A tunnel at the end of the light

Charities and the cost-of-living crisis

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PRO BONO ECONOMICS

Summary

Charities and social sector organisations across the country have been a crucial part of our national response to the pandemic, and MPs and policymakers throughout local government believe charities will be crucial to the recovery and to levelling up.

Yet, just as the Covid crisis enters what we hope is its end game, the country is now facing up to a new challenge in the shape of soaring inflation and an accompanying squeeze on incomes. The social sector is already being called upon to once again play its part in helping the country navigate the situation. But after two years of running hot, its ability to fulfil that role is stretched.

The cost-of-living crisis currently unravelling will impact people across the country. Already in the month to March 13, 2022, more than four in five (83%) adults across the UK have reported experiencing an increase in their cost of living. However, lower income households already most severely impacted by the pandemic will bear the brunt.

New analysis of the Bank of England's NMG survey of households shows that, even before inflation began to bite:

- Almost half (46%) of the country's highest income households reported that the pandemic had caused them to increase their savings, while three in 10 (30%) of the lowest income households reported a fall in their savings associated with Covid-19.
- Almost three in 10 (29%) of the lowest income households reported having no savings whatsoever, with more than half (53%) having less than £1,000 to fall back on.
- Two-fifths (42%) of the lowest income households were already concerned about their levels of debt – with nearly one in five (17%) saying they were "very concerned".

- One in six (17%) households reported last autumn that they had faced difficulty keeping up with their housing payments over the previous year due to Covid-19, with one in three (33%) of the lowest income households in this position.
- One in three (35%) of the lowest income households reported needing to cut back on spending in order to pay their rent or mortgage.

Many thousands of charities across the country provide vital support to those households which have felt the financial impact of the pandemic. Not only those charities providing essential goods to those who can't afford them, but those organisations which support individuals to access work, to recover from crime, to deal with mental health difficulties, to overcome housing challenges and many more. These areas of need are likely to grow as the cost-of-living crisis deepens.

It is inevitable that organisations within the sector will step up – they always do. But the capacity of charities and others to meet any surge in requests for help is likely to be constrained by the extent to which they are already running hot having faced elevated demand for much of the last two years. PBE surveys show that more than half (55%) of charities were reporting a Covid-related elevation in demand persisting towards the end of 2021, against a backdrop of funding challenges for a substantial proportion of the sector. Three in four sector leaders polled in October 2021 were already worried about burnout among their managers (76%) and other paid staff (75%), with no end in sight.

There is cause for optimism: social sector organisations are nimble, many have invested in new technology capabilities through the pandemic which will help them scale, and public sentiment towards charities and community action is strong. The response to the outbreak of war in Ukraine and the resulting increase in refugees demonstrates that keenly.

But there is no mistaking the pressure on those organisations key to supporting the lowest income households, who were already in a perilous position before inflation began to escalate. Whether the Chancellor uses the opportunity of the Spring Statement to provide adequate support to those families will be watched carefully throughout the charity sector.

Introduction

Two years on from the beginning of the UK's battle with Covid-19, it is clearer than ever that charities and social sector organisations across the country formed a crucial part of our national response. It is a fact recognised by the public (with three in four saying charities and community groups played an important role in supporting society) and by policymakers (with more than four in five MPs drawing the same conclusion).

With the crisis spawned by the pandemic now subsiding, though not yet ending altogether, the sector will play a similarly key role in the nation's recovery. And not just in the near-term: close to three in four MPs and local councillors believe that charities and community groups will be important in delivering the government's levelling up agenda – a central component of its plans for longer-term renewal across the country.

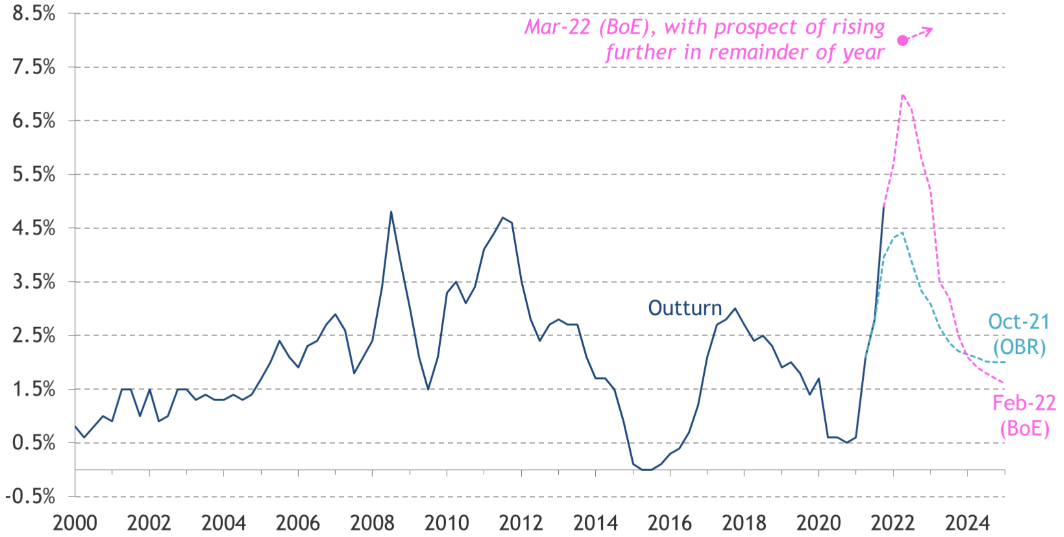
Yet, just as the Covid crisis enters what we hope is its end game, the country is now facing up to a new challenge in the shape of soaring inflation and an accompanying squeeze on incomes. The social sector is already being called upon to once again play its part in helping the country navigate the situation. But after two years of running hot, its ability to fulfil that role is stretched.

