000s recession and stabilised over the next three years, our latest forecast suggests that spending will return to its pre-crisis share of GDP by 2018-19. This decomposition is explained more fully below.

Table 8.1: Drivers of changes in unemployment benefits spending

	Per cent of GDP					
	1983-84 to 1989-90	1989-90 to 1992-93	1992-93 to 2007-08	2007-08 to 2009-10	2009-10 to 2012-13	2012-13 to 2018-19
Spending at start of period	1.52	0.62	1.12	0.15	0.33	0.33
Spending at end of period	0.62	1.12	0.15	0.33	0.33	0.16
Change	-0.89	0.50	-0.97	0.17	0.00	-0.17
of which:						
Caseload	-0.63	0.47	-0.56	0.15	-0.01	-0.12
of which:						
LFS unemployment ¹	-0.42	0.30	-0.29	0.10	0.00	-0.08
Claimant count vs LFS ²	-0.21	0.17	-0.27	0.05	-0.01	-0.04
Average awards	-0.26	0.03	-0.41	0.02	0.02	-0.05

¹ Changes explained by changes in the ratio of LFS unemployment to the adult population.

² Changes explained by changes in the ratio of claimant count to LFS unemployment.

Note: Data prior to 1996-97 represent income support for the unemployed and unemployment benefit. Data from 1996-97 onwards represent jobseeker's allowance.

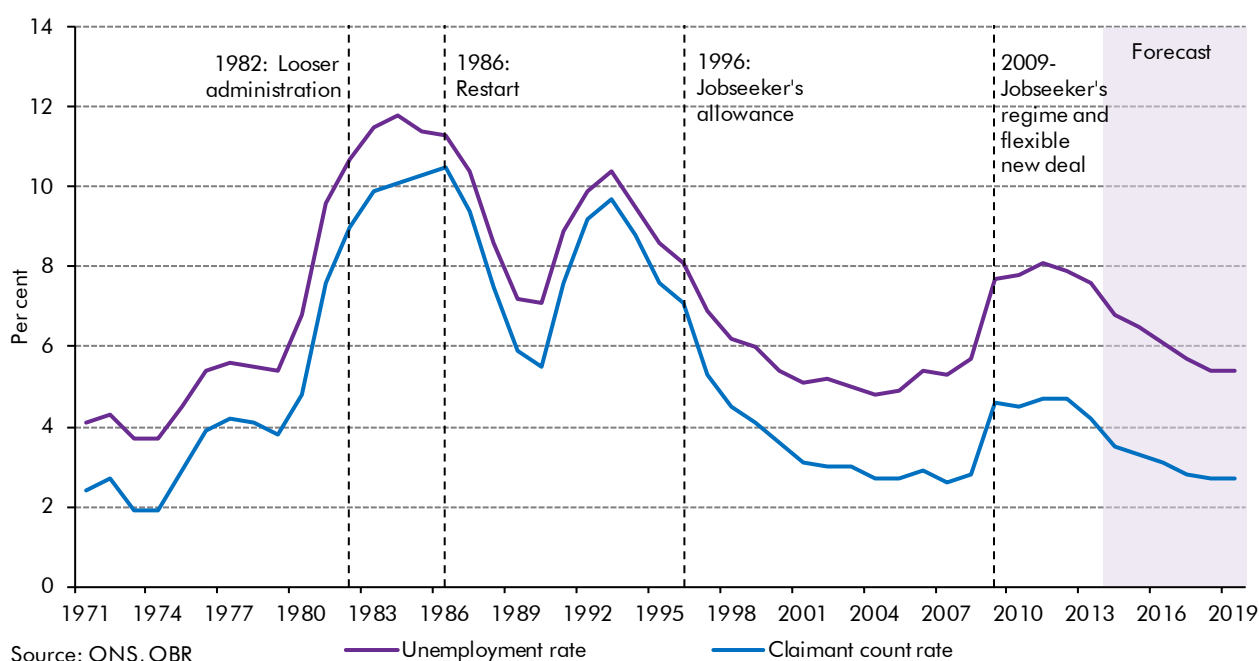
Changes in caseloads

Economic factors

- 8.6 Spending on unemployment benefits is closely linked to the cyclical position of the economy. Box 4.1 presented estimates of the sensitivity of different benefits to the economic cycle, with JSA spending and caseloads found to be the most sensitive. This is consistent with the figures in Table 8.1, which show that changes in the caseload explained most of the fluctuations in spending between cyclical peaks and troughs.
- 8.7 Chart 8.1 shows two measures of unemployment that are relevant to spending on unemployment benefits. The first is the internationally-comparable Labour Force Survey (LFS) measure, which is based on a household survey and aims to measure the proportion of people out of work who are actively seeking employment. This should have a relatively stable relationship with the cyclical position of the economy over time. The second is the administrative claimant count measure, which measures the proportion of people out of work and claiming unemployment benefit, thereby directly measuring the caseload for such benefits. While also closely linked to the economic cycle, this can also be affected by policy and administrative changes, some of which are marked on the chart and discussed below.

8.8 Differences between the LFS and claimant count measures of unemployment partly reflect differences in coverage. For example, the LFS measure captures students looking for part-time work and pensioners that are not entitled to JSA, while the claimant count includes some low earners who are in work but still entitled to JSA. The difference between the two measures also changes over time. Having peaked at similar levels during the early 1990s recession, a gap has opened up since, with the claimant count roughly 1 million below the LFS measure since 2010. As well as coverage differences, this will reflect changes in eligibility for, and take-up of, JSA. These could be affected by many factors, including changes to conditionality or sanctions rules. Box 8.1 looks more closely at recent trends.

Chart 8.1: Measures of UK unemployment and associated policy interventions



Policy interventions

8.9 Over the past 30 years, a number of policy interventions have affected the number and proportion of people claiming unemployment benefits.³ Since 1986, these interventions have tightened conditionality on unemployment benefits, which has been associated with a downward trend in caseloads relative to the adult population.

8.10 Table 8.2 summarises the main policy changes affecting unemployment benefits since the early 1980s. While the cyclical position of the economy appears to be by far the biggest driver of year-to-year changes in the claimant count, policy changes have had a significant effect at different times.

8.11 One recent change that has increased the caseload was the lone parent obligation, which moved people from income support to JSA and increased the number of lone parents

³ See, for example Layard and Nickell (2011) and Van Reenen (2004).

claiming. The share of lone parents in the claimant count has risen from around 1 per cent before its introduction to around 10 per cent now (Chart 8.2).

Chart 8.2: Lone parents on jobseeker's allowance

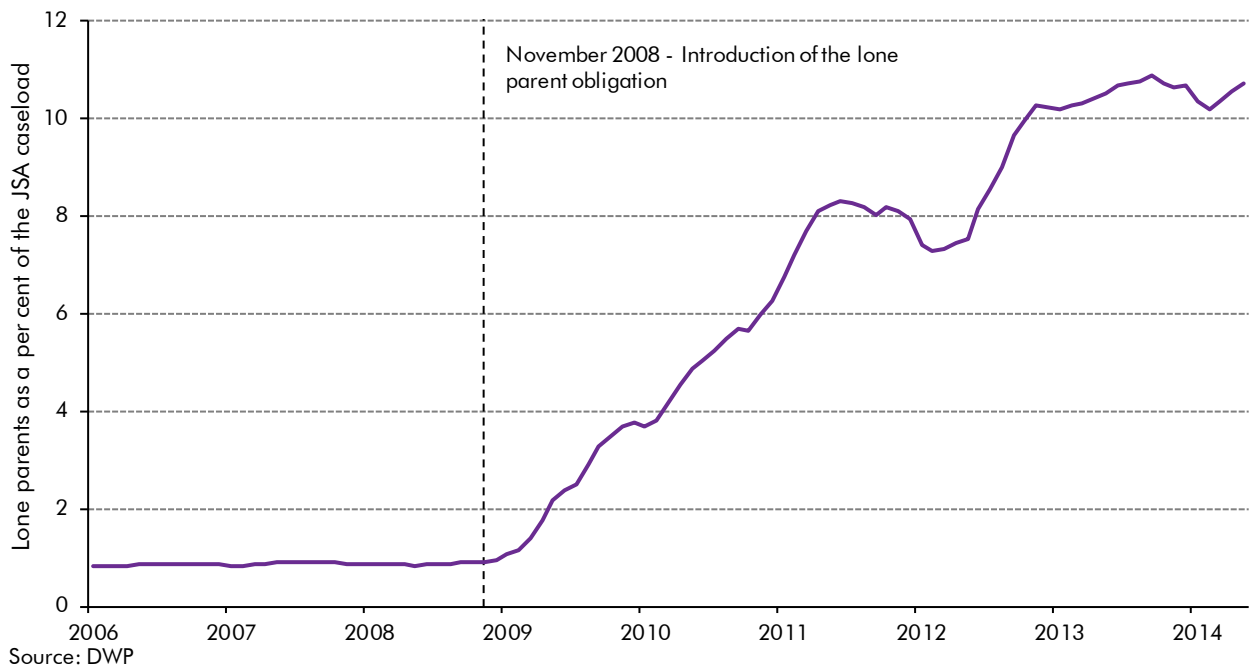


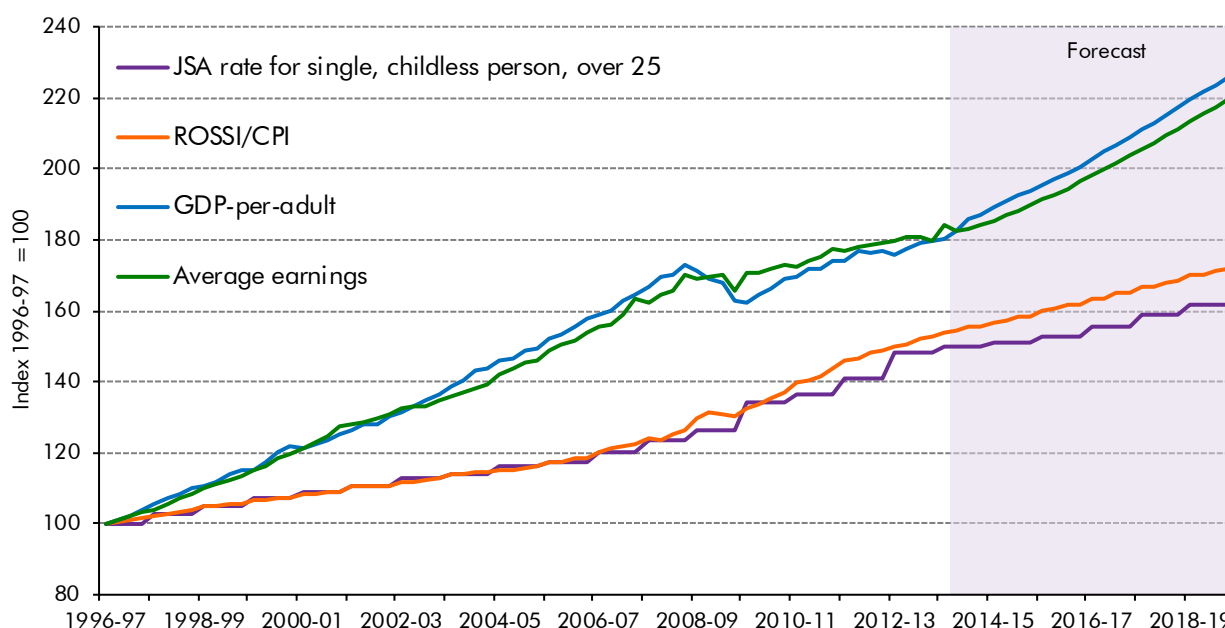
Table 8.2: Policy changes affecting unemployment benefits

Period	Policy change affecting the claimant count
1982 - 1986	Relaxation of rules for claiming unemployment benefits: The increase in unemployment in the early 1980s coincided with a relaxation of the rules for claiming unemployment benefits in 1982, where it was no longer a requirement to visit Jobcentres to receive these benefits.
1986 - 1996	Restart: Policy was tightened through the introduction of 'Restart' in 1986 in which long-term (over a year) and subsequently medium-term unemployed (over 6 months) were invited to an interview at a Jobcentre. This coincided with a fall in unemployment in the context of a broader cyclical improvement in economic conditions. Training for employment: A 1987 white paper - 'training for employment' - announced a variety of other programmes to increase employment, including the new job training scheme, available to those unemployed for over 6 months. Stricter benefit regime: In the 1980s, there was a gradual tightening of conditionality making the benefit regime more strict. An example from the 1989 Social Security Act was the provision that the unemployed could no longer refuse a job on grounds of its unsuitability, without good cause.
1996 - 2009	Introduction of jobseeker's allowance: Jobseeker's allowance was introduced in 1996, further increasing conditionality since claimants would only receive benefit if they had actively been seeking work. Furthermore, in 1998 the new deal for young people and subsequently the new deal 25+ were introduced. These policy changes coincided with a continued fall in unemployment, again in the context of a broader cyclical improvement in economic conditions.
2009 - 2013	Lone parent obligation: The caseload for JSA has been boosted by the lone parent obligation (LPO) moving people from income support to JSA. By the end of 2012-13, there were around 150,000 more lone parents on JSA than there were prior to the introduction of the LPO. Policy changes during the late 2000s recession: JSA was adapted in 2009, with the introduction of the young person's guarantee and the creation of the new jobseeker's regime and flexible new deal, which increased conditionality. Work programme: The flexible new deal was replaced by the work programme, to which claimants are directed for 2 years if they fail to find work in 9 months (claimants aged under 25) or 12 months (claimants over 25). This would be expected to slightly increase caseloads (because the claimant count will include people who were previously on training programmes) and slightly reduce inflows (by no longer counting claimants returning from such training programmes). State pension age changes: The rise in the state pension age for women is increasing the number of older JSA claimants (both women and men are entitled to claim pension credit once they reach the qualifying age, which is linked to the female state pension age). Migration from incapacity benefit to ESA: There is a small effect on the caseload from the migration of cases from incapacity benefit to employment and support allowance, where those found fit for work were expected to move to JSA in the first instance.

