

The IFS Deaton Review: Inequalities in the 21st Century

LACEA-LAMES 2019

Invited Session

Santiago Levy

Chair

Richard Blundell

Inequality, Redistribution and the Labour Market

Orazio Attanasio

Inequality and Human Development

Tim Besley

Inequality: Some Political Economy Issues

First, a little background to the Review.....

<https://www.ifs.org.uk/inequality/>



The IFS Deaton Review

The IFS Deaton Review: Inequalities in the 21st Century

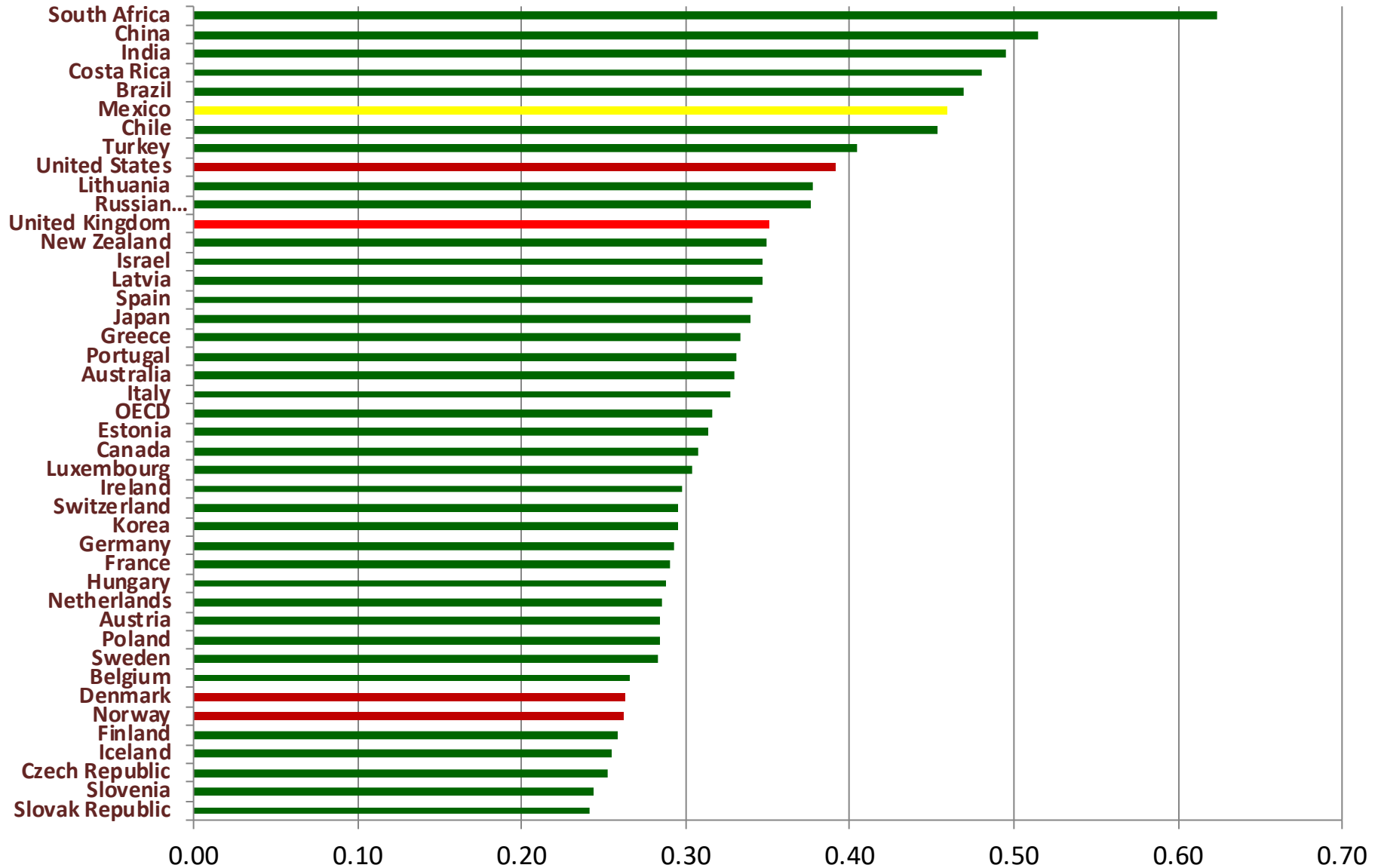
An ambitious 5-year study of inequality

Bringing together the best available evidence from across the social sciences to answer the big questions:

- Which inequalities matter most?
- How are different kinds of inequality related?
- What are the underlying forces that come together to create them?
- What is the right mix of policies to tackle adverse inequalities?
- For developed economies with the UK as the running example, but comparative in nature....

Inequality across OECD and selected other countries

Gini for equivalised net household income in 2016 or latest year



Source: <http://www.oecd.org/social/soc/IDD-Key-Indicators.xlsx>



Inequality

The IFS Deaton Review

Inequality is not just about income

- Income inequality is important, but so are inequalities in
 - wages, wealth, consumption, health, family life, political voice,
- Need to look at inequalities between groups as well as individuals
 - gender, ethnicity, generations, places,
- The focus is on understanding the *drivers* of these inequalities and the *best policy mix* to mitigate their adverse impacts.

The IFS Deaton Review: An International Panel

Chair



Angus Deaton
Princeton University

Panel



Orazio Attanasio
IFS & Yale



James Banks
IFS & Manchester University



Lisa Berkman
Harvard University



Tim Besley
London School of Economics



Richard Blundell
IFS & UCL



Pinelopi Goldberg
Yale University & World Bank



Paul Johnson
IFS & UCL



Robert Joyce
IFS



Kathleen Kiernan
University of York



Lucinda Platt
London School of Economics



Imran Rasul
IUCL & IFS



Debra Satz
Stanford University



Jean Tirole
Toulouse School of Economics



The IFS Deaton Review

Format of the Review

Much like the *Mirrlees Review*, this Review will be published in two volumes:

- I. A volume of commissioned studies and commentaries
 - detailed studies on different aspects of inequality, with commentaries that offer complementary perspectives or alternative views.
 - II. A book written by the panel, aimed at the general public
 - sets out what has happened to inequality, why, and what can be done.
- With a sequence of workshops and public policy events...
Hopefully, joining with CORE economics curriculum too.

Commissioned studies and areas - with commentaries and interactions...

1. Why inequality, what inequality?
2. Political economy and political polarisation
3. Attitudes to inequality
4. Gender
5. Immigration
6. Health
7. Race and criminal justice
8. Geographical (im)mobility and spatial inequality
9. Family dynamics and social mobility
10. Early child development
11. Education systems
12. Labour markets
13. Firms and market power
14. Trade and globalisation
15. Corporate, capital and top taxes
16. Transfers, tax and tax credits at the bottom

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UCL and IFS

Motivating theme: We can't address all the concerns about earnings inequality through the tax and welfare system alone.

Key challenge: How do we balance tax/welfare-benefit policy with other policies: minimum wages, labour market regulation, competition policy, human capital policies, etc?

Inequality, Redistribution and the Labour Market

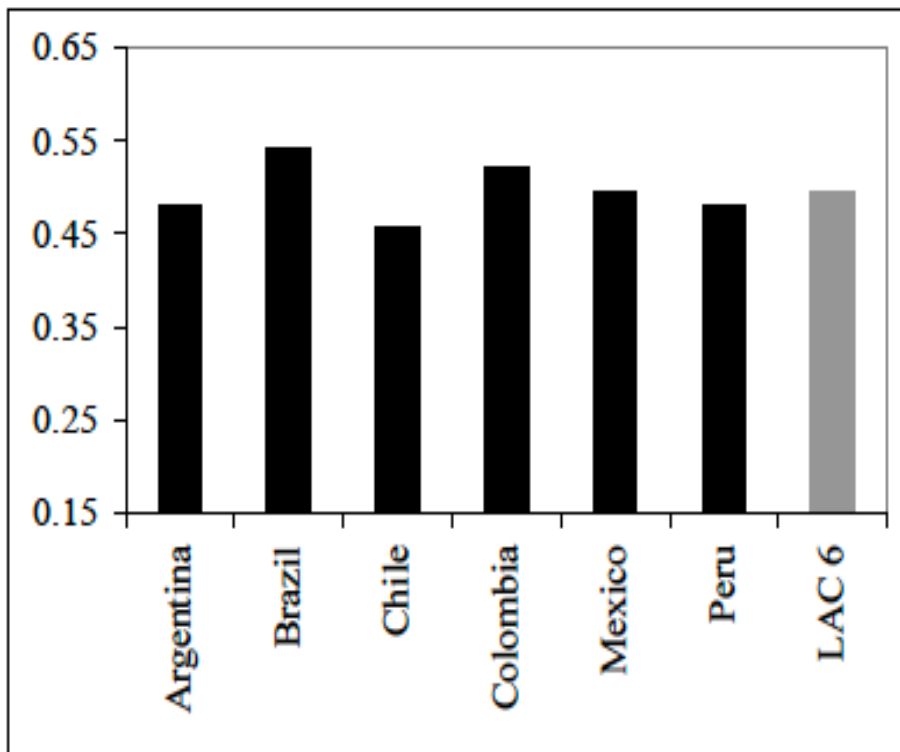
- The structure of work and of families has changed over the last three decades, with growing earnings inequality in many economies, strong growth at the top and adverse labour market ‘shocks’ at the bottom.
 - When we place people in families in local labour markets, with childcare, marriage, savings and human capital decisions we get a different take on some key tax and welfare design questions.
 - When we put families in a dynamic context, redistribution and insurance become intrinsically linked.
- How should we balance tax & welfare benefit reform with minimum wages and policies to address low levels of human capital?
- How should we balance the taxation of top incomes with competition policy that targets rents of firms and innovators?
- Let’s turn to some key facts....

Inequality in LACs and Europe

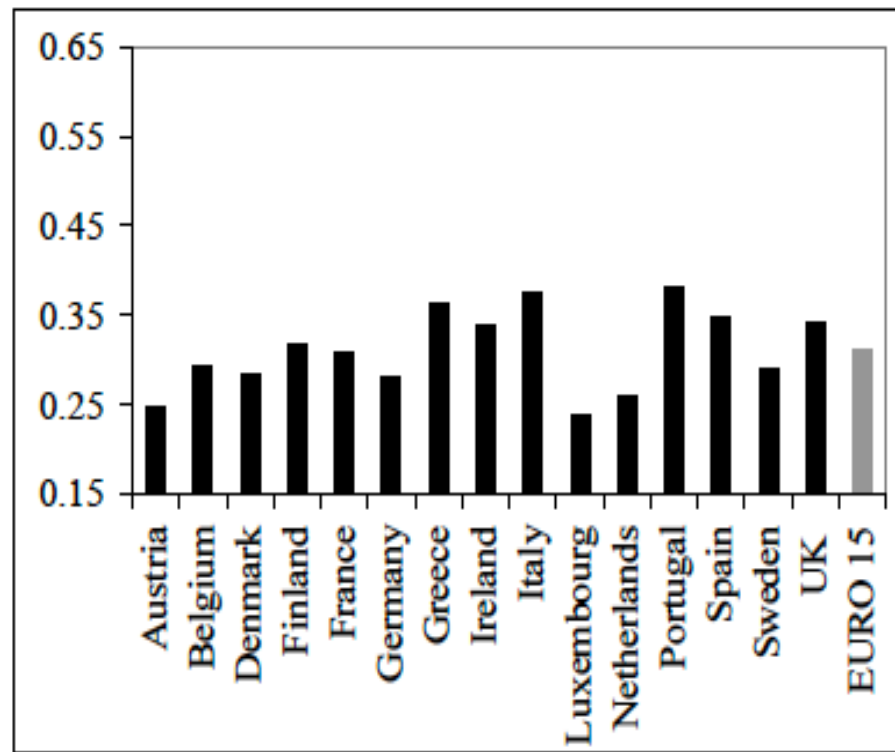
Inequality of Disposable income in Latin America and Europe (Gini coefficients)

Disposable Income

Panel A. Latin America



Panel B. Europe



Source: Figure 1: Goñi, Lopez and Serven, 2008; and Lustig (2011).