The cost-of-living crisis is set to hit hard over the coming months

At the time of the Budget in October, the Office for Budget Responsibility (OBR) projected that CPI inflation would continue to rise over the early part of 2022, peaking at 4.4% in the second quarter of the year. Yet the rate has already surpassed this level, hitting a 30-year high of 5.5% in January. And, as Figure 1 shows, it is now projected to rise further still in the coming months.

Figure 1: Inflation might surpass 8% this year

CPI annual rate (quarterly averages), outturn and selected projections



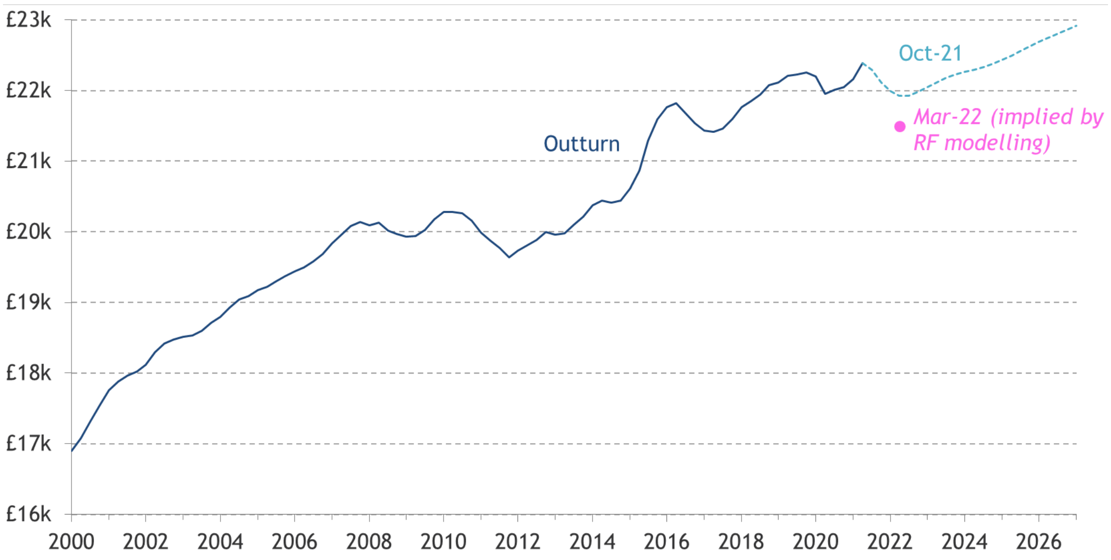
Source: PBE analysis of OBR, *Economic and Fiscal Outlook*, October 2021 and Bank of England Monetary Policy Report, February 2022 and Bank of England, Monetary Policy Summary, March 2022

Reporting in February, the Bank of England suggested that the peak could hit 7%, well above anything seen over recent decades. With the subsequent crisis in Ukraine putting further upward pressure on energy and food costs, the Bank has now stated that inflation is more likely to reach 8% by quarter two, with the potential to go higher still in the latter part of the year.

Even at today's rates, inflation is outstripping pay growth. The increases implied by the Bank of England will therefore only serve to tighten the squeeze on incomes that is already underway. Based on its projection in October of a 4.4% peak in inflation (and taking account of announced government tax and benefit policy), the OBR suggested that average household income would fall by £465 per person over the course of 2022. As Figure 2 shows, incomes were only projected to return to their peaks at the end of 2024.

Figure 2: Average incomes could drop by around £1,000 a year per person on average in 2022

Real household disposable income per capita (four-quarter total), outturn and OBR projection



Source: PBE analysis of OBR, *Economic and Fiscal Outlook*, October 2021; Resolution Foundation, *Catch 22: Spring Statement 2022 preview*, 14 March 2022

With inflation now due to climb at least three percentage points higher than the OBR had previously projected, the depth of the income squeeze and the time taken for recovery to occur will almost inevitably grow. Indeed, the Resolution Foundation has suggested that 2022 will record the largest drop in disposable incomes since the 1970s, roughly doubling the cash loss implied by the OBR's figures.