Changes in average awards

- 8.12 For most of the period covered in this report, average awards have risen more slowly than earnings and GDP-per-adult (Chart 8.3). This reflects the uprating of unemployment benefits in line with different measures of inflation, which have on average been lower than the growth in GDP-per-adult. Between 1983-84 and 2010-11, unemployment benefits were linked to the ROSSI measure of inflation (RPI less certain housing costs). Since 2011-12, uprating has been linked to CPI inflation, which is typically lower than ROSSI. For the period from 2013-14 to 2015-16, unemployment benefits are being uprated by 1 per cent a year.

Chart 8.3: Relative generosity of unemployment benefits



Source: DWP, ONS, OBR

Unemployment benefits spending in the medium-term forecast

Spending, caseloads and average awards

- 8.13** In our latest medium-term forecast, spending on JSA is forecast to fall from £4.4 billion (0.27 per cent of GDP) in 2013-14 to £3.2 billion (0.16 per cent of GDP) in 2018-19. This is driven by reductions in the caseload – in absolute terms and relative to the adult population – and by average awards rising more slowly than GDP-per-adult. That reflects the decision to uprate JSA by 1 per cent until 2015-16 and then to return to uprating by CPI inflation thereafter, both of which are lower than our forecast for growth in GDP-per-adult.
- 8.14** The main economic forecast judgement driving our JSA forecast is the pace at which spare capacity in the economy – the output gap – closes. This judgement informs our forecast of the speed with which LFS unemployment falls to our estimate of its steady-state rate of 5.4 per cent. But an additional judgement needs to be made about how the claimant count will evolve relative to the LFS measure of unemployment. In our March 2014 forecast, we assumed that this ratio would continue to fall in the near term before stabilising through the remainder of the forecast. As Box 8.1 explains, the latest data mean that this judgement will need to be revisited in our December 2014 *Economic and fiscal outlook*.

Table 8.3: Jobseeker's allowance spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	5.2	4.4	3.7	3.4	3.3	3.2	3.2
Caseload (million)	1.51	1.29	1.13	1.06	0.99	0.93	0.90
Average annual award (£ thousand)	3.4	3.4	3.3	3.2	3.3	3.4	3.5
Forecast in the context of total welfare spending							
Per cent of total welfare spending	2.4	2.1	1.7	1.6	1.5	1.4	1.3
Forecast relative to the economy							
Spending (% of GDP)	0.33	0.27	0.21	0.19	0.18	0.16	0.16
Caseload (% of adults)	3.0	2.5	2.2	2.1	1.9	1.8	1.7
Average award (% of GDP-per-adult)	11.1	10.6	9.7	9.3	9.3	9.2	9.1

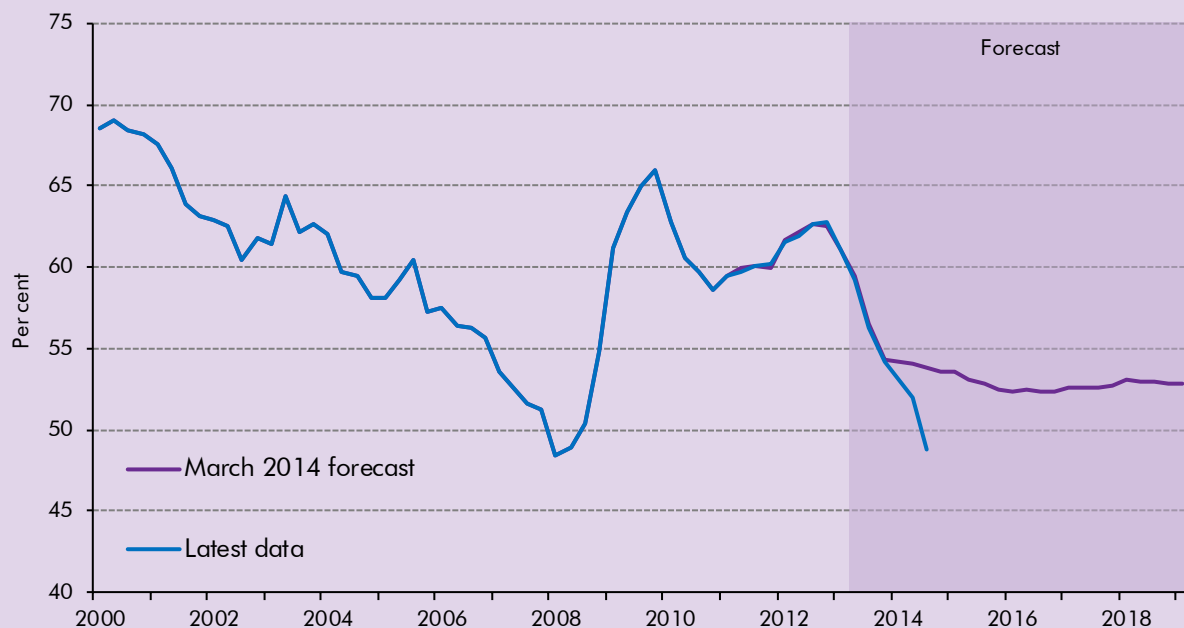
Key risks to the forecast

- 8.15** With volatility in the caseload responsible for most of the variation in spending on unemployment benefits from year-to-year, it is clear that the main risk to our spending forecast is related to the cyclical position of the economy. If the output gap were to close faster or slower than we expect, that would be likely to feed through to the JSA forecast.
- 8.16** The claimant count has fallen by 17.5 per cent relative to the level known when we completed our March 2014 forecast. It moved below 1 million in August 2014 – a level we had not expected it to reach until 2017 – having fallen at a faster rate over the past year than at any time since 1973. This suggests we will need to revise down our forecast of spending on jobseeker's allowance significantly in our December forecast.
- 8.17** The JSA forecast is consistent with the substantial gap between the LFS and claimant count measures of unemployment being stable in proportional terms over the forecast period. But as Box 8.1 describes, the gap has increased by more than expected in recent months. Even if our latest output gap and LFS unemployment forecasts were to prove correct, any changes in the ratio of the claimant count to LFS unemployment would affect the JSA forecast.

Box 8.1: The ratio of JSA claimants to LFS unemployed

The labour market has continued to perform better than we expected this year. Growth in real GDP has mainly reflected rising employment, with little contribution from productivity growth. The Labour Force Survey (LFS) measure of unemployment has therefore fallen faster than our March 2014 forecast suggested. The fall in JSA claimants has exceeded our forecast by even more, pushing the ratio of the claimant count to LFS unemployment well below the level implied by our March forecast (Chart A).

Chart A: Ratio of claimant count to LFS unemployment



Source: ONS, OBR

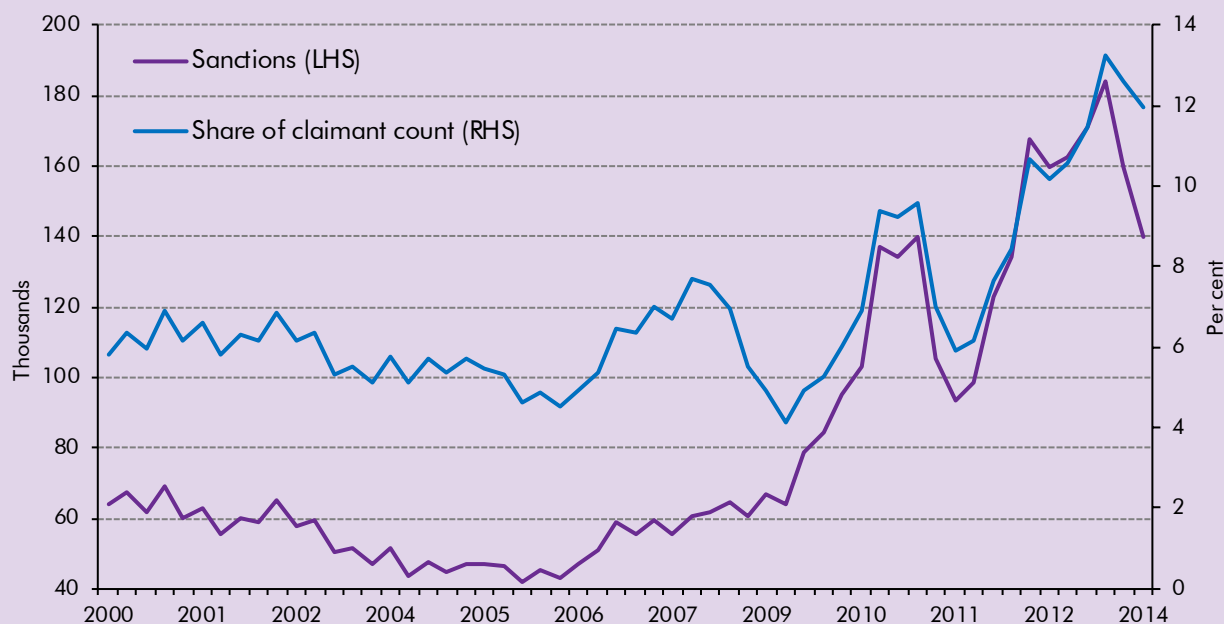
Between its recent peak in November 2012 and July 2014, the number of LFS unemployed fell by 474,000 while the claimant count fell by 573,000. This is despite the level of LFS unemployment having been 916,000 higher in November 2012. The claimant count fell by 36 per cent over the period compared to 19 per cent for LFS unemployment.

The main driver of the sharp fall in the claimant count has been a drop in the rate of inflows. In November 2012, 0.6 per cent of the working-age population moved into the claimant count. The rate had fallen by a third to only 0.4 per cent in August 2014. A rise in the rate of outflows also played a role. In August 2014, 24.5 per cent of claimants moved off the claimant count compared to 19.6 per cent in November 2012. The increase in the outflow rate from LFS unemployed to employment has been smaller than that in the outflow rate from the claimant count to employment. This suggests that a disproportionate share of people moving into employment from unemployment were previously on the claimant count.

The reduction in the rate of inflows could partly be the result of a new JSA sanctions regime, the set of penalties applied when people break the rules they have to keep to receive their benefit. In October 2012 – just before the claimant count ratio started falling – the Department for Work and Pensions introduced a stricter three-step sanction system. A first failure to comply with the

JSA rules results in sanctions broadly in line with the previous system. But second and subsequent failures result in harsher sanctions.^a Neither the level nor the rate of sanctions has increased dramatically since October 2012 (Chart B), but the existence and perception of the new regime may have deterred some unemployed people from applying for JSA. That would push down the claimant count ratio.

