HARGREAVES
LANSDOWN

A SAVINGS AND RESILIENCE BAROMETER FOR GREAT BRITAIN

A landmark study by Oxford Economics

January 2022

CONTENTS

ABOUT OXFORD ECONOMICS

Oxford Economics was founded in 1981 as a commercial venture with Oxford University's business college to provide economic forecasting and modelling to UK companies and financial institutions expanding abroad. Since then, we have become one of the world's foremost independent global advisory firms, providing reports, forecasts and analytical tools on more than 200 countries, 250 industrial sectors, and 7,000 cities and regions. Our best-in-class global economic and industry models and analytical tools give us an unparalleled ability to forecast external market trends and assess their economic, social and business impact.

Headquartered in Oxford, England, with regional centres in New York, London, Frankfurt, and Singapore, Oxford Economics has offices across the globe in Belfast, Boston, Cape Town, Chicago, Dubai, Dublin, Hong Kong, Los Angeles, Melbourne, Mexico City, Milan, Paris, Philadelphia, Stockholm, Sydney, Tokyo, and Toronto. We employ 450 full-time staff, including more than 300 professional economists, industry experts, and business editors—one of the largest teams of macroeconomists and thought leadership specialists. Our global team is highly skilled in a full range of research techniques and thought leadership capabilities from econometric modelling, scenario framing, and economic impact analysis to market surveys, case studies, expert panels, and web analytics.

Oxford Economics is a key adviser to corporate, financial and government decision-makers and thought leaders. Our worldwide client base now comprises over 2,000 international organisations, including leading multinational companies and financial institutions; key government bodies and trade associations; and top universities, consultancies, and think tanks.

JANUARY 2022

To discuss the report further please contact:

Henry Worthington: **hworthington@oxfordeconomics.com**

Oxford Economics

4 Millbank, London SW1P 3JA, UK

FOREWORD

CHRIS HILL
CEO, HARGREAVES LANSDOWN

Financial resilience, the ability to withstand income shocks in the short and longer term, has come to the fore over the last two years as we continue to experience and live with the consequences of the pandemic and the economic uncertainty it has created.

At Hargreaves Lansdown, we have been at the heart of building resilience for over 40 years and helping the nation save and invest with confidence. There has been a step change in people needing to engage with their finances, from having to manage their own pensions to the rise of self-employment. As our client base has grown, doubling in number since 2016, it has also widened: the median age of our clients has dropped from 58 in 2007 to 46 in 2021.

This more diverse client base across the UK also has more diverse needs. That's why we launched our 5 to Thrive campaign in July 2021 – a campaign that is focused on boosting financial resilience whatever your background, occupation, age, or financial expertise. The campaign focuses on five essential pillars: Control your debt, Protect you and your family, Save a penny for a rainy day, Plan for later life, and Invest to make more of your money. It is underpinned by a belief in the need to democratise finance – to share our expertise with a wider community of savers and investors and, ultimately, do what we can to help to improve their financial resilience.

But we wanted to go one step further – to better understand the UK's financial resilience as a whole, looking beyond our client base and to create a unique report that helps policy-makers better understand where are some of the biggest risks, and which groups need the most help and attention. Working with Oxford Economics, we are delighted to present the first nationwide analysis into exactly this area.

Our first Savings and Resilience Barometer for Great Britain report demonstrates how financial resilience has increased through the pandemic, but also shows that this increase has been uneven. The demographic analysis draws out the varying levels of resilience across different geographical areas and groups. From low levels of pensions and savings for the self-employed, and the need for more single parents to consider insurance against life events to the opportunity that 14% of households have to invest to make more of their money, the barometer draws out the stark challenges British households face. These are real issues for us all to address in 2022.

The dataset developed by Oxford Economics for the barometer also gives us the ability to project forward to predict what household's financial resilience may look like in different economic and policy scenarios. The impact of high inflation in 2022 is our focus: the analysis shows that this alone could reverse nearly half of the boost to financial resilience that households experienced during the pandemic.

Together with Oxford Economics, we will explore the issues around financial resilience every six months – creating a rich data set of how individual, economic and policy decisions can enhance or erode people's ability to withstand future income shocks. This will evolve based on feedback and to ensure it remains consistently relevant for the broader policy debates.

Building on these insights, Hargreaves Lansdown is delighted to launch a series of new tools that allow people to explore their own resilience. These tools will help to ensure households can better understand their own financial resilience and take more informed actions to build on their savings and improve their financial situation.

In launching this Barometer, we would like to thank the individuals who participated in our independent Sounding Board – a steering group of policy experts, consumer advocates, and industry peers who all contributed their experience, expertise and time to help improve the UK's financial resilience. We look forward to continuing to work with them, with government and with the wider industry to ensure that whatever future economic shocks occur, individuals and families across the UK are equipped to withstand them.

EXECUTIVE SUMMARY

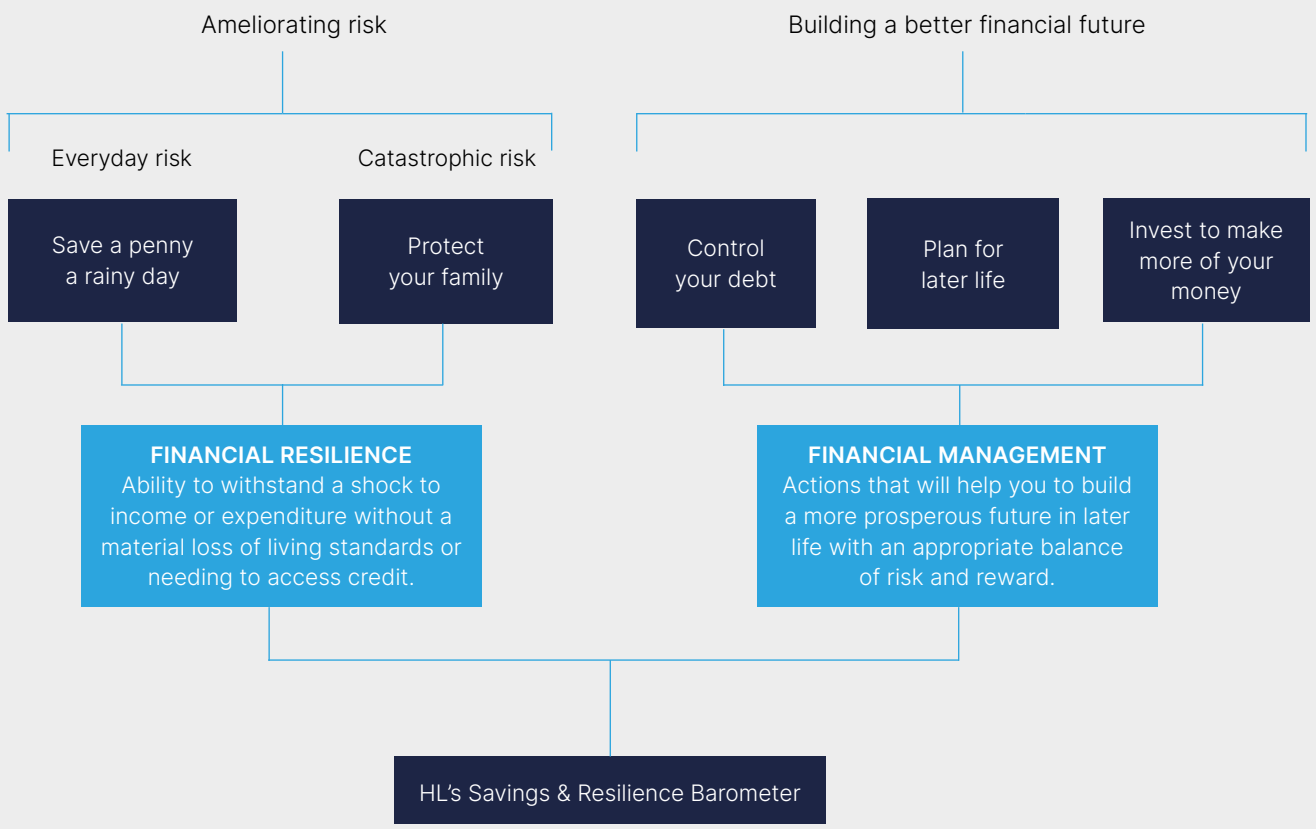
How are British households managing financially? A huge amount of data – both objective and subjective – is already collected and intensely scrutinized. However, more timely and comprehensive insights would help to promote awareness and enhance our understanding of this topic. This research programme has been motivated with this in mind.

INTRODUCING THE BAROMETER

The output from the research is the Savings and Resilience Barometer for Great Britain. It is designed to produce a holistic measure of the state of the nation's finances. It is structured around the five pillars of financial behaviour that we consider fundamental for households to prudently balance current and future demands whilst guarding against risks (Fig. 1).

We have mapped these pillars to a list of 17 individual indicators for which we have collected data for a representative group of British households by linking together official datasets. We then made use of macroeconomic data and forecasts from Oxford Economics' **Global Economic Model** (GEM) to assess, through the lens of the barometer, how financial resilience has been affected by the extraordinary economic developments associated with the pandemic and the recent sharp increase in the cost of living.

FIG. 1. SAVINGS AND RESILIENCE BAROMETER: CONCEPTUAL STRUCTURE

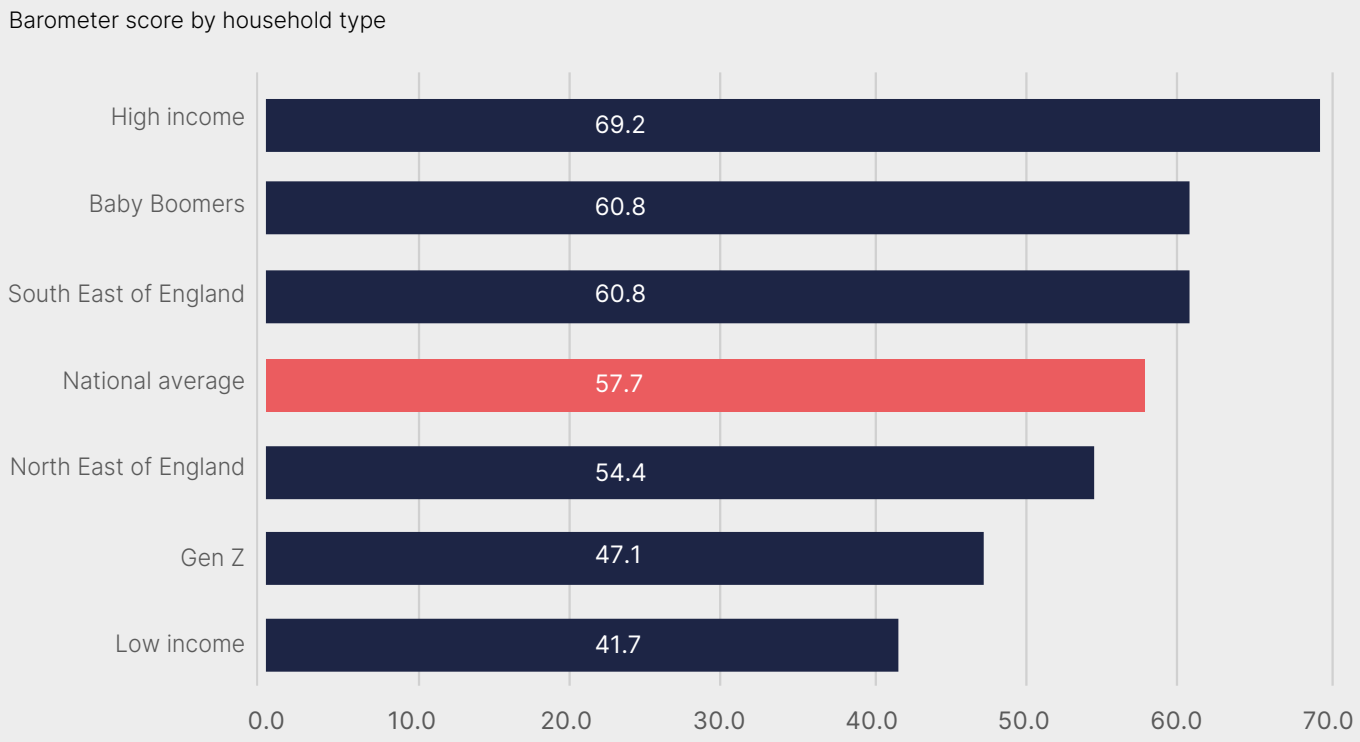


KEY FINDINGS

- The **headline resilience score** is 57.7 out of 100 for Great Britain, up from 54.5 in 2019. By Q4 2022 we expect resilience to fall back to 56.2 with inflation and interest rates squeezing household finances.
- However, analysis of the data at the level of the '5 to Thrive' pillars is more revealing.
- **Control your debt**: scores are notable for there being no discernible relationship with income, we all take out debt. However there is a significant problem with **lower income households who do take on debt find it much harder to control.** Over 15% of those low-income households are behind on a (non-mortgage) debt repayment or a household bill, more than four times the national average.
- **Protect you and your family:** less than half (41.2%) of families were found to have combined assets and life insurance that would cover mortgage liabilities and future living costs of their children. With **single-parent households particularly badly hit** with just 16.6% holding coverage.
- **Save a penny for a rainy day:** A third of the UK doesn't have access to savings that would cover at least three months of essential expenditure. There is a **big difference between the average score of employee households** (64.6) and self-employed households (48.1).
- **Plan for later life: Self-employed people have significantly lower pensions than the employed,** but slightly higher levels of home ownership and wealth: just 22.3% of them have adequate pensions compared with double that for employee households
- **Invest to make more of your money: 14.1% of British households do not hold any investments**, despite having highly liquid savings that could cover at least six months of essential spending.