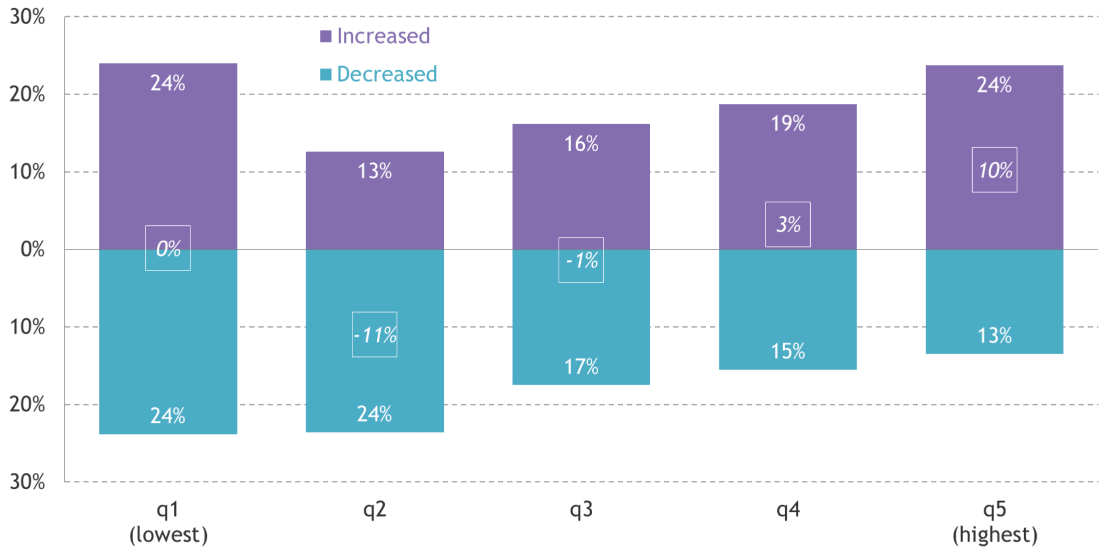
But it will affect some more than others, with many lower income households already hit by the financial effects of the pandemic

A squeeze of this magnitude is of course deeply worrying. But it will play out very differently across households, with lower income groups likely to fare especially badly for a variety of reasons.

For one, lower income households are more likely than higher income households to still be feeling the economic effects of the pandemic. Figure 3 uses Bank of England data from last autumn – before the recent rise in inflation – to consider how household finances were affected by Covid-19 across the income distribution. One in four (24%) households in both quintile one (the poorest fifth) and quintile two (the next poorest fifth) reported a pandemic-related reduction in their income, dropping to one in eight (13%) among households in quintile five (the richest fifth).

Figure 3: Lower income households are more likely to have faced a Covid-related drop in income

Proportion of households saying that their total income has changed as a result of Covid-19, by equivalised household income quintile: UK, Sep-2021



Notes: Survey carried out among 6,051 households during 1-21 September 2021. Household income is pre-tax, and equivalised using modified-OECD scale in order to account for household size. Children's ages are not known, so an equivalisation factor of 0.4 is used for all children. Where respondents are unable to provide income data, they are dropped from this analysis. Full question reads: “Thinking about all of your income, including any pay or benefits you receive when off work, such as sick pay or government support, how has your total income changed relative to usual because of coronavirus?”

Source: PBE analysis of Bank of England, *NMG Survey H2 2021*

Interestingly, households in quintile one were as likely as those in quintile five to report an *increase* in income associated with Covid-19 (24% in both groups) – most likely reflecting the fact that many at the bottom end of the income distribution were already out-of-work ahead of the pandemic and therefore benefitted from additional government support without facing any offsetting labour market damage. But this is prior to the end of the Universal Credit uplift, which is likely the leading source of this reported rise. And it nevertheless remains the case that lower income households were significantly more likely to face a drop in income – with those in work but on low incomes perhaps hit hardest of all.

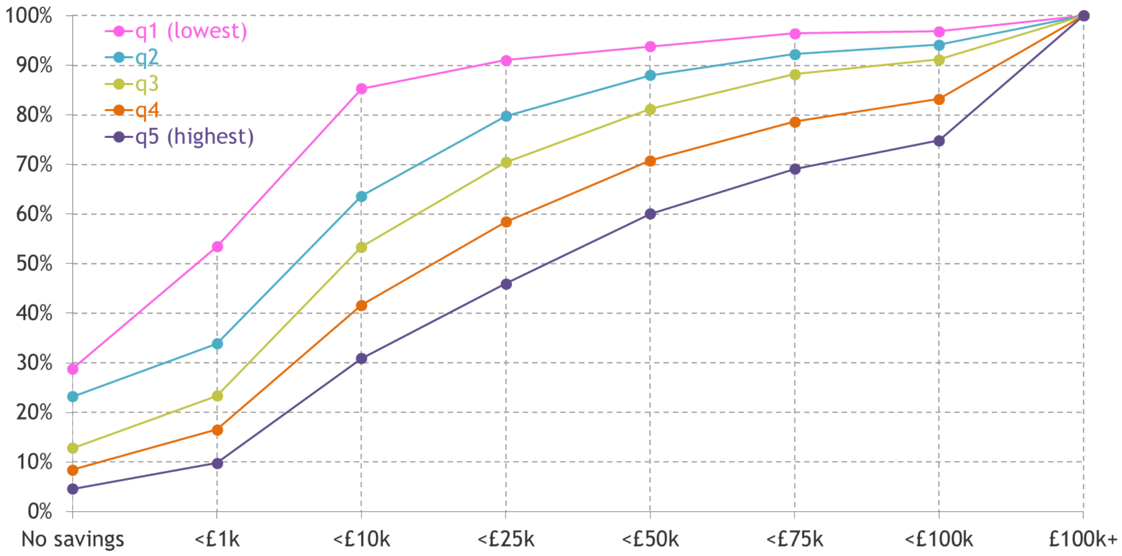
Today's growing cost-of-living crisis is also likely to be more harshly felt at the lower end of the income distribution due to the *type* of inflation we're seeing. It is being driven largely by 'staples' such as basic foodstuffs and fuel – items that lower income households spend a much larger proportion of their income on compared to higher income households. Just as it was coming out of the financial crisis, the headline rate of inflation that emerges over the course of 2022 is likely to understate the situation for those already close to the financial edge.

