

Annexes

Annex B

Defining the low to middle income group

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The Commission's work, and the wider work of the Resolution Foundation, focuses on people living on low to middle incomes, a group that faces unique challenges as a result of their position in the income distribution. People on low to middle incomes are, in many senses, both 'too rich and too poor'. They are too rich to be traditionally considered in need of state support, yet too poor to thrive independently in important private markets, from the housing market to the market for childcare. Similarly, members of the group are mostly in work, and so have limited time, but are often also on low or modest wages, and so have limited money.

For the purposes of analysis, the Resolution Foundation defines this group as people living in households below middle (median) income, but above the bottom ten percent, and not heavily reliant on means-tested benefits. In technical terms, the Resolution Foundation's full definition of people on low-to-middle income is:

adults living in working-age households in income deciles 2-5 who receive less than one-fifth of their gross household income from means-tested benefits (excluding tax credits).

This is an income-based definition (rather than one based on earnings). Individual earnings and household income map onto one another in complex ways. For example, low earning individuals are spread very widely across the household income distribution. Where the Resolution Foundation's work, and the work of the Commission, focuses on earnings, it relies on a proxy of people earning below the median wage, which in gross terms is around £26k per year. More than three quarters of employees living in low to middle income households are in the bottom half of the earnings distribution.

For the purposes of the income distribution the Resolution Foundation uses 'equivalised' household incomes to take account of the importance of different household sizes and compositions. In some cases, where data makes it necessary, a simplified version of the definition is adopted.

The Resolution Foundation defines two other income groups by way of contrast with the low to middle income group:

- A 'benefit-reliant' group, containing people who live in households in the bottom ten percent of the income distribution and/or households that receive more than one fifth of their income from means-tested benefits (excluding tax credits).
- A 'higher income' group, containing those who live in households in the top half of the income distribution.

Defined as above, 10 million working-age adults live in low-to-middle income households in Britain today, making up one third of the working-age population. Because the Resolution Foundation's definition takes into account household size, the income boundaries of the group depend on the number of children living in a household. For example, couples with no children fall into the group if their incomes range from £12,000-£30,000 a year (from all sources), while couples with three children fall into the group if their incomes range from £19,000-£47,000 a year.

Many of the time series data set out in Resolution Foundation research represent series of snapshots. That is, they look at the characteristics of a different group of low to middle income households in each year, rather than tracking the same households over time. This approach gives a good sense of the changing realities of life on a low to middle income in Britain, but it does not track specific households over time.

Around two-thirds (67 per cent) of households on low to middle incomes remain in the group from one year to the next, with one-quarter (24 per cent) moving up and one in ten (9 per cent) moving down. The proportion staying in the group declines to half (54 per cent) after three years and drops again (46 per cent) after five years. This proportion appears to reach a plateau of around one-third (34 per cent) after around ten years however, suggesting that a large proportion of households stay in the group for an extended period.

After ten years around half of previous low to middle income households move up the income ladder, becoming classified as on higher incomes, reflecting life-stage earnings effects. The proportion falling into the benefit-reliant group is largely unchanged over the period with low to middle incomes households as likely to join this group in a year's time as they are in ten years.