Through the lens of the barometer, we can compare the average level of resilience across different parts of society as defined by the socioeconomic and demographic characteristics of households. On one level, such comparisons yield few surprises. They are consistent with many of the well-established trends in financial inequality that run through British society—for example, above-average scores were recorded by high-income households, those from the South East and from the Baby Boomer generation (Fig. 2).

FIG. 2. SAVINGS AND RESILIENCE BAROMETER AVERAGE SCORES FOR DIFFERENT HOUSEHOLD TYPES



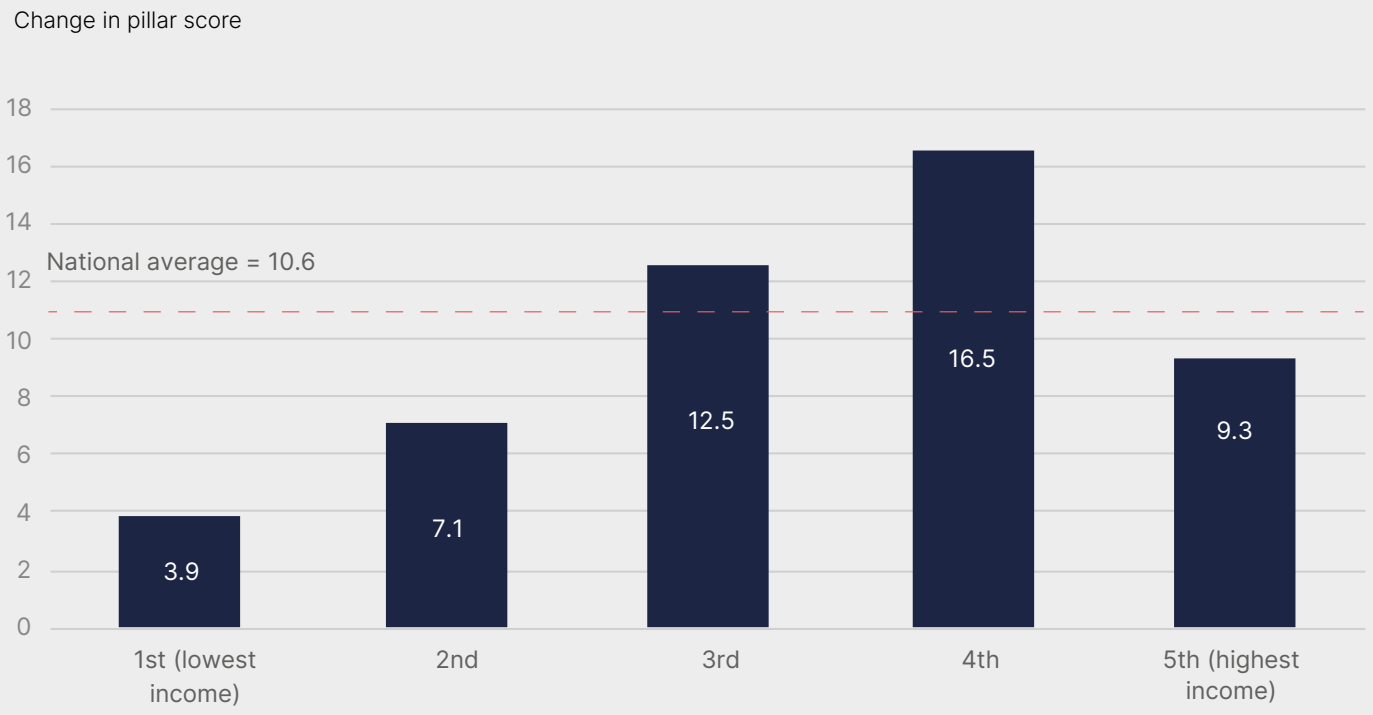
Source: Oxford Economics

However, this rich dataset can provide us with a lot more insight. This barometer looks at the differential impacts of economic changes on different groups, gives us the ability to track this over time and crucially, in these uncertain times, a framework to consider future economic trends.

Despite the enormous level of human suffering and turmoil, the pandemic was associated with a marked improvement in the aggregate financial resilience of British households as measured by the barometer. This was driven by a period of enforced expenditure restraint due to social distancing measures as households took the opportunity to collectively deleverage and build up their savings.

Our research, however, has demonstrated that such changes were highly uneven across society. For example, we estimate that whilst high-income households (those in the top 20% pre-pandemic) reduced their expenditure by 14.6%, on average, across the pandemic, low-income households (in the bottom 20% pre-pandemic), whose expenditure is much more skewed towards day-to-day essentials, saw their spending flatline. As a result, despite seeing their incomes well protected, low-income households enjoyed the least significant improvement in their savings rate during the pandemic, as reflected in our 'save a penny for a rainy day' pillar scores (Fig. 3).

FIG. 3. CHANGE IN 'SAVE A PENNY FOR A RAINY DAY' PILLAR SCORE BY INCOME QUINTILE: 2021 Q2 VS 2019



Source: Oxford Economics

As we look ahead, economic headwinds for 2022 have been building. At the time of writing, the impact of the new Omicron variant remains highly uncertain. Nevertheless, the recent sharp uptick in inflation, expected interest rate rises and the removal of certain elements of policy support all seem set to squeeze household finances this year. As measured though the scales of the barometer, we expect these changes to reverse approximately half of the boost to financial resilience that households experienced during the pandemic (Fig. 4).

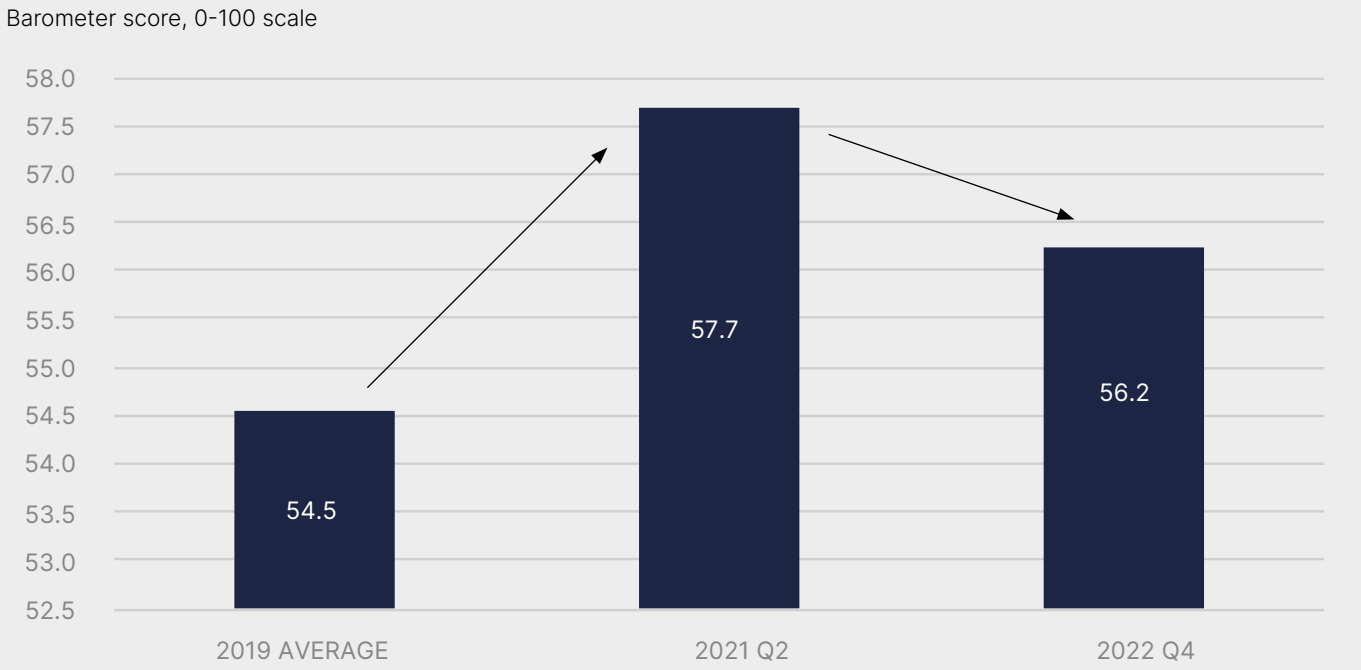
NEXT STEPS AND RESEARCH AIMS

We are confident that the findings unveiled in the first wave of this research provide useful insights to stakeholders and promote awareness of this topic; our ambitions do not stop here. Going forward, we plan to publish barometer updates, including forward-looking scenarios, every six months. Beyond this, we intend to continue to invest in the research, drawing on feedback from the project sounding board to enhance and tailor our approach and provide access to data to interested third parties so they can build on our work. This report embarks on that journey.

THE SAVINGS AND RESILIENCE SOUNDING BOARD

We are grateful for the initial thoughts from the savings and resilience sounding board in November. Hargreaves Lansdown established this sounding board to bring a broader set of views and insights into this research project. Members are drawn from a variety of backgrounds. Representatives from StepChange, Nationwide Building Society and Legal & General shared their expertise from working with client groups particularly impacted by resilience issues in specific pillars. The Money and Pensions Service, HM Treasury, Department for Work and Pensions and the Financial Conduct Authority all shared perspectives from the research and work they conduct. Finally, the Personal Finance Research Centre at the University of Bristol, the Resolution Foundation and Nest Insight have all shared views from their research backgrounds.

FIG. 4. SAVINGS AND RESILIENCE BAROMETER FOR GREAT BRITAIN SCORE: 2019 VS 2021 Q2 VS 2022 Q4



Source: Oxford Economics

1. INTRODUCING THE BAROMETER

BACKGROUND CONTEXT

How are British households managing financially? There is a huge range of research and data that has enriched our understanding of this topic. Despite such a focus, to-date a single comprehensive measure underpinned by a gold standard methodology remains elusive. Indeed, in her task force report on the matter, Baroness Drake concluded that "only a regular and granular measure can illuminate the changing factors which contribute to low financial resilience" as part of her call to action to develop an index measure.[1]

Of course, the challenges of financial management can be quite different for households across the country depending on their age, family structure, income volatility, housing tenure and so on. For many low-income households careful financial planning is necessary from week-to-week whereas the more affluent have the luxury of taking a more long-term view, weighing up alternative saving and investment options.

This research programme and report have been motivated in this context with a view to produce a holistic measure of the state of the nation's financial resilience. We hope that the findings and insights will help to promote awareness of the topic, enrich understanding and provide a basis to understand the impact of economic and policy change on households' resilience.