Lower income households are also much less likely to have protection in the form of savings to help them withstand the coming squeeze. In the month to March 13, 2022, more than four in five (83%) adults across the UK said they'd experienced an increase in their cost of living. Of these, one in four (24%) said they'd responded in part by dipping into their savings. It's a strategy which will prove very short-lived for those with minimal savings in place.

Figure 4 sets out cash savings profiles for the different parts of the income distribution ahead of the recent rise in inflation. It shows that almost three in 10 (29%) households in the bottom fifth of the distribution reported having no savings whatsoever, with more than half (53%) having less than £1,000 to fall back on. In contrast, just one in 10 (10%) households in the top fifth of the distribution reported being in this position; with one in four (25%) having access to savings in excess of £100,000.

Figure 4: Half of households in the bottom fifth of the distribution report savings of less than £1,000

Cumulative proportion of savings values held by equivalised pre-tax household income quintiles: UK, Sep 2021



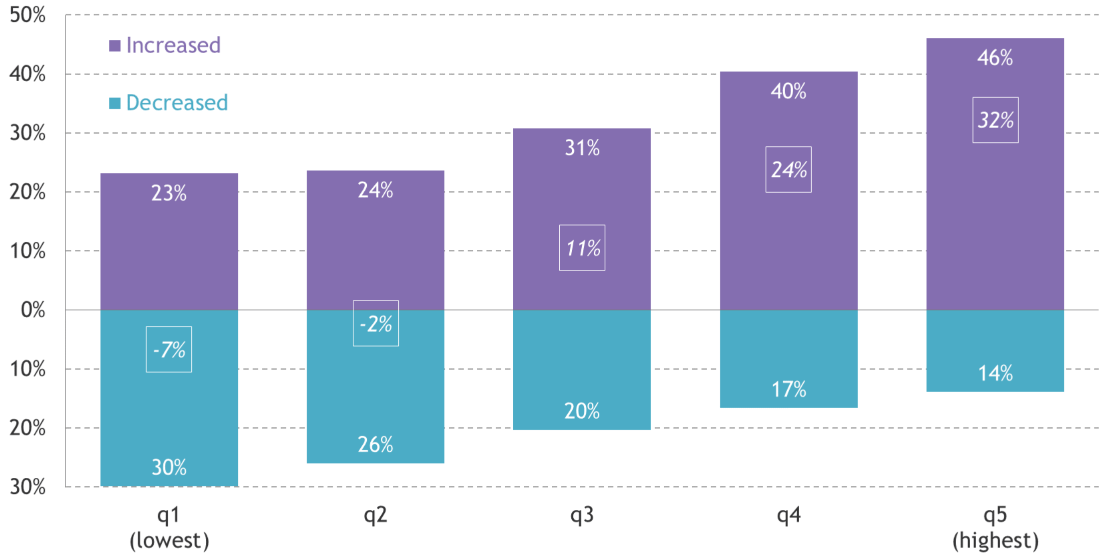
Notes: See notes to Figure 3. Full question reads: "Using the following ranges, could you state how much you (and all other members of your household) currently have in total, saved up in savings accounts?"

Source: PBE analysis of Bank of England, *NMG Survey H2 2021*

And this distributional skew in savings has been exacerbated by the pandemic. Faced with an enforced curtailment of spending on foreign travel, eating out and commuting, significant numbers of households boosted their savings in the first 18 months of the Covid-19 crisis. As Figure 5 shows, this is especially true at the top end of the income distribution. Almost half (46%) of households in quintile five said the pandemic had caused them to increase their savings, compared with one in four (23%) of those in quintile one.

Figure 5: A net balance of one-in-three households in the top fifth of the income distribution have boosted their savings during the pandemic

Proportion of households saying that changes in their income or spending brought about by Covid-19 have prompted a change in their level of savings, by equivalised household income quintile: UK, Sep-2021



Notes: See notes to Figure 3. Full question reads: "The next question is about how much savings your household has. By savings we mean the amount of money your household has in bank/building society accounts, including current accounts, or fixed rate savings bonds, cash ISAs, and NS&I account/bonds. We do not mean any pensions or investments you might have where returns are linked to stock market performance. As a result of any changes in income or spending due to the coronavirus pandemic, would you say that your household's total savings have increased, decreased, or stayed the same?"

