



OECD Centre for
Opportunity and Equality

Evidence-based, policy-oriented research on inequalities

Inequality in the OECD Area: Trends, causes, consequences and remedies

Workshop *Inequality By The Numbers*, June 6 – 11, 2016

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Inequality – in the heart of policy discourse and debate



- “Rising income inequality is the **defining challenge of our times**” (President Obama, US)
- “Inequality can no longer be treated as an afterthought. We need to focus the debate on **how the benefits of growth are distributed**” (A. Gurría, OECD)
- “Reducing excessive inequality is not just morally and politically correct, but it is **good economics**” (C. Lagarde, IMF)

2008

Growing Unequal?
INCOME DISTRIBUTION
AND POVERTY IN OECD COUNTRIES



2011

Divided We Stand
WHY INEQUALITY KEEPS RISING



2015

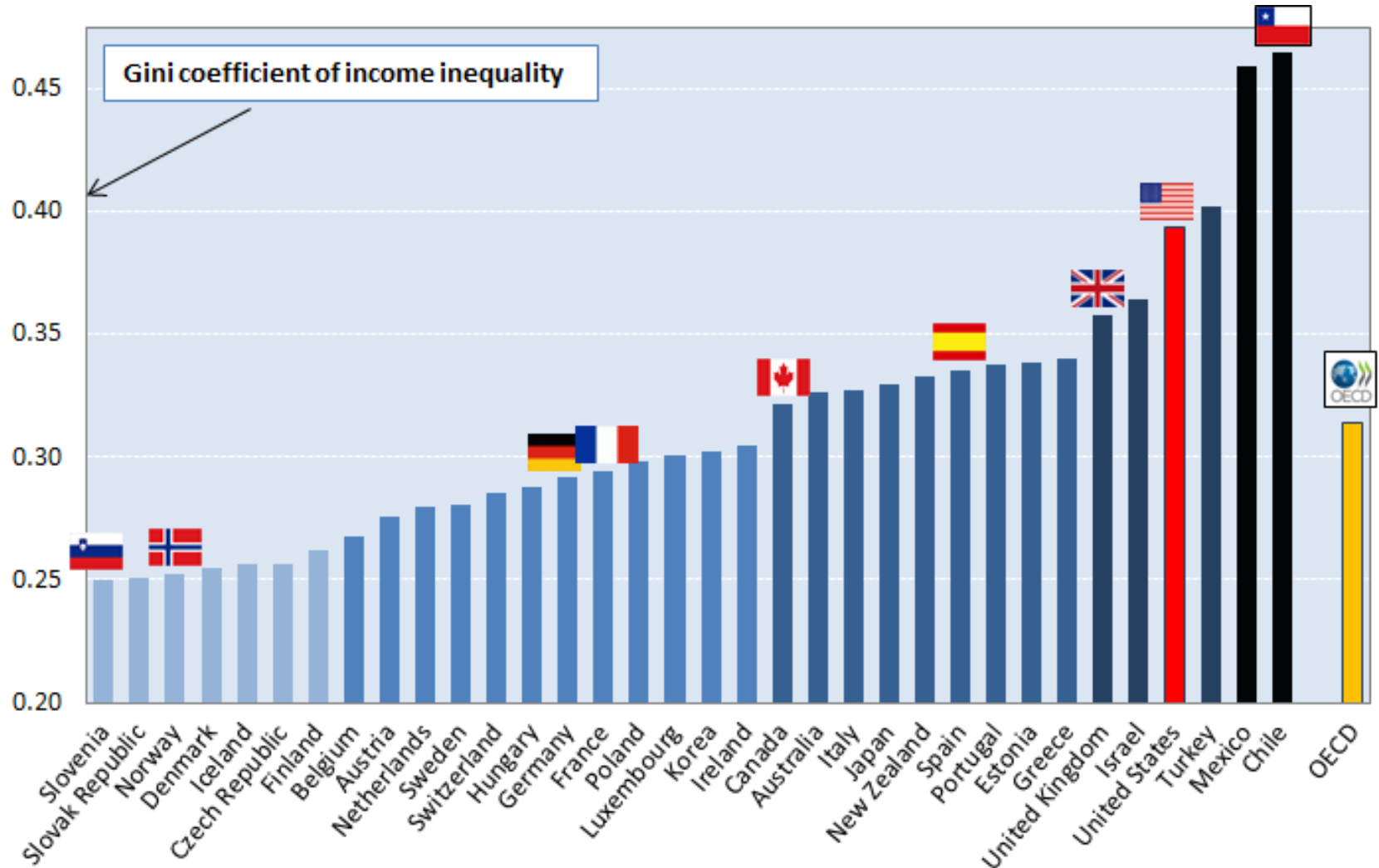
In It Together
Why Less Inequality Benefits All





1. **TRENDS:** How do inequality levels compare and how have inequalities developed over the longer run? Was the crisis a game changer?
2. **CAUSES:** What are the major underlying forces behind increases in inequality?
3. **CONSEQUENCES:** Why do we care? What are the links between inequalities, opportunities and economic growth?
4. **REMEDIES:** Which policies are most promising to tackle high and increasing inequality?

Large country differences in levels of *income* inequality



Source: OECD Income Distribution Database (www.oecd.org/social/income-distribution-database.htm),



Note: the Gini coefficient ranges from 0 (perfect equality) to 1 (perfect inequality). Income refers to cash disposable income adjusted for household size.

Data refer to 2014 or latest year available.

It is not just about income: *Wealth* is much more unequally distributed



Share of income and wealth going to different parts of the income and wealth distribution, respectively, around 2012

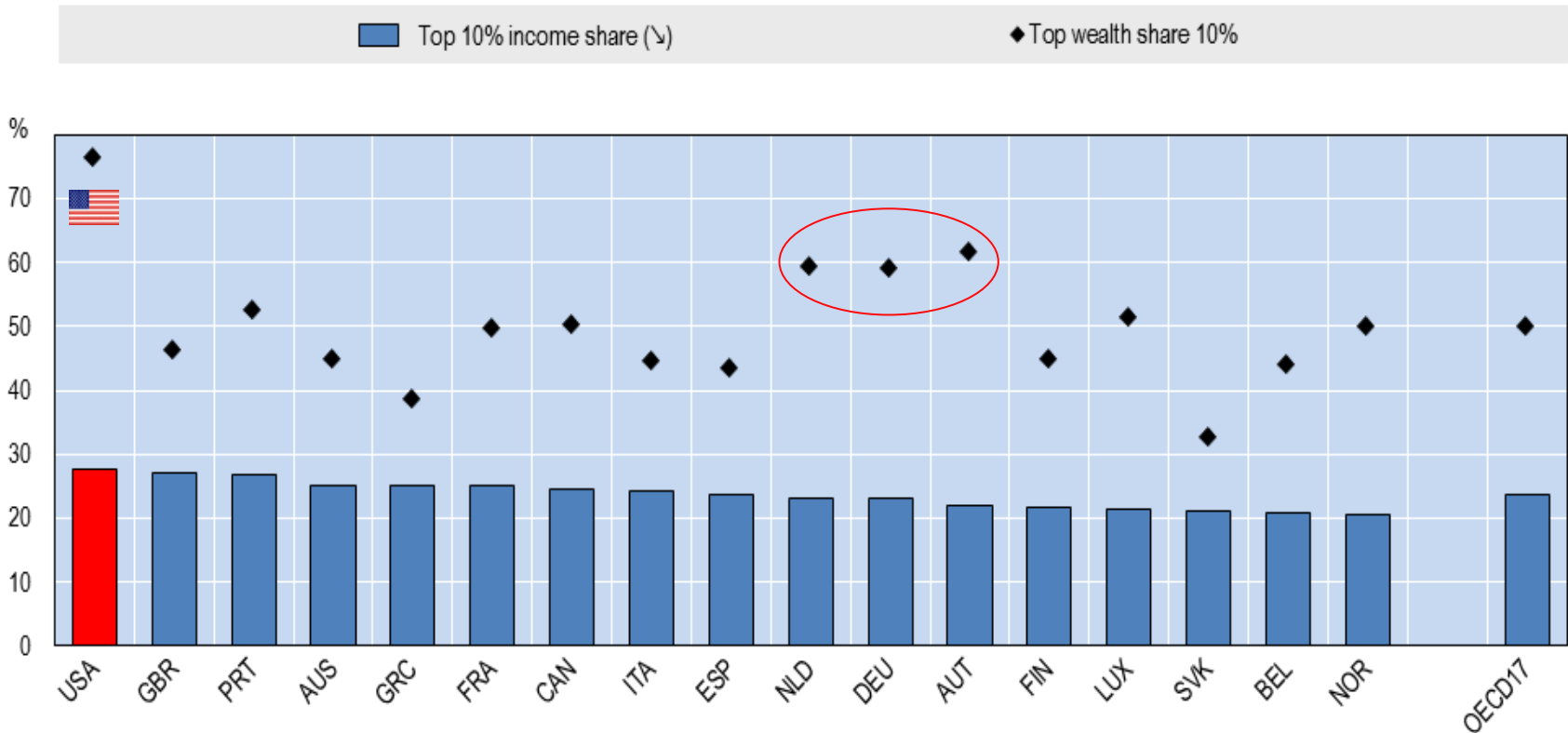
	OECD 		USA 	
	income	wealth	income	wealth
top 10%	25%	50%	29%	76%
next richest 50%	55%	47%	55%	24%
bottom 40%	20%	3%	16%	0%

Source: OECD (2015), "In It Together", <http://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm> .
 OECD wealth questionnaire and ECB-HFCS survey and OECD Income Distribution Database (www.oecd.org/social/inequality.htm)
 Note: : Income refers to disposable household income, corrected for household size. Wealth refers to net private household wealth.