THE FIVE PILLARS OF FINANCIAL RESILIENCE

Financial resilience is conventionally defined with reference to the ability to withstand an unexpected shock to income or expenditure. For example, in their recent report, the Financial Resilience Task Force suggested the following definition: "The ability to cope financially when faced with a sudden fall in income or unavoidable rise in expenditure." [2]

Being able to cope with such everyday risk is undoubtedly of crucial importance but solely focusing on this aspect would neglect choices and behaviours that influence the financial wellbeing of households around the country. In shaping the barometer to Hargreaves Lansdown's '5 to Thrive' model[3], we have sought to develop a holistic measure that can produce a comprehensive overview and means to monitor financial resilience. The barometer is structured around five pillars as illustrated in Fig. 5:

1. **Control your debt:** it is not that debt is inherently a bad thing for consumers. Indeed, there are very sound reasons why households need and do take on debt, for example to finance educational courses or a house purchase. However, ensuring that debt repayments are sustainable is a crucial first step to successful financial management.
2. **Protect your family:** once debt is under control, ensuring that there is an adequate safety net to ensure the financial future of dependents in the event of catastrophe should be a priority for households.
3. **Save a penny for a rainy day:** having access to a pool of savings that can help to mitigate the consequences of an unexpected shock to income or spending is a prerequisite of sound financial planning.
4. **Plan for later life:** age comes to us all and planning for the associated drop in income during retirement is integral to preserve purchasing power during this period. Ensuring adequate pension contributions through working life and more actively managing funds closer to retirement are important in this respect.
5. **Invest to make more of your money:** finally, once households have accomplished the above, they have the freedom to invest any excess savings into assets that can help to build a better financial future.

[1] Baroness Drake, "Measuring Household Financial Resilience" (The report of the Financial Resilience Task Force, 2019).
[2] Ibid
[3] https://www.hl.co.uk/features/5-to-thrive

FIG. 4. FIG. 5. SAVINGS AND RESILIENCE BAROMETER: CONCEPTUAL STRUCTURE

MAPPING THESE TO INDIVIDUAL INDICATORS

In collaboration with Hargreaves Lansdown, Oxford Economics mapped each of these pillars to a set of concepts that could be measured by specific indicators which comprise our barometer data. A full description of each indicator can be found in Appendix 1 of this document. In doing so, we were guided by the following core principles:

- **Avoid double counting:** when choosing indicators, we have been careful to avoid double counting of measures. Various measures of households' balance sheets are, therefore, included in a single indicator and not duplicated elsewhere.
- **Life cycle effects:** when evaluating the position of household finances, age matters. Younger households can, on average, expect to enjoy higher future working-life income and have had less time to accumulate wealth. Where appropriate, we have controlled for such life cycle effects to create a more meaningful intergenerational benchmark.

THE FINANCIAL RESILIENCE BAROMETER – A BRIEF EXPLAINER

The barometer results reflect a complex modelling effort underpinned by high quality statistical data from official sources. A detailed description of the technical work that underpins our findings can be found in a methodology paper that has been published separately. In this section, though, we provide a brief explanation of our approach and data sources.

Underlying data
The barometer is underpinned by a household panel dataset—effectively a database of households who provide a representative sample to derive conclusions about the both the state of the nation and how conditions vary across households of different socioeconomic characteristics. The original source for our panel dataset is the Wealth and Assets Survey (WAS) conducted by the Office for National Statistics (ONS) on a biennial basis. The WAS is the most detailed financial survey run in the UK with information on all aspects of households' balance sheets together with demographic information such as the age of household members, whether residents own or rent their home, and the household's region.

Imputation and extrapolation
Despite such exceptional detail, the WAS did not contain all the information we wished to use when constructing measures of financial resilience. We therefore imputed additional variables, exploiting the correlation between these indicators and household characteristics evident from other survey data. For example, we used the Financial Lives Survey (FLS) conducted by the Financial Conduct Authority to model the likelihood of households being covered by income protection policies dependent on key characteristics. This was then matched probabilistically to the households in the WAS dataset. Other sources used for imputation include the Living Costs and Food Survey (LCFS) and the Labour Force Survey (LFS).

The major downside of the WAS compared to other data sources is that it is published with a very long reporting lag meaning that the data is not timely. At the time of modelling, the latest WAS dataset was based on interviews conducted between 2016 and 2018. To bring this up-to-date we have **extrapolated** it forward through to 2021 Q2 using a wide range of macroeconomic and survey data and different modelling techniques.

Constructing barometer scores from this raw data with the underlying data in place, the final step in our analysis was to transform this data into an barometer measure as structured in Fig. 1. A barometer is simply an analytical tool that allows indicators measured in different units to be combined. Therefore, it is often used to measure multi-faceted concepts, such as financial resilience, where it is advantageous to synthesize information from a wide range of variables.

The first step in this process was to normalise each indicator into a common unit of measurement. We chose to transform each variable into a **0 to 100 scale**. In many cases, these boundaries were **not defined by the maximum and minimum values** in our dataset but by reference to **threshold values from external sources**.

For example, the variable used to measure the adequacy of a household's liquid assets is the number of months essential expenditure covered by the value of their liquid savings. We set the threshold score for 100 as coverage of at least 3 months of essential spending based on the official advice offered by the **Money Advice Service**[4]. Therefore, a household with more than 3 months coverage would score 100 for that indicator and households with less than 3 months coverage were scored between 0 and 100 depending on the proximity to this value e.g. a household with 1.5 months of coverage would score 50. A full list of the threshold values specified for each indicator can be found in Appendix 1.

Once each individual indicator had been converted into a 0 to 100 scale, they were then aggregated together to form pillar scores and an overall barometer value. Each indicator was assigned a weight based on the perceived relative importance of this indicator to the relevant pillar concept. These weights can also be found in Appendix 1 and were discussed and agreed between Oxford Economics and Hargreaves Lansdown. Weights of indicators within each pillar and between pillars all sum to 1 so that each pillar score and the overall barometer is also measured on a 0 to 100 scale.

[4] https://www.moneyadviceservice.org.uk/en/articles/emergency-savings-how-much-is-enough%23how-to-build-up-your-fund

2. THE CURRENT STATE OF FINANCIAL RESILIENCE

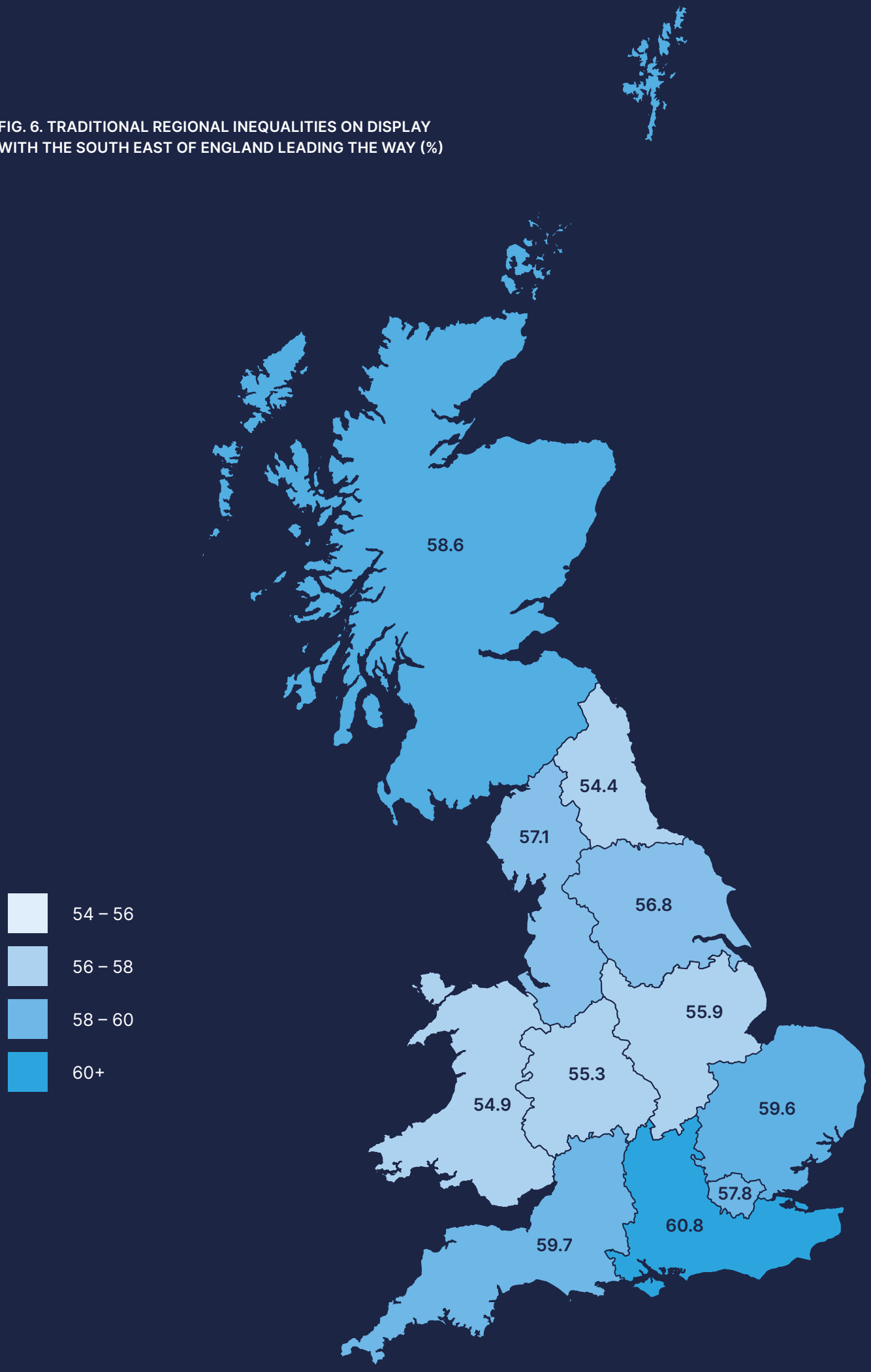
In this section, we describe the current state of financial resilience in Great Britain through the lens of the barometer and the five pillars. All the results presented in this section refer to the estimated situation based on data up to 2021 Q2 and, therefore, account for the extraordinary impact of the coronavirus pandemic on household finances.

2.1 THE STATE OF THE NATION

As described in the previous section, each indicator in the barometer has been constructed on a 0 to 100 scale with the theoretical maximum indicating that a household has achieved the specified resilience threshold. According to our latest data, the current average barometer score for British households is 57.7—tracking how this value evolves over time will provide a timely headline measure to understand the state of the nation's finances.

As shown in Fig. 6, traditional regional divides are apparent in our barometer. Across Britain's 12 government office regions (GORs) the highest average scores were recorded in the south of England with the South East emerging as the country's top performing geography. Despite having a significantly higher income per capita than the rest of the UK, London's barometer score is only a little higher than the national average, a reflection of higher living costs (particularly housing) and a higher level of financial inequality.

FIG. 6. TRADITIONAL REGIONAL INEQUALITIES ON DISPLAY WITH THE SOUTH EAST OF ENGLAND LEADING THE WAY (%)



CONTROL YOUR DEBT

15.3%

The share of indebted low-income households in arrears – more than four times the national average.

2.2 DELVING DEEPER: A PILLAR-BY-PILLAR VIEW

Although these aggregate scores offer a useful high-level picture, we can also exploit the breadth and depth of the underlying data to develop more granular and nuanced insights. In this section, we review more in-depth trends taking each pillar in turn.