Source: PBE analysis of Bank of England, *NMG Survey H2 2021*

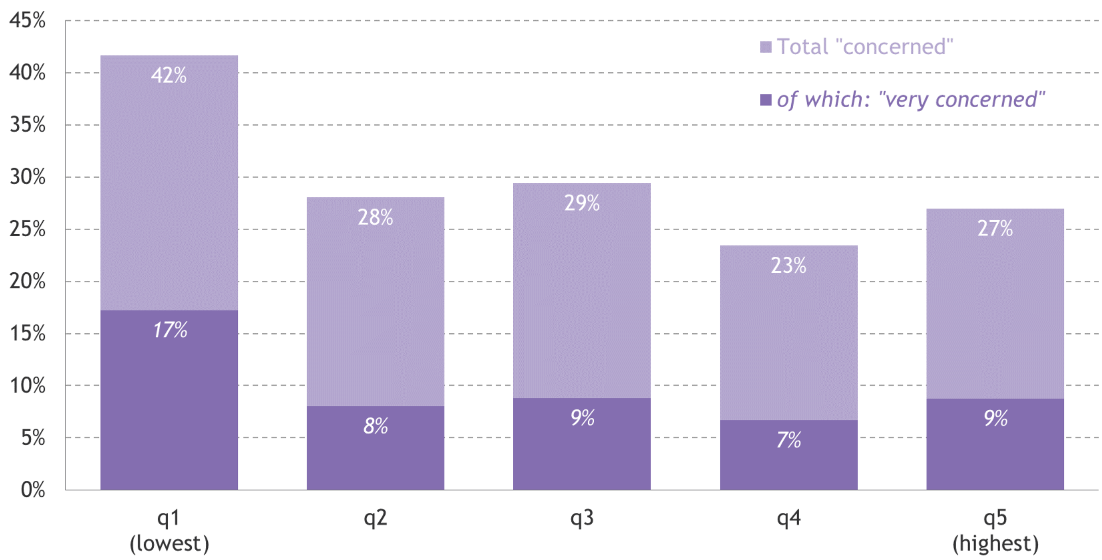
The flip side of this rise in savings at the top end of the income distribution has been an increase in *dissaving* at the bottom end, with three in 10 (30%) households in quintile one and one in four (26%) in quintile two reporting a fall in their savings associated with Covid-19.

And this profile is reflected in reported levels of concern about debt, with those on the lowest incomes most likely to be worried about keeping up with secured and unsecured debt repayments. Figure 6, reporting on the situation ahead of the recent run of Bank of England base rate rises, shows that two in five (42%) households in quintile one were already concerned about their levels of debt – with nearly one in five (17%) saying they were "very concerned".

Another striking feature of Figure 6 is that a non-trivial level of debt concern was reported across the *entirety* of the income distribution, even ahead of the recent cost-of-living increases. With the Bank of England indicating that it may need to raise interest rates further over the remainder of 2022, this concern is likely to rise higher still.

Figure 6: Concern about debt is present across the distribution, but especially pronounced at the bottom end

Proportion of households saying that they are in some way concerned about their unsecured and secured debt, by equivalised household income quintile: UK, Sep-2021



Notes: See notes to Figure 3. Full question reads: "How concerned are you about your current level of debt? Please consider all debt, including any balances on credit/store cards, loans, or secured debt such as your mortgage."

Source: PBE analysis of Bank of England, *NMG Survey H2 2021*

It is worth noting too, that these figures take no account of debts associated with utility bills. Research from Citizens Advice has highlighted the additional stress associated with such costs, with fuel debt cited as the most common debt problem in 2021. With energy prices now surging, increasing numbers of families are likely to face falling behind on payments.

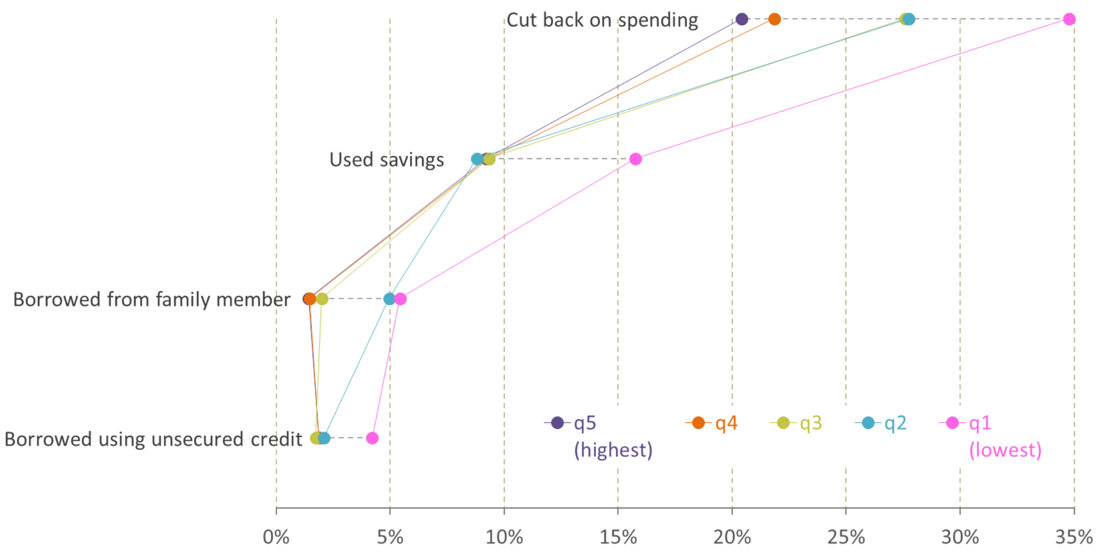
Perhaps more fundamentally still, it should be of concern that one in six (17%) households reported last autumn that they had faced difficulty keeping up with their housing payments over the previous year due to Covid-19. Once again, those at the bottom end of the income distribution were most affected, with one in three (33%) households in quintile five being in this position.