Inequality trends in LACs

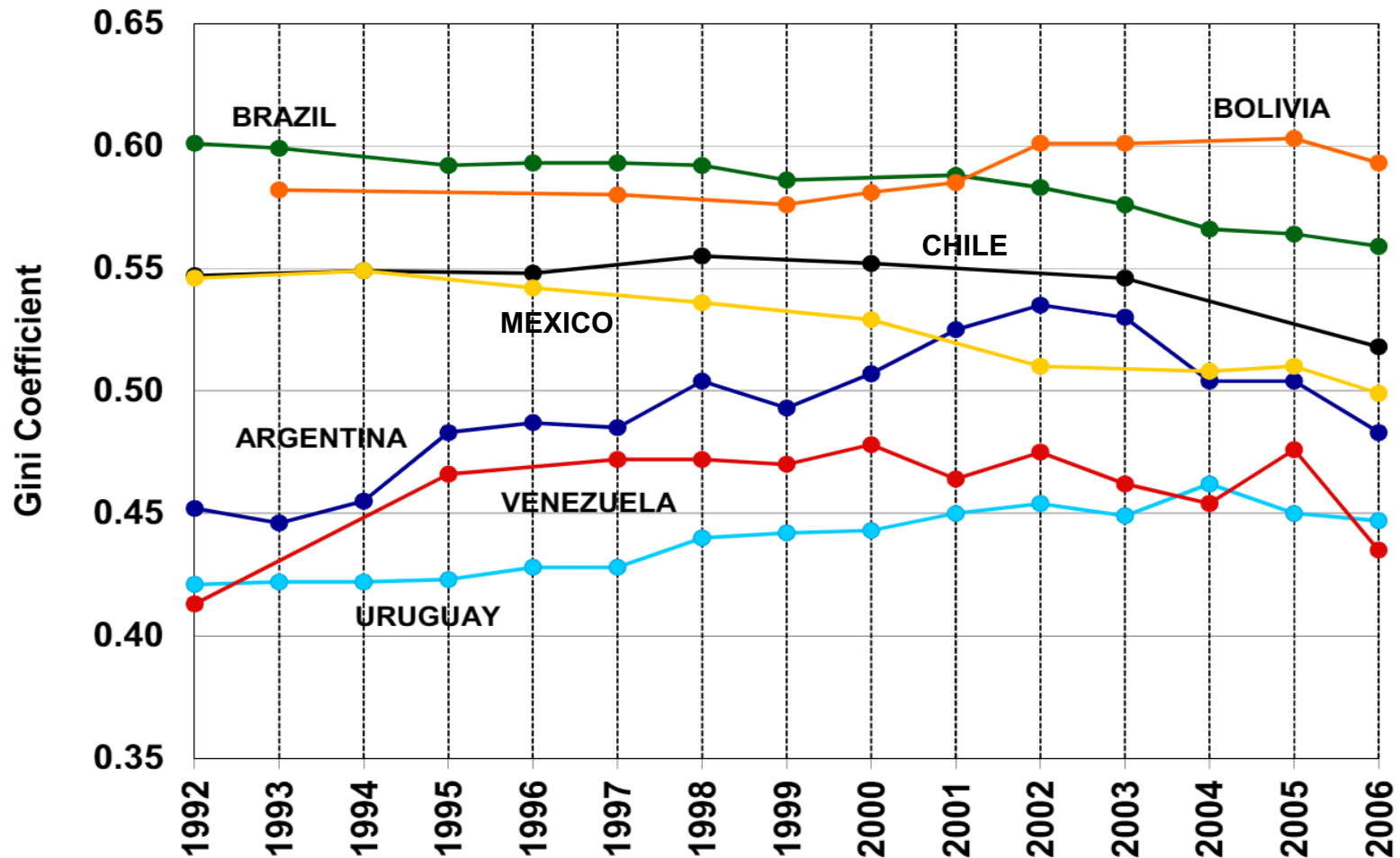
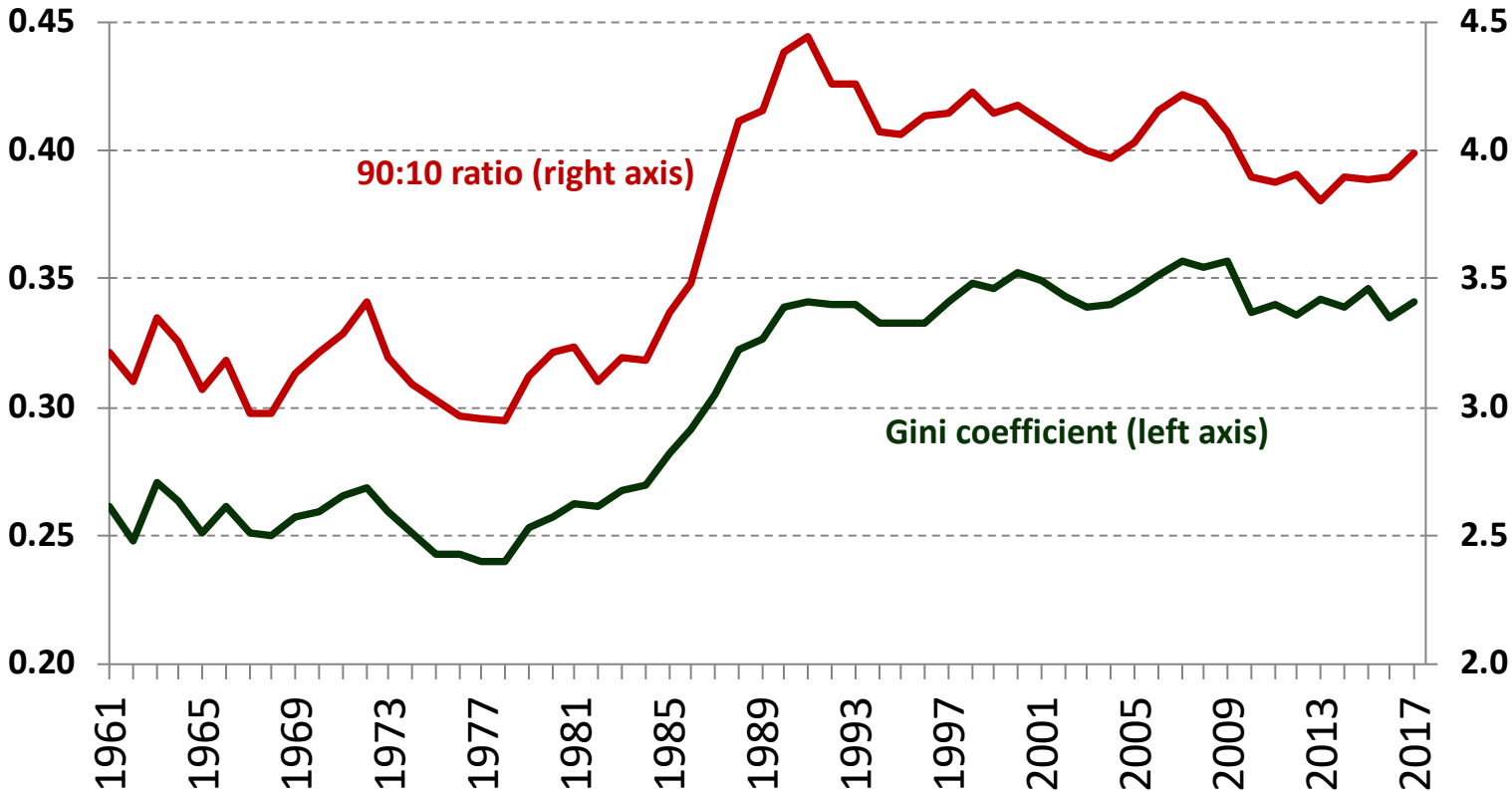


Fig. 15 Gini Coefficients in Latin America 1992–2006. Household per capita income Source: own calculations based on SEDLAC (CEDLAS and The World Bank)

Source: Alvaredo, Cruces and Gasparini (2018).

UK has relatively high inequality but household income 90:10 and Gini has not risen in recent years