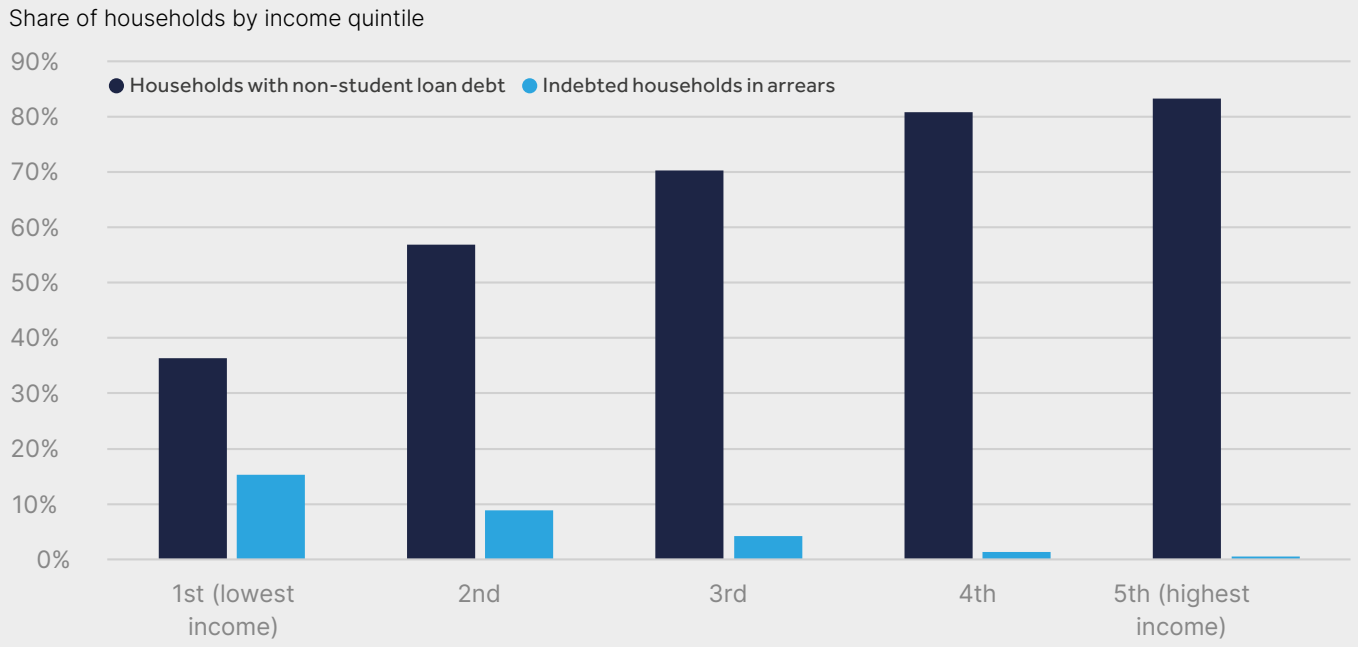
Control your debt

The 'control your debt' pillar is notable for there being no discernible relationship with income. In other parts of the barometer, as one would expect, more affluent households record higher scores, on average. The average score for this pillar was very flat across the income distribution and, indeed, the highest score was recorded by households in the lowest income band.

Although somewhat unintuitive, the result is driven by the fact that lower income households are, either through choice or lack of access, significantly less likely to hold any debt (Fig. 7). According to our data, just one-in-three households in the lowest income quintile held any debt less than half of the national average[5]. On the other hand, those lower income households who do take on debt typically find it much harder to control, as suggested by a much higher rate of arrears. Indeed, we estimate that over 15% of those low-income households, who have taken on debt, are behind on a (non-mortgage) debt repayment or a household bill, more than four times the national average.

The data highlights the primacy of debt control to financial resilience. Indeed, in Hargreaves Lansdown's model it is identified as the number one financial management priority as it is with careful budgeting and debt management that you can build the foundations for more aspirational elements of financial resilience.

FIG. 7. LOW-INCOME HOUSEHOLDS MUCH LESS LIKELY TO HOLD DEBT BUT THOSE THAT DO FIND IT HARDER TO CONTROL



Source: ONS data, Oxford Economics estimate

[5] In our discussions with Fair4All Finance, it was noted that the most indebted households on low incomes are likely to be underrepresented in the type of surveys that we have used to construct the barometer.

PROTECT YOUR FAMILY

16.6%

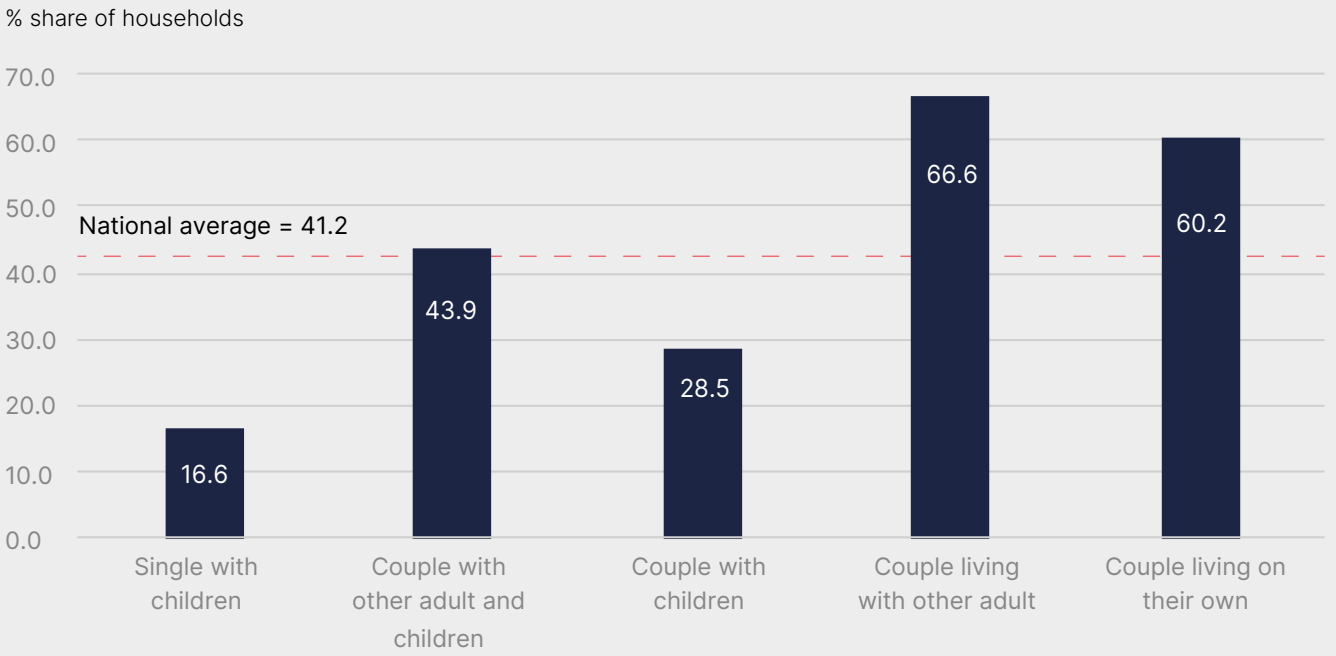
Just one-in-six of single-parent households have combined assets and life insurance to cover mortgage liabilities and future living costs for their children in the event of their death.

Protect your family
The 'protect your family' pillar in the barometer is unique in being non-universal—for obvious reasons we have evaluated this data for multi-person households only. For working adults, insuring against catastrophe risk is a mundane but necessary action to ensure that your dependents would not face a highly adverse financial situation in the event of these tail risks.

Our data highlights substantial gaps in the adequacy of life insurance coverage for families across Britain. Overall, less than half (41.2%) of families were found to have combined assets and life insurance that would cover mortgage liabilities and future living costs of their children. For this group, the untimely demise of the primary earner would result in greater financial stress for their loved ones.

As shown in Fig, 8 the gaps vary substantially across different family types. In general, households with children (aged under 18) are much less likely to meet this resilience threshold, with single-parent households particularly more likely to fall short. This trend is, in part, built into our measure – the presence of children increases the value of liabilities that are used to calculate this ratio. Nevertheless, the data does underscore the widespread jeopardy faced by a majority of younger families.

FIG. 8. SHARE OF FAMILY HOUSEHOLDS WITH ADEQUATE LIFE INSURANCE COVERAGE BY FAMILY TYPE



Source: FLS data, Oxford Economics analysis

SAVE A PENNY FOR A RAINY DAY

73.2%

Households with access to liquid savings that would cover at least three months of essential spending.

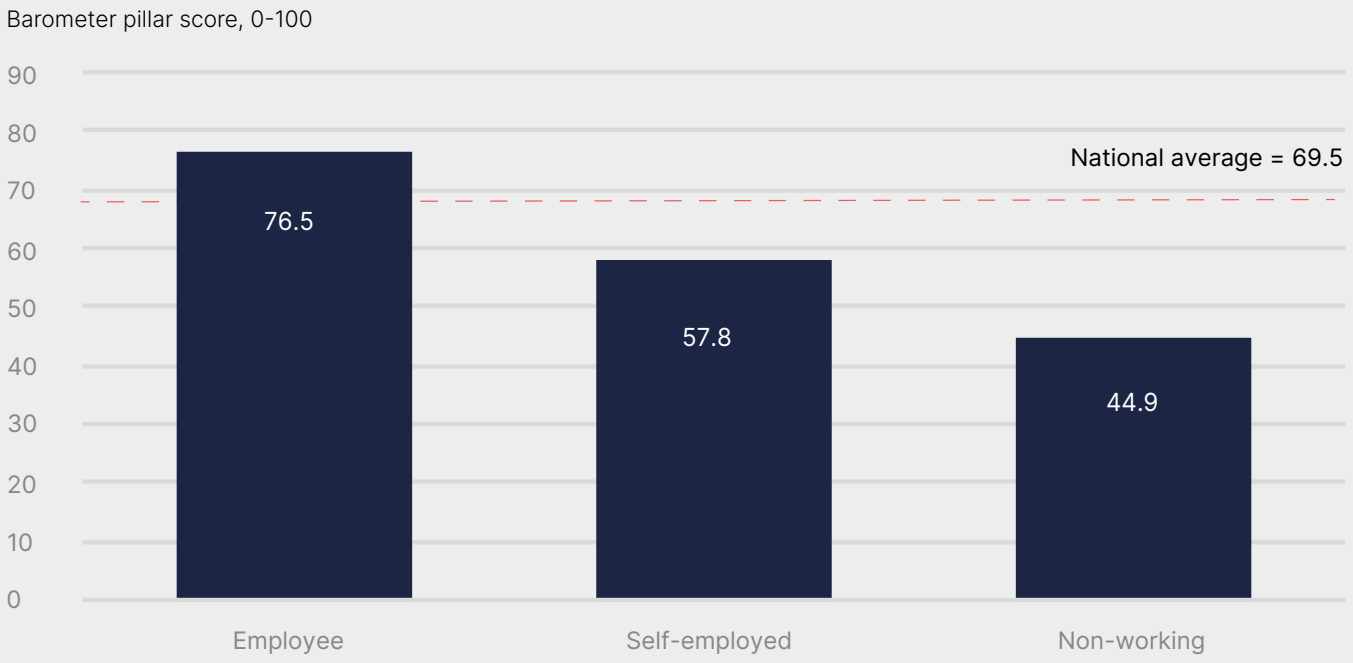
Save a penny for a rainy day
The ability of a family to weather the ups and downs of everyday financial life is a core tenet of financial resilience. Our 'save a penny for a rainy day' pillar combines information on a household's stock of liquid savings—the most conventional resource used to deal with such an event—with indicators that aim to speak to the risk of the event occurring.

In terms of the former, we estimate that at the end of the pandemic, just over seven-in-ten households across the nation achieved our benchmark of having access to savings that would cover at least three months of essential expenditure.

Diving deeper, the barometer data highlights interesting differences between households depending on employment type (Fig. 9). Straightforwardly, non-working households scored well below the national average with the lack of employment being associated with lower income and a less ability to build a savings buffer. The significant difference between the average score of employee households (64.6) and self-employed households (48.1), however, is more noteworthy.