Figure 7 sets out the action taken by households in different income groups to deal with these difficulties. Even among those in the top fifth of the income distribution, one in five (20%) said they'd needed to cut back on spending in order to pay their rent or mortgage. Among those in the bottom fifth of the distribution, the proportion jumped to one in three (35%).

While only reported by a relatively small number, the one in 50 (2%) who said they'd used unsecured credit to meet their housing commitments are of particular concern – especially as we would expect this figure to now be on an upward trajectory given how the economic backdrop has shifted in the period since this data was collected.

Figure 7: A significant minority of families have had to take action to meet housing costs in response to Covid-19

Proportion of households saying they have taken action to pay their rent, mortgage repayment or other accommodation charges, by equivalised household income quintile: UK, Sep-2021



Notes: See notes to Figure 3. Full question reads: "As a result of coronavirus, have you taken any of the following actions in order to pay your rent, mortgage repayments or other accommodation payments? I have cut back on spending a little; I have cut back on spending a lot; I have used savings; I have borrowed using unsecured credit; I have borrowed from family members; Other; No action; Don't know."

Source: PBE analysis of Bank of England, *NMG Survey H2 2021*

A cost-of-living squeeze of the magnitude expected to befall the UK over the course of 2022 would be cause for concern at any time. But coming as quickly as it does on the heels of the Covid-19 disruption, it has the potential to tip very significant numbers of households over the edge into serious financial distress.

Charities will again play a critical role in supporting households in need, but are themselves under extreme pressure

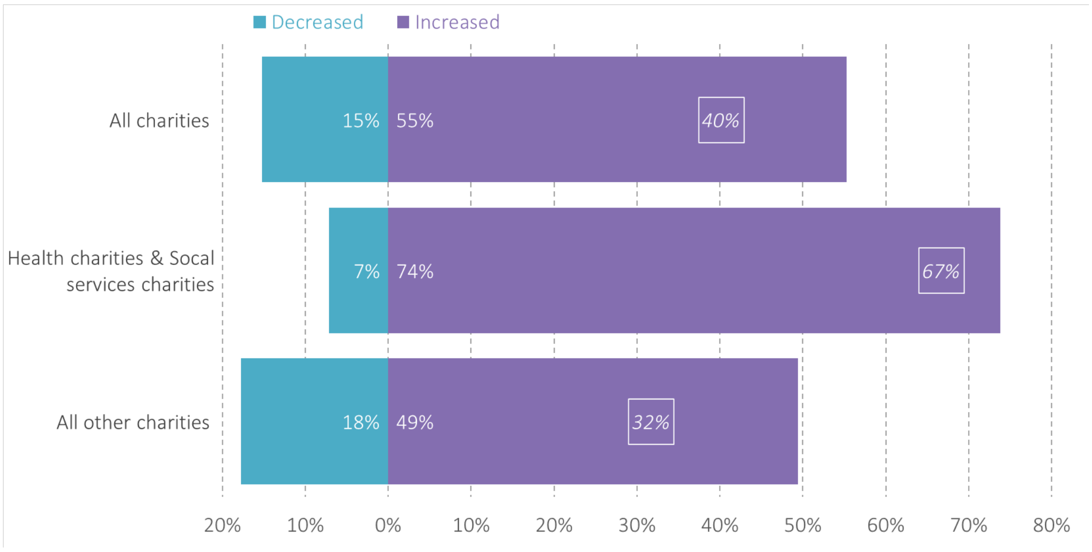
Against this backdrop, charities will provide crucial support. Not just those that work specifically with people in financial difficulty, but also the thousands of organisations across the country that support individuals with accessing work, recovering from crime, dealing with mental health difficulties, overcoming housing challenges and the many more areas of need that are likely to grow alongside the cost-of-living crisis.

With the shadow of austerity continuing to fall across many of our public services, and with inflation rapidly eroding the value of the cash settlements set out in last year's Spending Review (removing at least one quarter of the real-terms departmental increases previously planned for, according to the IFS), the social sector will likely need to play an even more central role.

It is inevitable that organisations within the sector will step up – they always do. But the capacity of charities and others to meet any surge in requests for help is likely to be constrained by the extent to which they are already running hot; having faced elevated demand for much of the last two years. Figure 8 provides some context, showing that more than half (55%) of charities were reporting a Covid-related elevation in demand towards the end of 2021.

Figure 8: Charities have faced elevated demand over the course of the pandemic

Has the current level of demand for the services of your organisation increased or decreased since the pandemic started (March 2020)? October 2021



Notes: N=84 for 'Health charities and Social services charities', N=265 for All other charities, N=349 for 'All charities'. Residuals are 'About the same' and 'Don't know/can't recall'.