Gini coefficient and the 90:10 ratio in Great Britain, 1961–2017

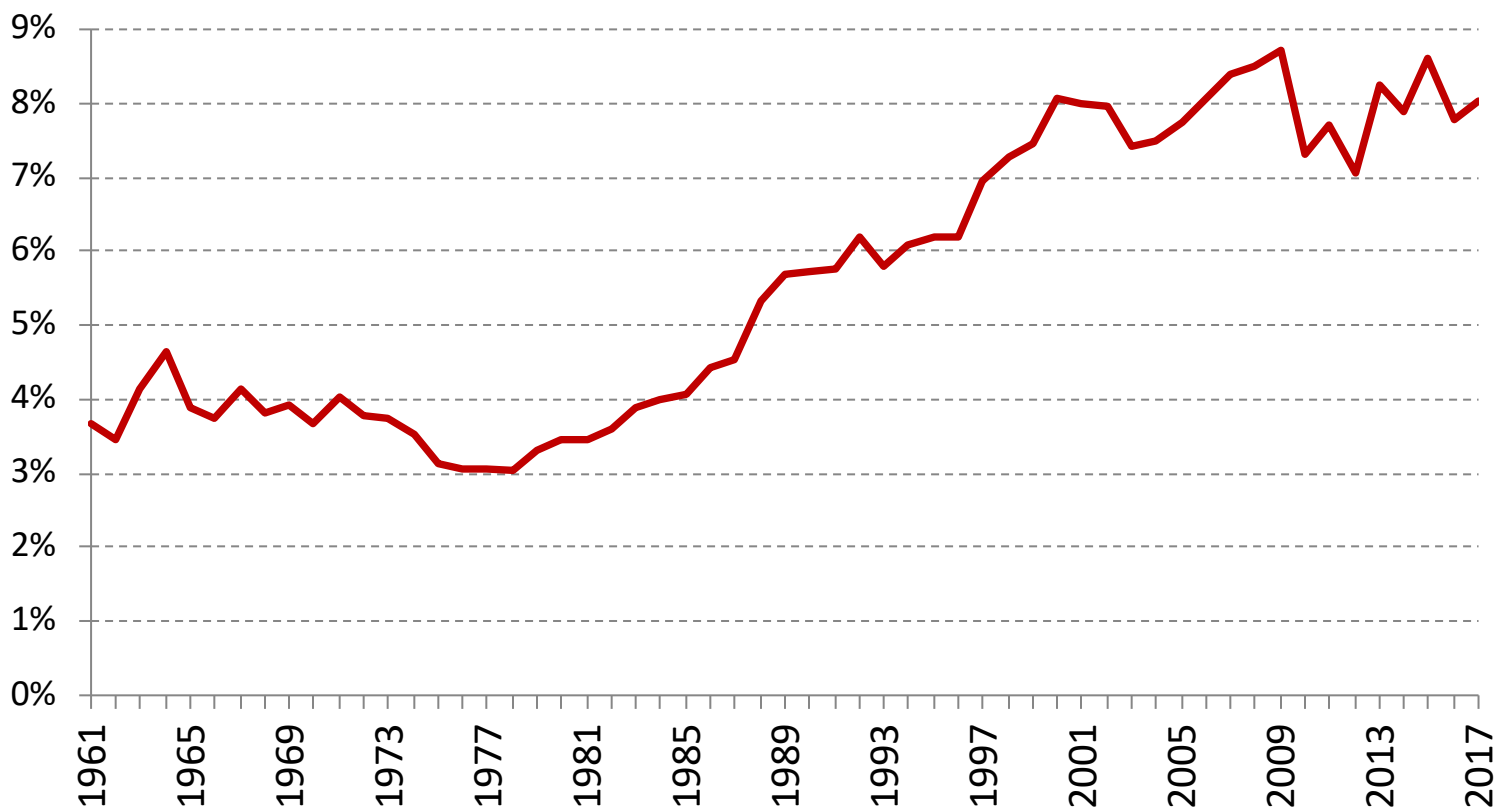


But note the top 1% share rose year on year to almost triple since 1977

Source: Joyce and Xu, 2019

The top 1% share has nearly tripled in the last 4 decades

Top 1% share of net household income, UK 1961–2017

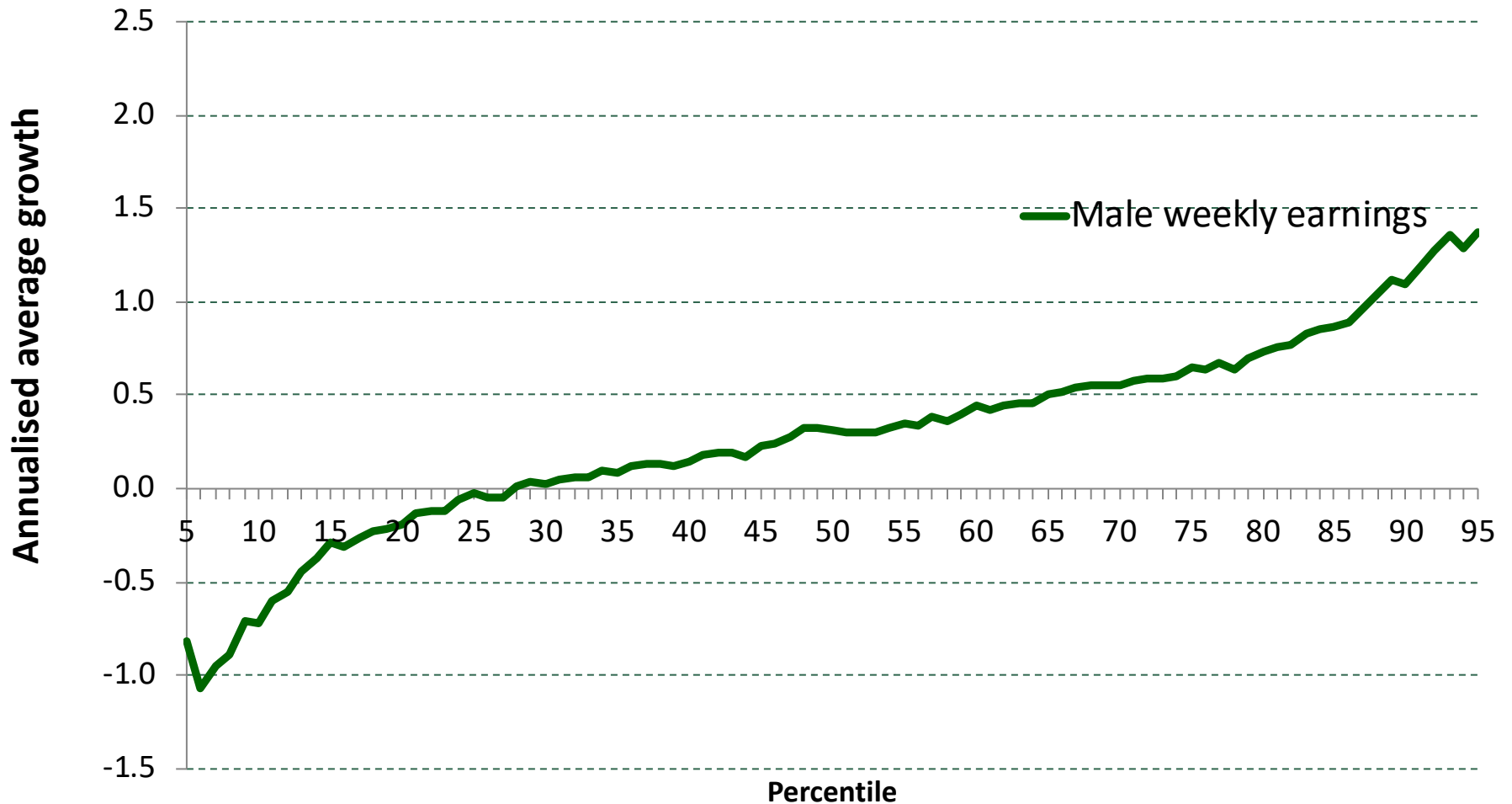


Gini and household survey income data do not capture the very top well, see also Campos-Vazquez, Chavez and Esquivel (2018) for Mexico.

Note: Years refer to calendar years up to and including 1992 and to financial years from 1993–94 onwards, corrected with tax data. Source: Joyce and Xu, 2019

Growth in male weekly earnings:

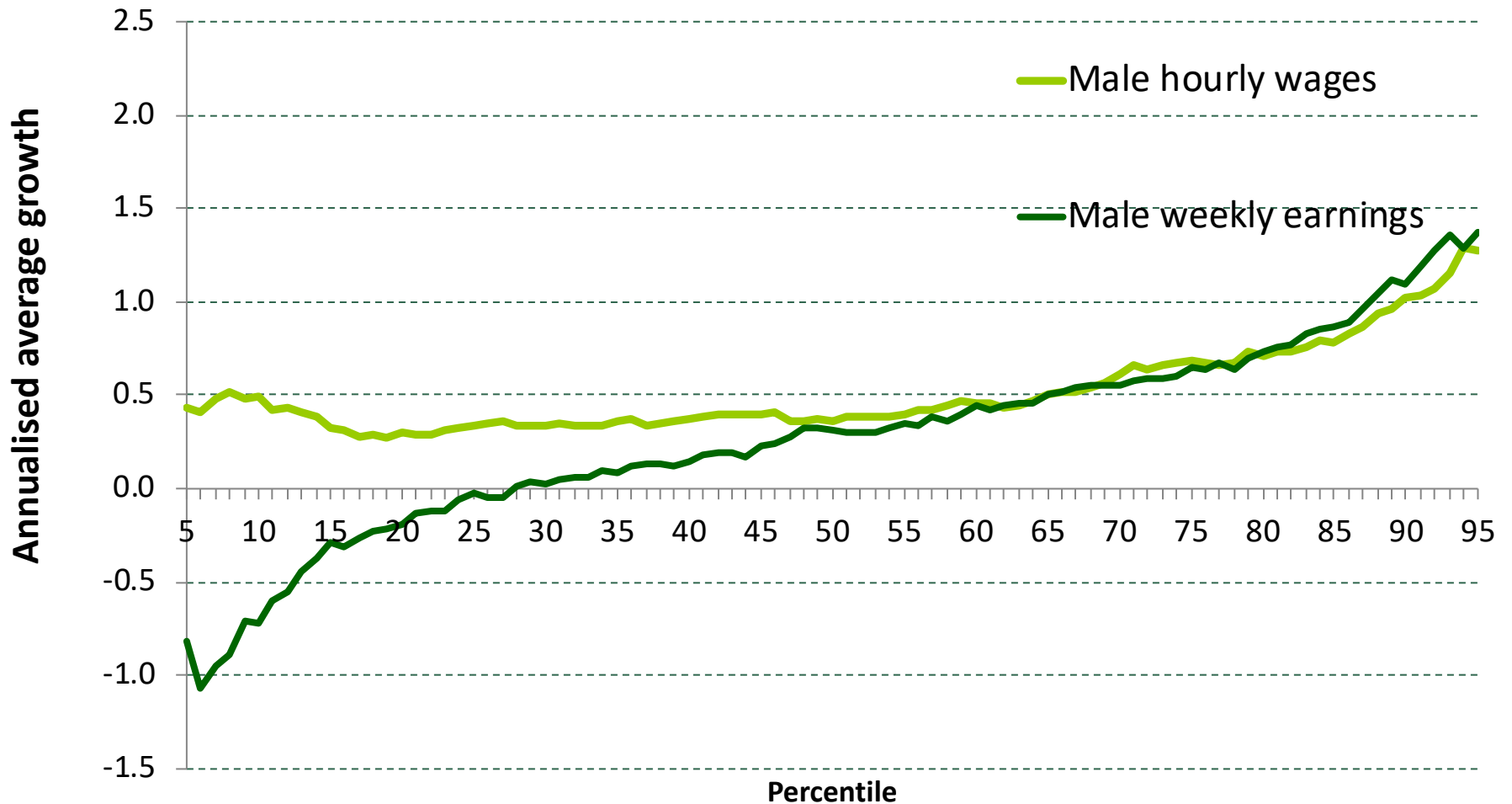
UK, 1994/95 – 2015/16



Source: Blundell, Joyce, Norris Keiller and Ziliak (2018):

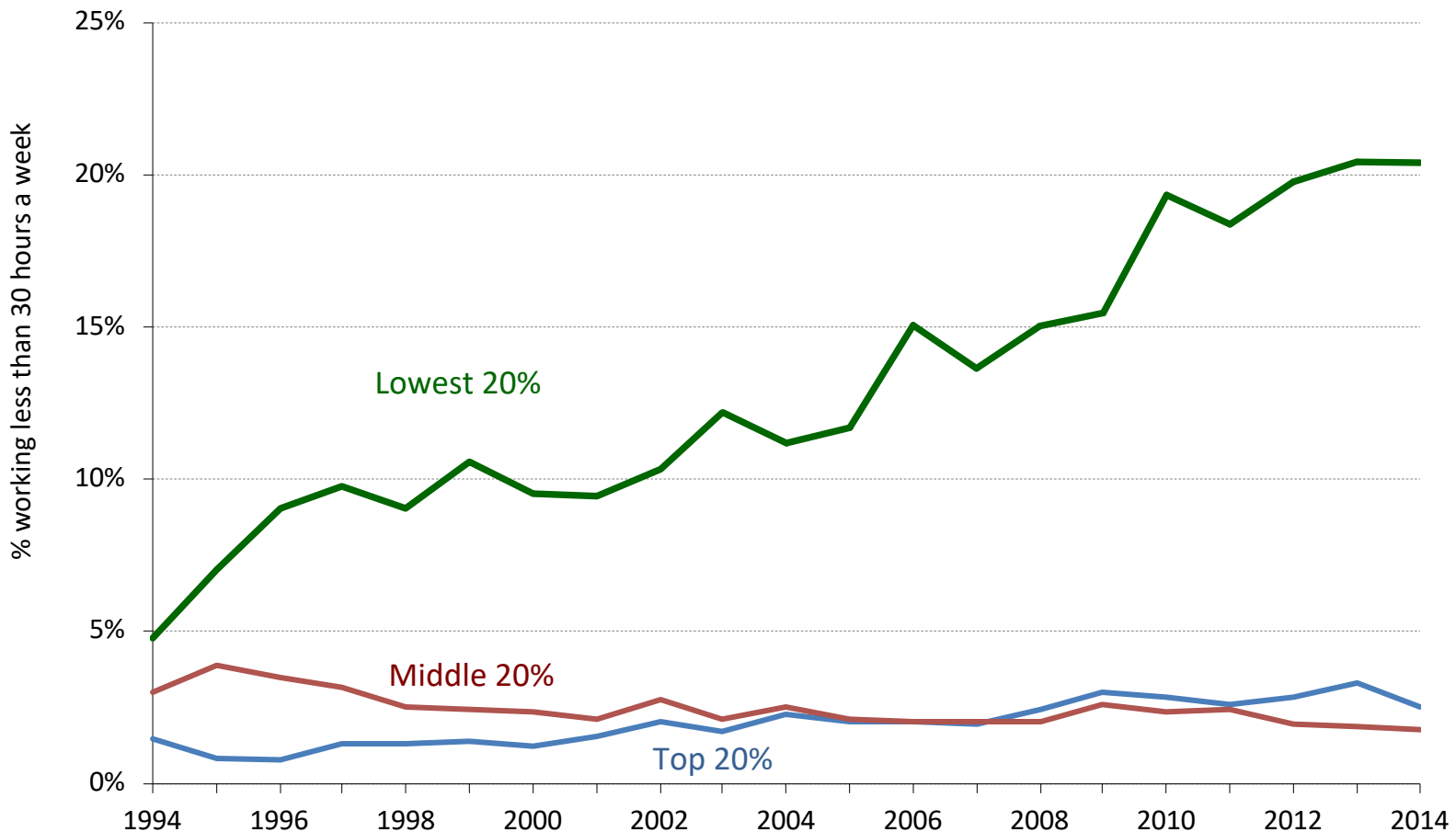
www.ifs.org.uk/publications/10031. Data used is UK FRS 1994-95 and 2015-16.