Chart B: Total jobseeker's allowance sanctions



Source: DWP, ONS, OBR

Another potential reason for the fall in the claimant count ratio is labour market inactivity, which has fallen faster than expected. Between November 2012 and July 2014, labour market activity increased by 435,000, with some previously discouraged workers likely to have started looking for work as labour market conditions improved. If any of these people who are newly active in the labour market did not move into employment, but also did not move onto JSA, it would hold LFS unemployment up relative to the claimant count.

The recent unexpected fall in the claimant count ratio has also partly coincided with a rise in the number of people claiming incapacity benefits. Since August 2013, the number of claimants has risen by 70,000. But even if there were a direct link with the falling claimant count, this would only explain a small part of the 390,000 fall over the same period.

^a See DWP (2013c)

Long-term projection of unemployment benefits spending

- 8.18 Our 2014 *Fiscal sustainability report* contained long-term projections for unemployment benefits spending to 2063-64. The projections show spending remaining broadly flat as a share of GDP beyond our medium-term forecast.
- 8.19 Our long-term projections reflect the assumption that LFS unemployment remains constant at our estimate of the steady-state NAIRU⁴ of 5.4 per cent. We assume awards rise in line with earnings rather than prices. The projections therefore show that demographic factors are not expected to drive changes in spending on JSA as a share of GDP. But due to the effect of demographics on state pensions, spending on unemployment benefits is expected to fall as a share of total welfare spending.
- 8.20 Assuming no policy changes, the key sensitivities for spending on unemployment benefits in the long term are the structural rate of unemployment and the rate at which awards are uprated. A higher or lower NAIRU would feed through to the caseload relative to the adult population. If awards were uprated by less than earnings growth, spending would be expected to fall as a share of GDP.

Table 8.4: Jobseeker's allowance long-term spending projections

	Forecast		Projections				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP	0.3	0.2	0.2	0.2	0.2	0.2	0.2
Per cent of welfare spending	2.2	1.4	1.4	1.2	1.2	1.1	1.1

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis, consistent with our 2014 *Fiscal sustainability report* projections.

⁴ Non-accelerating rate of unemployment.

9 Spending on support for housing costs

- 9.1 In this chapter, rather than group benefits by the type of recipient, our main focus is on housing benefit. This is the third largest item of welfare spending covered in this report. It is relatively unusual in that recipients of some out-of-work benefits who rent their homes receive housing benefit automatically ('passporting'), but the income from other out-of-work benefits is normally low enough to make recipients eligible for it in any event. Another difference in this chapter is that our analysis is based on a per-household decomposition rather than the per-adult approach used in other chapters.
- 9.2 Reforms to housing benefit – and to the benefits system more widely – have increased the cost of another element of the welfare system: discretionary housing payments. But the funding of these payments was recently transferred to departmental budgets, so it lies outside the definition of welfare spending on which we are focused, even though these are cash transfers. Another housing-focused element of the welfare system that has recently been changed is council tax benefit. Financing of this support has been transferred to local councils as council tax support and therefore also lies outside the spending envelope analysed in this report. So this chapter focuses on housing benefit, but briefly describes the past behaviour of discretionary housing payments and the former council tax benefit.¹

Housing benefit

- 9.3 Housing benefit is an income-related benefit to help households pay their rent. It is available to people on low incomes – from benefits or work – who rent their homes in the private- or social-rented sectors. Unlike many benefits, there is no set amount paid to an individual for housing benefit. The amount received depends on a measure of 'eligible' rent – local housing allowance rates in the private sector – and other household circumstances. These include household income, whether there are any non-dependants, whether there is a spare room in the home, and the age and disability status of those in the household.
- 9.4 Spending on housing benefit forms a large part of the welfare bill. In 2013-14, it was estimated at £23.9 billion, 11 per cent of total welfare spending. That included £23.5 billion from the Department for Work and Pensions (DWP) annually managed expenditure budget and £0.4 billion of housing benefit that was funded directly by local authorities.

¹ The main figures on welfare spending and its drivers used in this report are consistent with data available at the time of our March 2014 *Economic and fiscal outlook*. Spending data cover Great Britain and are drawn from DWP expenditure tables produced at the time of our March EFO.

- 9.5 The Government announced in Autumn Statement 2013 that jobseeker's allowance spending – and associated housing benefit spending – would not be subject to the welfare cap, as they were identified as *“the most cyclical elements of welfare”* that *“allow the automatic stabilisers to operate”*.² That means that £3.2 billion of the DWP-funded housing benefit paid in 2013-14 would lie outside the welfare cap, with the remaining £20.3 billion lying within – 17 per cent of spending that will be subject to the welfare cap from 2015-16.³ Box 4.1 confirms that housing benefit outside the cap is far more sensitive to the economic cycle than housing benefit inside the cap, although both are cyclically sensitive to a degree.

Trends in housing benefit spending

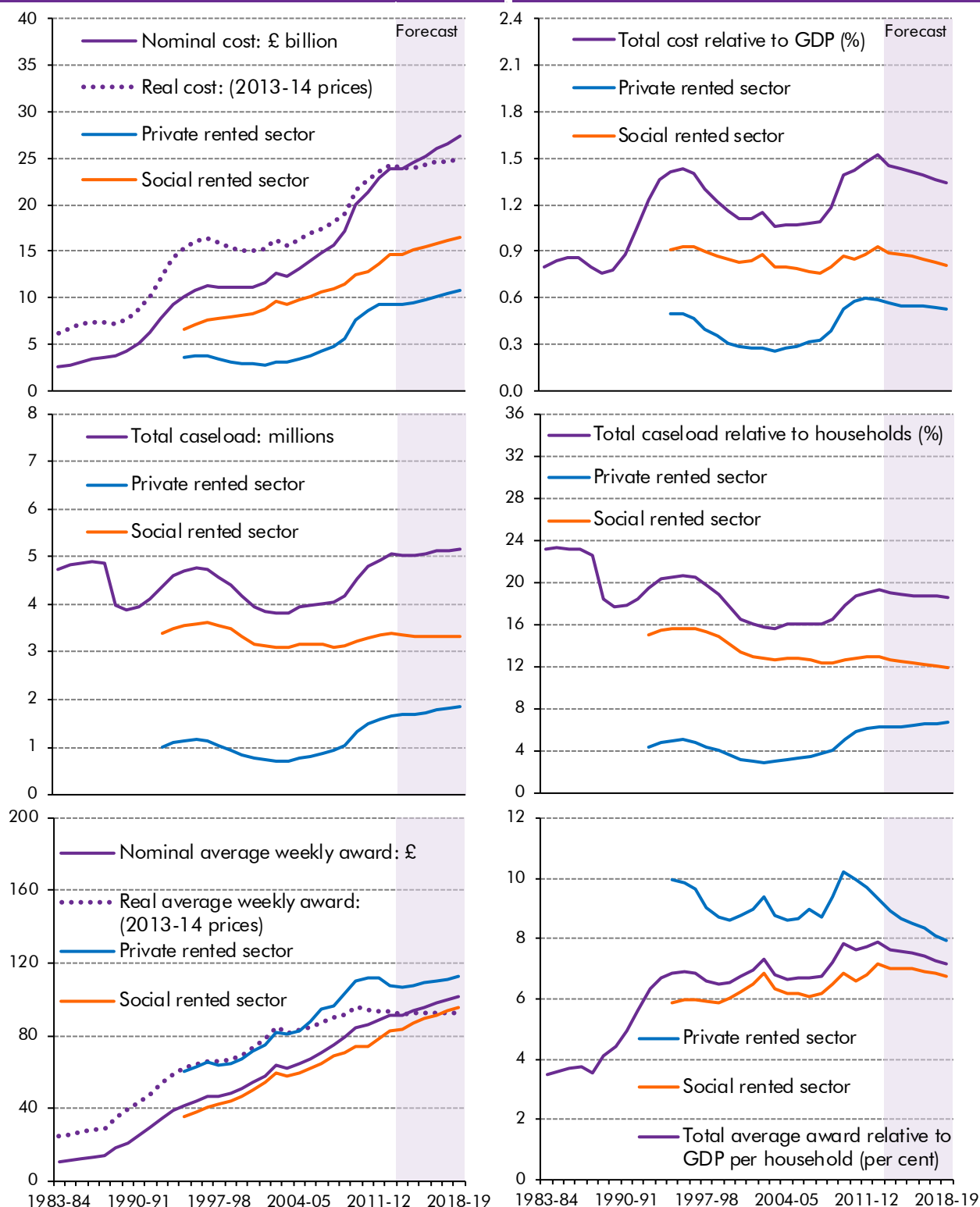
- 9.6 Housing benefit spending increased from 0.8 per cent of GDP in 1983-84 to 1.5 per cent of GDP in 2013-14 (Figure 9.1). Spending on housing benefit has fluctuated with the economic cycle, but on a generally upward trend over time. Housing benefit for those claiming unemployment benefits tends to rise and fall with the economic cycle, while housing benefit for other groups has tended to rise during downturns and then plateau during recoveries. Since the early 2000s, the share of spending accounted for by the private-rented sector has risen.
- 9.7 Spending on some elements of housing benefit is closely associated with spending on other benefits discussed in preceding chapters. If you are claiming an income-related benefit, such as income support (Chapter 7), income-based jobseeker's allowance (Chapter 8), income-based employment and support allowance (Chapter 6) or the guarantee credit element of pension credit (Chapter 5), and are living in rented accommodation, then you are automatically entitled to housing benefit. As of May 2014, people in receipt of these income-related benefits made up 63 per cent of the total housing benefit caseload. We return to some of these trends later.

² HM Treasury (2013).

³ A further £0.4 billion of housing benefit in 2013-14 was funded directly by local authorities. That spending will not be subject to the welfare cap, but not for the reasons of cyclicity set out in HM Treasury (2013).

Figure 9.1: Housing benefit: key facts

Average weekly award (2014-15)		Total cost (2013-14)	
	£ per week	£ billion	
Average weekly award - total	93.99	23.9	Per cent of GDP
Average weekly award - social rented sector	87.03	11.4	Per cent of total welfare spending
Average weekly award - private rented sector	107.66	17.4	Per cent of welfare cap (capped only)



Source: DCLG, DWP, ONS, OBR

- 9.8** The increase in spending on housing benefit between 1983-84 and 2012-13 has been driven by average awards, which have typically risen faster than GDP-per-household. Caseloads relative to the total number of households have generally risen and fallen with the economic cycle.
- 9.9** Table 9.1 shows the main rises and falls in spending as a per cent of GDP since 1983-84, and in our latest medium-term forecast. The main changes have been:
- **1988-89 to 1995-96:** spending increased. Deregulation of the private-rented sector in 1988 led to increased average awards, while the early 1990s recession led to an increase in caseloads, in particular for those on income-related benefits;
 - **1995-96 to 2000-01:** a fall in spending driven by the cyclical strength of the economy and policy changes restricting eligible rent levels for housing benefit;⁴
 - **2000-01 to 2007-08:** a small decline in spending, reflecting strength in the wider economy, partially offset by a shift in the caseload from the social- to the private-rented sector. The proportion of households renting started to rise during this period;
 - **2007-08 to 2012-13:** a rise in spending over the late 2000s recession driven by very weak nominal GDP growth, higher caseloads, and rising average awards relative to GDP-per-household. The proportion of households renting in the private sector increased further, continuing the shift in the caseload to the private-rented sector; and
 - **2012-13 to 2018-19:** an expected fall in spending in our medium-term forecast. Reforms to the private- and social-rented sector cut spending, while GDP growth is forecast to be stronger than in recent years. These factors more than offset a continued – but slower – rise in the proportion of households renting in the private sector.

Table 9.1: Drivers of changes in housing benefit spending

	Per cent of GDP					
	1983-84 to 1988-89	1988-89 to 1995-96	1995-96 to 2000-01	2000-01 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	0.80	0.76	1.43	1.12	1.09	1.52
Spending at end of period	0.76	1.43	1.12	1.09	1.52	1.34
Change	-0.05	0.68	-0.32	-0.03	0.43	-0.18
<i>of which:</i>						
Caseloads	-0.18	0.11	-0.31	-0.02	0.28	-0.04
Private-rented sector			-0.17	0.04	0.24	0.03
Social-rented sector			-0.14	-0.06	0.04	-0.07
Average awards	0.13	0.57	-0.01	-0.01	0.15	-0.14
Private-rented sector			-0.05	0.00	0.02	-0.09
Social-rented sector			0.04	-0.01	0.13	-0.05

⁴ For instance, the introduction of the shared room rate in 1996.