In terms of income and liquid savings, there is little to separate the two groups, but those in employment are significantly more likely to be entitled to more generous sick and redundancy pay that would help to ameliorate the consequences of two of the major sources of a personal income shock. Although somewhat crude, the divergence speaks to the trade-offs that confront the self-employed who typically face greater income uncertainty and volatility. [6]

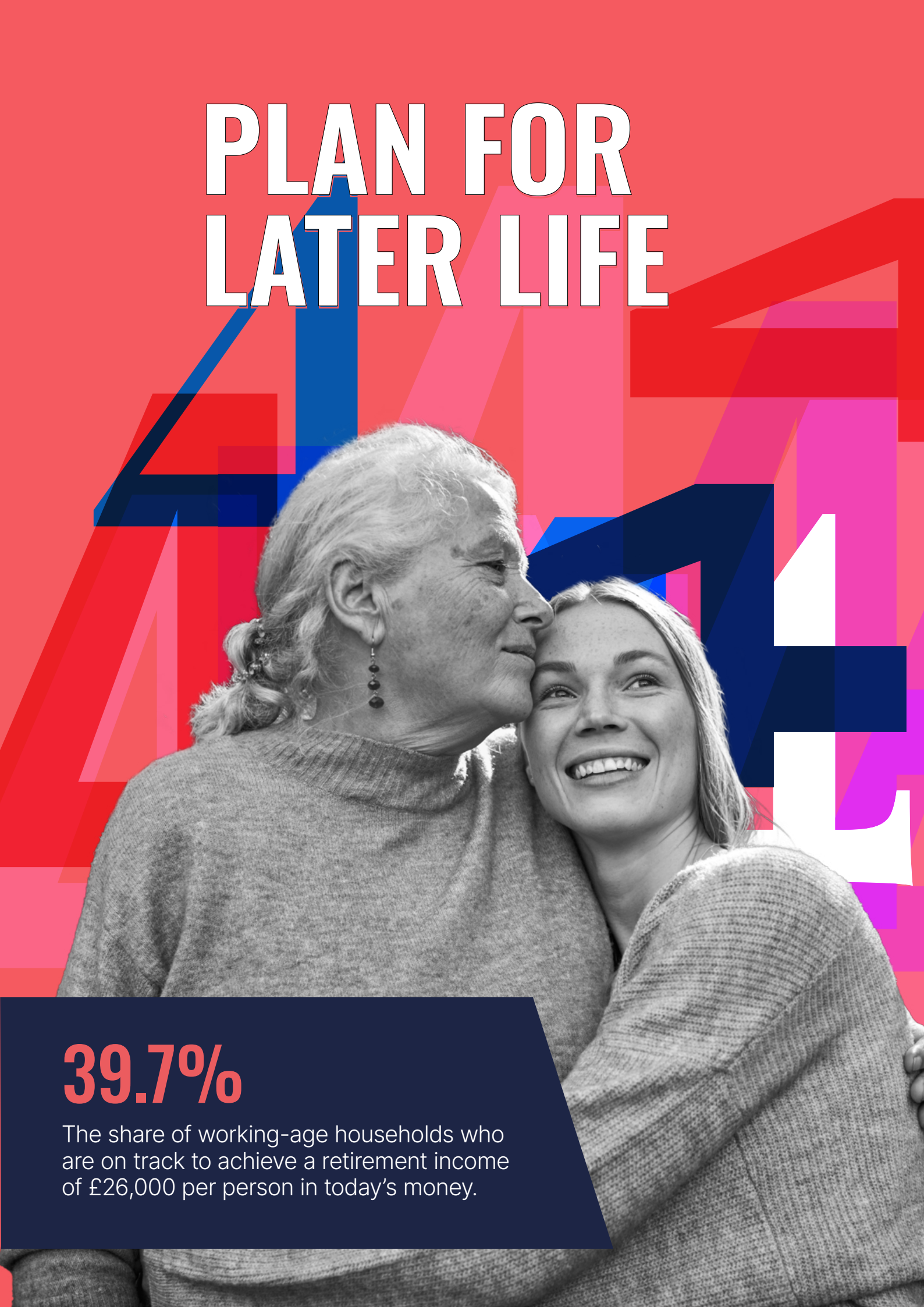
FIG. 9. 'SAVE A PENNY FOR A RAINY DAY' PILLAR SCORE BY EMPLOYMENT STATUS



Source: ONS data, Oxford Economics estimate

[6] Accurately measuring income volatility is very challenging and we have not attempted to include an indicator in the barometer which formally addresses this concept. This choice reflects our lack of confidence that we would be able to develop an indicator that could produce credible measurement.

PLAN FOR LATER LIFE



39.7%

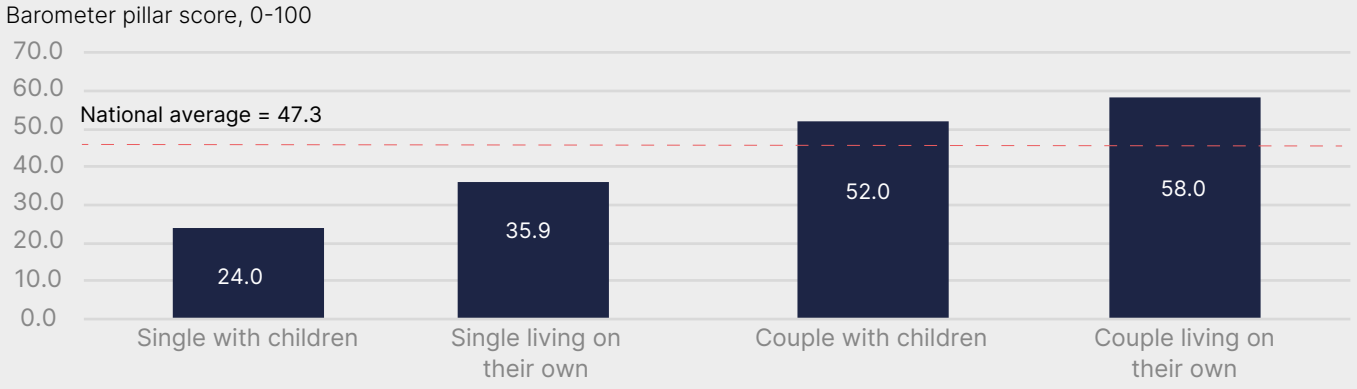
The share of working-age households who are on track to achieve a retirement income of £26,000 per person in today's money.

Plan for later life

Concerns that British households are failing to save sufficiently for retirement have been a persistent concern for policymakers, and, despite the success of the automatic enrolment scheme, our database highlights that this remains an ongoing issue. Our modelling framework takes the current value of each household's pension assets and projects how this can be expected to translate into a retirement income. This suggests that, even with the additional support of the State pension, less than 40% of working age households are on track to achieve a per capita retirement income of £26,000—roughly equivalent to the national average.[7]

Of course, a pension plan is not the only means through which households can plan for retirement and our 'plan for later life' pillar also incorporates data on the value of other assets. Fig. 10 displays the average pillar scores across different family types. The results highlight the challenges faced by a majority of single parent households in investing and planning for the future. This group's average barometer pillar score of 24.0 was half the national average.

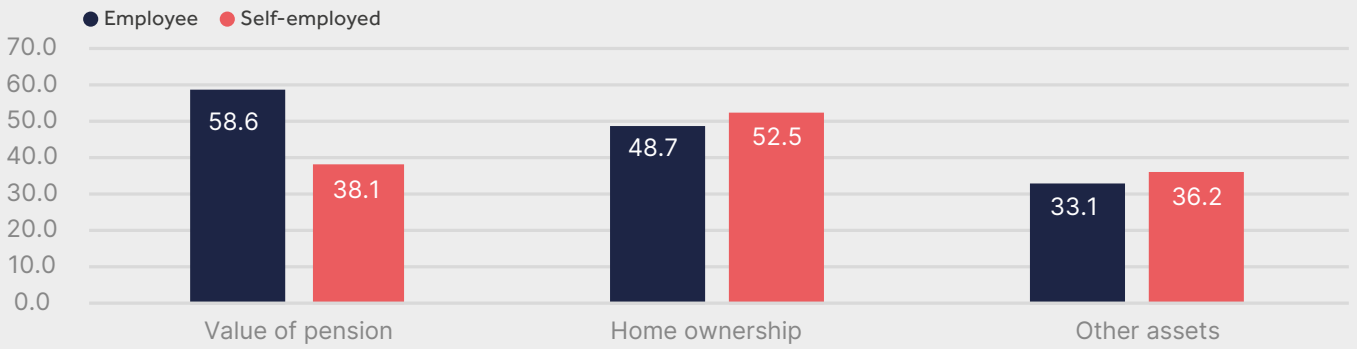
FIG. 10. PLAN FOR LATER LIFE SCORE BY FAMILY TYPE



Source: Oxford Economics estimates

Striking differences in this category also emerge by employment status. Overall, households where the primary earner was an employee enjoyed a significantly higher average pillar score compared to the self-employed. Pension plan provision for the former group was much more likely to be consistent with a comfortable retirement, with 42.8% of employee households achieving our threshold value for pension adequacy, almost twice the rate of the self-employed. However, lower lifetime contributions to their pension by the self-employed will have contributed to this group enjoying higher levels of wealth in terms of other assets. As shown in Fig. 11, self-employed households enjoyed higher average scores for both the 'home ownership' and 'other assets' indicators.

FIG. 11. SELF-EMPLOYED'S HIGHER LEVEL OF WEALTH NOT SUFFICIENT TO OFFSET THE PENSION GAP



Source: Oxford Economics

[7] The threshold was set based on research undertaken by Loughborough University on behalf of the Pensions and Lifetime Savings Association. See https://www.retirementlivingstandards.org.uk/ for more details.

INVEST TO MAKE MORE OF YOUR MONEY

5

14.1%

We estimate that 14.1% of British households do not hold any less liquid assets despite having liquid savings that could cover at least six months of essential spending.

Invest to make more of your money
The fifth barometer pillar—invest to make more of your money—tracks how households are allocating their savings in other less liquid assets. These typically offer a higher expected rate of return compared to standard savings accounts but are less readily available and come with higher risk.

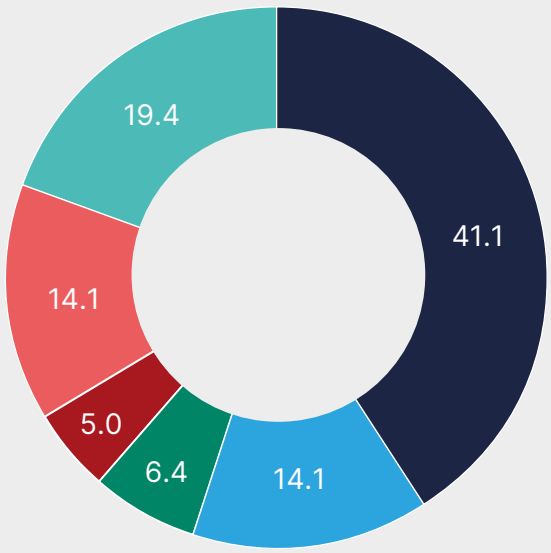
Striking the right balance between risk and reward in an asset portfolio is often challenging for households who typically lack the detailed financial knowledge of professional investors. The barometer is founded on a principle that the priority for any household should be to build up a highly liquid savings buffer (to cover at least three months of essential spending) before allocating any surplus income to other investments.

According to the data, just under 40% of households held some form of non-liquid investments, outside of their own home and pension. Of this group, a majority—nearly two-in-three—had access to highly liquid savings that could cover at least three months of essential spending. However, this still leaves around 14% of all households investing before they have built up adequate savings.

Equally, it is quite possible to skew too far in the opposite direction. According to our data, around one-in-three British households hold liquid savings that would cover at least six months of essential expenditure (Fig. 12). In isolation, more is better, but there comes a point at which these savings would be more wisely allocated to other investment opportunities. Of this group, around 40% do not hold any less liquid assets. Whilst we cannot infer from the data why people are holding higher liquid savings, one quite rational reason for holding a very large level of liquid savings would be for first-time buyers saving up for a deposit. However, nearly three-quarters of this group (10.3% of all households) are homeowners.

FIG. 12. OVER 14% OF BRITISH HOUSEHOLDS HOLD LESS LIQUID INVESTMENTS (OUTSIDE THEIR HOME) DESPITE HAVING ACCESS TO LIQUID SAVINGS THAT COULD COVER 6 MONTHS OF ESSENTIAL SPENDING

% share of British households



- Households with less than 3 months of essential spending, do not hold any less liquid investments.
- Households with less than 3 months of essential spending, hold less less liquid investments.
- Households with 3-6 months of essential spending, do not hold any less liquid investments.
- Households with 3-6 months of essential spending, hold less liquid investments.
- Households with more than 6 months of essential spending, do not hold any less liquid investments.
- Households with more than 6 months of essential spending, hold less liquid investments.