Growth in male weekly earnings and hourly wages: UK 1994/95 – 2015/16



Source: Blundell, Joyce, Norris Keiller and Ziliak (2018):
www.ifs.org.uk/publications/10031. Data used is UK FRS 1994-95 and 2015-16.

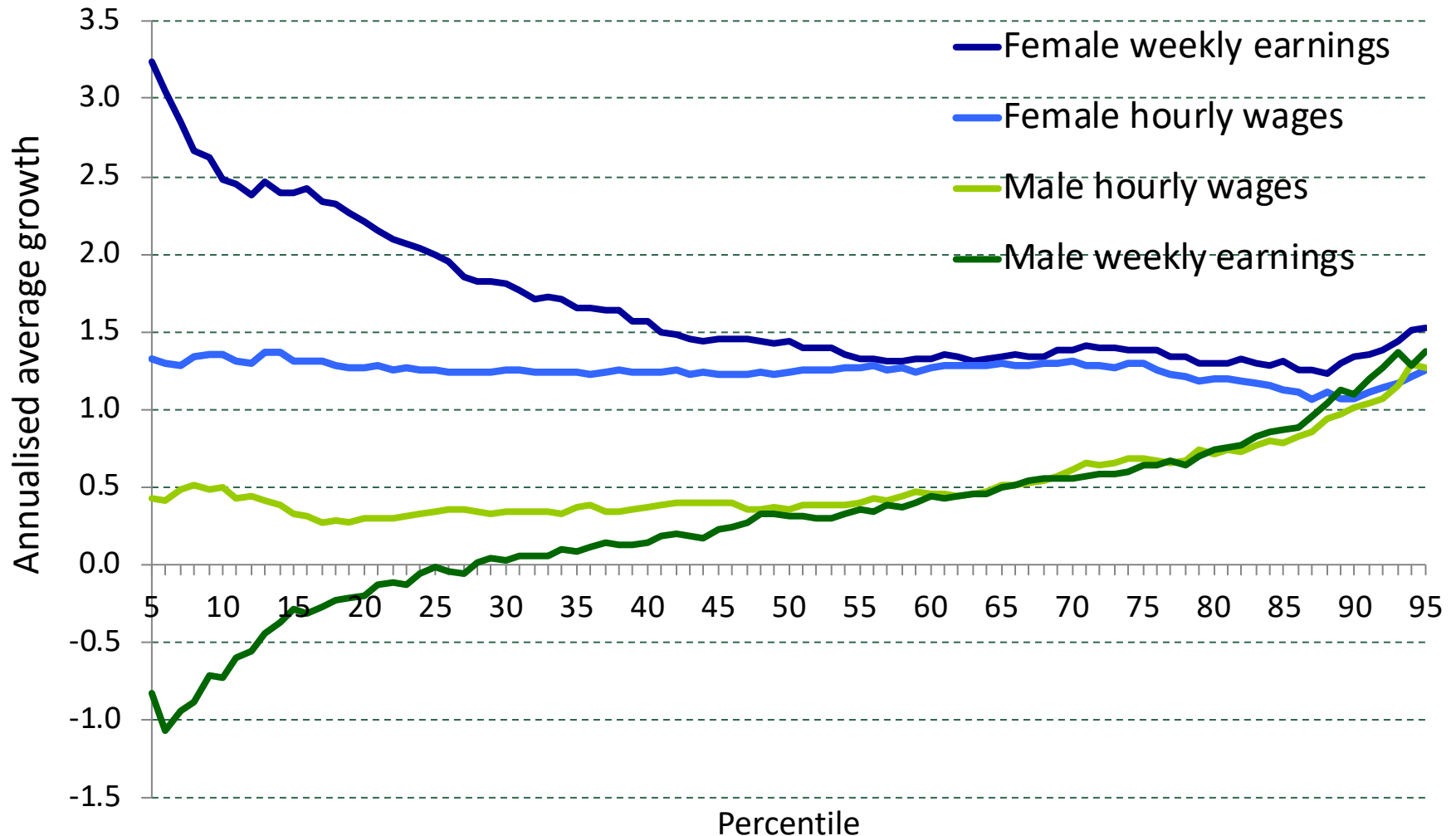
Proportion of men working less than 30 hours in the UK by hourly wage quintile – aged 25-55



Source: IFS calculations using Labour Force Survey

Notes: LFS: Male employees aged 25-55. Giupponi and Machin (2019) show even stronger for self-employed since 2008 where there has been a growing rate of Involuntary part-timers.

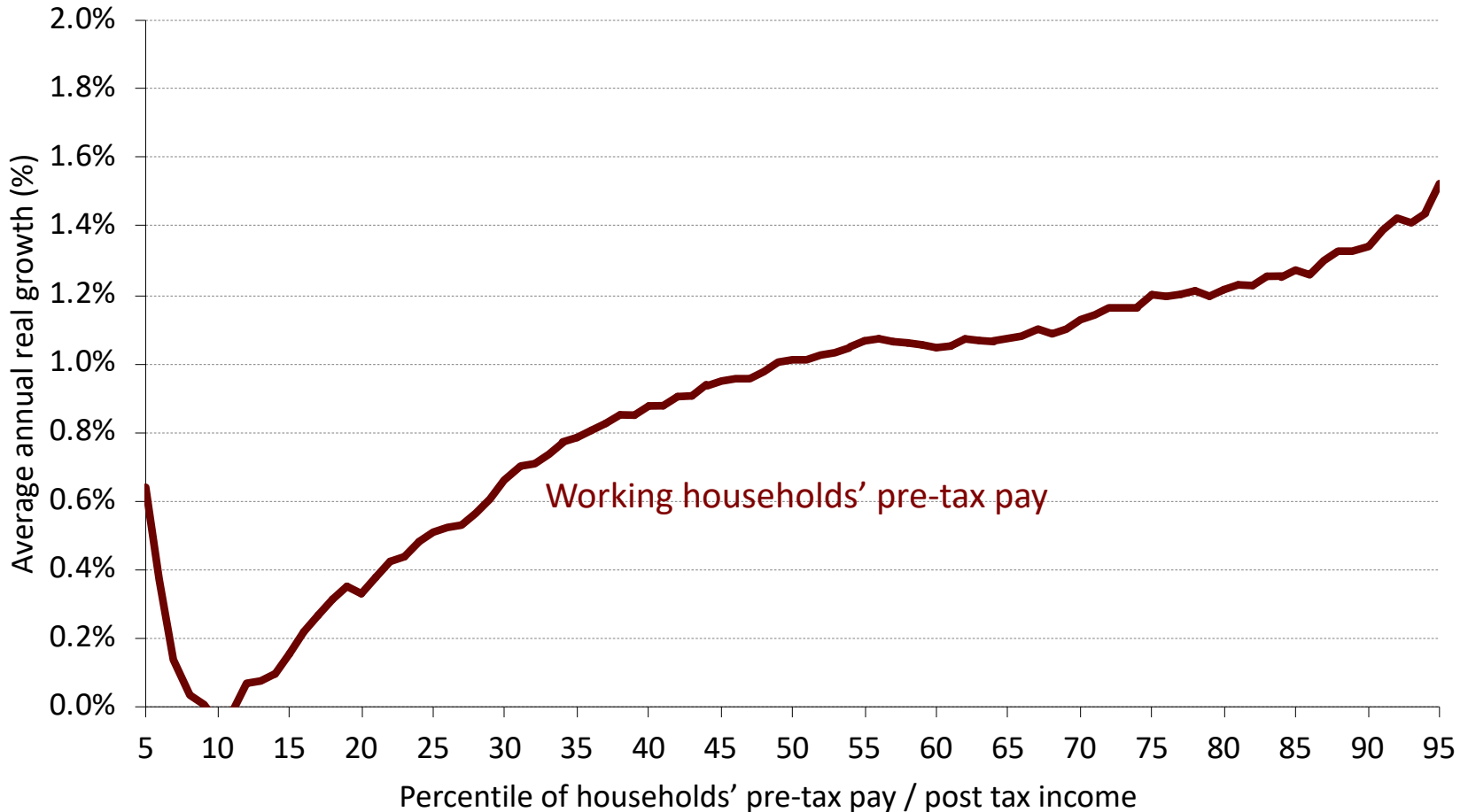
Very different growth in female hourly wages and weekly earnings: UK 1994/95 – 2015/16



But assortative partnering and the low female earnings share implies this has not improved between family inequality.... Similar results in the US. But LACs?

Earnings and Incomes

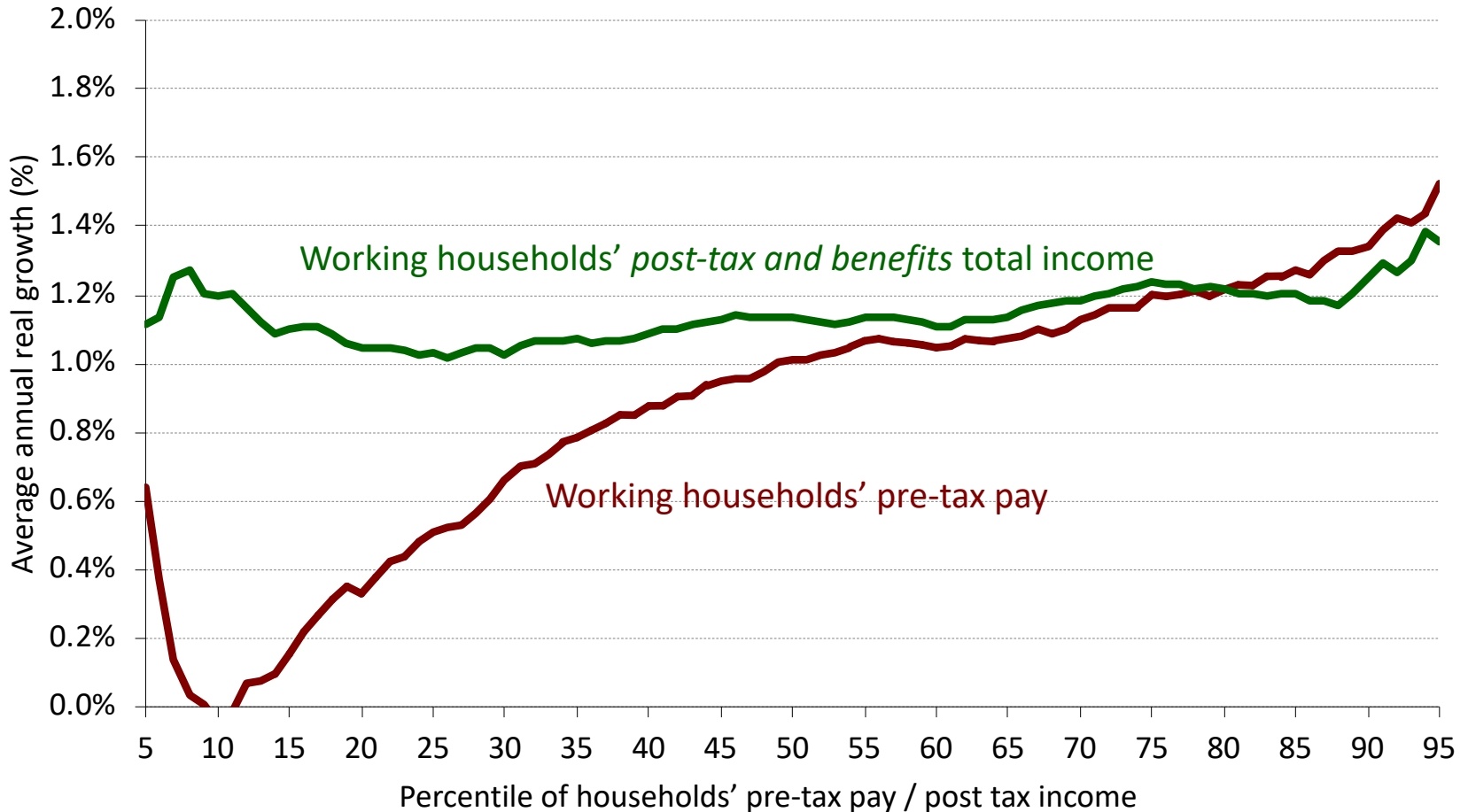
Growth in pre-tax earnings for working households in UK 1994/5 to 2015/6