Changes in caseloads

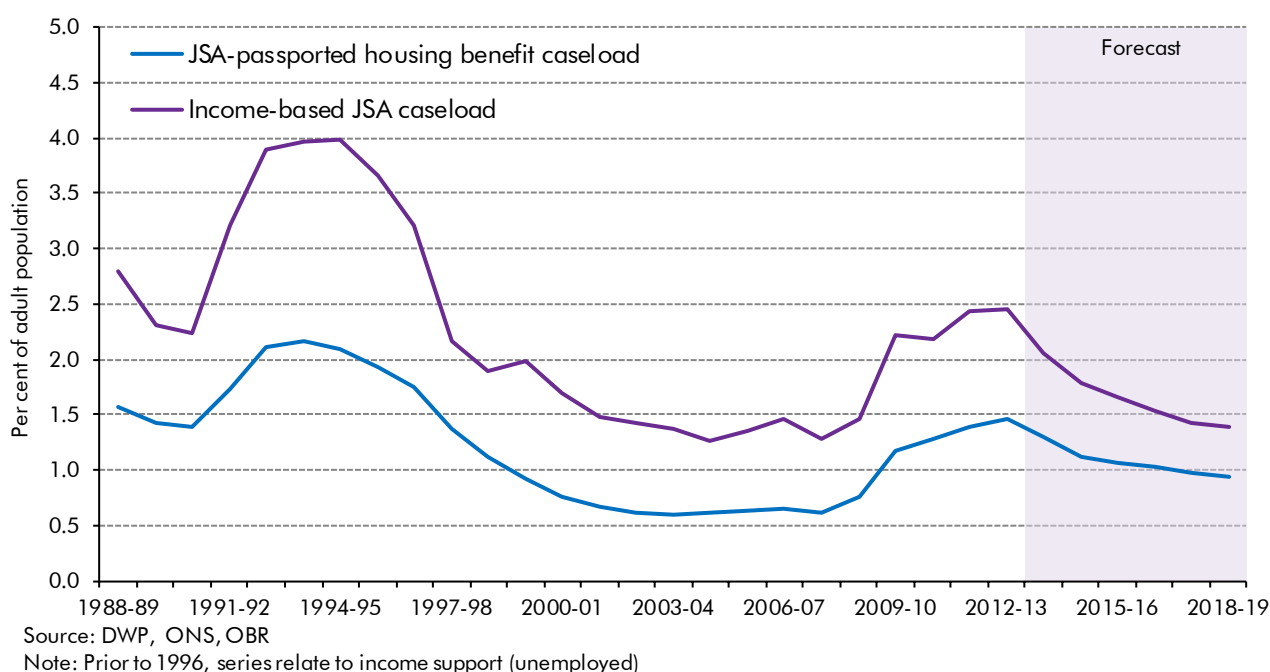
9.10 The three main drivers of changes in the caseload as a proportion of total households are:

- the economic cycle – particularly for the caseload linked to jobseeker's allowance;
- housing tenure and the earnings of the renting population; and
- trends in other benefits closely associated with housing benefit.

Economic cycle

9.11 As shown in Box 4.1, spending on housing benefit is sensitive to the economic cycle. The rise and fall in spending over the economic cycle can in part be explained by fluctuating spending on those claiming 'passporting benefits', notably income-based jobseeker's allowance, due to changes in employment status. This explains, for instance, a large part of the increase in housing benefit spending in the early 1990s. Chart 9.1 shows how the numbers of people claiming income-based unemployment benefits and jobseekers claiming housing benefit follow a similar trend over the economic cycle.

Chart 9.1: Unemployment benefit and passported housing benefit caseloads



Housing tenure and the renting population

9.12 Trends in housing tenure are discussed in Chapter 3. Most important for housing benefit has been the rise in the proportion of households in the private-rented sector since 2003-04, which gathered pace through the crisis (Chart 9.2). Increases in the total caseload have been driven by an increase in the number of claimants in the private-rented sector. Since the late 2000s recession, the weakness of real earnings has overlaid this trend, so that there are

Spending on support for housing costs

more people renting and more renters receiving support with their rent. These trends are illustrated in Chart 9.3.

Chart 9.2: Housing benefit caseloads by tenure

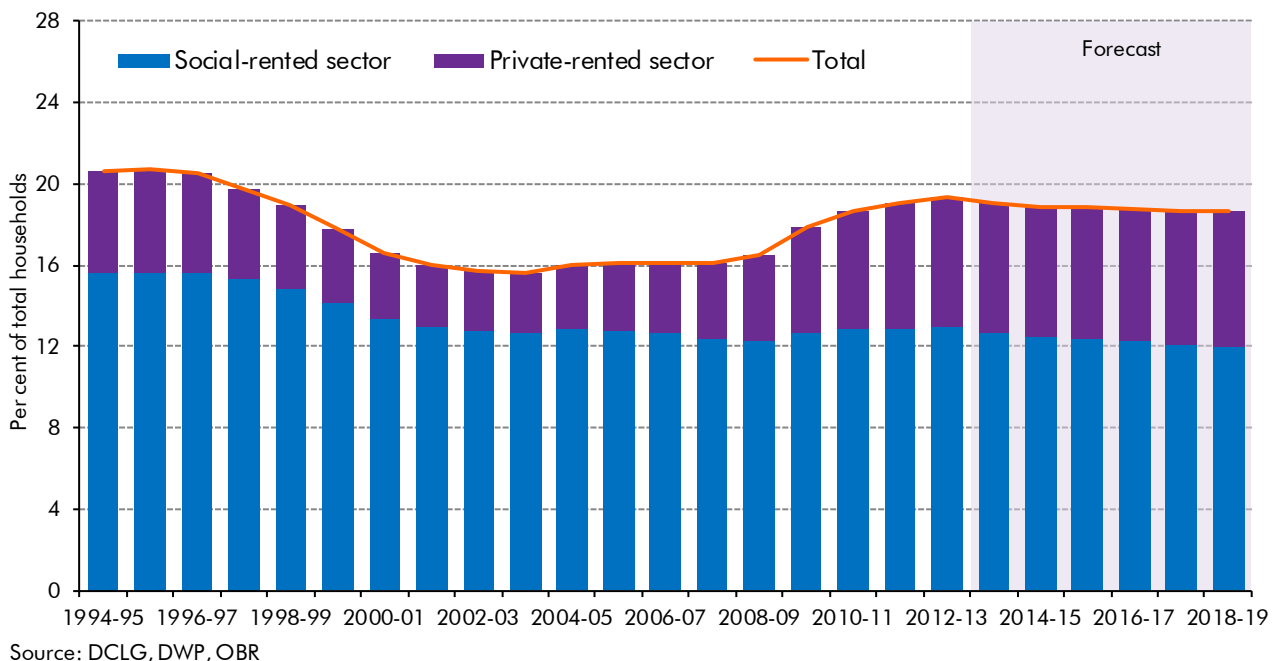
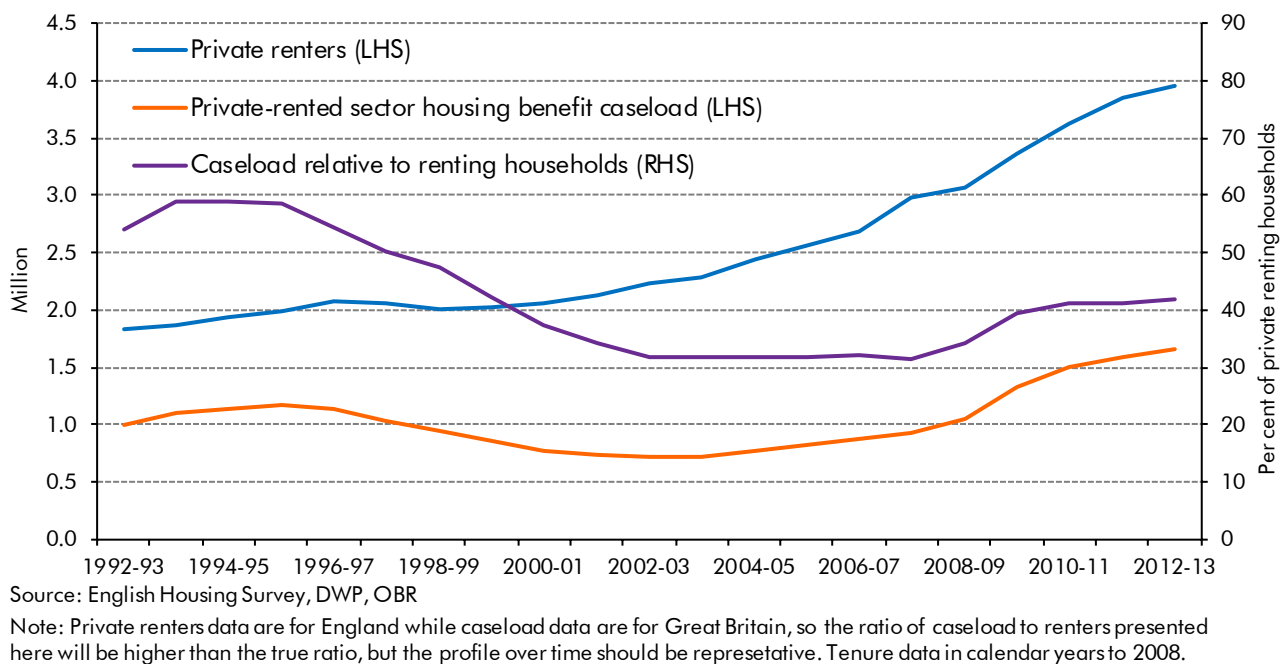


Chart 9.3: Private-rented sector housing benefit indicators

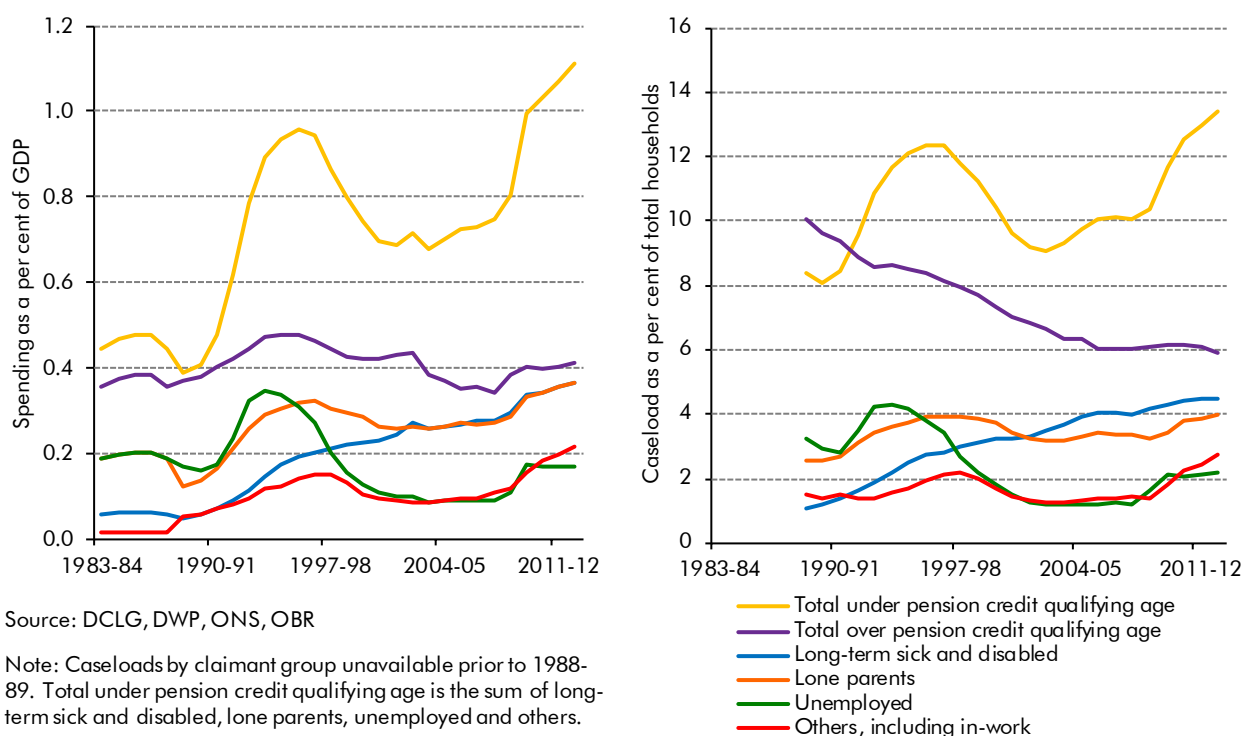


Other benefits associated with the housing benefit caseload

9.13 Drivers of trends in other benefits were discussed in preceding chapters. Changes in the caseloads for these benefits are important drivers of the housing benefit caseload.