Countries with high concentration of wealth are not (always) those with high income concentration



Share of top 10% of household disposable income and top 10% of household net wealth, 2012 or latest available year

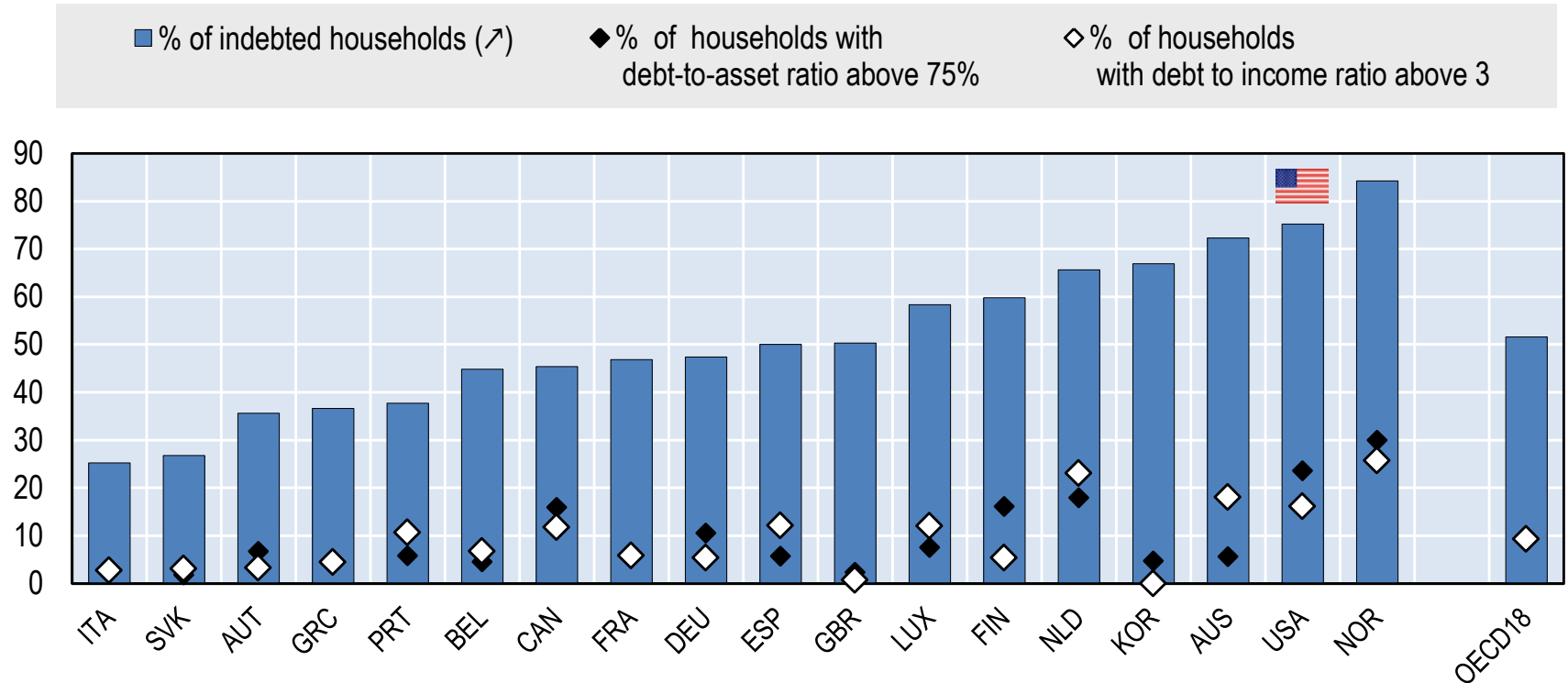


Source: Source: OECD (2015), "In It Together", <http://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm>
 OECD Wealth Distribution Database and OECD Income Distribution Database (www.oecd.org/social/income-distribution-database.htm).
 Note: Income refers to disposable household income, corrected for household size. Wealth refers to net private household wealth. Data refer to the shares of the richest 10% of income earners (bars) and of the richest 10% of wealth holders (diamonds), respectively.

The flipside of wealth: debt and over-indebtedness



Half of all households have debts and one tenth is over-indebted:
Percentage of indebted and over indebted households, 2012



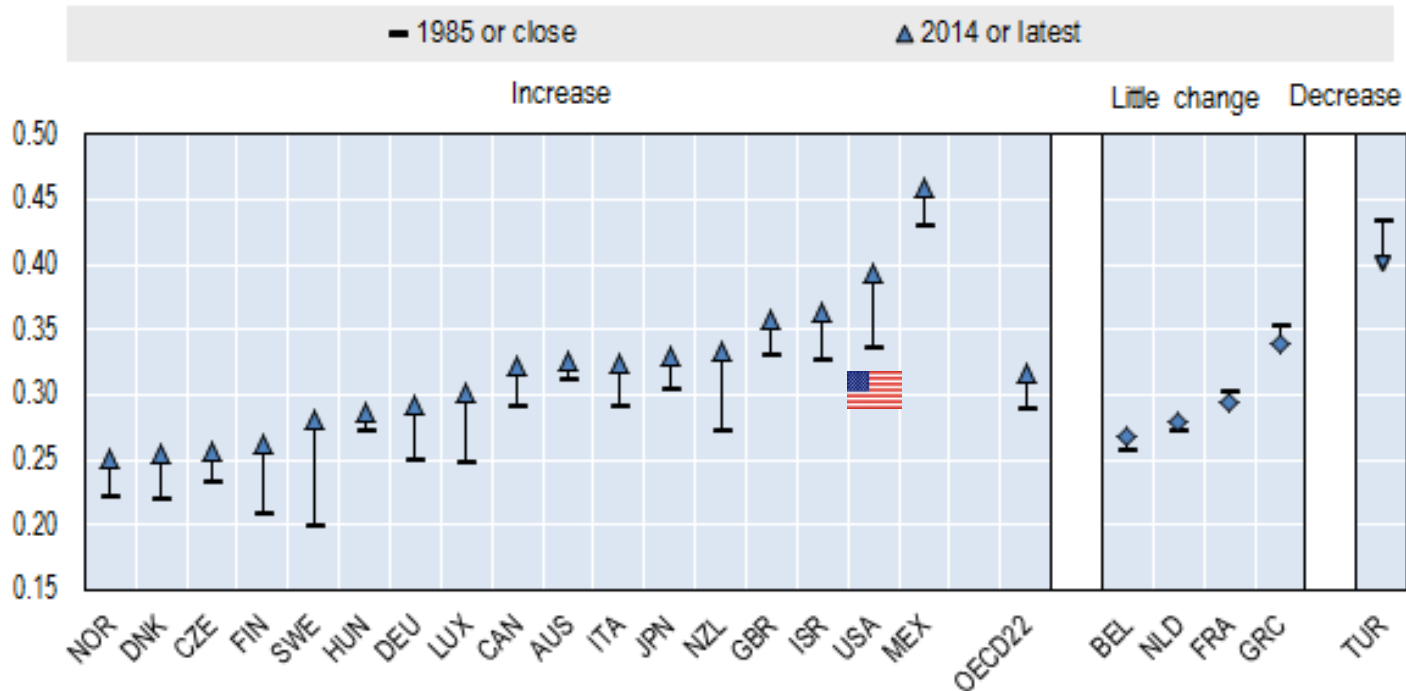
Source: OECD (2015), "In It Together", <http://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm>,
OECD Wealth Distribution Database and OECD Income Distribution Database (www.oecd.org/social/income-distribution-database.htm).

A long-term rise in *income* inequality



- The gap between rich and poor at its highest level since 30 years
- The richest 10% earn almost 10 times more than the poorest 10%
- This is up from a ratio of 7:1 (1980s); 8:1 (1990s); 9:1 (early 2000s)

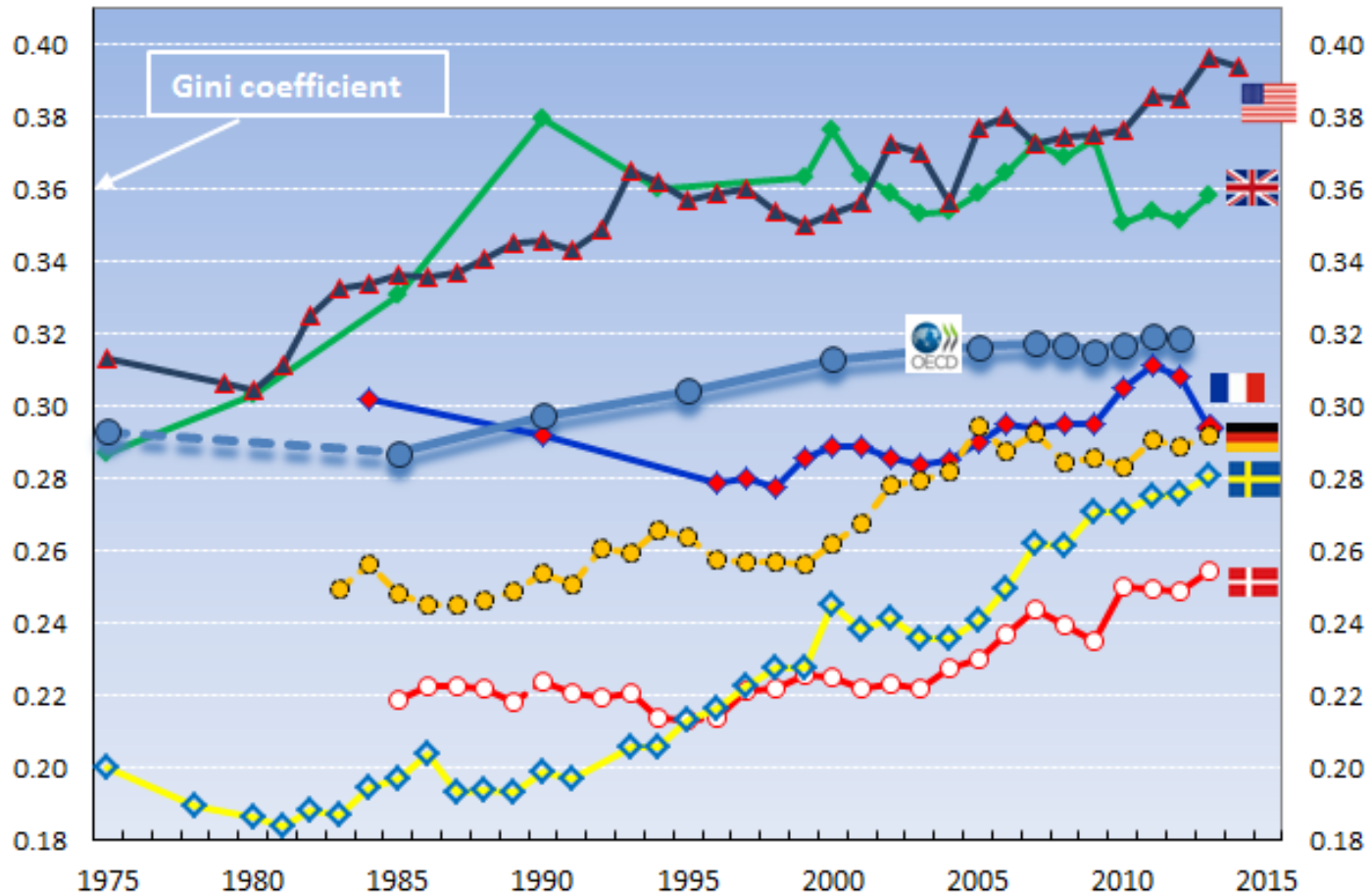
Gini coefficients of income inequality, mid-1980s and 2014, or latest date available



Rather than continuous long-term trends, “episodes” of inequality increases

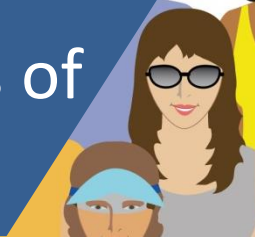


Long-term trends in inequality of disposable income (Gini coefficient)