Notes: Includes self employment income and self-employed households. Family Resources Survey. All income measures are equivalised.
Source: Blundell, Joyce, Norris Keiller and Ziliak (2018)

Family Earnings and Family Incomes

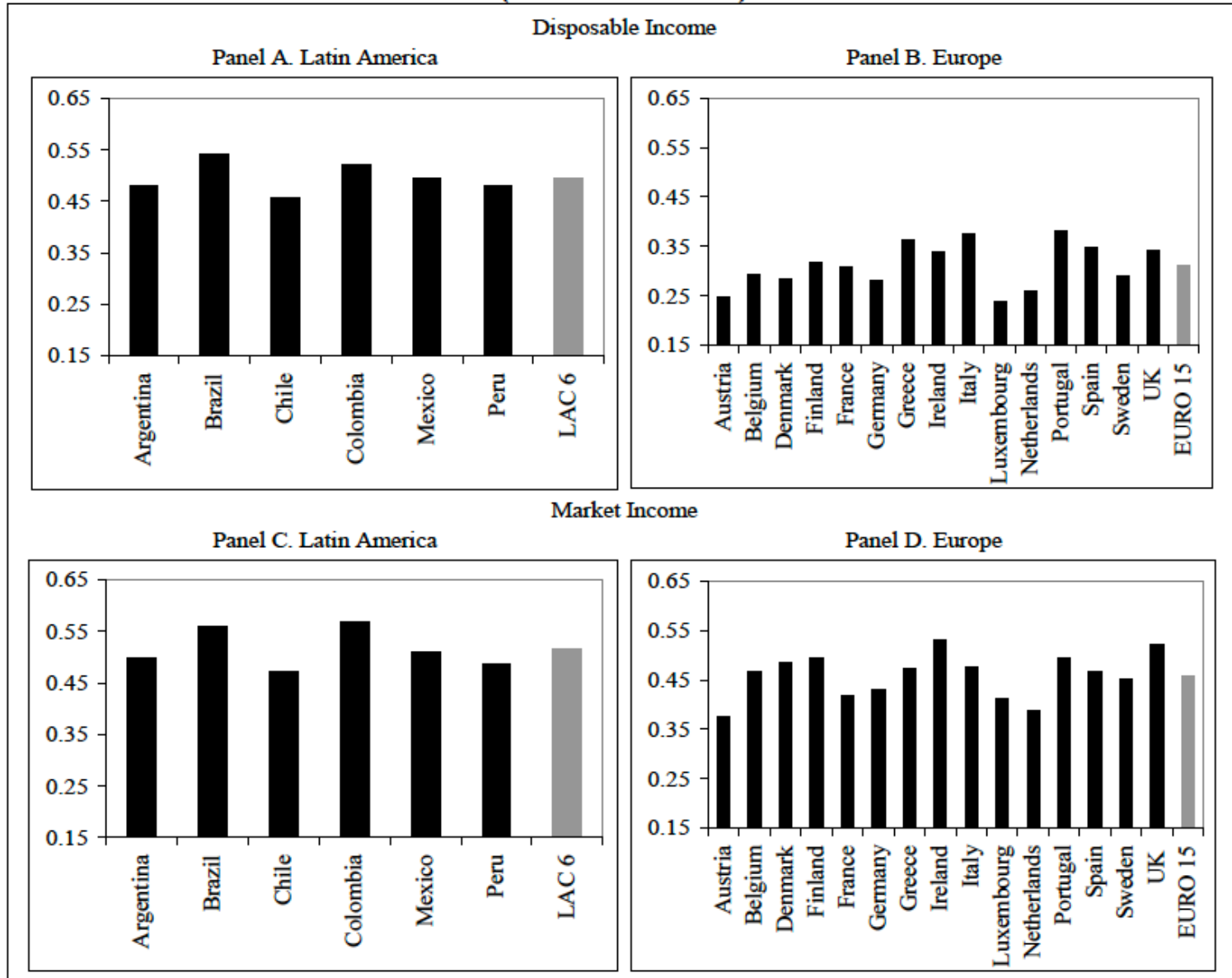
Household income growth for working households in UK 1994/5 to 2015/6



Notes: Includes self employment income and self employed households.
Family Resources Survey. All income measures are equivalised.
Source: Blundell, Joyce, Norris Keiller and Ziliak (2018)

Redistributive impact of taxes and transfers in LACs and Europe

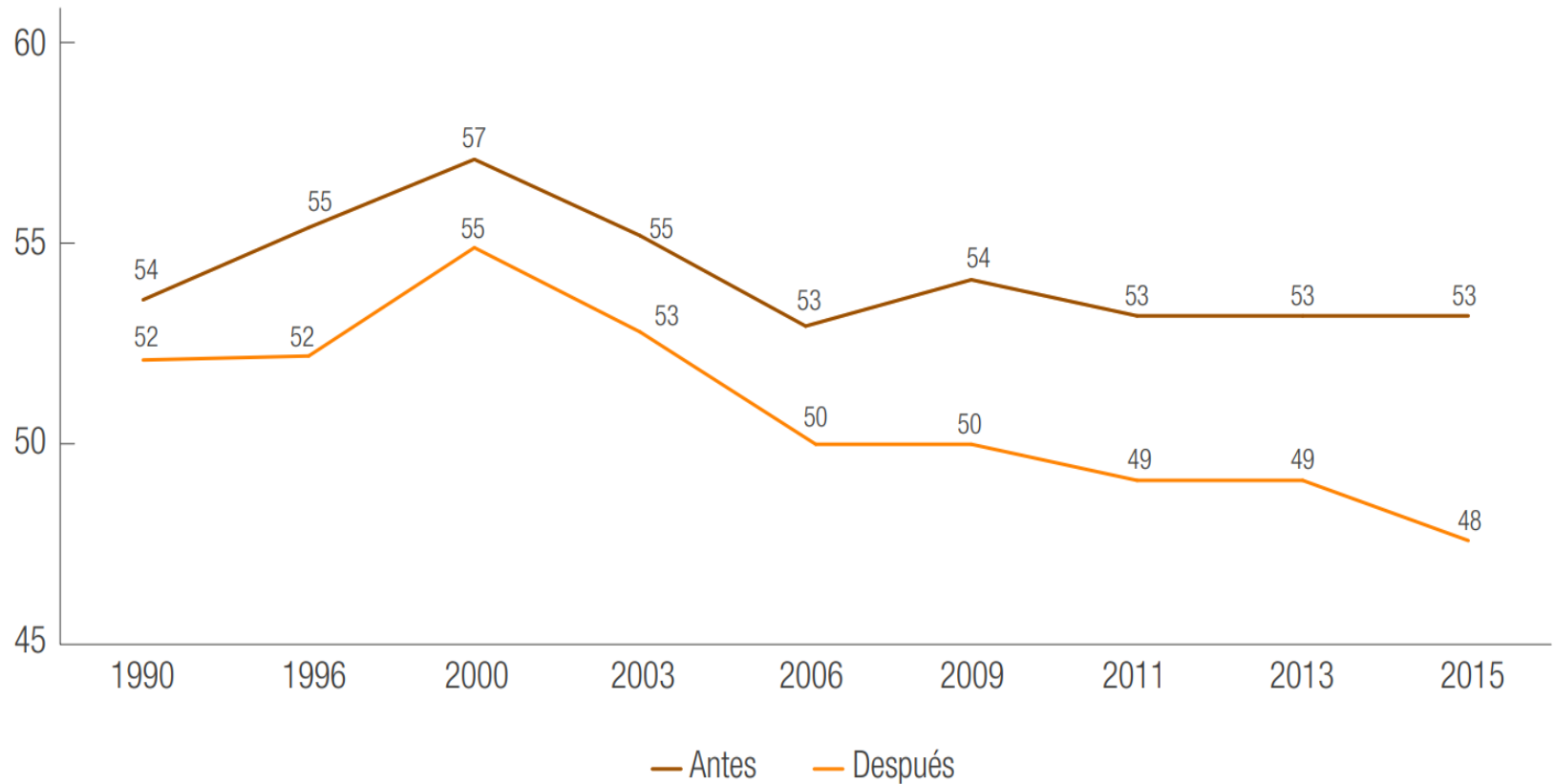
Inequality of Disposable and Market income in Latin America and Europe (Gini coefficients)



Source: Figure 1: Goñi, Lopez and Servén, 2008; and Lustig (2011).

Redistributive impact of taxes and transfers in Chile

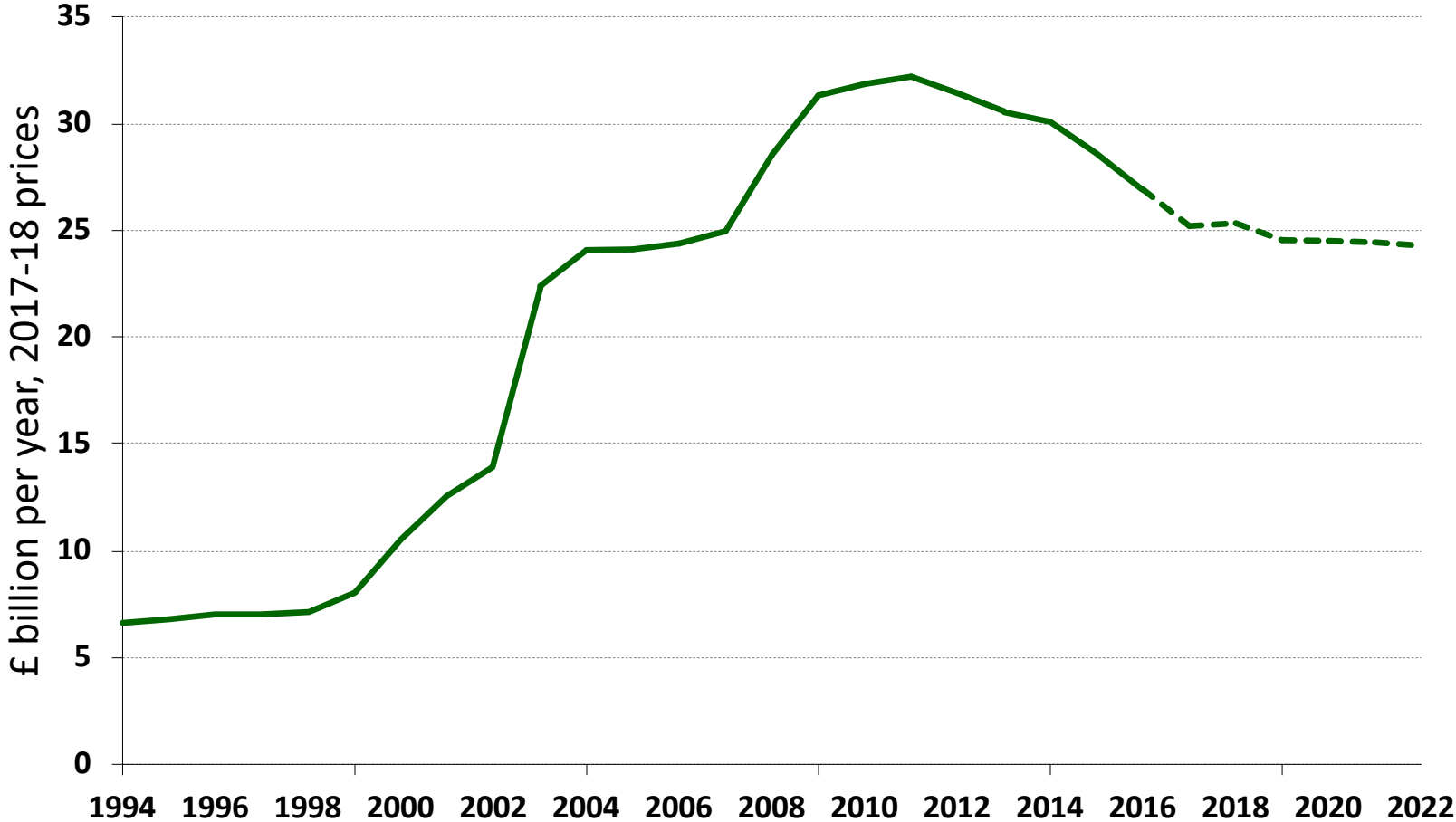
Efecto del impuesto a la renta y transferencias sobre el coeficiente de Gini



Elaboración propia a partir de datos de las encuestas Casen, años respectivos.