- 9.14 When looking at housing benefit by claimant type (Chart 9.4), the most striking trends have been in the working-age groups. There has been a continued rise among those classed as long-term sick or disabled – driven by trends in incapacity and disability benefits. Caseloads for claimants aged over the pension credit qualifying age have fallen, partly due to higher home-ownership rates among older people, as well as growth in pensioner incomes.

Chart 9.4: Housing benefit spending and caseloads by claimant group



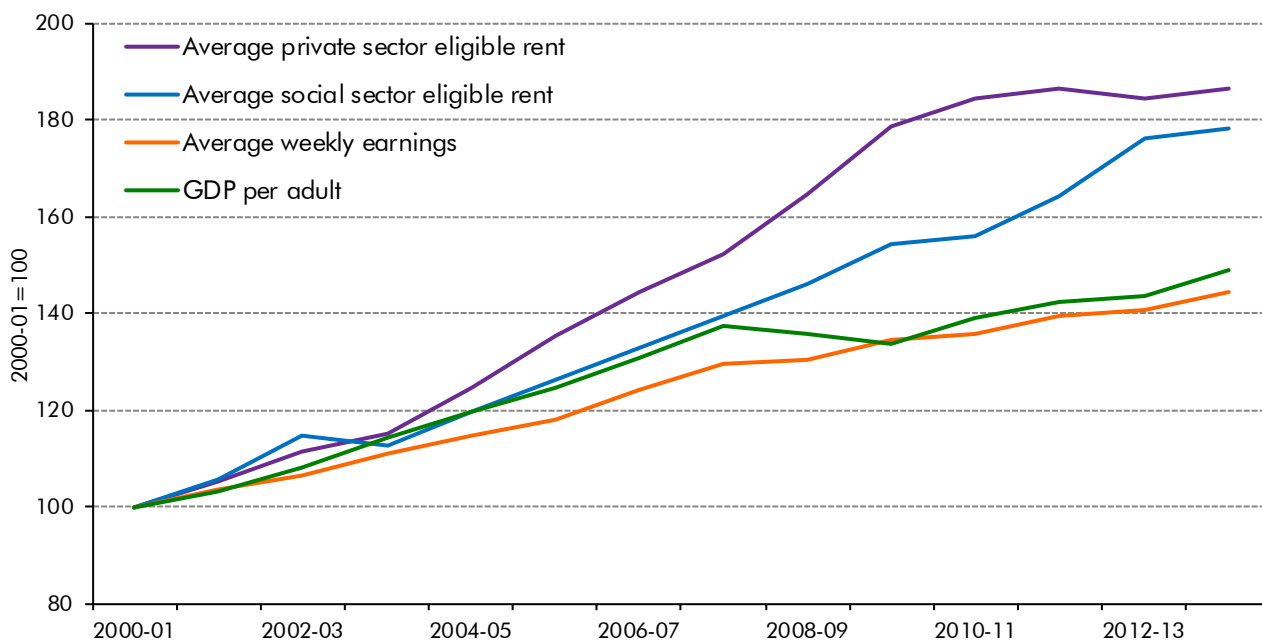
Changes in average awards

- 9.15 The main drivers of average awards are economic and policy drivers of rents and the composition of the caseload.

Rents

- 9.16 The Housing Act 1988 deregulated the private-rented sector. Alongside rising social rents and declining investment in social housing, this meant average awards and spending rose sharply in the early 1990s. This also coincided with the early 1990s recession, when there was an increase in spending on those claiming unemployment benefits.
- 9.17 Chart 9.5 uses administrative housing benefit data to show how rents – particularly private-sector rents – have risen faster than average earnings since 2000. The gap has widened since the late 2000s recession. This has combined with the compositional shift in housing benefit to the private-rented sector to push up housing benefit spending.

Chart 9.5: Rents and earnings growth

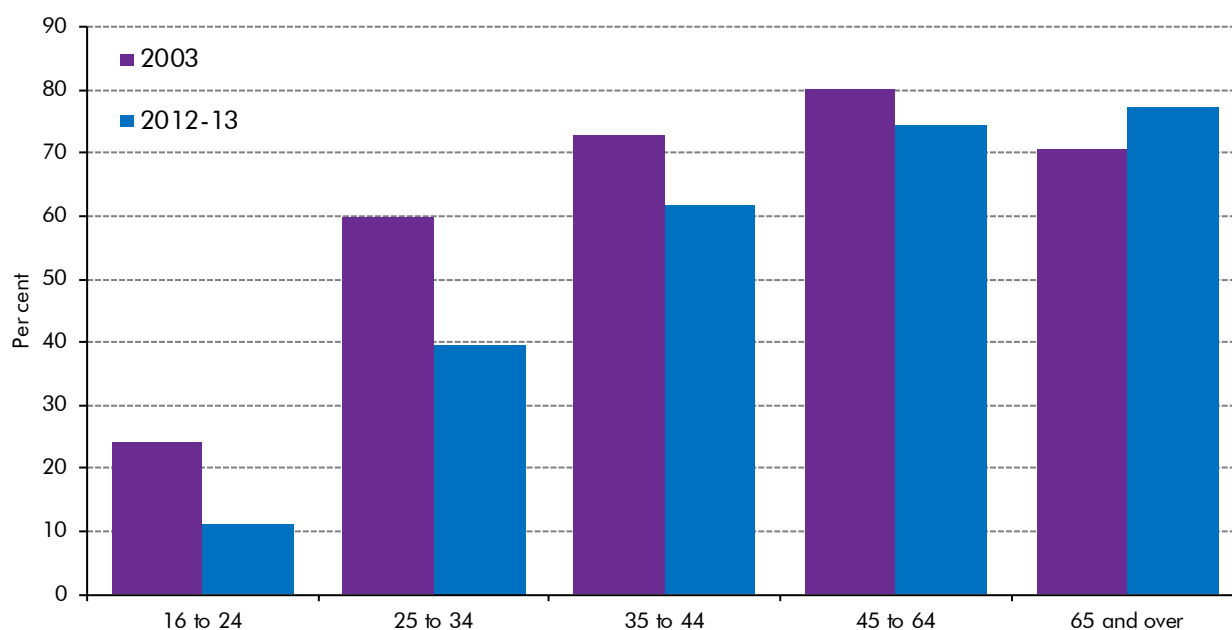


Source: DWP, ONS

Composition of the caseload

9.18 Average awards have also risen – in absolute terms and relative to GDP-per-household – due to changes in the composition of the caseload. As house prices have risen relative to incomes, and particularly following the tightening of lending conditions since the financial crisis, home-ownership rates have declined (see Chapter 3). The shift towards renting has been particularly pronounced among younger people (Chart 9.6). With a relatively fixed social housing stock, much of this increase has been in the private sector, where rents and average awards are typically higher. Among 25 to 34-year olds, the proportion living in the private-rented sector doubled over the decade to 2012-13 to reach 45 per cent.

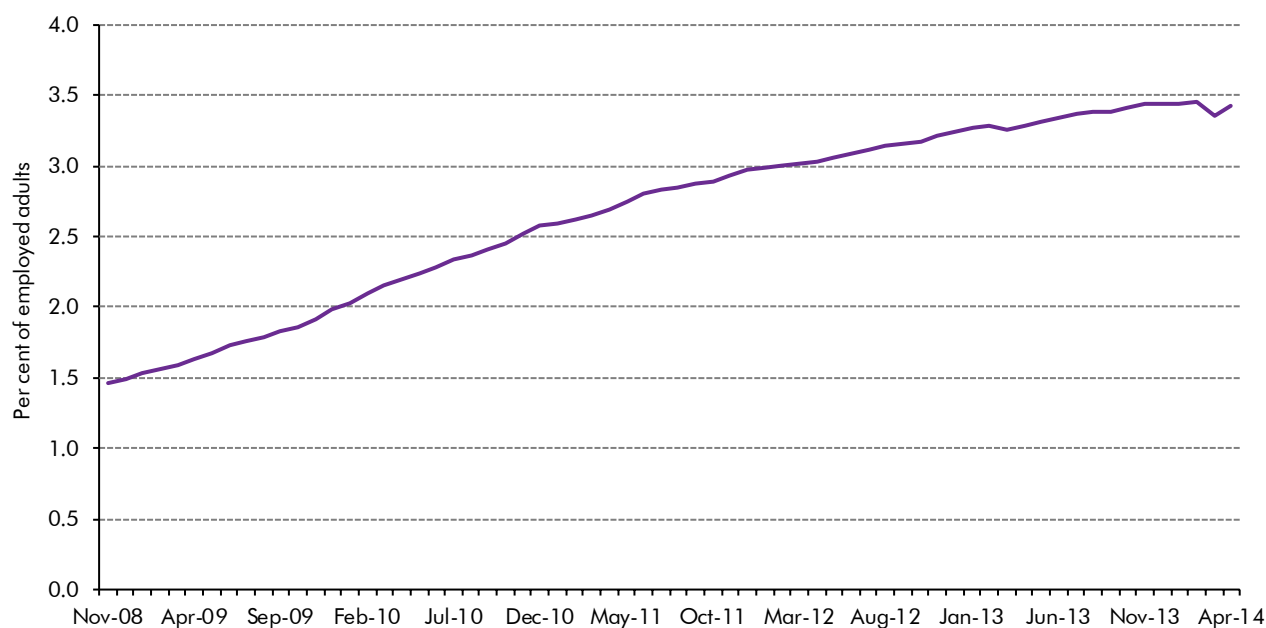
Chart 9.6: Owner-occupation rates by age group: 2003 and 2012-13



Source: English Housing Survey, Survey of English Housing, ONS, OBR

9.19 One trend that has been apparent in recent years – and that helps explain why we have underestimated housing benefit spending in our recent forecasts – is the growing number of claimants that are in employment. As Chart 9.7 shows, the rise from 0.4 million at the end of 2008 to 1.1 million by mid-2014 means that the proportion of employed adults that are claiming housing benefit has more than doubled to around 3½ per cent.⁵

Chart 9.7: Housing benefit claimants in employment

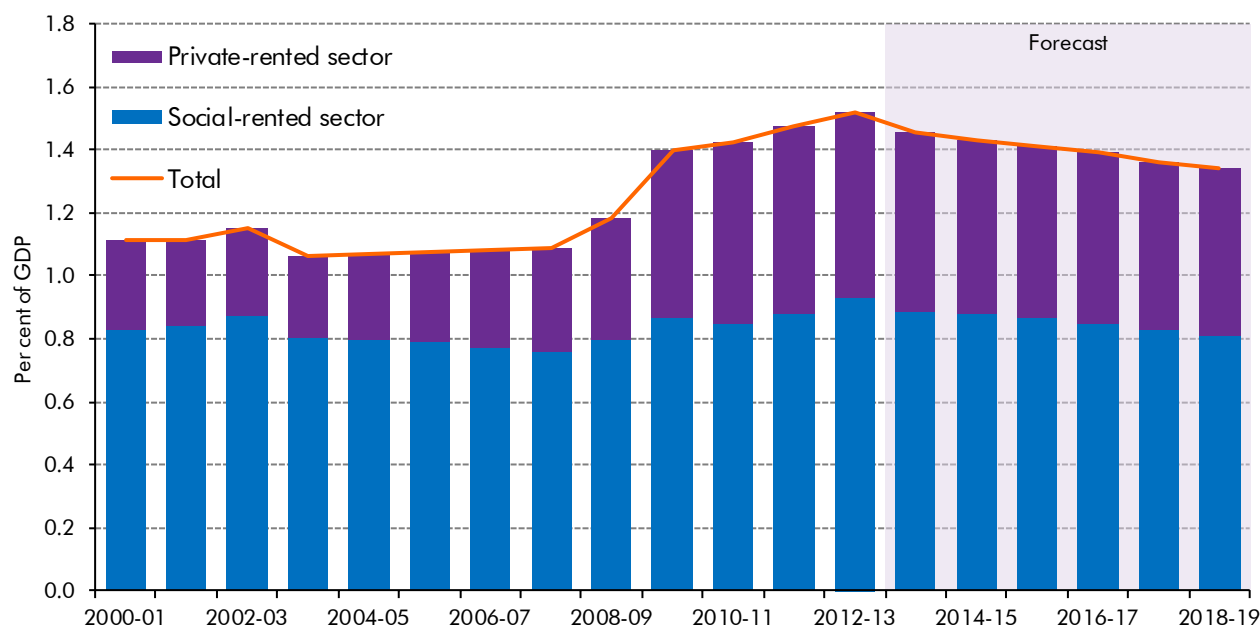


Source: DWP, ONS, OBR

⁵ See, for example, National Housing Federation (2014).