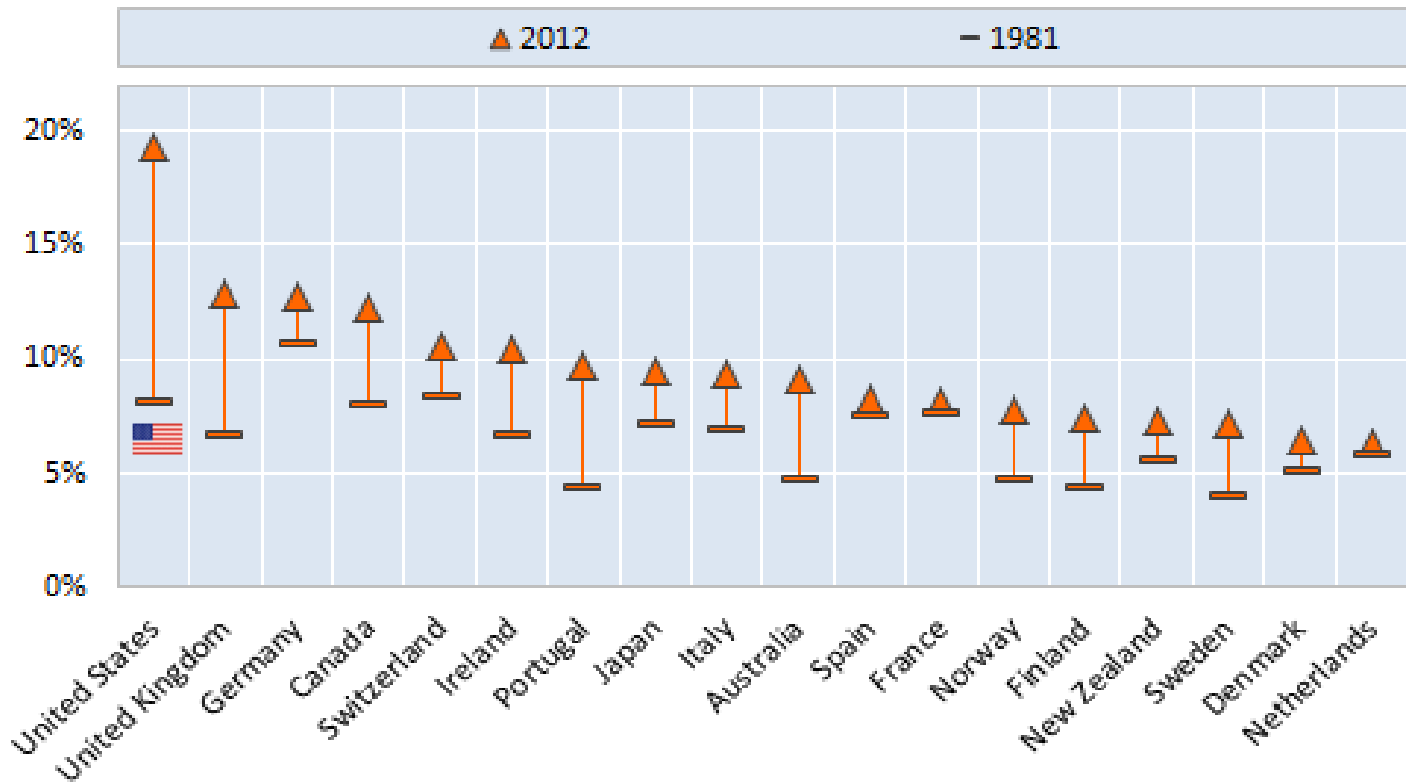


Source: OECD (2015), “In It Together”, <http://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm> OECD Income Distribution Database, www.oecd.org/social/income-distribution-database.htm.

Note: Income refers to disposable income adjusted for household size.



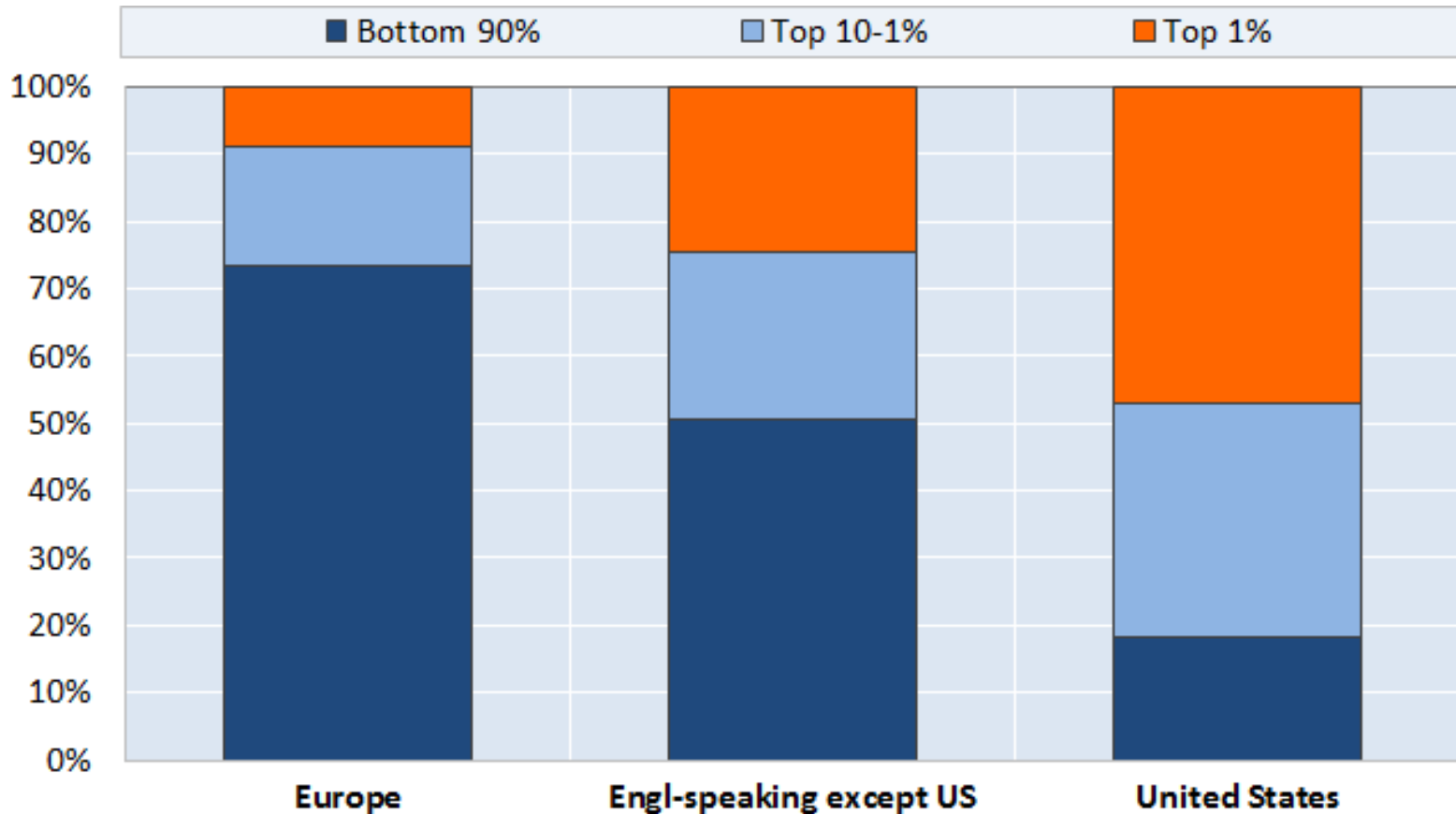
Shares of top 1% incomes in total *pre-tax* income, 1980 – 2012 (or closest)



Source: OECD 2014, *Focus on Top Incomes and Taxation in OECD Countries: Was the Crisis a Game Changer?* (<http://www.oecd.org/els/soc/OECD2014-FocusOnTopIncomes.pdf>), Based on World Top Income Database. Note: Incomes refer to pre-tax incomes, excluding capital gains, except Germany (which includes capital gains). Latest year refers to 2012 for the Netherlands, Sweden and the United States; 2011 for Norway and the United Kingdom; 2009 for Finland, France, Italy and Switzerland; 2007 for Germany; 2005 for Portugal; and 2010 for the remaining countries.



Share of income growth going to income groups from 1975 to 2007



Source: OECD 2014, *Focus on Top Incomes and Taxation in OECD Countries: Was the Crisis a Game Changer?* (<http://www.oecd.org/els/soc/OECD2014-FocusOnTopIncomes.pdf>), Based on World Top Income Database.

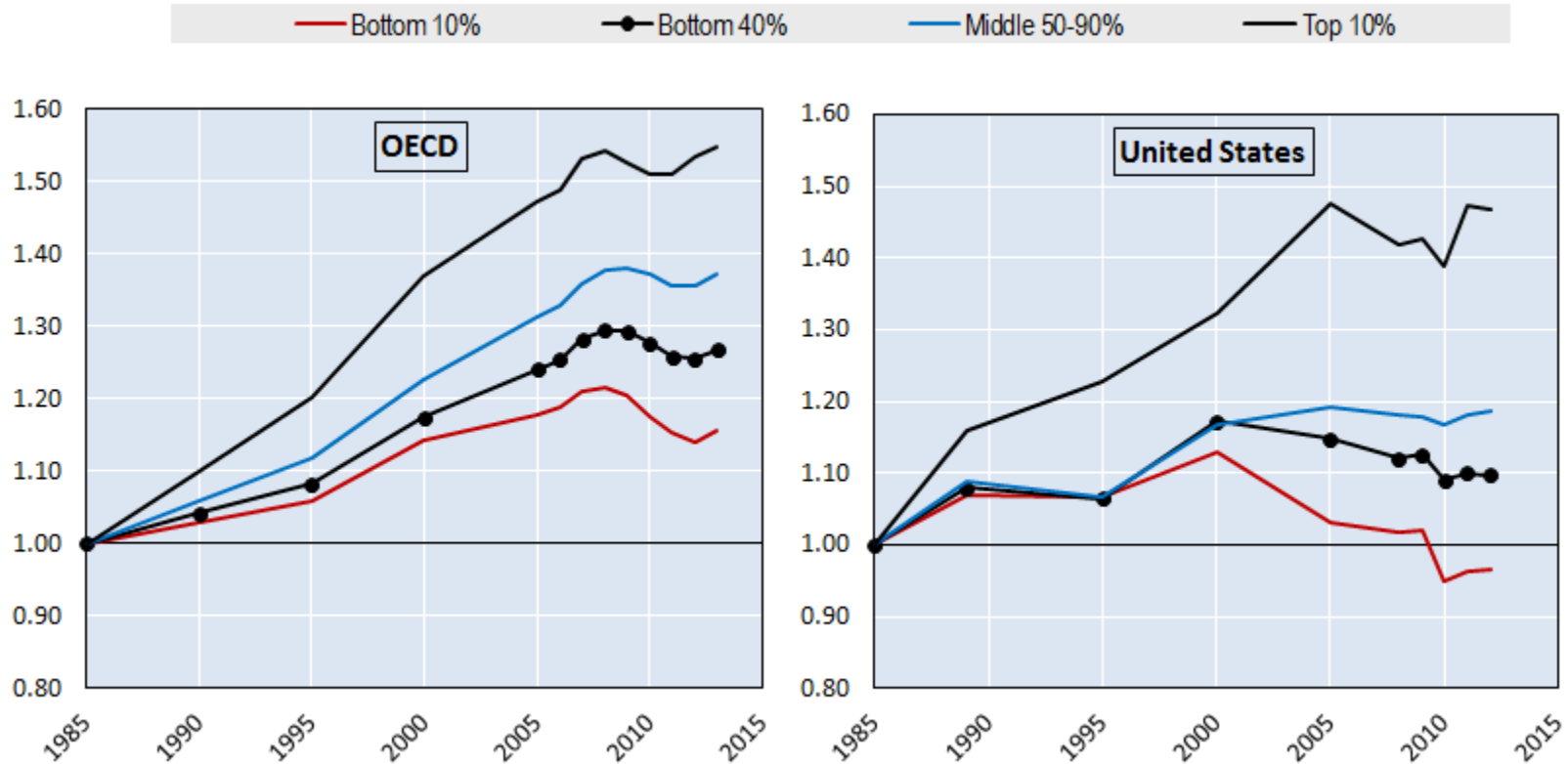
Note: Incomes refer to pre-tax incomes, excluding capital gains