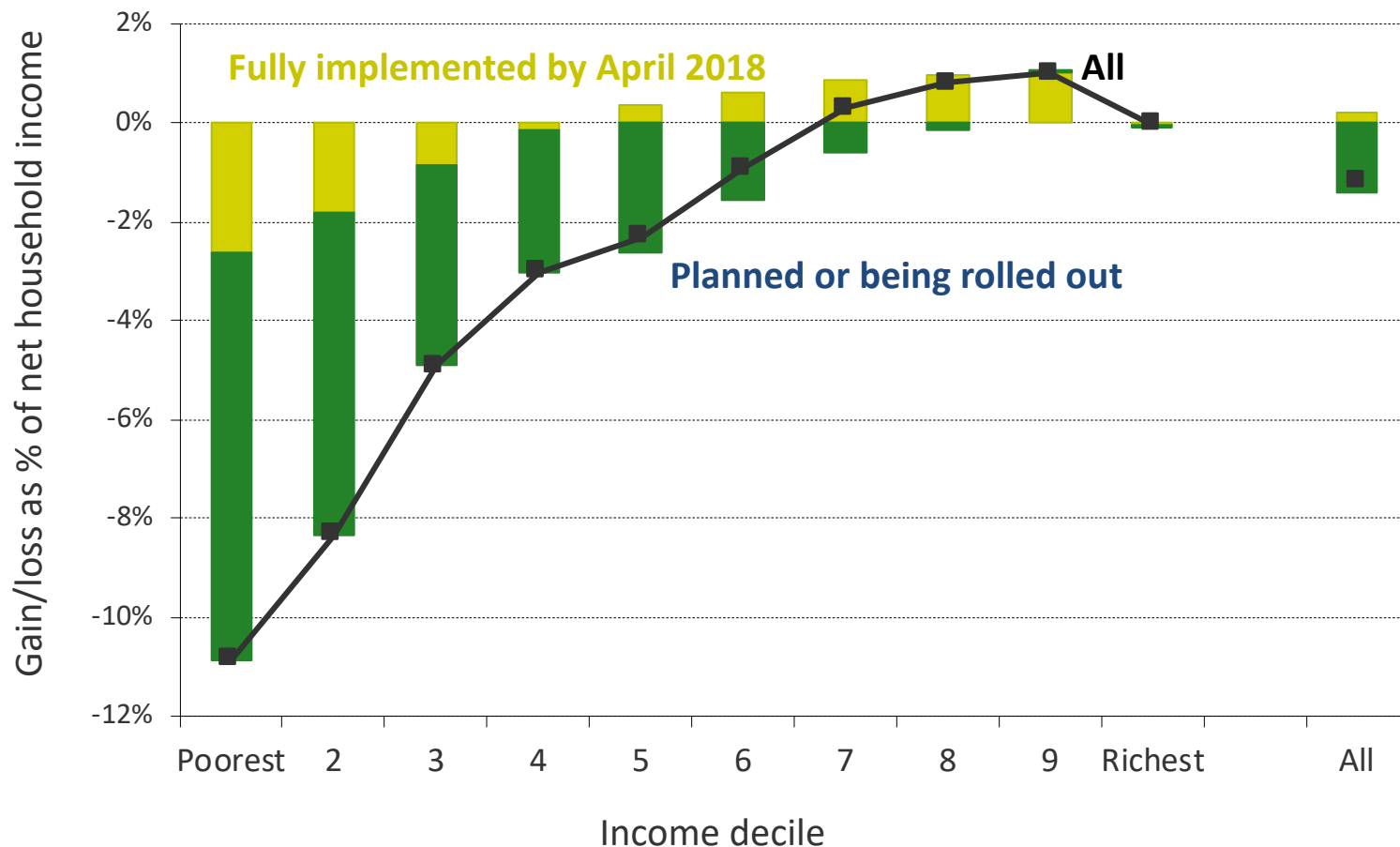
Source: Cociña, Frei and Larrañaga, 2017; Notes: Brown line is before taxes.

Real spending on tax credits and equivalents in the UK



Source: IFS calculations from DWP (UK) benefit expenditure tables.

Long run distributional impact of personal tax/benefit reforms in the UK since 2015, going forward...

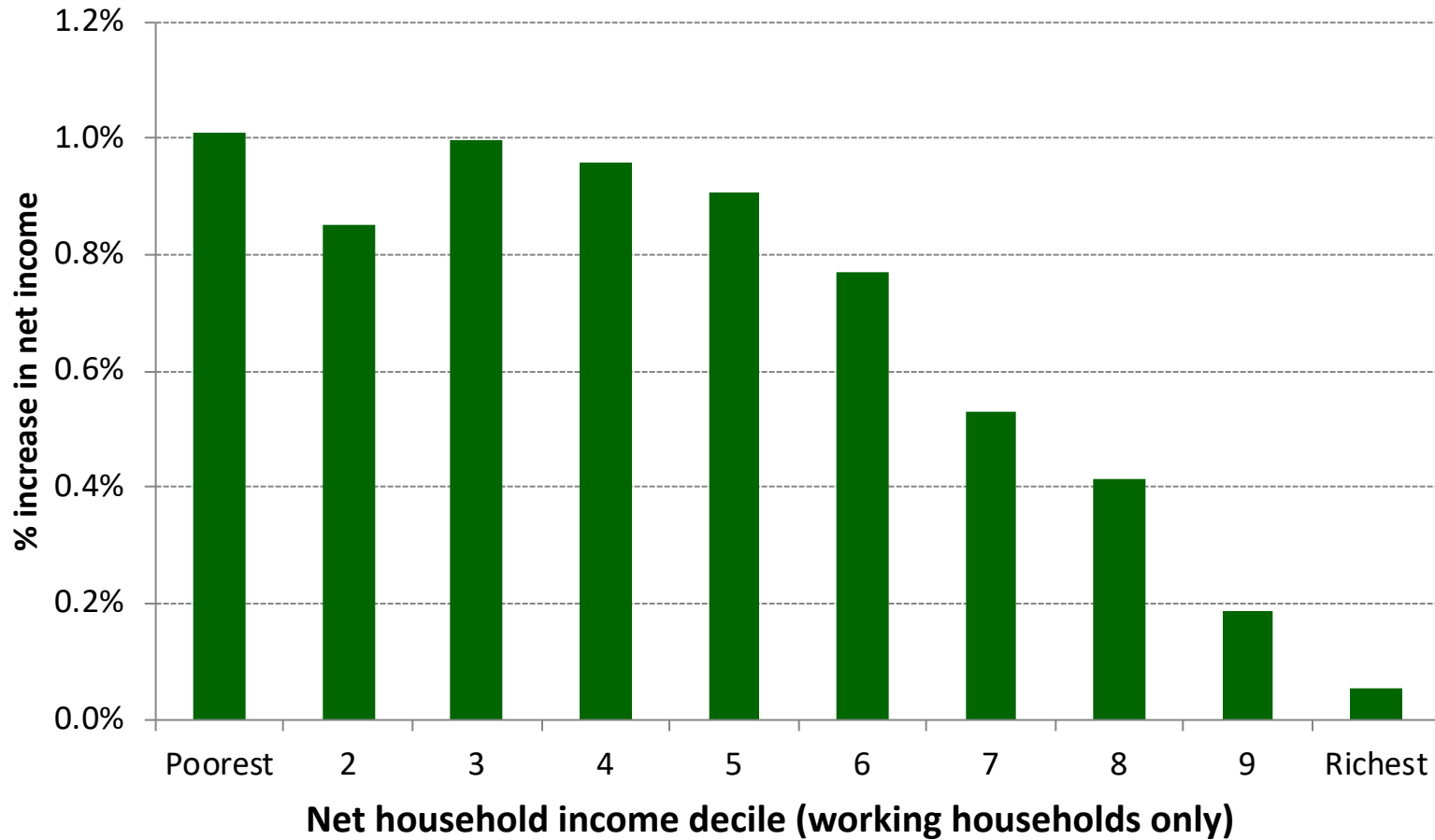


Note: Assumes full take-up of means-tested benefits and tax-credits. Policies partially rolled are Universal Credit, the 2-child limits, the replacement of DLA with PIP and the abolition of the WRAG premium in ESA.

Source: IFS calculations using the IFS micro-simulation model run on the 2015–16 FRS and 2014 LCFS.

Higher minimum wage targets the lowest-wage people, *not* the lowest-earning households

The increase in the minimum hourly wage between now and 2020 in the UK.

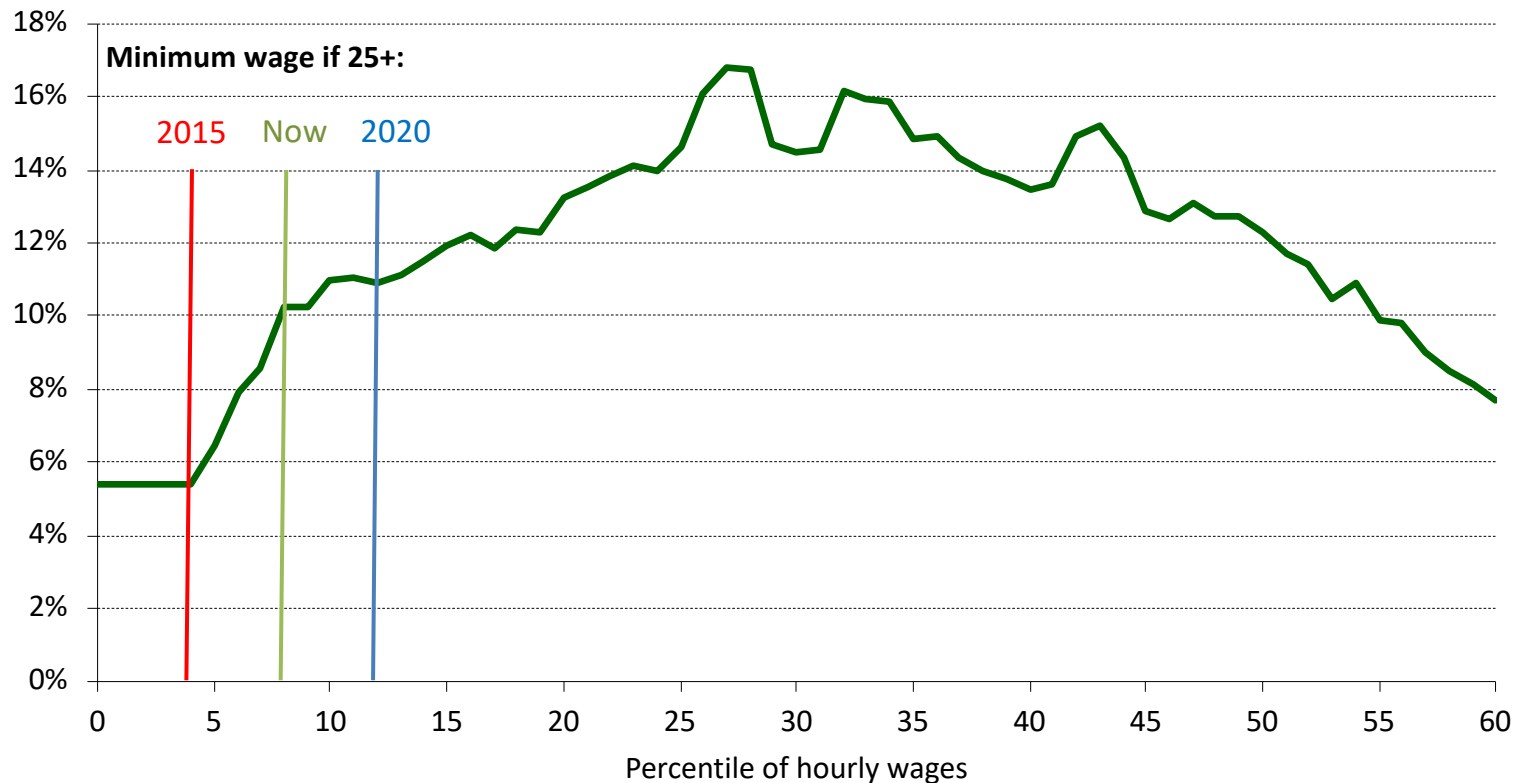


Note: Shows mechanical increase in net income arising from minimum hourly wage rises planned between now and 2020, allowing for interaction with tax payments and benefit entitlements.