9.20 These trends mean that a greater proportion of people are living in the private-rented sector (where rents are higher on average than in the social sector) and, more recently, that a greater proportion of renters have been receiving housing benefit. As a result, spending on recipients in the private-rented sector has doubled from 0.28 per cent of GDP in 2002-03 to 0.59 per cent in 2012-13. Housing benefit in the social-rented sector has been broadly flat.

Chart 9.8: Housing benefit spending by tenure



Source: DWP, ONS, OBR

Housing benefit spending in the medium-term forecast

9.21 Housing benefit is a challenging benefit to forecast, due to its interactions with a wide range of other benefits as well as with developments in the labour market and housing market. Our caseload forecast is constructed on the basis of judgements that we take about other driver benefits and judgements specific to the 'housing benefit only' group.⁶ This process delivers a forecast made up of 10 separate and mutually exclusive caseload groups.⁷ Average awards are applied to each of these caseloads to reach an overall spending forecast. These reflect our forecast judgements about housing tenure, employment growth and rent inflation, which are then related to the latest administrative data on claims.

Housing benefit forecast assumptions

9.22 Table 9.2 sets out the main tenure and rent assumptions associated with our latest housing benefit forecast. It shows that:

⁶ This 'housing benefit only' caseload is described as 'only' in DWP data because recipients are not also in receipt of another DWP benefit. From the broader perspective of welfare spending, such claimants will typically receive some income from tax credits and, if they have children, will also receive income from child benefit.

⁷ These groups form a hierarchy, so that, for example, a claimant that was both a lone parent and in receipt of incapacity benefits would be counted in the incapacity caseload group (see Table 9.4).

- the proportion of households renting continues to rise, but at a slower pace than in recent years. This reflects our judgement that age-specific owner-occupation rates will start to pick up as the labour market strengthens and access to finance becomes easier as the financial system continues to heal. Beyond our forecast horizon, our assumptions are consistent with a stable owner-occupation rate; and
- recent reforms to both private- and social-sector rents are expected to reduce growth in housing benefit average awards and spending in the forecast period. Local housing allowance rates have been capped at the 30th percentile of local rent rather than the median rent since 2011.⁸ For two years from 2014-15, local housing allowance rates will be uprated by 1 per cent rather than CPI inflation. These policies reduce spending growth in the private-rented sector, where we would otherwise expect amounts paid to rise broadly in line with earnings. Reforms to reduce average awards in the social-rented sector include the Government's removal of the 'spare room subsidy'.

Table 9.2: Housing benefit-related forecast assumptions

	Forecast				
	2014-15	2015-16	2016-17	2017-18	2018-19
Proportion of households renting (per cent, calendar years)					
Working age	40.4	40.8	41.3	41.7	42.0
Pensioners (excl. residential care)	21.9	21.8	21.4	21.2	21.1
Total	35.2	35.5	35.7	35.8	36.0
Private sector rent growth (percentage change on a year earlier)					
Local housing allowance	1.8	1.7	2.1	2.1	2.1
Regulated (RPI + 0.8 per cent)	4.0	3.3	4.1	4.5	4.6
Non-LHA deregulated	1.2	1.2	1.2	1.2	1.2
Social sector rent growth (percentage change on a year earlier)					
Local authorities	5.4	3.0	3.3	3.3	3.4
Regulated social landlords	4.0	2.9	3.2	3.2	3.3

Spending, caseloads and average awards

9.23 On the assumptions set out above, our latest medium-term forecast shows spending continuing to rise slowly in cash terms, with lower spending on jobseekers offset by rising spending on those in work. Spending is expected to rise more slowly than GDP, reducing it from 1.5 per cent of GDP in 2013-14 to 1.3 per cent by 2018-19 (Table 9.3).

⁸ See DWP (2013).

Table 9.3: Housing benefit spending forecast

	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	23.9	23.9	24.6	25.3	26.1	26.6	27.4
Inside the welfare cap	19.9	20.3	21.3	22.1	22.9	23.5	24.2
Outside the welfare cap	3.6	3.2	2.8	2.8	2.8	2.7	2.7
Locally funded	0.4	0.4	0.5	0.5	0.5	0.5	0.5
Caseload (million)	5.1	5.0	5.0	5.1	5.1	5.1	5.2
Average annual award (£ thousand)	4.7	4.7	4.9	5.0	5.1	5.2	5.3
Forecast relative to welfare spending							
Per cent of total welfare spending	11.2	11.4	11.5	11.6	11.6	11.5	11.6
Per cent of welfare cap spending ¹	17.1	17.4	18.1	18.5	18.7	18.9	19.1
Forecast relative to the economy							
Spending (% of GDP)	1.5	1.5	1.4	1.4	1.4	1.4	1.3
Inside the welfare cap	1.3	1.2	1.2	1.2	1.2	1.2	1.2
Outside the welfare cap	0.2	0.2	0.2	0.2	0.1	0.1	0.1
Locally funded	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Caseload (% of households)	19.3	19.3	19.3	19.3	19.3	19.3	19.3
Average award (% of GDP-per-h'hold)	7.9	7.6	7.6	7.5	7.4	7.3	7.2

¹ Spending within the cap only.

9.24 Table 9.4 provides the decomposition of our latest forecast into the 10 claimant groups on which it is based. The 14½ per cent rise in cash spending on housing benefit between 2013-14 and 2018-19 is largely explained by:

- a 39 per cent rise in the 'housing benefit only' caseload. Based on recent trends, we assume that renters will account for 100 per cent of net employment growth and that 38 per cent of those employed renters will receive housing benefit. As a result, in-work 'housing benefit only' claimants are expected to rise by around 0.4 million over the forecast period, more than explaining the overall rise in the housing benefit caseload;
- a 22 per cent rise in spending on the incapacity benefit-related caseload, which largely reflects higher average awards; and
- smaller contributions from caseload-driven growth in housing benefit spending on the disabled and carers.

9.25 Slightly offsetting these sources of higher spending are:

- caseload-driven falls in spending on housing benefit for those on jobseeker's allowance – as unemployment is expected to fall; and
- a caseload-driven fall in housing benefit for pensioners on income-related benefits – as the rising pension credit qualifying age and other factors reduce the number of people eligible for the driver benefits relative to the adult population.

Table 9.4: Housing benefit forecast by claimant group

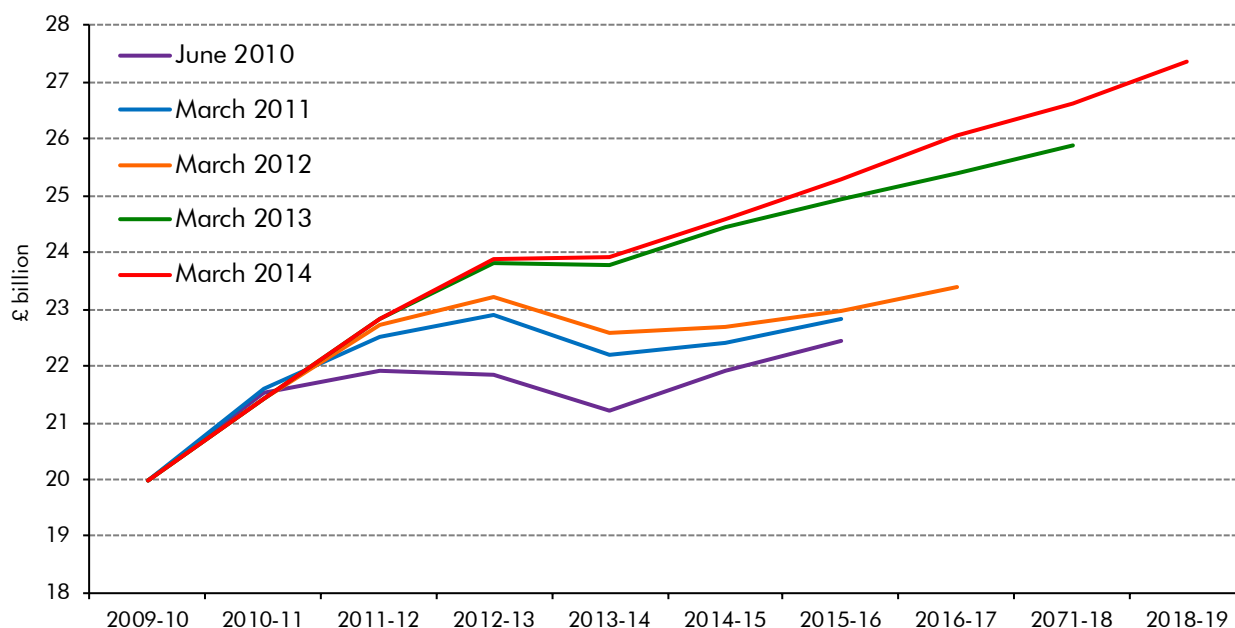
	Outturn	Forecast					
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	23.9	23.9	24.6	25.3	26.1	26.6	27.4
Jobseekers	3.6	3.2	2.9	2.8	2.8	2.7	2.7
Incapacity benefits	6.1	6.2	6.6	6.9	7.1	7.3	7.5
Lone parents	2.8	2.5	2.5	2.5	2.6	2.6	2.6
Carers	0.6	0.7	0.8	0.9	0.9	1.0	1.1
Other IRB ¹ - pensioners	0.6	0.5	0.4	0.3	0.3	0.2	0.2
Other IRB ¹ - working-age	4.7	4.8	4.8	4.8	4.8	4.8	4.8
Disabled	0.2	0.3	0.3	0.3	0.4	0.4	0.4
Bereaved	0.0	0.0	0.0	0.0	0.0	0.0	0.0
State pension	1.0	1.0	1.1	1.2	1.2	1.2	1.3
Housing benefit only	4.3	4.7	5.1	5.5	5.9	6.3	6.7
Caseload (million)	5.1	5.0	5.0	5.1	5.1	5.1	5.2
Jobseekers	0.7	0.7	0.6	0.5	0.5	0.5	0.5
Incapacity benefits	1.3	1.3	1.3	1.3	1.4	1.3	1.4
Lone parents	0.5	0.4	0.4	0.4	0.4	0.4	0.4
Carers	0.1	0.1	0.2	0.2	0.2	0.2	0.2
Other IRB ¹ - pensioners	0.1	0.1	0.1	0.1	0.1	0.0	0.0
Other IRB ¹ - working-age	1.1	1.1	1.0	1.0	1.0	0.9	0.9
Disabled	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Bereaved	0.0	0.0	0.0	0.0	0.0	0.0	0.0
State pension	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Housing benefit only	0.9	1.0	1.1	1.1	1.2	1.3	1.4
Average annual award (£ thousand)	4.7	4.8	4.9	5.0	5.1	5.2	5.3
Jobseekers	4.9	4.8	5.0	5.1	5.3	5.4	5.5
Incapacity benefits	4.8	4.8	5.0	5.1	5.2	5.4	5.5
Lone parents	6.0	5.9	6.1	6.2	6.4	6.5	6.7
Carers	4.8	4.8	5.0	5.1	5.2	5.4	5.5
Other IRB ¹ - pensioners	4.9	5.0	5.2	5.4	5.7	5.8	6.1
Other IRB ¹ - working-age	4.3	4.5	4.7	4.9	5.0	5.1	5.2
Disabled	4.5	4.5	4.6	4.7	4.8	5.0	5.0
Bereaved	4.7	4.7	4.9	5.1	5.3	6.3	6.5
State pension	3.3	3.5	3.6	3.6	3.7	3.9	4.0
Housing benefit only	4.8	4.8	4.8	4.8	4.8	4.8	4.8

¹ Income-related benefits

Key risks to the forecast

- 9.26** Our forecasts for housing benefit have, on average, underestimated spending. In the four Budget forecasts we made for spending in 2012-13, the average forecast error was a £1.0 billion or 4.3 per cent underestimate. These errors have reflected both higher-than-expected caseloads – particularly among the ‘housing benefit only’ group and among those also receiving incapacity benefits – and higher-than-expected average awards.