But the rise of income inequality is, not only, about the top of the distribution



→ When looking at the long run, lower and lowest incomes were increasingly left behind

Trends in real household incomes at the bottom, the middle and the top, 1985 = 1



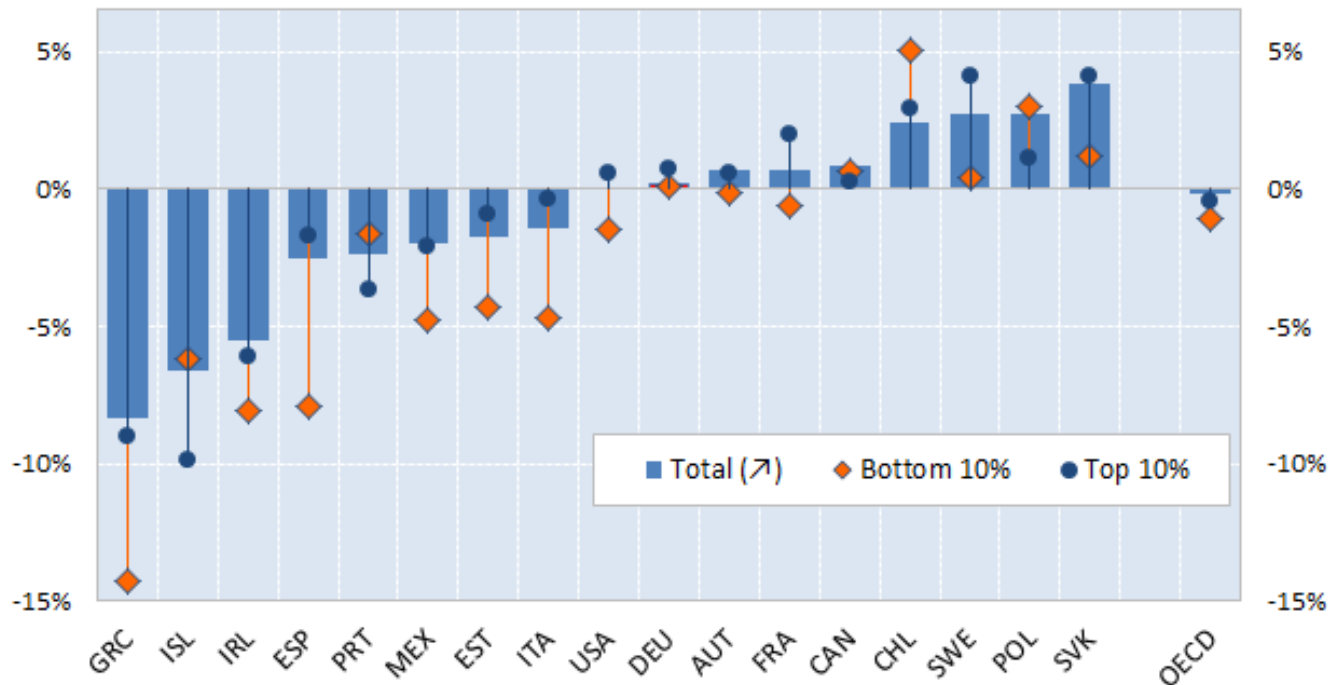
So was the crisis a game changer?



→ .. also during the crisis, in a majority of countries incomes of the poorest households fell behind in relative and, often, in absolute terms

Annual percentage changes in household disposable income between 2007 and 2011

2007-2011



Source: OECD 2014, *Rising Inequality: youth and poor fall further behind*. <http://www.oecd.org/els/soc/OECD2014-Income-Inequality-Update.pdf>

Note: 2008 – 2011 for France, Germany, Sweden.

Effects of tax and benefit policy changes on household incomes: two (or three?) different phases since the crisis



→ In many countries, households tended to gain from the policy changes implemented in 2008/09 and to lose from those in 2010/12. Effects in 2013 were less homogenous.

Simulated overall effect of tax-benefit measures, 10 OECD countries

	2008	2009	2010	2011	2012	2013	2007-2013
Estonia	+		-	-	-	+	+
France	-	+	-	-	-	+	+
Germany	-	+	+	-	+	+	+
Greece	+	+	-	--	-	--	--
Iceland	-	-	-	-	-	+	--
Ireland	+	-	-	--	-	-	--
Portugal	+	+	-	--	-	--	--
Spain	+	+	-	-	-	-	-
United Kingdom	+	+	-	-	-	-	-
United States	+	+			-	-	+
OECD10	+	+	-	-	-	-	-

Source: OECD 2015, "In It Together", Note: + sign indicates a measure that has a positive effect on household income (i.e. a tax cut or benefit rise). – sign indicates a measure that has a negative effect on household income (i.e. a tax rise or benefit cut).



Income inequality trends in the OECD area over the past three decades: the bottom line



- Inequality increased in good times, and it increased in bad times: *income* inequality has reached record highs in most OECD countries;
- The distribution of *wealth* is (much) more unequal than that of income;
- Inequalities go beyond resources: *education* and *health*
- Poorer households are losing ground. But it is not only about poverty – it is about the bottom 40%;
- OECD countries recorded a historically high level of inequality as they were shattered by the Great Recession in 2008;
- The GR squeezed market incomes but the welfare state has prevented *net* income inequality going from bad to worse in the *first years* of the crisis..
- ..but as the jobs crisis persists and fiscal consolidation takes hold, inequality has been on the rise again in many countries.



- Globalisation;
- Skill-biased technological change;
- Changes in labour market institutions and regulatory reforms;
- Changes in employment patterns;
- Changes in family formation and household structures;
- Changes in tax and benefit systems.



Main culprits

- Changes in employment patterns and working conditions
- Weaker redistribution via the tax/benefit system
- Skill-biased technological change

Indirect effects

- Globalisation (trade, FDI)

Ambiguous effects

- Changes in labour market regulations and institutions

Lesser culprit

- Changing household/family structures

Off-setting factors

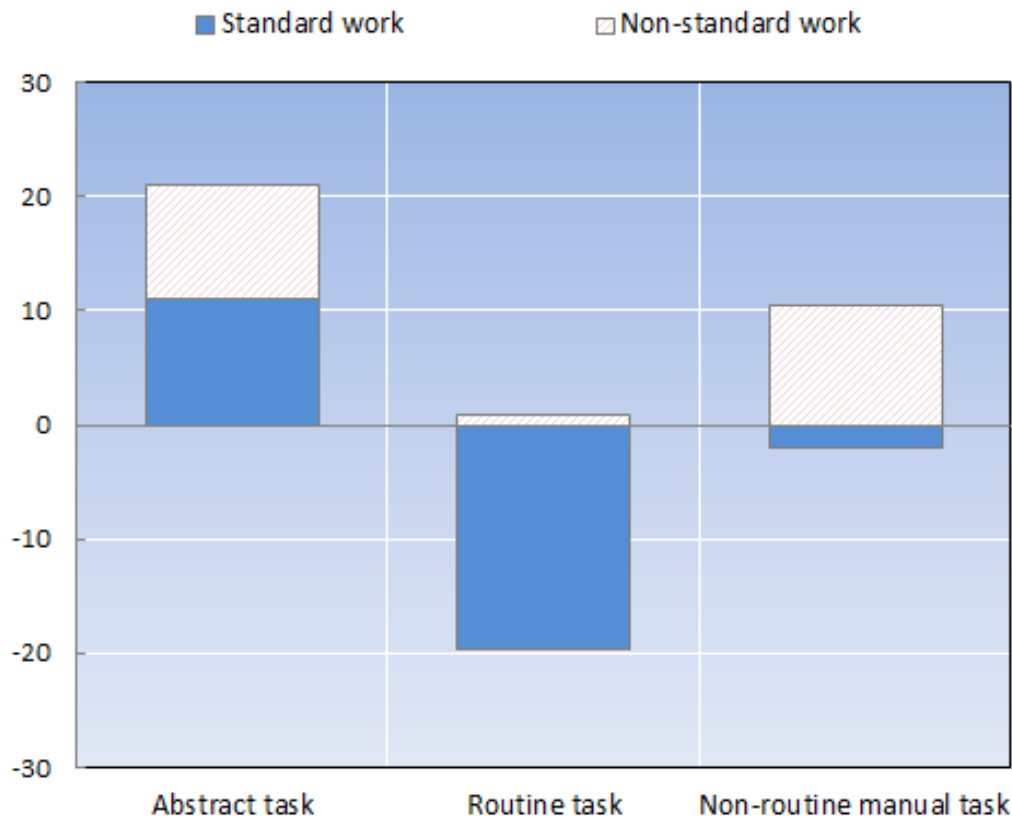
- Increase in education
- Higher female employment participation
- Both off-set part of the drive towards rising inequality



- Non-standard work arrangements increased:
 - temporary jobs, part-time, and self-employment make up 34% of all employment
 - they accounted for 43% of all job creation 95-07 (54% 95-13)
- How do they fare wrt job quality?
- Are they “stepping-stones”, or rather “dead ends” for sustainable work careers?
- Do they increase the risk of in-work poverty?



Percentage change in employment shares by task category, 1995/98-latest available year



Source: OECD (2015), "In It Together", <http://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm> Note: Abstract occupations (ISCO88: 12-34); Routine (ISCO88: 41-42, 52, 71-74, 81-82 and 93); Non-routine manual (ISCO88: 51 83 and 91). The overall sample restricted to workers aged 15-64, excluding employers as well as students working part-time.