Source: Online survey carried out by YouGov Plc on behalf of the Law Family Commission on Civil Society, 18-24 October 2021

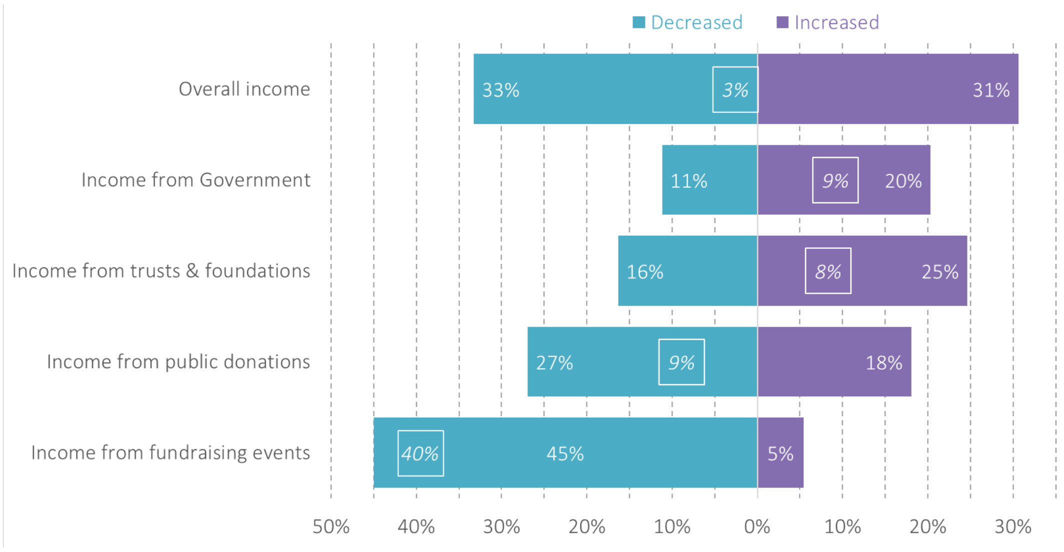
The situation is made more difficult still by trends on the other side of the equation: namely resources. Figure 9 shows that, overall, charities are as likely to have secured an increase in funding over the course of the pandemic as they are to have suffered a decrease. But this is no reason to be sanguine.

It remains the case that one in three charities suffered a drop in income over the first 19 months of the Covid crisis, with those organisations relying most on public donations or on fundraising events especially likely to have been hit. And, while the net balance of increases in funding recorded in relation to income from government, as well as from trusts and foundations, is good to see, there is a clear question mark over the extent to which this position will be maintained in 2022. Evidence from throughout the pandemic also suggests that the increases in income which were achieved by a proportion of charities were of a magnitude smaller than income falls.

Government funding was boosted during the pandemic by the explicit support package provided in recognition of the extraordinary situation facing charities. There is no indication that similar support will be forthcoming as the sector grapples with today's new crisis. And there is concern that at least some of the emergency funding provided by trusts and foundations in 2020 and 2021 will be money brought forward from future years, resulting in a potentially tighter funding environment in 2022.

Figure 9: One-in-three charities have faced a drop in income over the pandemic, with public donations especially affected

Has your organisation's current level of income increased or decreased since the pandemic started (now compared to before March 2020)? October 2021



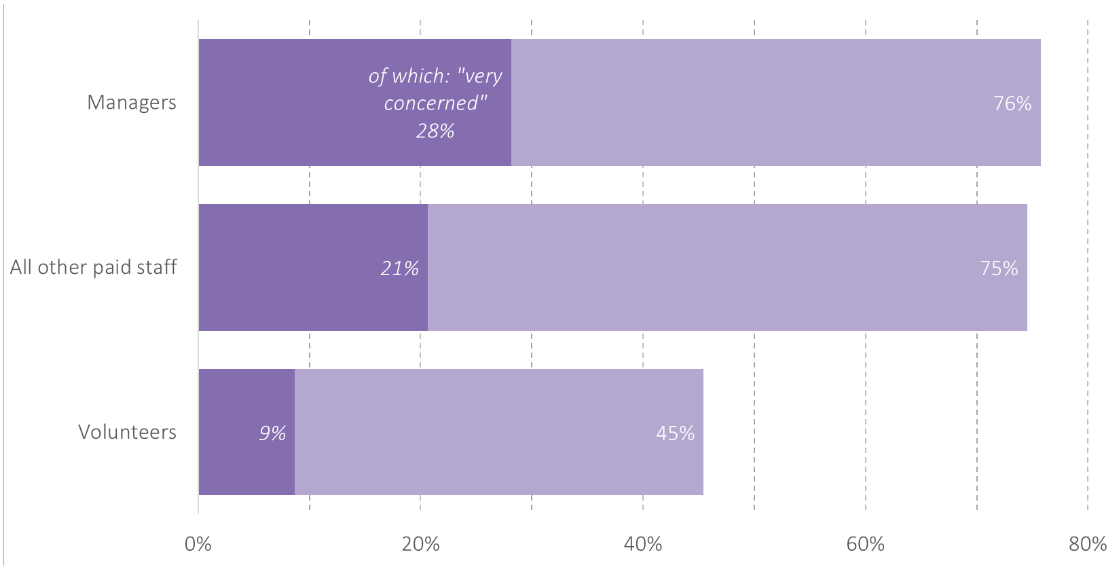
Notes: N=349 senior managers or above working for a registered charity or voluntary group.
Source: Online survey carried out by YouGov Plc on behalf of the Law Family Commission on Civil Society, 18-24 October 2021

And, however those questions play out in the coming months, social sector organisations will face significant constraints as a result of the very same cost pressures that are set to push demand for their help higher. Surging inflation will mean that pre-existing pledges, long-established regular donations and cash reserves will all face rapid erosion in the forthcoming period. As with everyone else, charities will simply find that their money doesn't stretch as far as it did.