Chart 9.9: Successive OBR housing benefit forecasts since June 2010



Source: DWP, OBR

9.27 The most substantial errors have been associated with the 'housing benefit only' caseload group, for whom eligibility is not associated with the receipt of other benefits. This caseload has risen by 44 per cent between 2010-11 and 2013-14 and we expect it to rise by another 39 per cent by 2018-19. The errors here have been associated with three inter-related developments in the economy:

- the rise in the share of the population renting has continued at a faster pace than expected, perhaps associated with house prices remaining high relative to incomes and reduced post-crisis supply of high loan-to-value and loan-to-income mortgages;
- employment growth has been much stronger than expected, but earnings growth has been much weaker, so that the number of people in work but earning sums that would leave them eligible for housing benefit has been higher than expected; and
- rent inflation, as measured by the housing benefit administrative data, has been higher than expected. This interacts with subdued earnings to increase the eligible population further.

9.28 We have revised our forecasts to reflect this evidence, but significant uncertainties remain. The relevant judgements underpinning our latest forecast are:

- that the proportion of households renting will rise more slowly and eventually stabilise. There are risks in both directions. The prevalence of renting might continue to rise as house price inflation outstrips earnings growth and the Mortgage Market Review affects mortgage availability at higher loan-to-value or loan-to-income ratios. Conversely, as the financial system continues to heal and Government schemes like

Help to Buy support borrowing at higher loan-to-value ratios, the decline in homeownership of recent years could begin to reverse;

- that productivity growth will start to pick up, leading to stronger earnings growth and slower employment growth. Relative to our March 2014 forecast, employment growth has continued to surprise on the upside and earnings growth to the downside; and
- that measures of rent inflation relevant to the housing benefit forecast will remain higher than average earnings growth until 2014-15, and lower thereafter. The average awards used in this report reflect variations in rents across regions and housing benefit tenures, with the difference between the highest and lowest average award more than 350 per cent.⁹ As such, there is considerable scope for regional variations and changes in the composition of the caseload to push average rents above or below forecast. Moreover, data on rent inflation at the whole economy level are currently being reviewed,¹⁰ adding further uncertainty to the forecast.

Long-term projection of housing benefit spending

9.29 Our 2014 *Fiscal sustainability report* contained long-term projections for housing benefit spending to 2063-64. The projections show spending falling slightly as a per cent of GDP beyond our medium-term forecast.

9.30 Our housing benefit projections are based on assumptions for the number of households and house ownership. We assume that the average household size will remain broadly constant, and that the proportion of owner-occupiers will stabilise soon after the end of our medium-term forecast. Spending on housing benefit falls by 0.2 per cent of GDP, from 1.4 per cent in 2018-19 to 1.2 per cent in 2063-64. This largely reflects rising home-ownership rates for pensioners due to cohort effects – newly-retired pensioners groups have higher home-ownership rates than the oldest pensioners, which all else equal means fewer newly-retired pensioners are eligible for housing benefit.

9.31 Our spending projections would be sensitive to changes in assumptions about average household size and the proportion of households renting rather than owning their home. Due to the effect of demographics on state pensions, spending on housing benefit is expected to fall as a share of total welfare spending.

Table 9.5: Housing benefit long-term spending projection

	Forecast		Projections				
	2013-14	2018-19	2023-24	2033-34	2043-44	2053-54	2063-64
Per cent of GDP	1.5	1.4	1.3	1.3	1.3	1.3	1.2
Per cent of welfare spending	11.8	11.9	11.3	10.2	9.8	9.2	8.6

Note: Figures for 2013-14 and 2018-19 presented on a UK-basis, consistent with our 2014 *Fiscal sustainability report* projections.

⁹ Based on DWP Stat-Xplore data on average weekly awards by local authority and tenure in May 2014. These ranged from a low of £51 a week in the social-rented sector in Moray to a high of £233 a week in Westminster.

¹⁰ See ONS (2014).

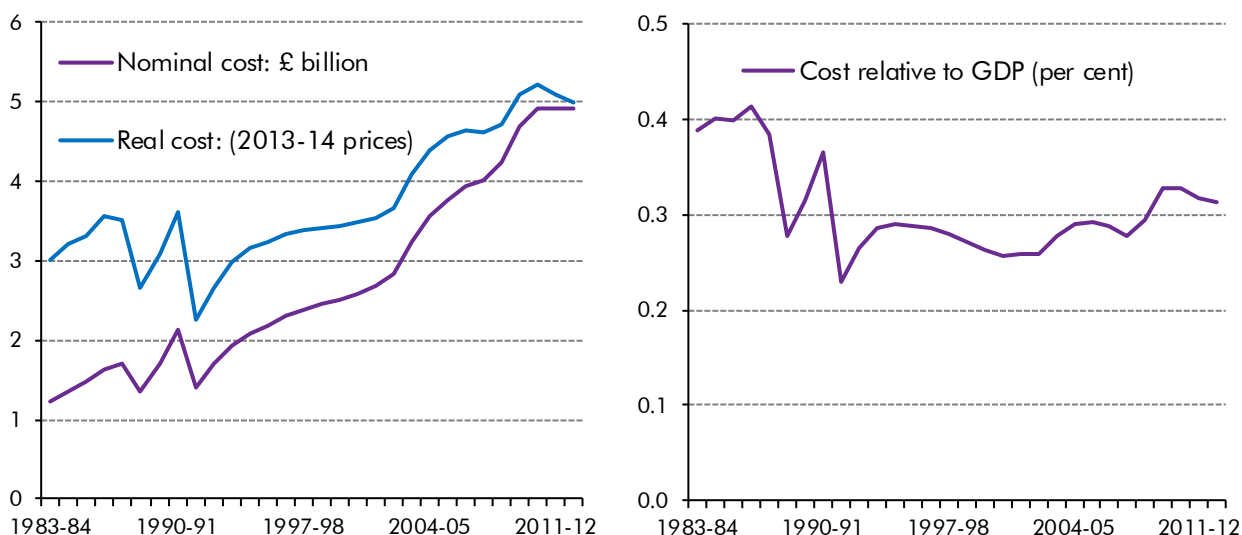
Discretionary housing payments

- 9.32** Discretionary housing payments provide extra money to people when their council decides that they need further help to meet housing costs. The funding for these payments was transferred to departmental budgets at the same time as the welfare cap was introduced, so it lies beyond the scope of welfare spending covered in this report.
- 9.33** The central government contribution to discretionary housing payments has increased significantly to allow local authorities to provide additional support to those affected by the Government's welfare reforms, including the removal of the 'spare room subsidy' and local housing allowance reforms.¹¹ Government spending on discretionary housing payments has increased from £20 million in 2010-11 to an estimated £180 million in 2013-14.

Council tax benefit and council tax support

- 9.34** Council tax benefit was an income-related benefit payable to families on low income to assist with the costs of council tax. In 2012-13, there were 5.9 million recipients of an estimated £4.9 billion of council tax benefit. As Chart 9.10 shows, spending on predecessors to council tax benefit fell as a share of GDP during the 1980s. From 1991-92 onwards, council tax benefit spending increased slightly faster than GDP – rising from 0.23 per cent of GDP at the start of the period to 0.31 per cent of GDP in 2012-13.

Chart 9.10: Council tax benefit spending



- 9.35** From April 2013, council tax benefit was abolished, with support switched to being funded locally as part of council tax support.¹² This now forms part of our local government forecast, so is not a component of the welfare spending covered in this report or subject to the welfare cap. There is significant overlap between the housing benefit and council tax support caseloads, suggesting the drivers of housing benefit spending discussed in this chapter will be likely to be relevant for local authorities' spending on council tax support.

¹¹ DWP (2014b)

¹² See, for example, Adam and Browne (2012).

10 Spending on bereaved people

10.1 This chapter covers the following benefits:¹

- bereavement benefits; and
- industrial death benefit.

Bereavement benefits

10.2 Bereavement benefits provide financial support to people on the death of their husband, wife or civil partner. This is generally paid to people below the state pension age. Since 2001, they have consisted of:²

- a one-off, £2,000 tax-free bereavement payment (payable to all); and
- either a bereavement allowance (a regular taxable payment payable for one year, if the claimant is over 45 and has no dependent children);
- or widowed parent's allowance (a regular taxable payment if the claimant has dependent children, payable until entitlement to child benefit ceases).

10.3 Bereavement benefits are non-means tested and contribution based. They cannot be paid alongside overlapping benefits – claimants receive the benefit that pays the highest award.³

10.4 Spending on bereavement benefits is relatively small. It will be subject to the welfare cap. In 2013-14, spending was estimated at £0.6 billion, with the majority paid to working-age female claimants. It is forecast to account for 0.3 per cent of total welfare spending and 0.5 per cent of welfare spending that will be subject to the welfare cap from 2015-16.

Trends in spending on bereavement benefits

10.5 Figure 10.1 shows that spending on bereavement benefits has fallen sharply from 0.25 per cent of GDP in 1983-84 to 0.04 per cent of GDP in 2013-14. It is forecast to fall further over the next five years. The falls have been driven by declining caseloads relative to the adult population, in part reflecting declining mortality rates.

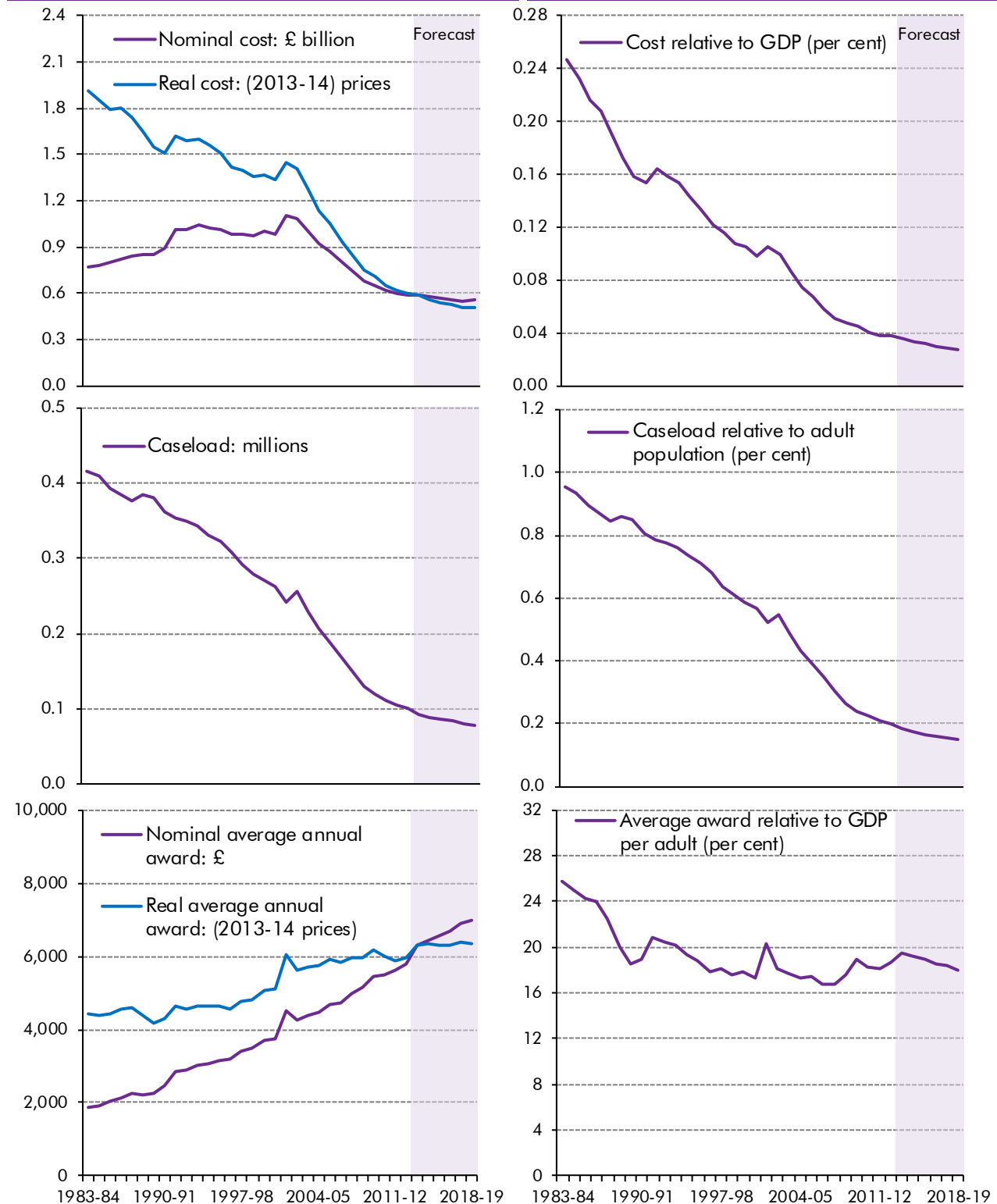
¹ The main figures on welfare spending and its drivers used in this report are consistent with data available at the time of our March 2014 *Economic and fiscal outlook*. Spending data cover Great Britain and are drawn from DWP expenditure tables produced at the time of our March EFO.

