INEQUALITY: Are we really ‘all in this together?’

New #ElectionEconomics policy briefing from the Centre for Economic Performance

Inequality of pre- and post-tax income has risen remarkably in the UK since the late 1970s. And while inequality of net income fell in the aftermath of the financial crisis, there are signs that it is rising once again.

What’s more, the tax and benefit changes since 2010 have been largely regressive, with people in the bottom half of the income distribution losing more than they have gained. The main cleavage is between pensioners who have done well compared with those of working age, especially the young and households with children.

These are among the conclusions of a new report from the Centre for Economic Performance (CEP) – the latest in a series of background briefings on key policy issues in the May 2015 UK general election. The CEP reports that:

• The UK’s richest 1% have between 12.5% and 15.5% of all income. This is midway between the United States (with a top 1% share of 20%) and continental Europe (where in France and Spain, it is 8%).

• The income share of the UK’s top 1% has been rising steadily since the late 1970s, mainly due to labour income (wages) but also with a role for capital income (dividends, capital gains, housing rents, etc.).

• Wage inequality has steadily escalated for the top half of the earnings distribution. In 1978, the top 10% earned 1.6 times those in the middle. By 2013, this had risen to a factor of three to one.

• For the bottom half of wage earners, inequality expanded rapidly in the 1980s before stabilising for men from the mid-1990s and actually falling for women.

• Changing wage inequality is partly due to increased demand for skilled workers because of new technologies. But institutions such as unions and minimum wages also matter.

• In the 2008-09 crisis, inequality fell but it has been stable since then. Average wages and incomes have fallen for just about every group since the crisis. It is too soon to tell whether inequality will resume its rising trend as the economy fully recovers.

• Net income (after tax and benefits) is more equally distributed than pre-tax and benefit income. The richest fifth have 15 times the pre-tax income of the poorest fifth, but only four times as much after taxes and benefits. Nevertheless, the increase in post-tax income inequality has followed the same trends as that of pre-tax inequality.

• Modelling changes to direct taxes, tax credits and benefits since the coalition government came to power shows that overall policies have been mainly
regressive. The bottom half of the income distribution lost more from cuts to tax credit and benefits than they gained from higher income tax allowances. Pensioners have done especially well compared with the young.

- The top 1% enjoy about 40% of capital income flows. There is much uncertainty on the stock of wealth inequality. Wealth will be increasingly important for inequality as it is rising faster than aggregate income, and the concentration of capital income is much greater than the concentration of labour income.

Gabriel Zucman, author of the report, concludes:

‘To combat wage inequality, increasing skills, especially for the disadvantaged, is vital.’

‘In terms of capital inequality, Labour’s proposals to abolish non-domiciled residents’ tax status will reduce inequality, whereas the Conservatives’ policy of boosting inheritance tax allowances will increase inequality.’

ENDS

Notes for editors:

‘Inequality: Are we really ‘all in this together?’ by Gabriel Zucman is the latest in CEP’s #ElectionEconomics series.

Objective, brief and non-technical, CEP Election Analysis is a series of background briefings on the policy issues in the May 2015 UK General Election

This series discusses the research evidence on some of the UK’s key policy battlegrounds, including immigration, austerity, real wages and living standards, productivity and business, Europe, the NHS, schools, tuition fees, gender gaps, urban and regional policy, top tax rates, inequality, housing and planning, crime, climate change and energy, and mental health.

These analyses are provided by some of our expert researchers and draw on some of our past and current research.

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