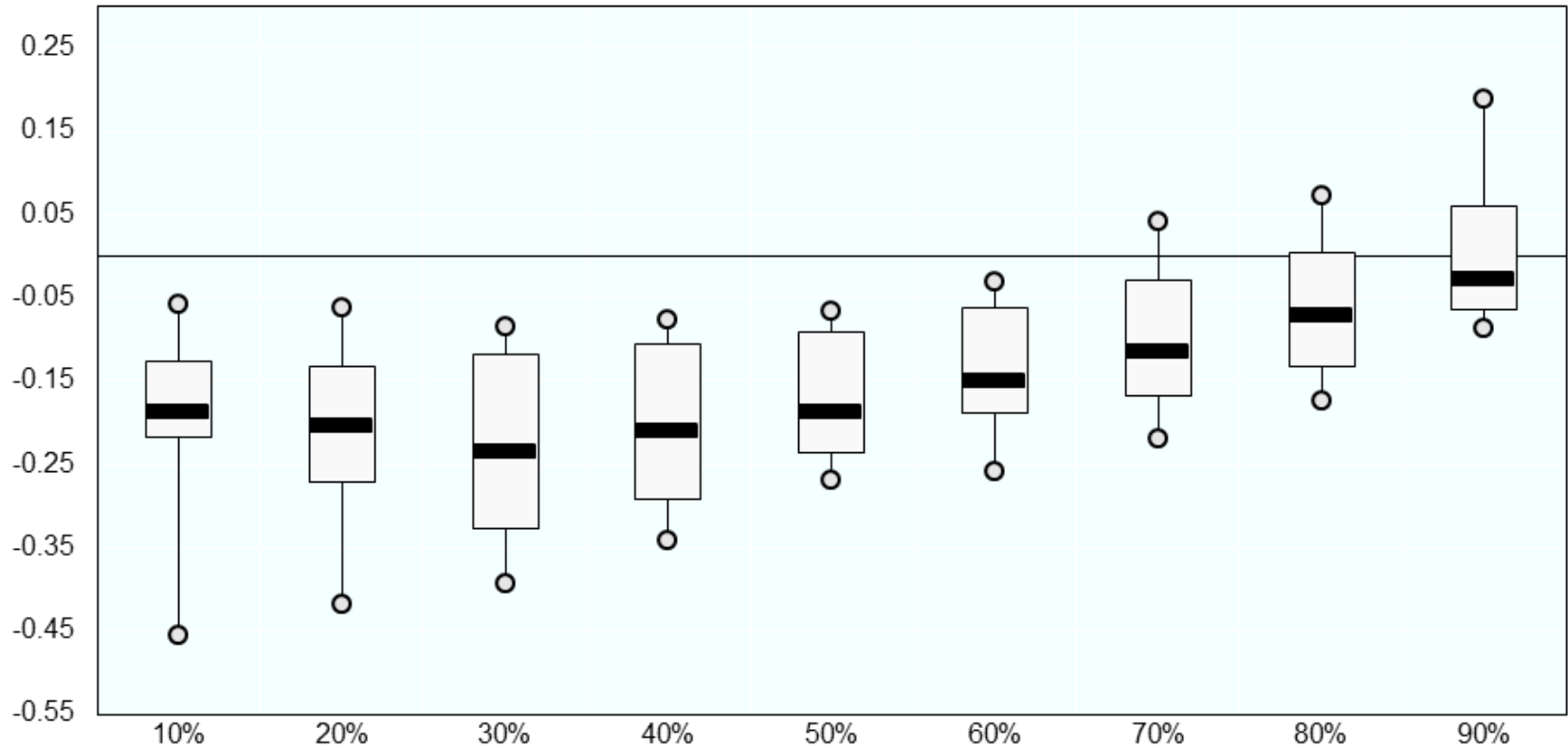
Is there a wage penalty for non-standard workers?



- Temporary workers have 30% lower hourly wages; they still face a wage penalty, about 12% controlling for observable characteristics, and 5-8% once unobservables are taken into account
 - The penalty is higher for younger workers
- For part-time workers
 - in permanent contracts, the penalty is small or a wage *premium* is found in some countries, mainly for women, when controlling for individual and job characteristics
- Sticky floors: the earnings gap for non-standard workers is (much) higher at the bottom of the wage distribution



Effect of non-standard work on (log) hourly wages by decile



Source: OECD (2015), "In It Together", <http://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm>

Note: The box for each quantile represents the interval of the impact of NSW on log hourly wages ranging between 25% and 75% of values, with the black line representing the median impact. The circles represent the country with the highest and lowest impact on wage associated with NSW for each decile.



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Other measures of job quality also suggest that non-standard workers are worse off



- hourly wages are lower;
 - job insecurity is higher;
 - they provide less training.
 - and report a higher level of job strain
- but do they improve labour market prospects, e.g. by a higher probability to move to a more stable job?



- Controlling for characteristics and initial employment status, temporary workers are 12-13 points more likely than the unemployed to be in standard work after one year
- But only prime-age and older temporary workers exhibit higher transition probability into permanent jobs; a stepping-stone effect for young temporary workers (15-29) is generally not found
- In addition, transition rates remain low over a longer time span (less than 50% move to a permanent contract after 3 years)
- Temporary workers are at higher risk of both unemployment and inactivity than those with standard work in $\frac{3}{4}$ of countries

Will more non-standard work lead to higher *income* inequality and poverty?



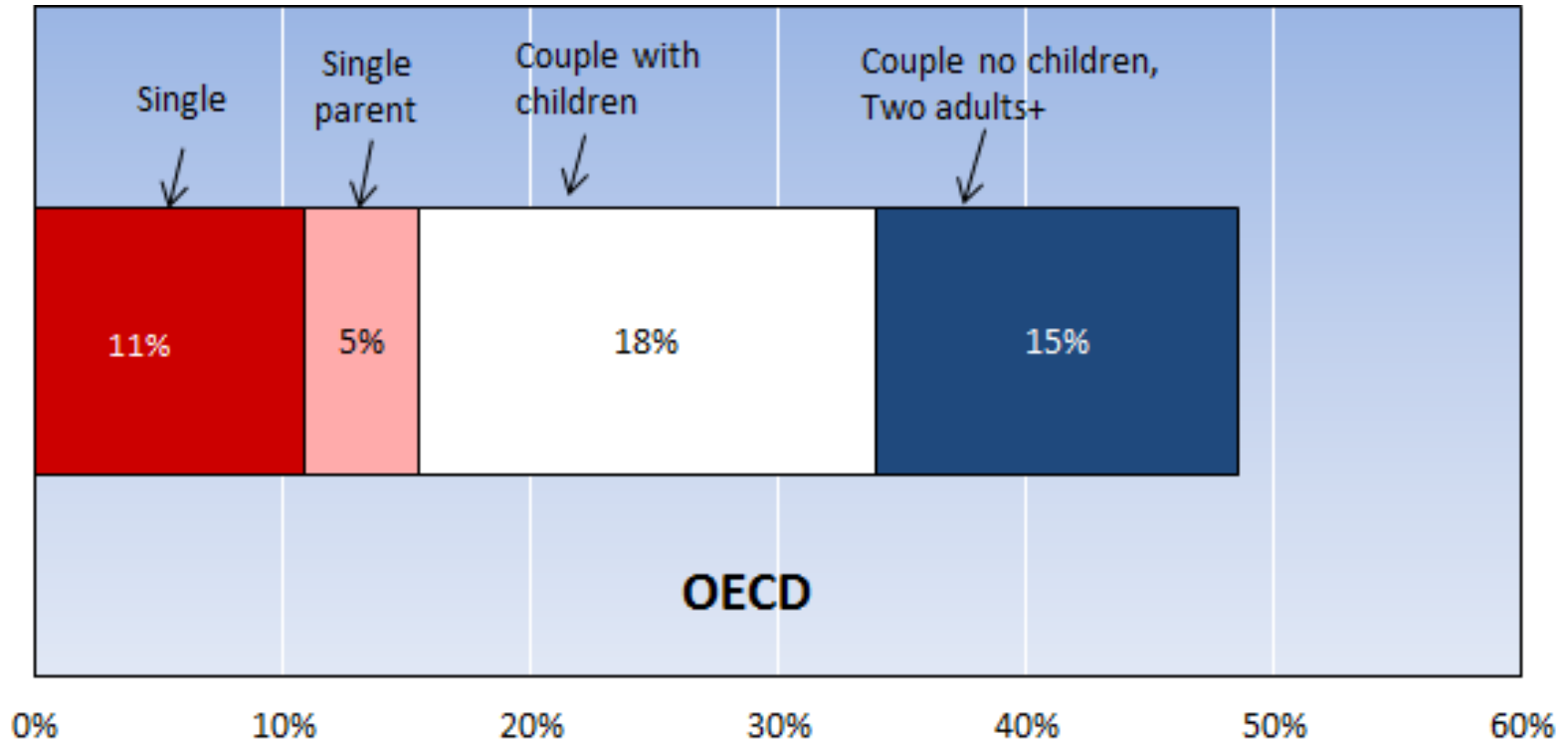
An increase in the share of non-standard workers (NSW) is likely to contribute to increased *individual earnings* dispersion, but the impact on *household income* depends on:

- “Demography”: in which household do NSW live, and are they main or secondary earners
- “Earnings”: what is the contribution from NSW earnings at the household level and how are they distributed
- “Incomes”: what is the position of NSW workers in the overall income distribution and how do different work arrangements affect the risk of poverty

Half of all non-standard workers are the main breadwinners in their household



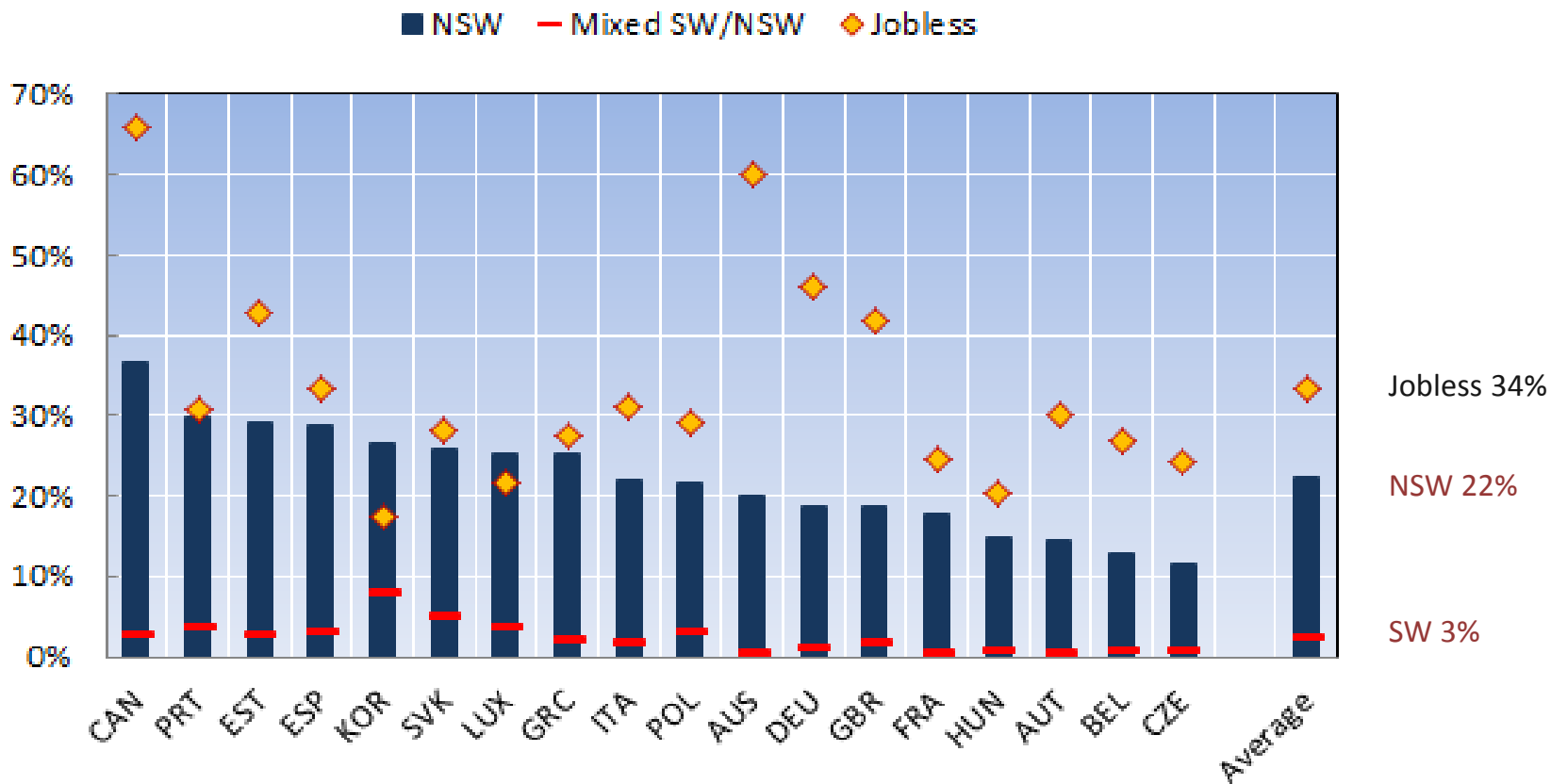
Share of non-standard workers who are main earners, by family type