² Some claimants are still able to claim elements of the predecessor 'widow's benefits' system (such as widow's pension and widowed mother's allowance).

³ Overlapping benefits include contributory JSA, contributory ESA, incapacity benefit, carer's allowance, severe disablement allowance, maternity allowance and unemployment supplement.

Figure 10.1: Bereavement benefits: Key facts

Current main rates (2014-15)	£	Total cost (2013-14)	
		£ billion	0.58
		Per cent of GDP	0.04
Bereavement payment (one off payment)	2,000	Per cent of total welfare spending	0.3
Average annual award	6,446	Per cent of welfare cap	0.5



Source: DWP, OBR

Table 10.1: Drivers of changes in bereavement benefits spending

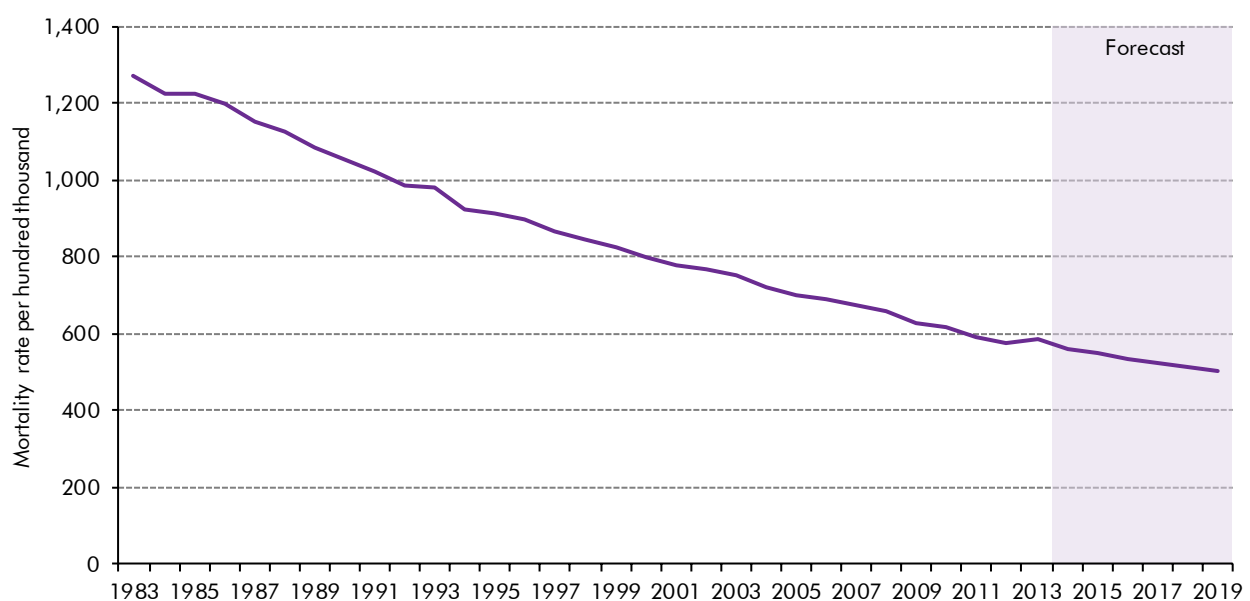
	Per cent of GDP				
	1983-84 to 1989-90	1989-90 to 2001-02	2001-02 to 2007-08	2007-08 to 2012-13	2012-13 to 2018-19
Spending at start of period	0.25	0.16	0.11	0.05	0.04
Spending at end of period	0.16	0.11	0.05	0.04	0.03
Change	-0.09	-0.05	-0.05	-0.01	-0.01
of which:					
Caseloads	-0.02	-0.07	-0.04	-0.02	-0.01
Average awards	-0.06	0.01	-0.02	0.01	0.00

Changes in caseloads

10.6 Table 10.1 shows that spending on bereavement benefits has fallen as a per cent of GDP primarily because of declining caseloads relative to the adult population. This is due in part to social trends and, to a lesser extent, policy. Caseloads were already falling steadily as a share of the adult population prior to policy changes in 1998-99 and 2000-01 that are described below.

10.7 Mortality rates among those below pension age (for which the benefit is payable) have been falling consistently, and this is expected to continue through our medium-term forecast (Chart 10.1). Acting in the opposite direction, the state pension age for women has been rising since 2011-12, reaching 65 by the end of our medium-term forecast (2018-19). So more of the population are below state pension age, which may impact caseload trends. The proportion of the population in married and civil partnered couples has also been falling (Chart 10.2), and is assumed to continue doing so.

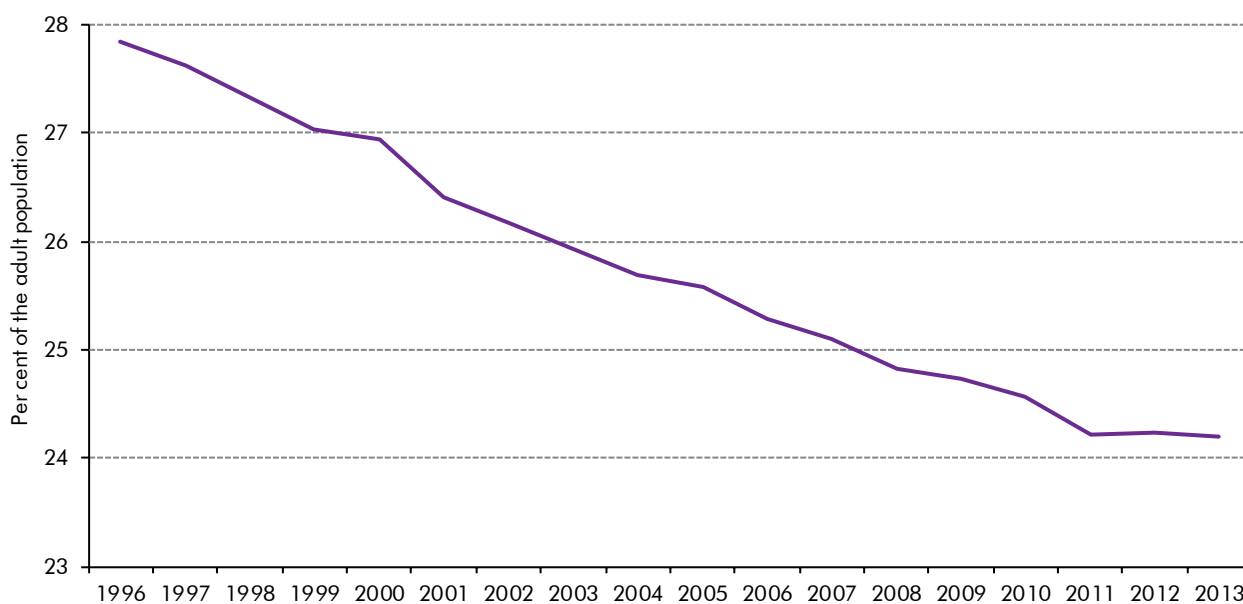
Chart 10.1: Mortality rate for men aged 45 to 65



Source: GAD, ONS

Note: Figures are on a Great Britain basis.

Chart 10.2: Married and civil partnered couples



Source: ONS

Note: Figures are on a United Kingdom basis.

10.8 Policy changes have also reduced caseloads. Reforms in 1998 tightened eligibility for the widow's pension,⁴ while also reducing the value of the widow's allowance and widow's pension.^{5,6} Reforms in 2001 replaced widow's pension with bereavement allowance, reducing the period over which payments were made to one year rather than through to retirement age.⁷ The slight rise in spending and caseload in 2001-02 is attributable to expanding eligibility to male widowers with children.

Changes in average awards

10.9 Average awards increased much more slowly than GDP-per-adult between 1983-84 and 1989-90 (when nominal GDP growth outstripped RPI inflation by a significant margin), and have since fluctuated within a relatively narrow range. The uprating of bereavement benefits has historically been linked to changes in the basic state pension (Chapter 5). But since 2011-12, uprating of bereavement benefits has been linked to CPI inflation, which is less generous than the triple lock.

Bereavement benefits spending in the medium-term forecast

Spending, caseloads and average awards

10.10 In our latest medium-term forecast, spending on bereavement benefits is forecast to be broadly flat in nominal terms and therefore to fall further from 0.04 per cent of GDP to

⁴ The lower age limit for widow's pension was increased from 40 to 45 years.

⁵ Widow's allowance – a regular weekly payment of £57.65 a week paid for 26 weeks, with additional payments for children – was replaced by a single £1,000 tax free lump sum 'widow's payment'.

⁶ 50 to 55 year olds now qualified for a reduced rate of basic pension rather than the full rate.

⁷ Spending on additional pension fell significantly after the 2001 reforms. Previously some widows could claim an additional state pension under widow's pension, but this was no longer the case under bereavement allowance.

0.03 per cent of GDP by 2018-19. This is mainly driven by the continuing fall in caseloads relative to the adult population, overlaid by CPI-linked uprating causing average awards to decline steadily relative to GDP-per-adult.

Table 10.2: Bereavement benefits spending forecast

	Outturn			Forecast			
	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Spending (£ billion)	0.59	0.58	0.57	0.56	0.56	0.55	0.55
Caseload (million)	0.10	0.09	0.09	0.09	0.08	0.08	0.08
Average annual award (£ thousand)	5.8	6.3	6.4	6.5	6.7	6.9	7.0
Forecast in the context of welfare spending							
Per cent of total welfare spending	0.28	0.28	0.27	0.26	0.25	0.24	0.23
Per cent of welfare cap spending	0.51	0.50	0.49	0.47	0.46	0.44	0.44
Forecast relative to the economy							
Spending (% of GDP)	0.04	0.04	0.03	0.03	0.03	0.03	0.03
Caseload (% of adults)	0.20	0.18	0.17	0.17	0.16	0.15	0.15
Average award (% of GDP-per-adult)	18.7	19.5	19.2	18.9	18.5	18.4	18.0

Key risks to the forecast

- 10.11 The Pensions Act 2014 reformed bereavement benefits once again. From 2017-18, the bereavement support payment will be introduced to replace existing bereavement benefits.⁸ The bereavement support payment changes the system, with support focused on the period immediately following bereavement. It also alters the contributory conditions, with a single rule irrespective of age and whether an individual has dependent children. The Government has estimated that the main fiscal impact of the reform is to add £100 million to net benefit related costs in cash terms over the four years from 2017-18. This reform has not yet been subjected to our policy costing certification process at a Budget or Autumn Statement.

Industrial death benefit

- 10.12 Industrial death benefit is part of the wider industrial injuries scheme (see Chapter 6). Industrial death benefit was designed as a benefit for dependents of people who die as a result of an accident at work or of a prescribed industrial disease. Industrial death benefit has been abolished and has not been payable in respect of deaths that occurred on or after 11 April 1988. But widows receiving the benefit before that date continue to receive payments at the same rate as the widowed mother's allowance. In 2013-14, spending on industrial death benefit is estimated to be £31 million, a tiny fraction of total welfare spending. Industrial death benefit is subject to the welfare cap.

⁸ DWP (2014c).

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