Source: Oxford Economics

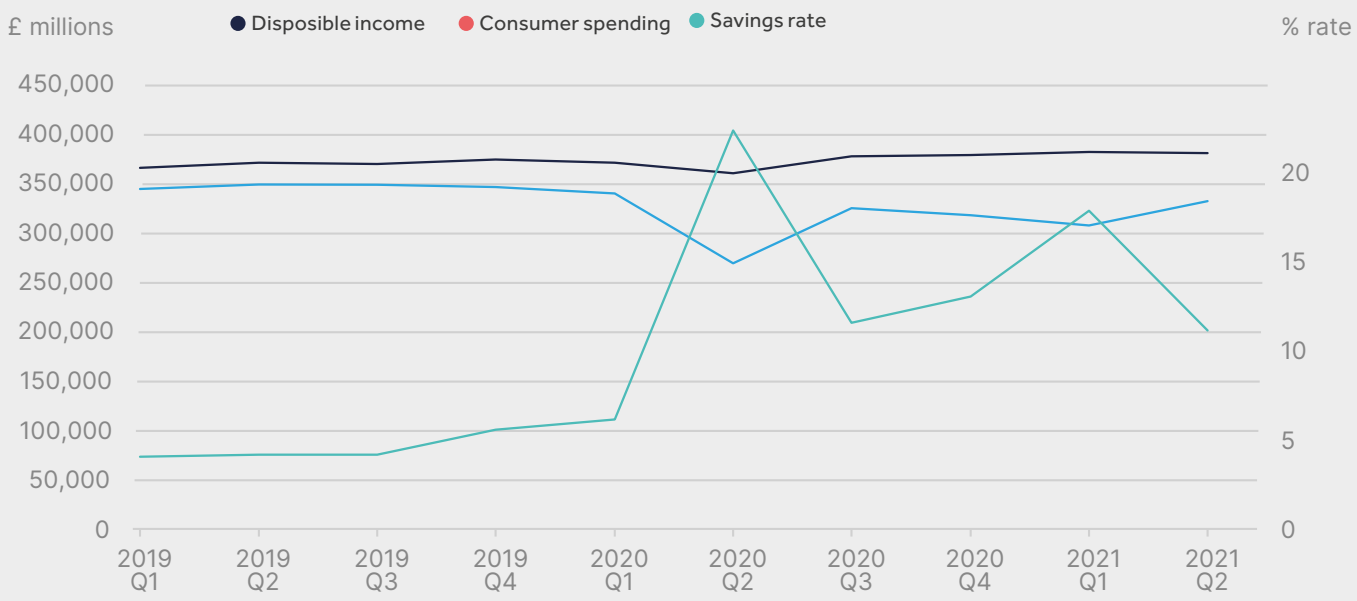
3. WHAT WAS THE IMPACT OF THE PANDEMIC?

In this chapter we examine the impact of the coronavirus pandemic, and its associated economic consequences, on financial resilience through the lens of the barometer. Specifically, we compare barometer scores at the end of 2021 Q2—just before the full reopening of society—with average conditions during 2019. Data limitations mean we have only been able to update indicators in three pillars: 'save a penny for a rainy day', 'control your debt' and 'plan for later in life'. Overall, these pillars account for two-thirds of a household's barometer score.

THE PANDEMIC WAS A PERIOD OF UNPRECEDENTED HOUSEHOLD DELVERAGING?

Despite triggering the deepest economic contraction in post-War history, UK household finances have remained surprisingly resilient. In contrast to the very large fall in economic output (GDP), household income remained broadly stable in 2020, supported by very generous levels of government finance through policy measures such as the job retention scheme (JRS) and the uplift to universal credit. Moreover, by enforcing a period of spending restraint, the pandemic period was associated with an extreme period of household deleveraging, with the savings rate increasing to a post-War high in 2020. At the same time, the stock of household consumer credit outstanding decreased by over 10%. [8]

FIG. 13. DISPOSABLE INCOME REMAINED BROADLY RESILIENT DURING THE PANDEMIC HELPED BY GOVERNMENT SUPPORT AS ENFORCED SPENDING CUTBACKS SAW THE SAVINGS RATE BALLOON



Source: ONS data

[8] According to Bank of England data, the stock of consumer credit outstanding fell from £224.4 billion in 2019 Q4 to £197.5 billion in 2021 Q2, a decrease of 12%.

...BUOYING FINANCIAL RESILIENCE IN AGGREGATE

Unsurprisingly, against this macroeconomic backdrop, UK households appear to have become more financially resilient, in aggregate, during this period. As displayed in Fig. 14, the barometer increased by 3.1 points during the pandemic. The largest contributor to this increase was from the 'save a penny for a rainy day' pillar, a reflection of the enforced belt tightening undertaken by most households. The fruits of the generally strong performance of assets held by UK households are reflected in the rise in the 'plan for later life' pillar score.

FIG. 14. PANDEMIC SAVINGS AND DELEVERAGING HAVE HELPED TO BOOST BRITAIN'S FINANCIAL RESILIENCE

Pillar barometer scores, 0-100 scale

Source: Oxford Economics

CHANGES IN SPENDING AND SAVING WERE FAR FROM EVEN...

Despite such a positive overall picture, there is clear evidence that the impact of the pandemic on spending patterns has been highly uneven. Using a combination of macroeconomic data and survey evidence we have estimated changes in income and spending per quarter up to 2021 Q2 for each household in our database controlling for characteristics such as income, family type and housing tenure. The results are displayed in Fig. 15 which highlights two particularly notable trends.

First, reductions in expenditure were disproportionately tilted towards higher income households. Indeed, our modelling suggests that, on average, spending by households in the lowest income quintile broadly flatlined during the pandemic compared to very significant average declines of over 10% for households in the top two income quintiles. This very stark difference, in part, reflects the fact that higher-income households allocate a much higher proportion of their spending to items such as travel, transport and leisure services that were disproportionately constrained by the pandemic.

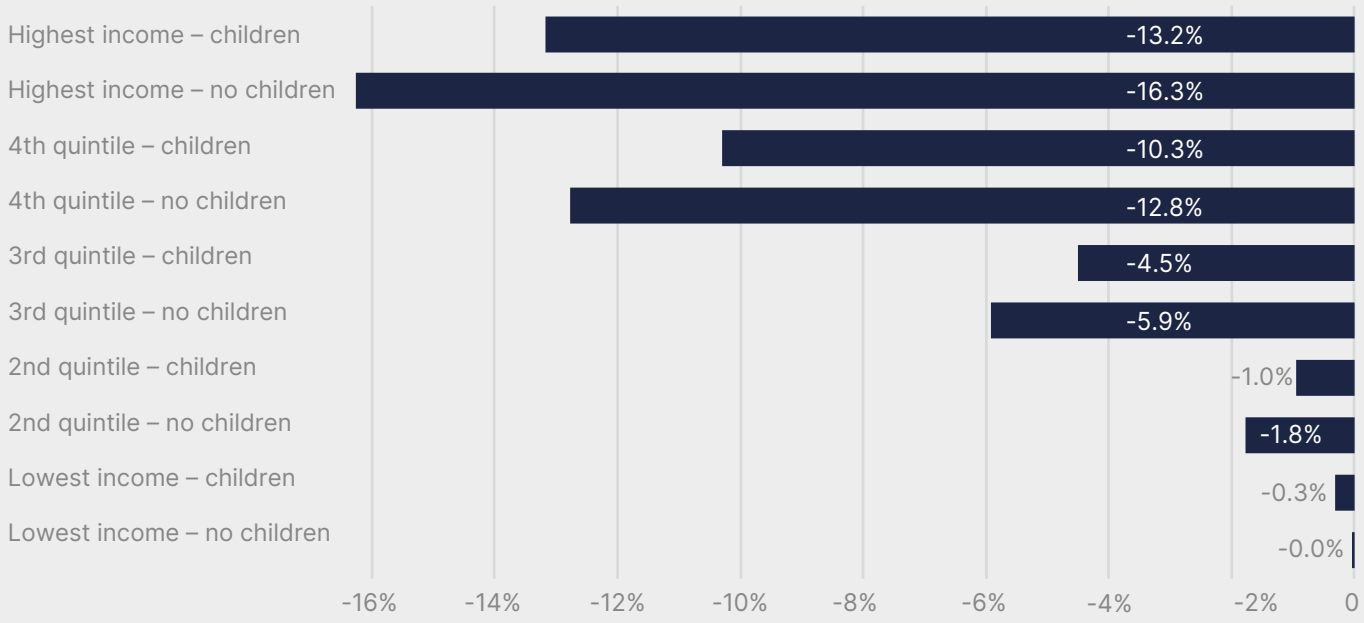
Second, Fig. 15 also highlights the divergence that was created by households according to the presence or otherwise of children. Across the income distribution, households with children registered lower average falls in spending, presumably linked keenly to the requirement for home schooling during this period which necessitated additional expenditure on items such as food.

-0.1%

Low-income households' monthly expenditure remained barely changed during the pandemic compared to an overall decline in household spending of over 9% during this period.

FIG. 15. PANDEMIC SPENDING RESTRAINT MUCH LESS EVIDENT FOR LOW-INCOME HOUSEHOLDS DUE TO HIGHER DEPENDENCE ON ESSENTIAL ITEMS...

% change, pandemic vs 2019 average



Source: Oxford Economics

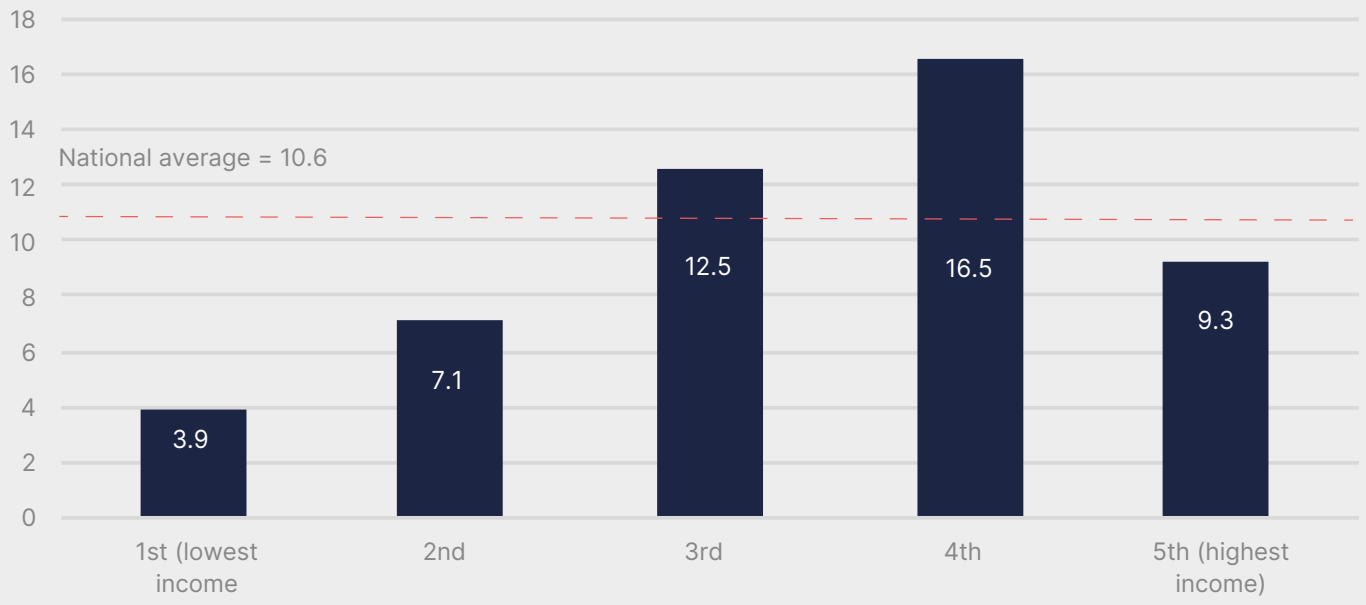
...AS REFLECTED IN THE BAROMETER

These dynamics can be more clearly explored through the lens of the 'save a penny for a rainy day' pillar, which saw the most significant changes during the pandemic. As illustrated in Fig. 16, the average increase in this barometer pillar score varied substantially across household income groups. [9]

Nevertheless, the across-the-board is encouraging and reflective of policy measures that were highly effective at providing income support to poorer households during this period. Our modelling suggests that income for low-income households was 1.6% higher (in nominal terms) on average during the pandemic period compared to 2019. A key driver of this was the decision to raise universal credit payments to £120 per week. Monitoring how the decision to phase out this uplift affects this group will, therefore, be of primary interest in 2022.