Source: OECD (2015), "In It Together – Why Less Inequality Benefits All"



Income poverty rates by household employment pattern



Source: OECD (2015), "In It Together", <http://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm>

Note: The poverty line is defined at 50% of the median equivalised household income for the entire population. NSW=non-standard work, SW=standard work

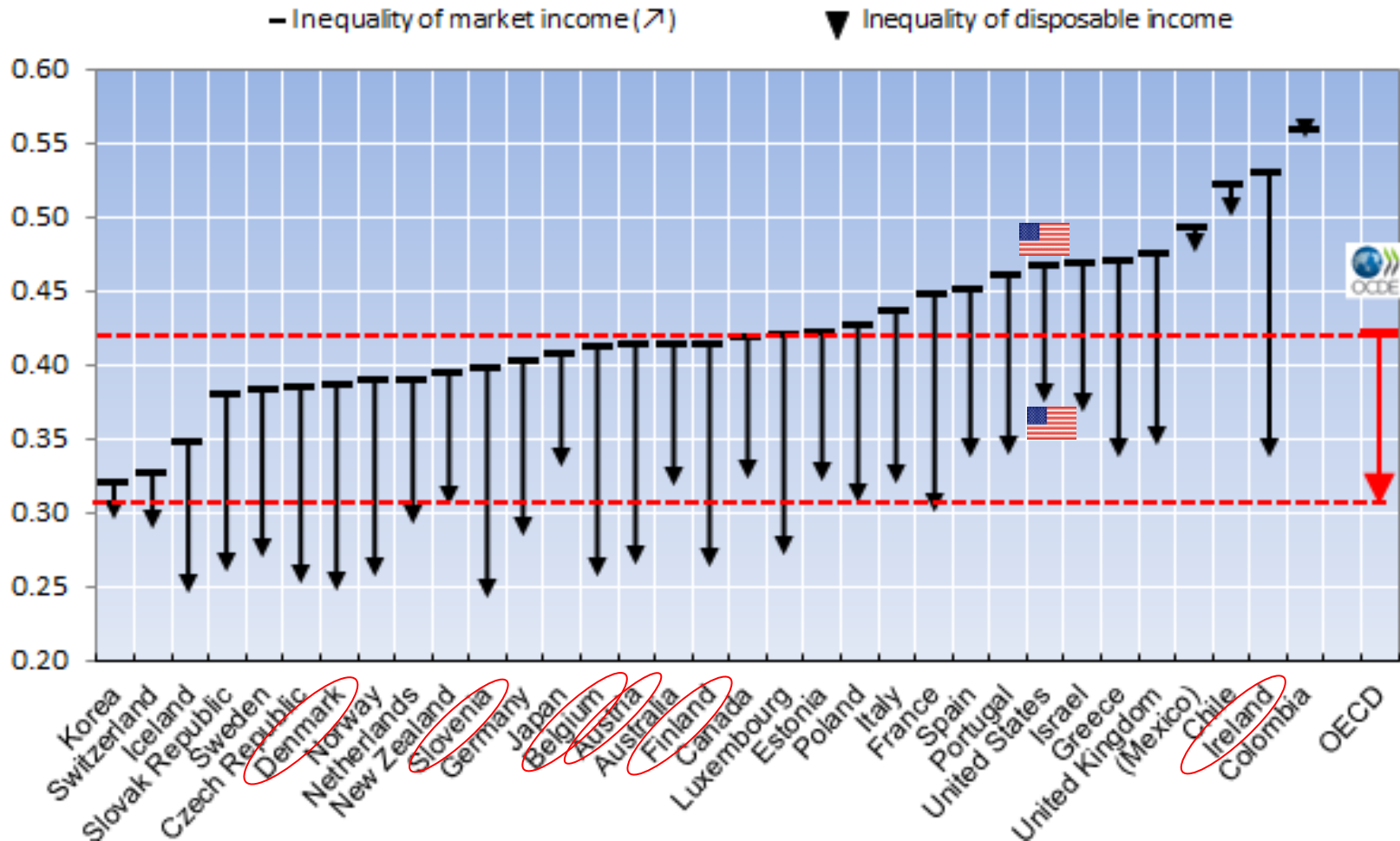


- Non-standard work arrangements increased:
 - Temporary work, part-time and self-employment now make up 1/3 of all employment
 - they accounted for more than half of all job creation since 1995
- Those jobs provide less job quality:
 - hourly wages;
 - job security;
 - training;
 - job strain;
 - social protection (esp. “new SE”).
- “Stepping-stone” effects do exist, but mostly for prime-age and older workers;
- For poverty risks, the household constellation matters

Redistribution via taxes and benefits plays an important role in (almost) all OECD countries



Inequality of (gross) market and disposable (net) income, working-age persons

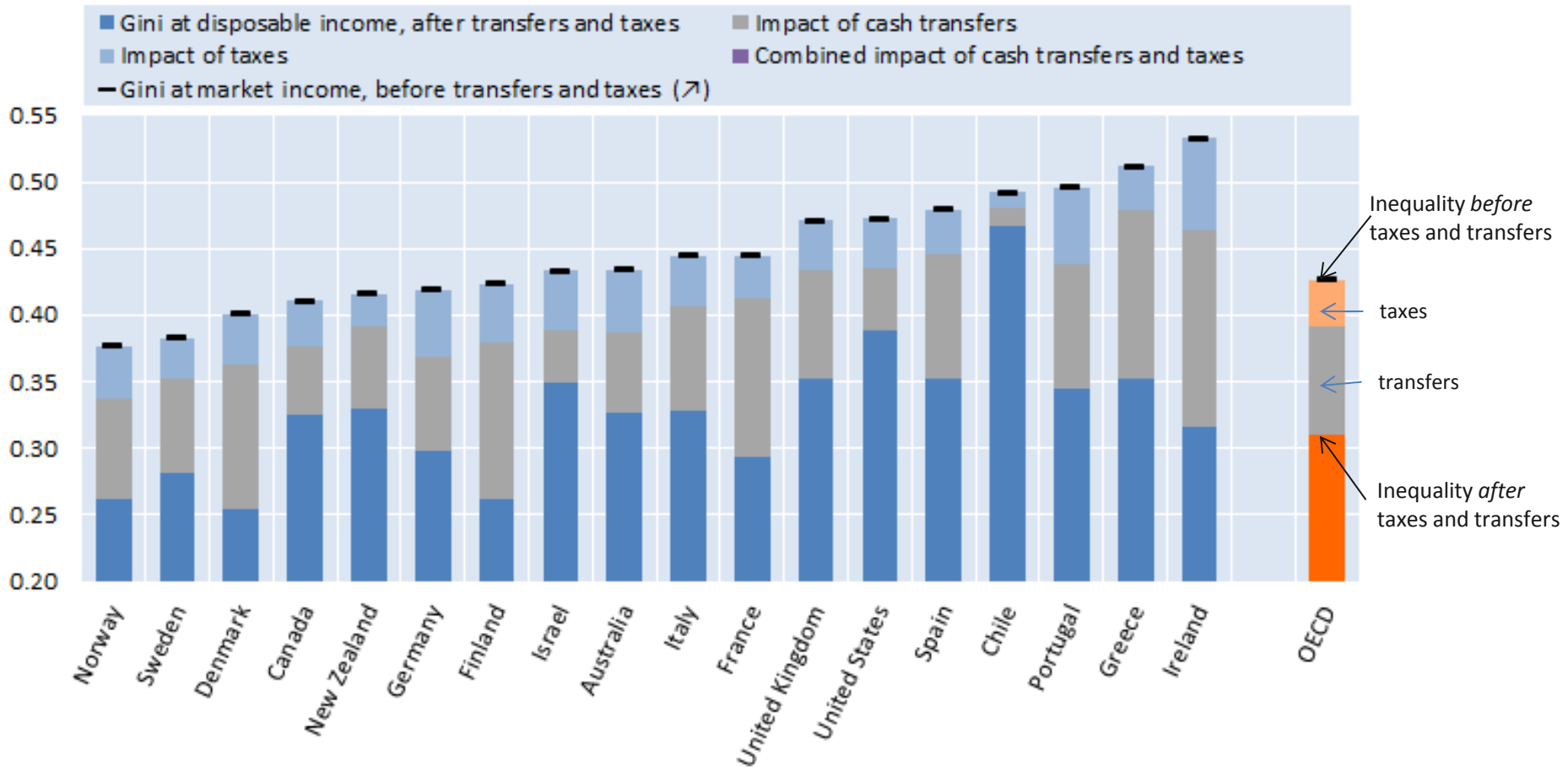


Source: OECD Income Distribution Database www.oecd.org/social/income-distribution-database.htm. Note: Data refer to the working-age population.

Among the two instruments, cash transfers play a more significant role in (almost) all countries