The capacity of the social sector to continue to do more with less is likely to be further impacted by the fatigue accumulated by its workforce over the past two years. Figure 10 shows that three in four sector leaders polled in October 2021 were already worried about burnout among their managers (76%) and other paid staff (75%). More than one in four (28%) declared themselves "very worried" in relation to managers, along with more than one in five (21%) in relation to other paid staff. Just as alarming, nearly half (45%) said they were worried about the wellbeing of their volunteers.

Figure 10: Three-in-four sector leaders are worried about burnout among their workforce

To what extent, if at all, are you concerned about wellbeing, stress, and burnout among people in the organisation you work for?



Notes: N=349 senior managers or above working for a registered charity or voluntary group. Respective proportions are calculated from the responses of: the 334 who worked in an organisation with a manager/s; the 326 who worked in an organisation with other paid staff; and the 264 who worked in an organisation benefiting from the work of volunteers. Residual proportions (not shown) are 'Don't know'.

Source: Online survey carried out by YouGov Plc on behalf of the Law Family Commission on Civil Society, 18-24 October 2021

This picture is of course a concern from the perspective of the individuals involved. But it also represents a significant challenge for organisations in the sector. And even more so against the backdrop of a very tight labour market, in which pay pressure is set to build. With staff shortages appearing across the economy – and increasing numbers of people leaving the labour market altogether – there is a real risk that charities will face a talent drain in the coming period.

Low pay is already an issue, with 17% of staff earning less than the real Living Wage. Given that the provision of inflation-matching pay rises across the sector is likely to cost well in excess of £2 billion in aggregate – money which most organisations do not have – an increasing number of individuals may choose to exit the sector in pursuit of higher rewards and lower stress.

This all adds up to a tough period ahead, albeit it with some cause for optimism

Entering a new crisis before fully emerging from the last one is extremely difficult, especially for a sector that operates so close to the edge, with thin reserves and a workforce that is already highly stressed. There is, though, at least some cause for optimism.

The first is that the sector always finds a way. It is in the nature of social sector organisations and those who work in them to respond rapidly to changed circumstances, finding nimble and opportunistic ways to continue to make a difference. The experience of the pandemic provides very clear evidence of this.

Three in four (76%) charities told PBE last spring that they had responded to the challenges of Covid-19 by adopting new delivery methods. Likewise, nearly six in 10 said they had increased their digital skills. And two in five (42%) said they'd collaborated more with other charities, while one in five (21%) said they'd collaborated more with business. Such innovations help to explain why the sector has been able to deliver such great support over the course of the pandemic. And they should leave organisations better placed now to deal with the new challenges they face.

The response of funders also bodes well for the future, with increasing numbers recognising the merit of providing more flexible and more timely support. Practices shifted in response to Covid-19, but there is an increasing sense that new approaches are here to stay.

We can also find room for optimism in public sentiment. The outpouring of financial support for the NHS and volunteering at the start of the pandemic has been much reported on, and survey after survey has highlighted the warmth the public has for charities and those stepping in to help. New analysis presented in the latest *World Happiness Report* highlights a "global upsurge in benevolence" in 2021 – with benefits for givers and receivers alike. The report finds that:

"In every global region, there have been large increases in the proportion of people who give money to charity, help strangers, and do voluntary work in every global region. Altogether the global average of these three measures was up by a quarter in 2021, compared with before the pandemic."

The huge outpouring of voluntary effort and donations we've again seen in response to the crisis in Ukraine reinforces the notion that people respond when called upon to do so. It may be tough to revisit this particular source of benevolence too often during a cost-of-living squeeze that will affect so many families, but the repeated willingness of the British public to pull together in difficult times should give cause for comfort.

And finally, we can draw some optimism from the reality that, despite everything, there *is* money out there. As Figure 5 showed, the pandemic has prompted an increase in savings for very large numbers of households. In aggregate, UK households were holding an estimated £224bn more in savings at the start of 2022 than they would have done in the absence of the pandemic. That's equivalent to roughly £3,400 per person. At the same time, an unexpectedly tax-rich mix of growth over the last year means the Chancellor is likely to be handed a sizeable (near-term) fiscal boost by the OBR at the Spring Statement.

There is no avoiding the reality that the country has been made poorer by all that's happened in the last two years, and that it will be made poorer still by rising energy costs. The outlook is a very difficult one. But much of the challenge facing households over the coming months is distributional in nature: some will be hit significantly harder than others.

There is scope then to mitigate the worst of the effects of the cost-of-living crisis by looking to rebalance the distributional picture. The Chancellor has the opportunity to take action in this regard at the Spring Statement, offering targeted support via benefit increases for instance (and not backtracking on the National Insurance increase which, while imposing additional costs across the income distribution, will bring in significantly more revenue from higher earners).

But the social sector provides another mechanism for rebalancing resources. By supporting those organisations that work with the millions of people up and down the country who will be affected by the unfolding of the cost-of-living crisis, those best placed to weather the coming storm can make a direct and meaningful difference to the country's experience of it.

The light at the end of the Covid-19 tunnel that appeared at the start of the year has dimmed all too quickly, with the onset of a very serious squeeze on household living standards. As a country, we will once again be reliant on our charities and social sector organisations to help us navigate the new crisis. But they will need our help too.

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