FIG. 16. ...LEADING TO A MUCH MORE MODEST BOOST TO SAVINGS RESILIENCE FOR THIS GROUP

Change in 'save a penny for a rainy day' pillar score, 2021 Q2 vs 2019



Source: Oxford Economics

[9] As displayed in Fig. 10, households in the highest income quintile registered a below-average increase in the 'save a penny for a rainy day' pillar score despite recording the largest proportionate decline in expenditure during the pandemic. This inconsistency can be explained by the fact that a relatively high proportion (76%) of this group had achieved the resilience threshold level for liquid savings prior to the pandemic, which naturally limits the extent of the subsequent increase.

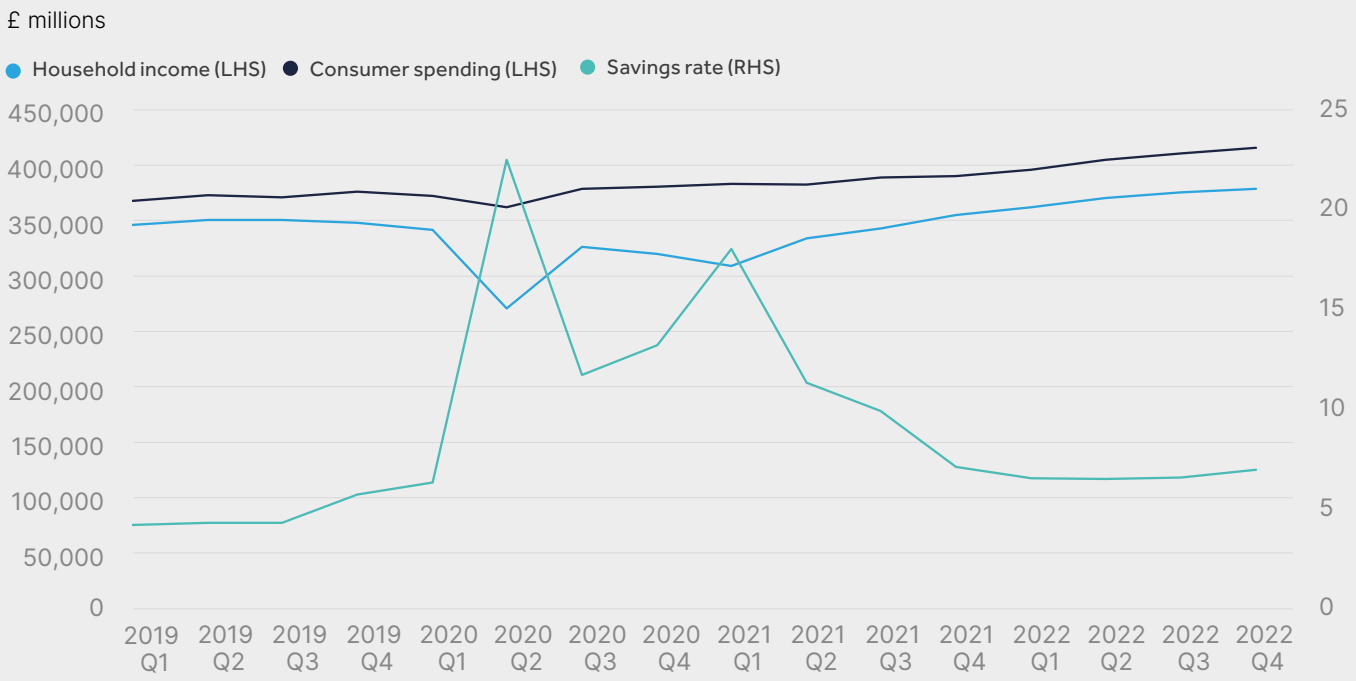
4. THE OUTLOOK FOR 2022

In this chapter, we explore the impact of projected changes in Oxford Economics baseline forecast would affect household's financial resilience through the lens of the barometer.

4.1 OXFORD ECONOMICS' BASELINE FORECAST POINTS TO TOUGHER TIMES IN 2022

As described, the aggregate resilience of household finances during the pandemic was supported by an unprecedented level of government support and an enforced period of consumer restraint. As the economy has further reopened since the summer the savings rate begun to normalize, a process we expect to continue in 2022 (Fig. 17).

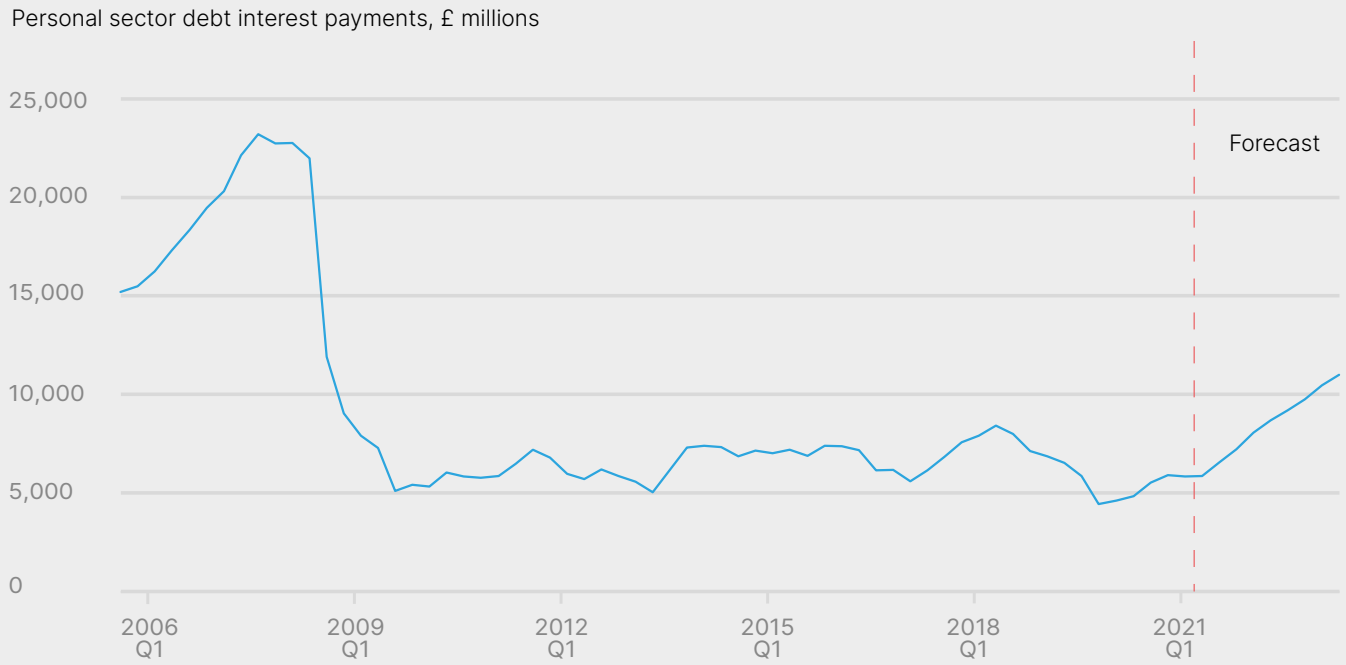
FIG. 17. UK HOUSEHOLD INCOME, CONSUMER SPENDING AND SAVINGS: 2019 Q1 – 2022 Q4).



Source: ONS data, Oxford Economics forecast

Although the new Omicron Covid variant has raised policy uncertainty, increases in the cost of living—inflation as measured by the Consumer Price Index (CPI) reached a decade-long high of 4.1% in October 2021 – has also raised speculation that the Bank of England will soon act to tighten monetary policy. At the time of writing, the forecast expects the Bank's policy rate to increase to 0.5% by the end of 2022 pushing up the cost of credit and mortgage finance. As shown in Fig. 18, such developments would see a steady increase in debt interest payments, squeezing household budgets, although they should remain well below levels seen before the global financial crisis.

FIG. 18. INFLATIONARY PRESSURES SHOULD SEE MODEST INTEREST RATE HIKES LEADING TO A RISE IN DEBT REPAYMENTS

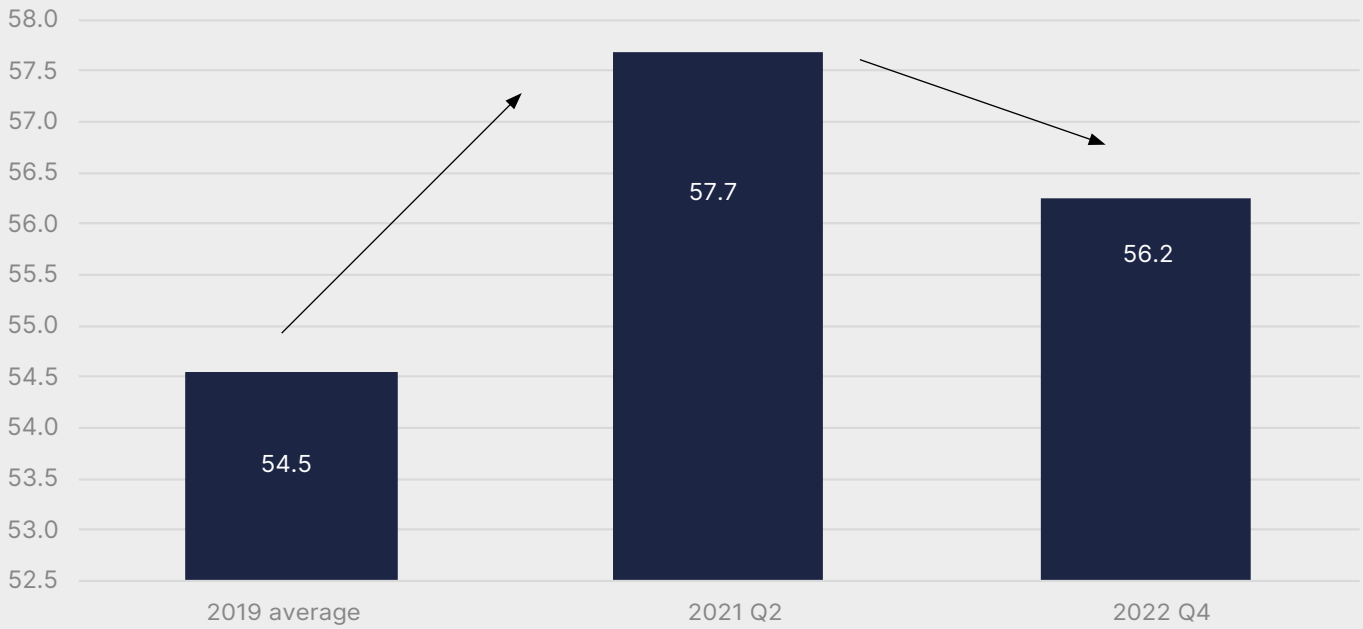


Source: ONS data, Oxford Economics forecast

Simulating these forecast trends through our barometer suggests that these events would reverse approximately half of the improvement in financial resilience experienced during the pandemic. The national average barometer score is projected to decline by 1.4 points to 56.2 (Fig. 19). The key drivers of these changes reflect the previously described macroeconomic trends. The largest contributor to the forecast decline in 2022 is a reduction in the level of surplus income, consistent with a return to pre-pandemic spending trends. On the face of it, this should not be a cause for concern. Higher interest rates, on the other hand, will reduce the affordability of debt repayments for households across the country manifested by a forecast 2.3 points fall in the 'control your debt' pillar score.