Respective redistributive effects of direct taxes and cash transfers

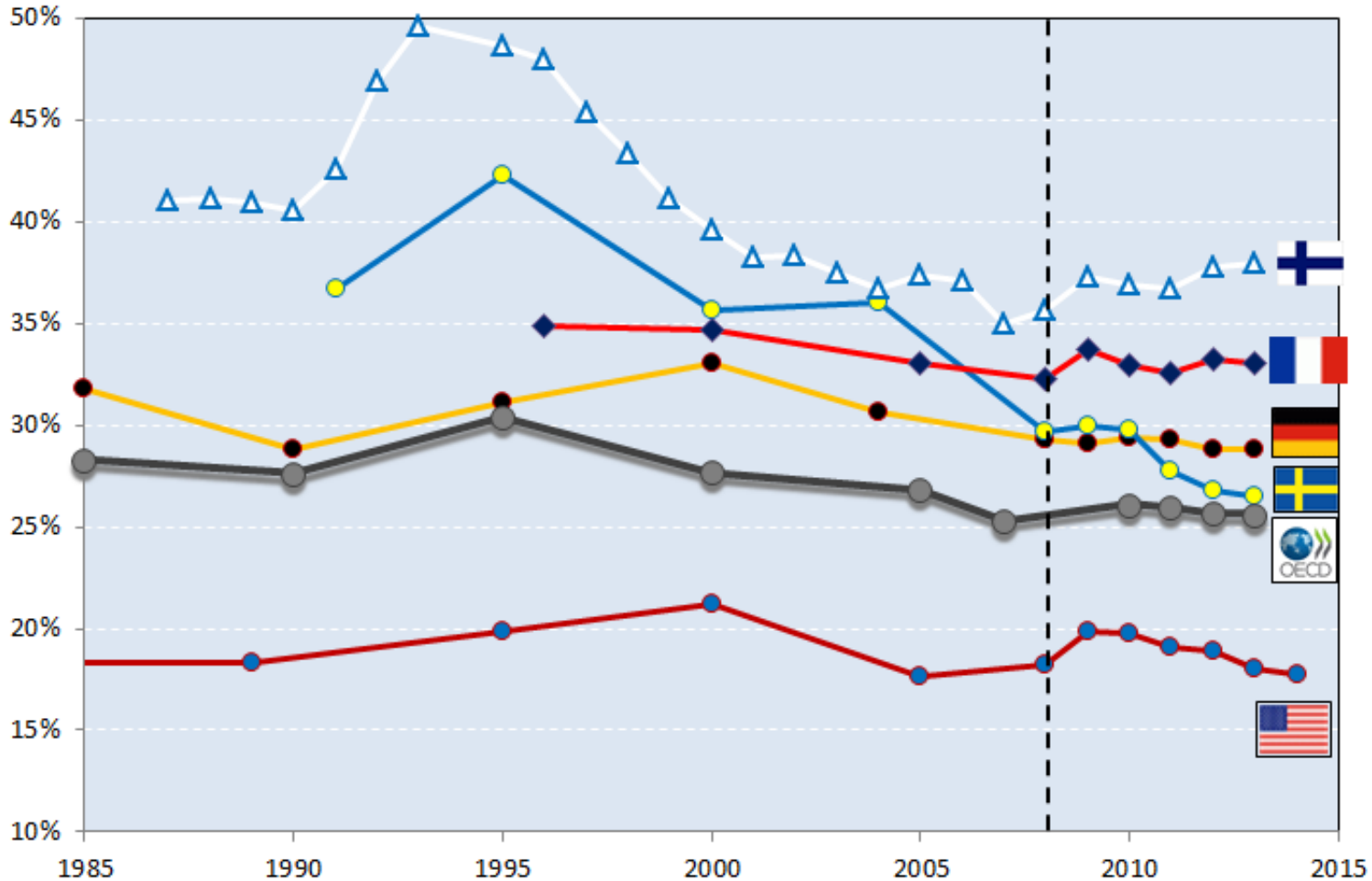


Source: OECD Income Distribution Database (www.oecd.org/social/income-distribution-database.htm).

Note: Data refer to the working-age population.



Trends in market income inequality reduction, working age population





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Why have tax/benefit systems become less successful at reducing inequality?



The weaker redistribution via taxes and benefits was one of the culprits of higher income inequality prior to the crisis:

- Such changes in overall redistribution were mainly driven by benefits: taxes also played a role, but to a (much) lesser extent;
- Spending levels have been a more important driver of these changes than tighter targeting of benefits;
- Spending shifted towards “inactive” benefits, leading to reduced activity rates and higher market-income inequality;
- In some countries, in-kind benefits i.e. public services in health, education etc. became less redistributive, too.

Why do we care about high and rising inequalities?



- Social concerns
- Political concerns
- Ethical concerns
- Economic concerns



Long standing, controversial debate:

- Inequality might **increase** growth by providing **incentives** to work, invest and take risks; or by increasing aggregate savings
- Inequality might **decrease** growth by inducing missed **opportunities** of investment by the poor (in particular, if they can not borrow money); or by favoring distortionary, anti-business policies.

OECD 2015 report uses standardised data to examine

1. the strength and sign of the inequality-growth nexus
2. the link between inequality, social mobility and human capital accumulation

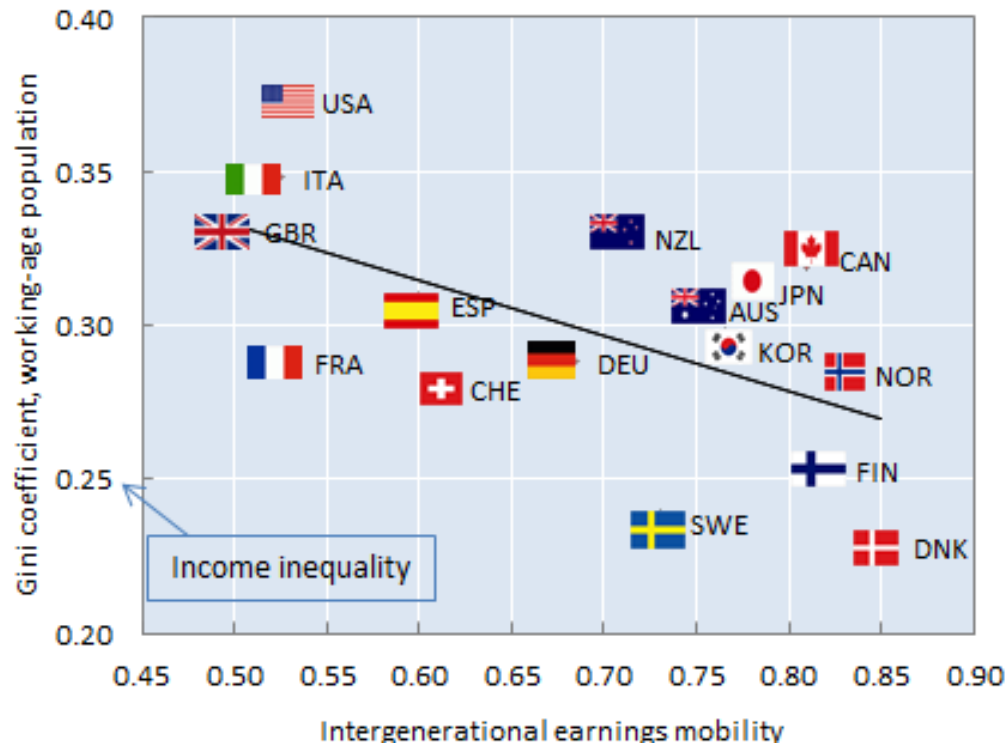


1. Higher income inequality is associated with *lower* subsequent economic growth in the long-term
 - Increasing income inequality by 1 Gini point tends to lower the growth rate of GDP per capita by ~ 0.12 %-points per year
2. This is driven by disparities at the lower end of the distribution, incl. lower middle classes, not just the poor
3. Redistribution through taxes and transfers does *not* necessarily lead to bad growth outcomes
4. Prominent mechanism: inequality narrows the set of investment opportunities of the poor. Hypothesis: inequality lowers social mobility and human capital stock

Inequality & mobility: what do we know?



1. OECD countries are far from “perfect” social mobility: e.g. children education (or income) *does* depend on parents’ education (or income) → intergenerational persistence
2. And mobility seems negatively correlated with inequality: intergenerational earnings mobility is lower in high-inequality countries:



Source: OECD 2008, *Growing Unequal?*, <http://www.oecd.org/els/soc/growingunequalincomedistributionandpovertyinoecdcountries.htm> and d’Addio (2012)

Note: Data refer to mid-2000s. Intergenerational earnings mobility is proxied by the degree to which sons’ earnings are correlated with that of their fathers. <http://oe.cd/cope>

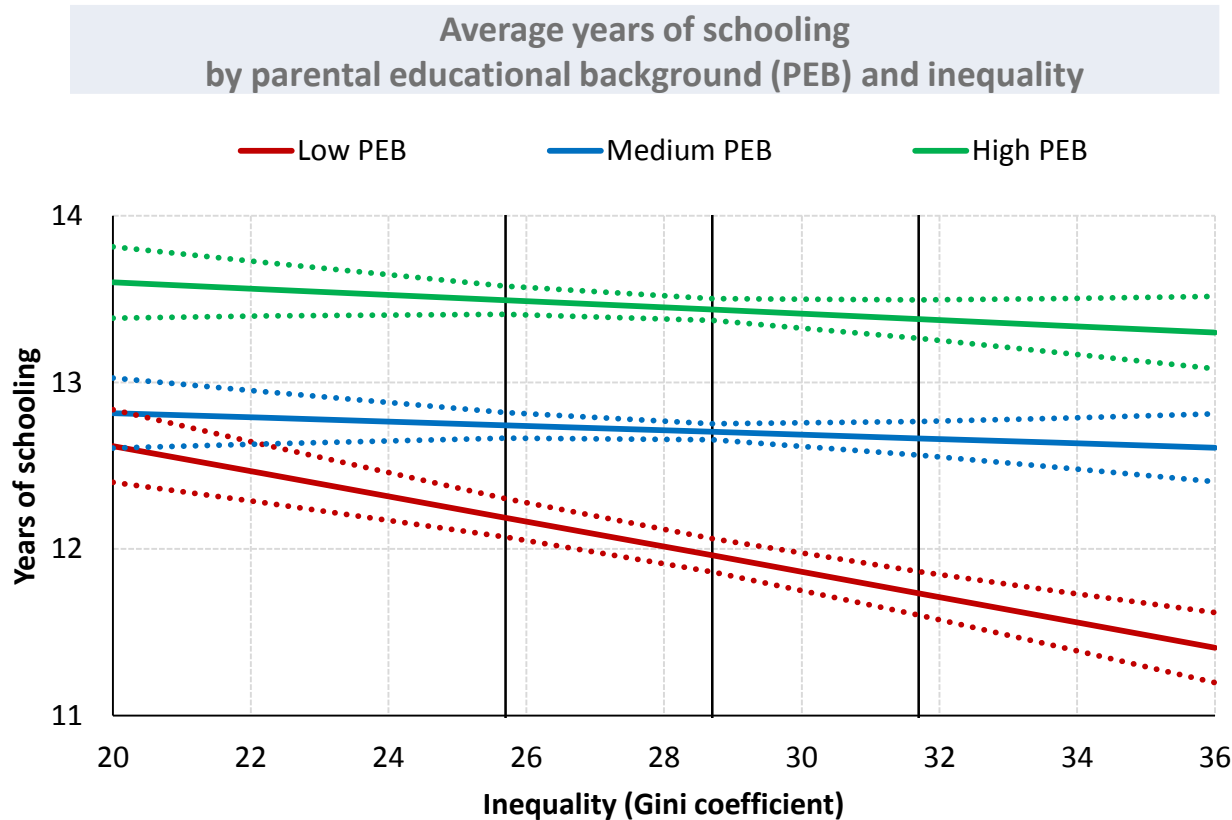


3. Does this imply that increasing inequality would lower mobility?

- Difficult to argue from cross country correlations
 - inequality might correlate with the quality of the educational system, or with other policies and institutions that affect outcomes
- Silent on underlying mechanism
 - is it due in particular to underinvestment by the poor?
- Used OECD PIAAC survey to test this hypothesis
 - In each country, distinguish individuals with “low”, “medium” and “high” Parental Education Background (PEB)
 - Relate average educational outcomes to the pattern of inequality in their country (over time)
 - Focus on both the quantity (e.g. years of schooling) and quality (e.g. skills proficiency) of education



Inequality decreases average years of schooling, but mostly among individuals with low parental education