Source: Cribb, Joyce and Norris Keiller (2017): www.ifs.org.uk/publications/9205

Jobs affected by higher minimum are not the same as those previously affected

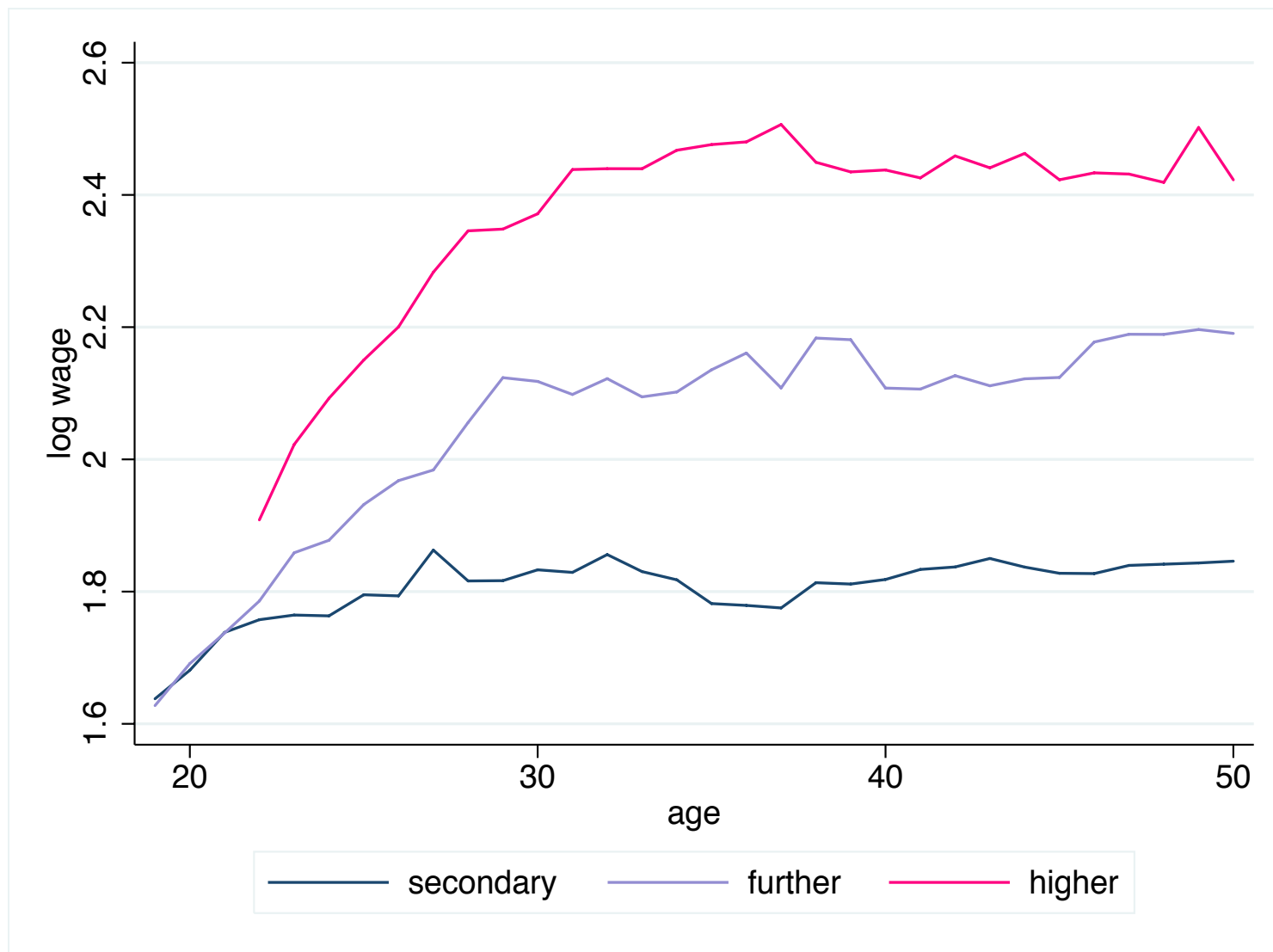
Proportion of employees aged 25+ in the most “automatable” jobs (top 10% of routine task intensity”)



Source: Cribb, Joyce and Norris Keiller (2018): www.ifs.org.uk/publications/10287. Data used is ASHE, 2015.

It's depressing at the bottom: wage profiles by education and age

- returns to experience appear strongly *complementary* with education



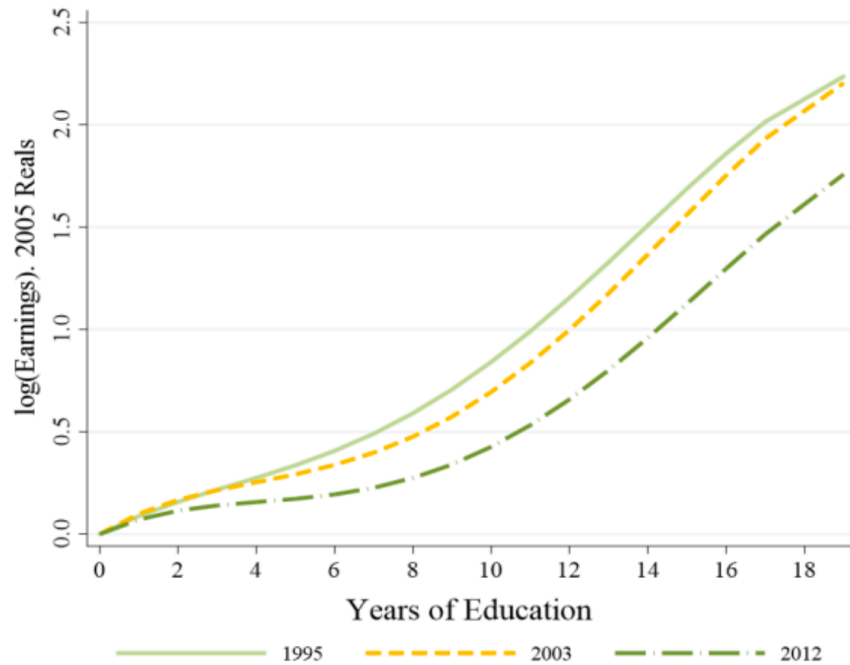
Source: Blundell, Dias, Meghir and Shaw (2016),

Notes: Women, UK BHPS. See similar for UK men and for recent cohorts in the US.

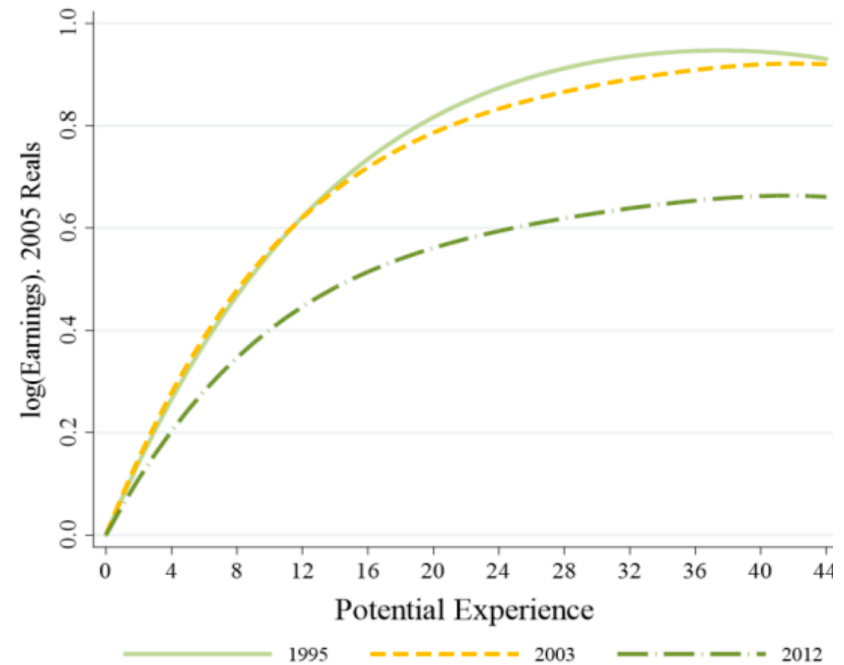
Returns to education and experience in Brazil

Figure 3. Education and experience premium by year.