FIG. 19. ECONOMIC HEADWINDS AND A RETURN TO MORE NORMAL SPENDING PATTERNS MEAN WE EXPECT RESILIENCE TO FALL BACK IN 2022 BUT TO REMAIN ABOVE THE PRE-PANDEMIC LEVEL

Barometer scale, 0-100 scale

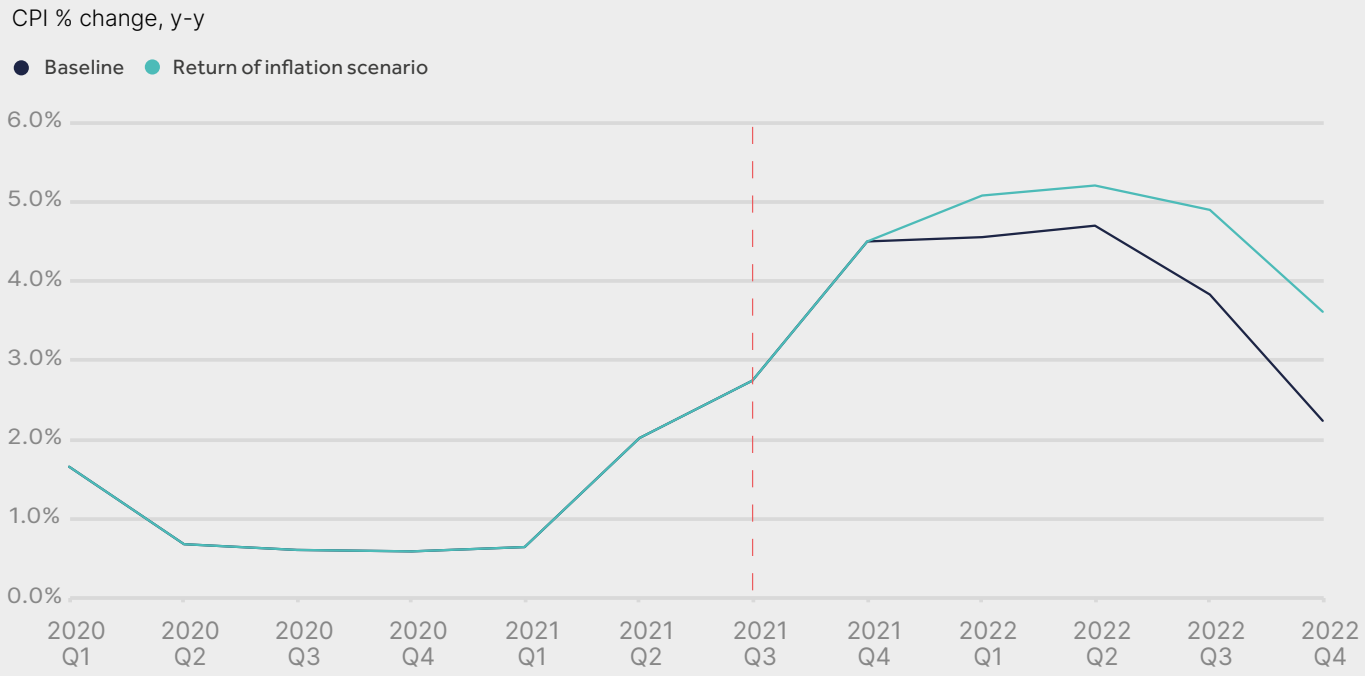


Source: Oxford Economics

4.2 HIGHER INFLATION MAY NOT SIGNIFICANTLY DENT FINANCIAL RESILIENCE

As discussed, inflation has become a much more talked-about economic risk over the past six months. Oxford Economics baseline view is that this will be a largely transient phenomenon with inflation returning to close to the Bank of England's 2% target rate by the end of 2022. Clearly though there are risks to this view with the potential for some of the 'supply side' factors which are currently driving higher inflation, such as higher commodity prices, labour shortages and supply chain disruptions, to persist for longer. To assess the implications of this eventuality for financial resilience, we have simulated the barometer results against Oxford's alternative 'return of inflation' scenario displayed in Fig. 20.

FIG. 20. INFLATION EXPECTED TO FALL BACK TO TARGET IN 2022 BUT RISKS THAT IT COULD PERSIST FOR LONGER



Source: Bank of England data, Oxford Economics forecast

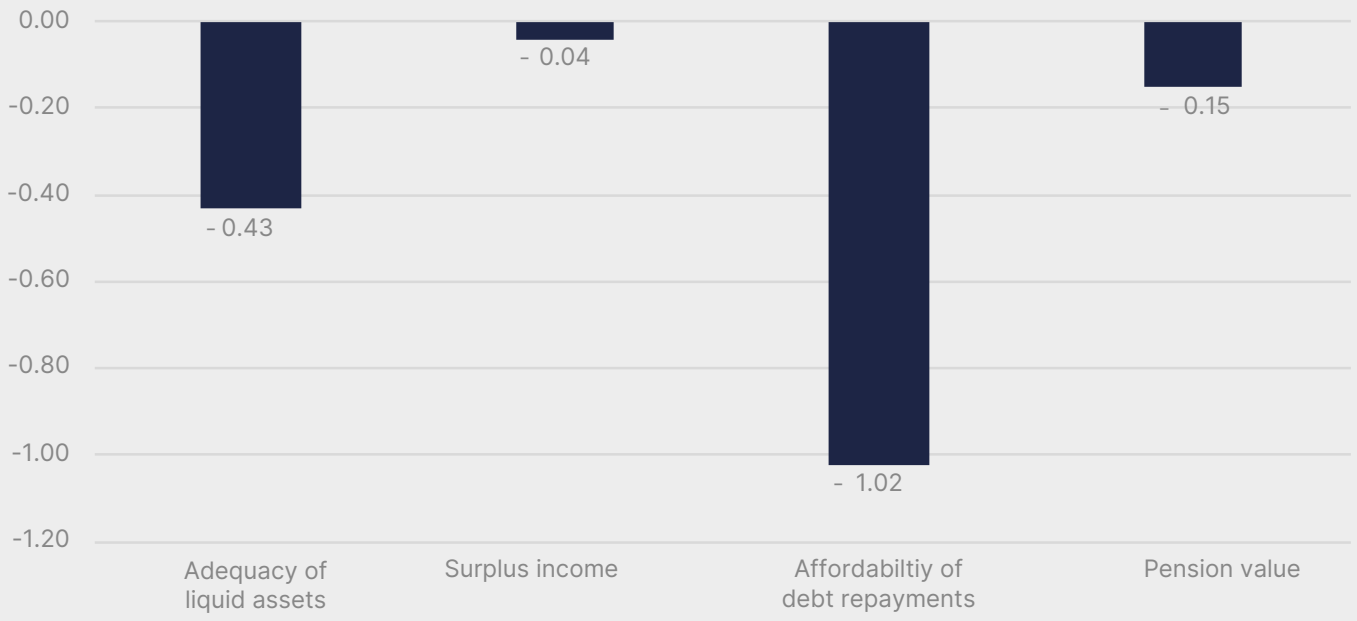
Such an outcome would certainly have negative economic consequences. Our modelling suggests that the UK economy would be 1.4% smaller, in real terms, by the end of 2022 compared to Oxford's baseline forecast. Such a reduced level of economic activity combined with higher inflation would inevitably depress living standards with average real household disposable income 1.7% below baseline.

Fig. 21 describes the impact of the scenario on three core pillars in the barometer. As displayed, the impact is, unsurprisingly, negative but is proportionately less severe than the impact on the real economy. The reason for this is the behavioural choices by both policymakers and households that help to moderate the impact on resilience, as measured. First, Oxford assume that the Bank of England would not react to such a period of higher inflation by raising interest rates, which helps to limit the impact of the scenario on the sustainability of household debt payments—the fall in that component of the barometer is principally driven by reduced income rather than higher repayments. This assumption reflects the nature of this inflationary shock. The drivers of higher prices, in this instance, do not point to an overheating economy, and, therefore, a need to tighten monetary policy.

Second, are choices made by households. As shown in Fig. 21 the impact of the scenario on the surplus income variable in the barometer is negligible. This reflects the simulated response of households to lower income which is to reduce expenditure broadly commensurately. The depth of households' liquid savings coverage would still weaken, as shown, due to the higher cost of day-to-day essentials.

FIG. 21. CHANGE IN SELECTED INDICATOR SCORES IN 2022 Q4: RETURN OF INFLATION SCENARIO VS BASELINE FORECAST

Change in indicator score, Scenario vs baseline



Source: Oxford Economics

5. CONCLUSION

The aim of this report has been to introduce HL's savings and resilience barometer, a tool that we believe can offer a holistic and timely measure to enhance our understanding of how economic events are shaping and future risks could shape the nation's finances. Our intention, however, is for this to be just the start. We plan to continue to update the barometer including new forward-looking scenarios every six months and to work with stakeholders to evaluate how the measure and underlying data can be enhanced and, potentially, used in support of policy.

As documented here, whilst the pandemic has wrought an immense human toll, policy support did much to mitigate the financial consequences for British households. Irrespective, our research has shone light on the significant gaps and challenges that confront families in handling the trade-offs inherent in financial planning. Going forward, as we continue to monitor and track developments through the lens of the barometer, we hope that such coverage will spur policymakers, support researchers and build awareness around these highly salient topics. This report embarks on that journey.

6. APPENDIX 1

Fig. 22. List of indicators, weights and threshold values used in the financial resilience barometer [13]

Pillar	Pillar Weight	Indicator	Indicator weight within pillar	Lower Threshold	Upper Threshold
Save a penny for a rainy day	0.22	Adequacy of liquid assets	0.5	0 = no liquid assets	100 = liquid assets covering at least 3 months' essential expenditure
		Surplus income	0.125	0 = no (or negative) surplus income	100 = surplus income at least 9% of net income [10]
		Sick pay	0.25	0 = no sick pay	100 = sick pay covering at least 3 months' essential expenditure
		Redundancy pay	0.125	0 = no redundancy pay	100 = redundancy pay covering at least 1.3 months' essential expenditure
Protect Your Family	0.22	Life insurance	0.67	0 = (assets + life insurance) covers mortgage, other liabilities and dependants' living costs with a shortfall of £163,831 or more [11]	100 = (assets + life insurance) covers mortgage, other liabilities and dependants' living costs fully
		Critical illness cover	0.08	0 = no income protection	100 = critical illness cover
		Income protection	0.08	0 = no income protection	100 = income protection
		Balance of earnings	0.17	0 = main earner earns all household income	100 = main earner earns 60% or less of household income

[10] 9% is the 90th percentile of the population

[11] £163,831 is the 10th percentile of the population

Pillar	Pillar Weight	Indicator	Indicator weight within pillar	Lower Threshold	Upper Threshold
Control Your Debt	0.22	Affordability of future debt repayments	0.44	0 = debt repayments are 45% or more of net income for those with a mortgage; or 19% or more of net income after rent for those without a mortgage [12]	100 = no debt repayments
		Uncertainty of future debt repayments	0.22	0 = all debt is variable rate	100 = no debt is variable rate
		Use of debt	0.11	0 = all debt is used for current consumption (e.g. holiday, leisure) and none for investment (e.g. student loan, mortgage) or capital consumption (e.g. car, furniture, home improvements)	100 = all debt is used for investment (student loan, mortgage) or capital consumption (car, furniture, home improvements) and none for current consumption (holiday, leisure)
		Arrears	0.11	0 = in arrears (excluding mortgage)	100 = not in arrears (excluding mortgage)
		Subjective evaluation of debt position	0.11	0 = debt is a burden	100 = debt is not a burden
Plan for Later Life	0.22	Value of pension	0.5	0 = no pension accumulated	100 = accumulated pension is on track to provide a moderate standard of living in retirement [13]
		Home ownership	0.25	0 = no housing equity	100 = housing equity at or above the national age-adjusted mean
		Other assets	0.25	0 = no (net) assets other than pension or housing equity	100 = (net) assets other than pension or housing equity at or above the national age-adjusted mean
Invest	0.11	Investment intensity	–	0 = no savings are invested in non-cash assets	100 = all savings are invested in non-cash assets

[12] 45% and 19% are the 90th percentiles of the populations with and without a mortgage respectively

[13] See the methodology document for more details

Hargreaves Lansdown, One College Square South,
Anchor Road Bristol BS1 5HL

Tel: 0117 900 9000
Registered number: 02122142
www.hl.co.uk

HL

0122

Issued by Hargreaves Lansdown plc.
Authorised and regulated by the Financial Conduct Authority.