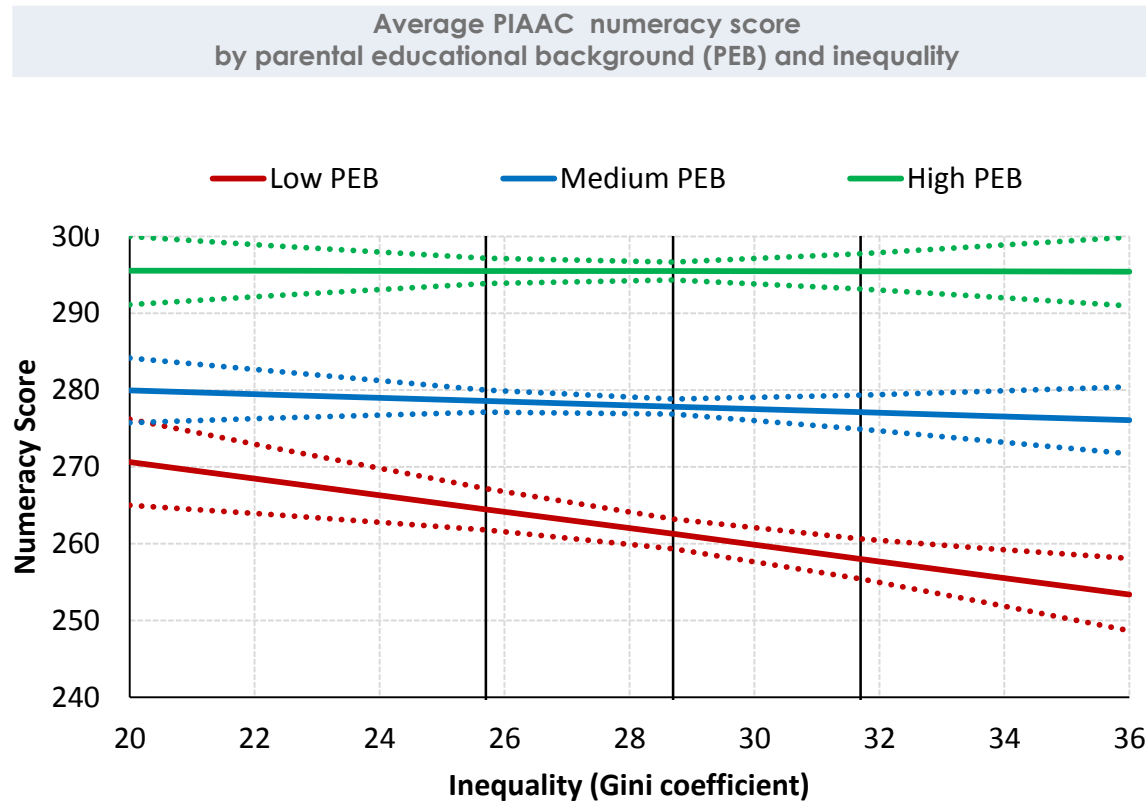
Source: OECD (2015),
"In It Together"

Increasing inequality by ~5-6 Gini pts. (the current differential between France and UK) is associated with less average schooling of low PEB individuals by ~half a year

Note: Low PEB: neither parent has attained upper secondary education; Medium PEB: at least one parent has attained secondary and post-secondary, non-tertiary education; High PEB: at least one parent has attained tertiary education. The bars indicate 95% confidence intervals.



Inequality lowers (literacy and numeracy) skills, but only among individuals with low parental education



Source: OECD (2015), "In It Together"

Increasing inequality by ~6 Gini pts. (the US – Canada differential in 2010) lowers Numeracy score by ~6 pts

Note: Low PEB: neither parent has attained upper secondary education; Medium PEB: at least one parent has attained secondary and post-secondary, non-tertiary education; High PEB: at least one parent has attained tertiary education. The bars indicate 95% confidence intervals. <http://oe.cd/cope>

Designing policy packages to tackle high inequality and promote social cohesion

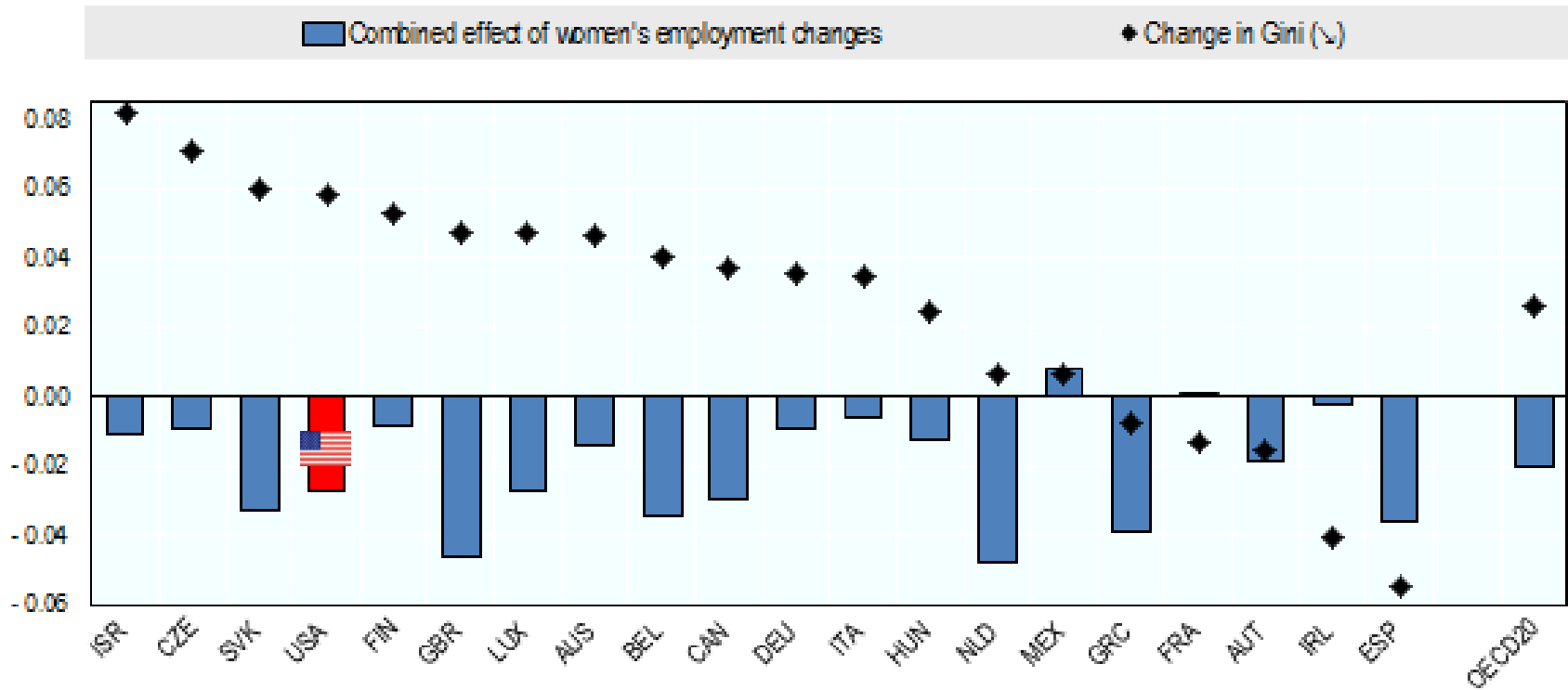


- 1 Foster **women's** participation in the labour market, and economic life
- 2 Promote **employment** and **good-quality jobs**
- 3 Strengthen quality **education** and **skills** development
- 4 Improve the design of **tax and benefit** systems for a more efficient **redistribution**

Trends in women's employment and earnings put a brake on increasing inequality



Contribution of composition and wage structure effects (women) to percentage point changes in Gini of household disposable income, mid-1990s to latest available pre-crisis year



Source: OECD (2015), "In It Together", <http://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm>, based on calculations from the Luxembourg Income Study (LIS), <http://www.lisdatacenter.org/>

Note: Data refer to working-age (25-64) households. Decomposition results are based on Recentered Influence Function (RIF) regressions. Combined effect of women's employment changes include both the composition and wage structure effects, each combining three covariates: participation, work intensity and job skill nature. Data refer to changes from the early/mid-1990s to the latest available pre-crisis year.



- Given the heterogeneity of non-standard workers and their households, it seems less promising to target policies specifically at atypical workers but rather
 - Design policies that enhance the employability of vulnerable workers who are overrepresented in non-standard work arrangements (e.g. youth; single parents), and
 - Target dual-earner policies such as child care provision to vulnerable households



- Promoting access to education, particularly for the low-skilled.
- Improving job-related training and education (on-the-job training) and access to formal education over their working lives
- Promoting access to other public services, such as high-quality childcare, or health
- Facilitating access to jobs (and career prospects) for under-represented groups (youth, older workers, women and migrants)



- Abolishing/scaling back tax deductions and exemptions;
- Taxing fringe benefits, stock options etc. as ordinary income;
- Greater reliance on recurrent taxes on immovable property;
- Reviewing other wealth taxes such as inheritance taxes;
- Harmonising capital and labour income taxation;
- Increasing transparency and international cooperation on tax rules to minimise “treaty shopping” and tax optimisation;
- Reducing avoidance opportunities and thereby the elasticity of taxable income;
- Improving transparency and tax compliance, including efforts for automatic exchange of information between tax authorities.

Designing policy packages to tackle high inequality and promote social cohesion



- 1 Foster **women's** participation in the labour market, and economic life
- 2 Promote **employment** and **good-quality jobs**
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thank you for your attention!



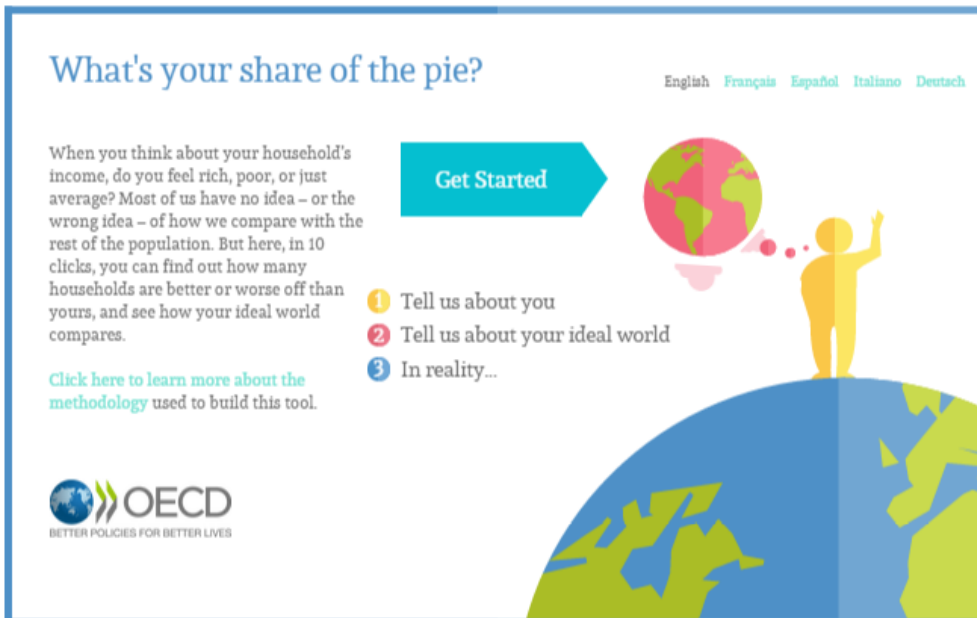
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