

## Press Release

# Poor experience higher inflation than rich

New research undertaken by researchers at the Institute for Fiscal Studies and funded by Consumer Focus reveals that:

- Poorer households have experienced higher inflation on average than richer households over the past decade. This difference has been especially marked since 2008 (during the recession).
- The poorest fifth of households faced an average annual inflation rate of 4.3% between 2008 and 2010, whilst the richest fifth experienced a rate of just 2.7% a year over the same period.
- Pensioners, and in particular those dependant on state benefits, experienced higher rates of inflation than non-pensioners.
- During the period of the recession, dramatic cuts to interest rates reduced mortgage payments, which tend to be more important for richer households. At the same time, the prices of gas, electricity and food increased and this hit poorer households harder on average.

### Inflation rates

Domestic energy prices more than doubled between 2000 and 2010. Poorer households spend on average twice as much, as a share of their expenditure, on energy as richer households. By contrast, mortgage interest rates, which are more important in richer households' budgets, have fallen sharply in recent years. These factors are important contributors to the finding, in a new report from the IFS, funded by Consumer Focus, that poorer households have experienced higher inflation on average than richer households over the past decade. This difference has been especially marked since 2008.

Differences in average household inflation rates are given in Table 1. While over much of the period the inflation rates of the poor and rich were quite similar, larger differences emerged over the period of the recession 2008-10. In these years, dramatic cuts to interest rates reduced mortgage payments, which tend to be more important for richer households. At the same time, the prices of gas, electricity and food increased and this hit poorer households harder on average.

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**Table 1: Average inflation rates**

Income Quintile	Average inflation rates	
	2000-2010	2008-2010
Lowest income	3.3	4.3
2	3.3	3.9
3	3.0	3.4
4	3.0	3.1
Highest income	2.9	2.7
<b>All</b>	<b>3.1</b>	<b>3.5</b>

Source: Authors' calculations from Living Costs and Food Survey  
Notes: Incomes are equivalised using the McClements scale

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Table 2 shows average inflation rates for pensioners and non-pensioners, split according to whether or not they are “benefit dependent” (those for whom benefits make up the largest single component of their income).

- Pensioners, and in particular those dependant on state benefits, experienced higher rates of inflation than non-pensioners;
- Amongst working age households, those who were dependent on benefits experienced higher inflation rates than those who were not.

**Table 2: Average inflation rates by benefit dependency**

	Average inflation rates	
	2000-2010	2008-2010
<b>Working age</b>		
Benefit dependent	3.0	4.0
Not benefit dependent	2.9	2.9
<b>Pensioner age</b>		
Benefit dependent	3.6	4.6
Not benefit dependent	3.4	4.3

Source: Authors’ calculations from Living Costs and Food Survey

To give an indication of what’s been driving these differences, table 3 shows the average budget shares of some selected goods in 2009 (the latest year for which we have spending data) for the poorest and richest households, and the total price changes reported by the Office for National Statistics (ONS) over the period 2000-2010. In 2009 food accounted for nearly a fifth of spending by the poorest 20% of households on average, but only a tenth of spending by the richest 20%. Domestic fuel tends to take up a much greater part of the budget of poorer households – and the price of this more than doubled between 2000 and 2010, while the RPI rose by just over 37%.

By contrast, richer households spent more on things such as mortgage interest and “leisure goods” on average. The prices of these rose less quickly than inflation as a whole. Indeed the price of leisure goods fell quite dramatically over the period.

**Table 3: Budget shares and price changes for selected goods**

	Budget shares 2009			Price Change 2000-2010
	Poorest 20%	Richest 20%	Average	
Food	19.6%	10.1%	14.7%	41.1%
Domestic fuel	9.4%	4.4%	6.5%	117.9%
Mortgage interest	1.7%	8.7%	4.9%	14.2%
Leisure goods	4.1%	4.7%	4.6%	-23.8%
RPI (all items)				37.1%

Source: Authors’ calculations from Living Costs and Food Survey and ONS price data

Research Economist Peter Levell said “Over the past few years relative price changes have tended to hit poorer and older households harder. Of course this pattern may well change in the future, but it does mean that poorer households will have fared worse over the period of the recession than poverty and inequality statistics that don’t account for these differential inflation rates would suggest.”

## Fuel prices going forward

Rises in gas and electricity prices have played a particularly important role in explaining these differentials between rich and poor. To take one year as an example, in 2008, the RPI rose by 4.0% but fuel prices rose by 18.9%. This rise in energy costs added 1.8 percentage points to the average inflation rate experienced by the poorest 20% of households, but just 0.8 percentage points to the rate experienced by the richest 20% in that year.

Looking forwards, the Department of Energy and Climate Change (DECC) projects that real domestic fuel prices will increase over the medium term as a result of trends in commodity prices and government policies aimed at meeting targets for increased use of renewable energy and reducing the UK's carbon emissions. Their central scenario (published in 2010) is that electricity prices will increase by around 15%, and that gas prices will increase by around 20%, in real terms between 2010 and 2015.

Households with different incomes may vary in how they respond to these price changes. Our modelling suggests that the average (median) household in the poorest fifth of the population will reduce fuel consumption by 6% in the face of a 10% fuel price increase (holding all else constant). Amongst the richest fifth, by contrast, we estimate the median response to be unchanged fuel consumption. This suggests that if prices do rise in the future (again holding other things equal), *spending* on fuel will increase on average more for higher income households than for lower income households, but that, at least in the short term, lower income households will heat their homes less.

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Notes to Editors:

1. This analysis was funded by Consumer Focus. The views expressed here are those of the authors and not those of the Institute for Fiscal Studies or Consumer Focus.
2. The paper referenced here is “The spending patterns and the inflation experience of low-income households over the past decade”, by Peter Levell and Zoe Oldfield of the IFS. Please contact Bonnie Brimstone on 020 7291 4818 / [bonnie\\_b@ifs.org.uk](mailto:bonnie_b@ifs.org.uk) for embargoed copies.
3. The method of calculating household level inflation rates is based on the data and approach used to calculate the RPI. However, a number of differences mean that an annual average of our household inflation rates will not in general equal the RPI. A detailed description of our method can be found in the full report.
4. This analysis was carried out using detailed expenditure data from years 2000 – 2009 of the Living Costs and Food Survey (LCFS) and price data published by the ONS. The inflation rates we calculate for 2010 assume that spending patterns have not changed since 2009, as the spending data for 2010 has not yet been released.
5. For queries please contact Bonnie Brimstone at IFS: 020 7291 4800, [bonnie\\_b@ifs.org.uk](mailto:bonnie_b@ifs.org.uk)



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