Panel A. Education



Panel B. Potential Experience

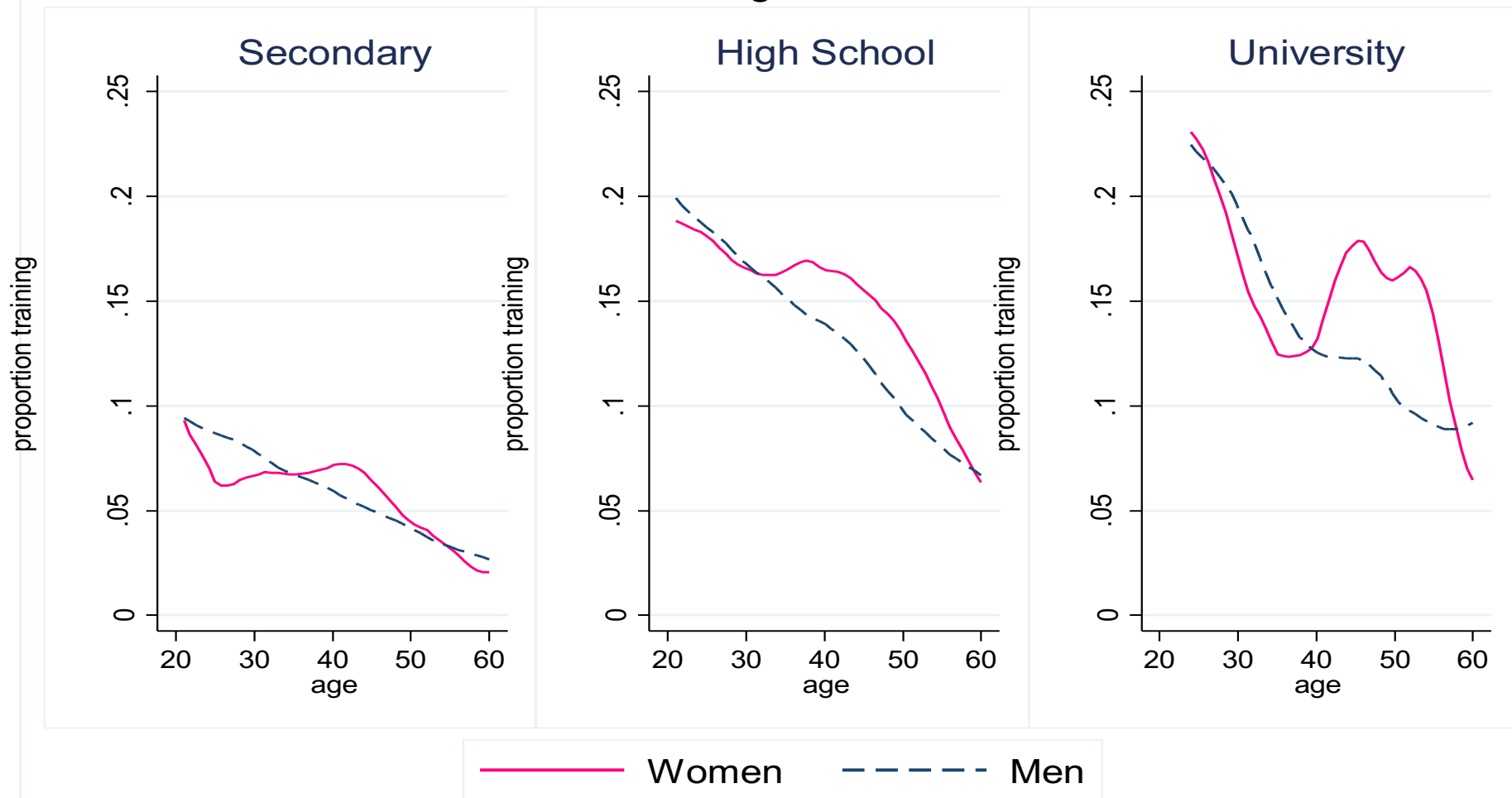


Note. All regressions include a quartic polynomial in education, a quartic polynomial in potential experience, two dummies for formality status, two race dummies, a gender dummy, four region dummies, sector dummies, and an indicator of work in rural areas (see Table 2). The year 1995 includes 1995 and 1996 PNAD samples, the year 2003 includes 2002 and 2003 PNAD samples, and the year 2012 includes 2011 and 2012 PNAD samples. Source: *Pesquisa Nacional por Amostra de Domicílios* PNAD.

Source: Ferreira, Firpo and Messina, 2019

Training in UK strongly complementary with education.

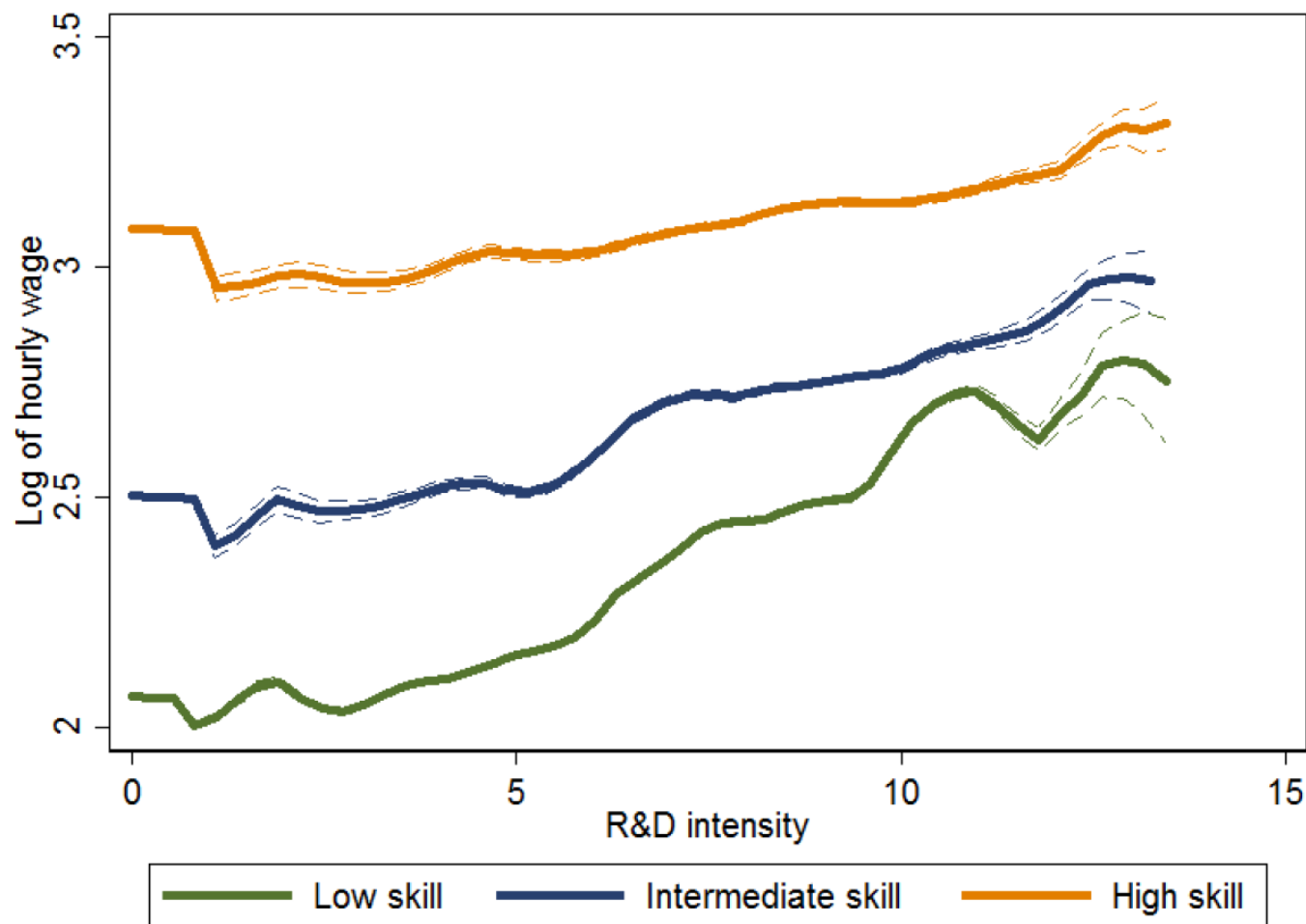
Prevalence of training over past year All training, 50+ hours



Source: Blundell, Costa-Dias, Goll and Meghir (2019), Notes: UK BHPS

Low skilled workers and 'good' firms: not all bad at the bottom

log hourly wage rate and R&D intensity: by skill group



Not all selection, some abilities of low educated are complementary with technology, they get training and the jobs are not outsourced....

Notes: Skill allocated by occupations in ASHE.
Source: Aghion, Bergeaud, Blundell and Griffith (2019)

Inequality, Redistribution and the Labour Market

➤ Policy options:

1. Earned income tax credits?

- encourage employment and well-targeted to low earning families, but may preserve low progression & have large incidence effects.

2. Minimum wage?

- not so well-targeted, due to family earnings and falling male hours/attachment. Should be a *complement* to tax credits. Basic income?

3. Human capital/training incentives/tax credits for low educated?

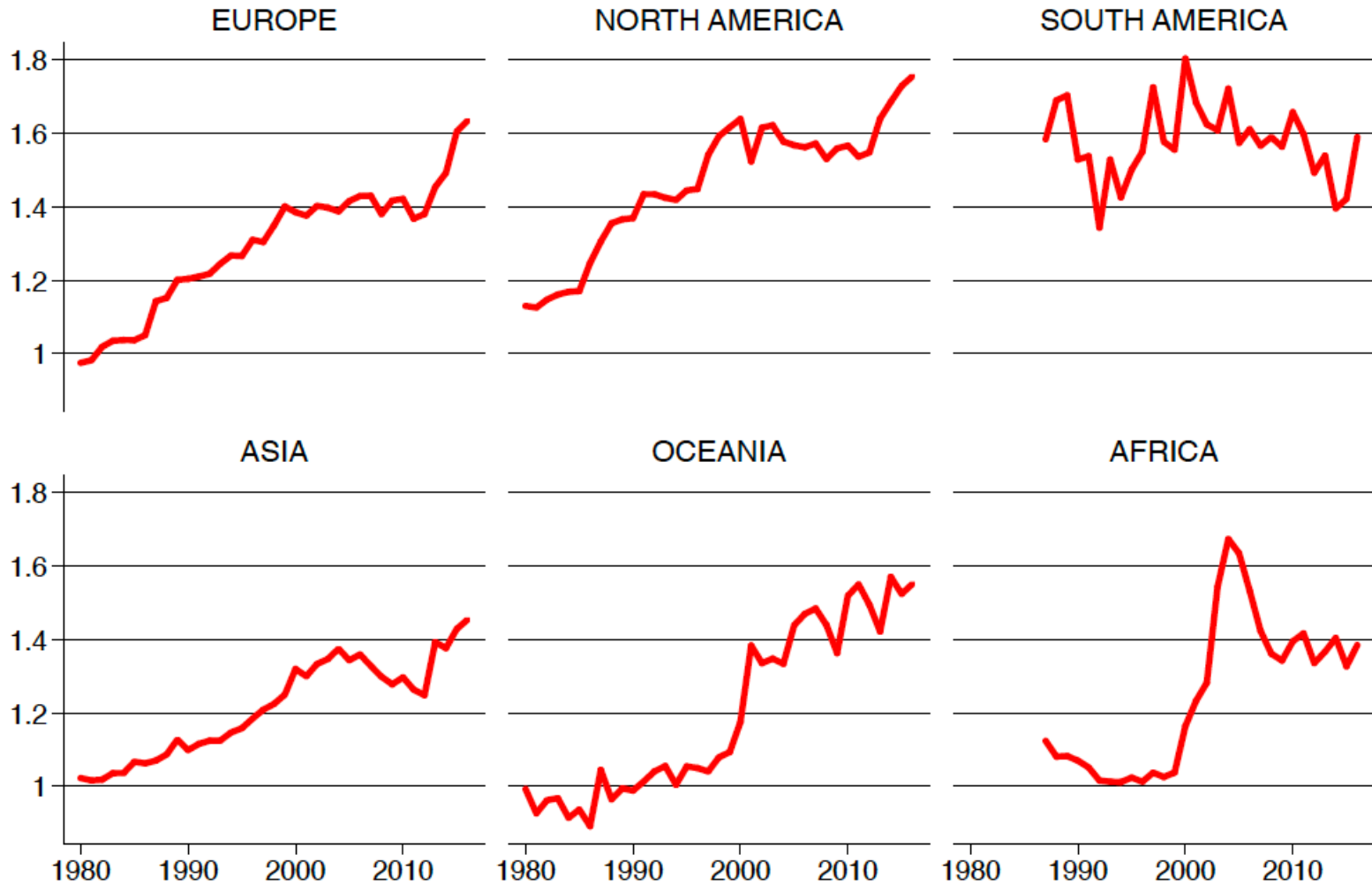
- focus on soft skills for low educated and training for women returning after children.

4. Competition policy and contract regulation?

- increasing mark-ups, solo self-employment and gig economy may signal declining bargaining power....

Firms and market power matter

Average markups across different regions



Source: De Leocker and Eeckhout (2018)

Appropriate policy mix depends on what explains earnings inequality

- **Technical change:** skilled workers more productive; easier to automate routine tasks
 - education and skills policy may be effective long-run responses
- **Globalisation and trade:** competition for mobile skilled labour; import competition and offshoring
 - regional policies, industrial policy and policies to facilitate mobility
- **Loss of bargaining power:** falling union membership; self-employment, gig economy
 - policies to empower workers, regulation of contracts and min wages
- **Pay and profits at the top:** bonuses and stock option; market power and super-star firms
 - corporation tax, competition policy, corporate/governance regulation
- **Redistributive tax and benefit policies are a key policy instrument**
 - *but not the only one!*



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