

Capital, labour and the distribution of income



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EXPLAINING
INEQUALITY

ROUTLEDGE




1. Trends

Times of extreme inequality

- **Worldwide:** 2016 the richest 1% of the world may own the same wealth of all the other human beings (Oxfam 2015)
- Lower disparities among **country averages**
- When the relevance of the incomes of the richest 1% is considered, **inequality has increased** in spite of higher average income in (highly unequal) emerging countries such as China and India (Anand and Segal, 2014).



The economics of inequality

- Need for a **comprehensive** view of distribution and inequality in the economic system, considering all relations, at diff. levels:
- **Functional distribution** of income between profits and wages
- Within **profits**: financial rents, retained profits, dividends, who gets them?
- Within **wages**: how equal? Top managers' "wages"
- How these incomes reach individuals: **personal distribution of income**, resulting **inequality**



1. Functional distribution of income

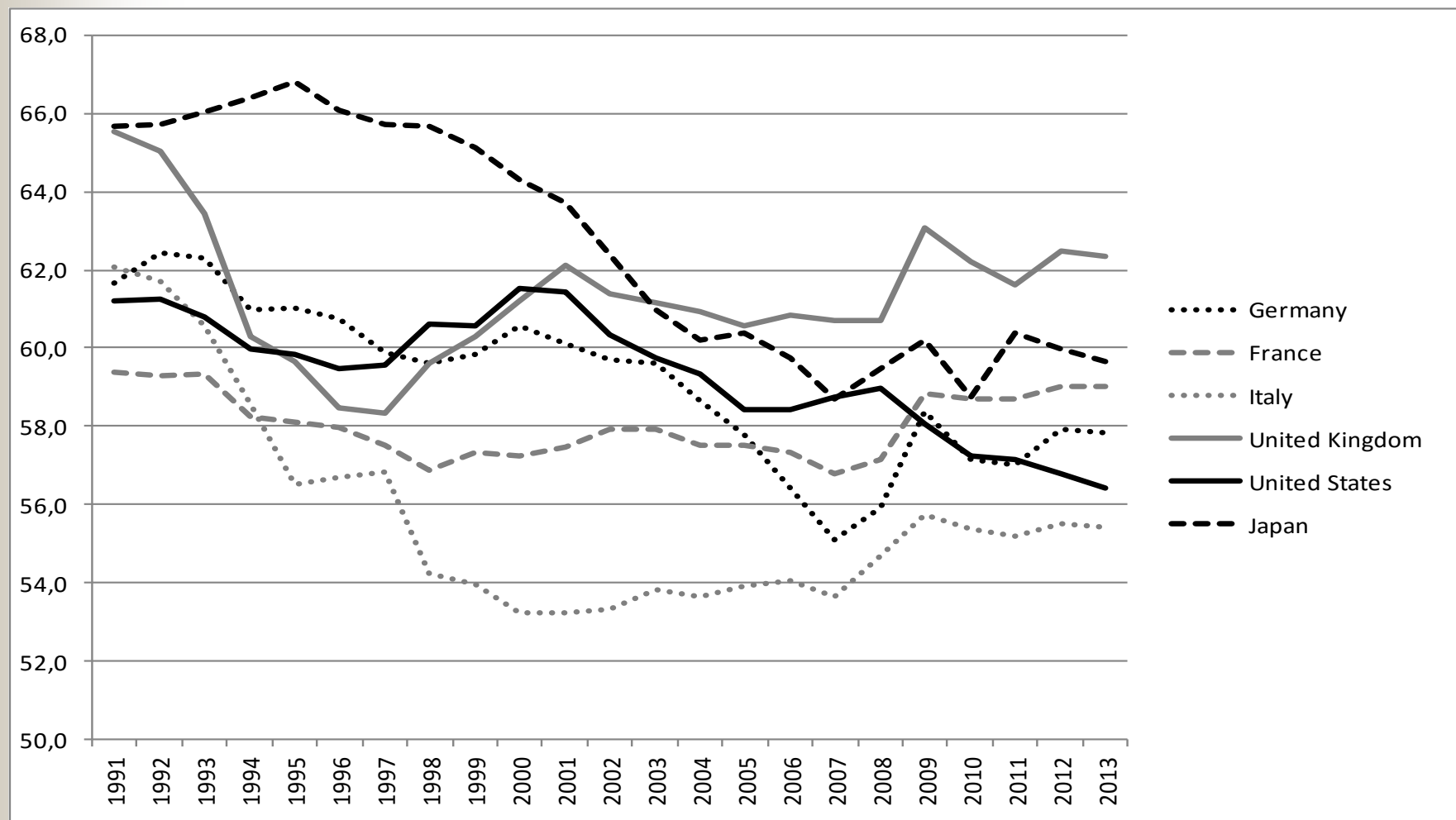
- Share of income going to capital and to labour – profits, rents, wages
- Data from national accounts
- Who gets profits: finance, entrepreneurial profits, dividends, top managers' pay (lead to investment? opulent consumption?)
- Who gets wages: differentiation of contracts, top managers' “wages” (lead to consumption?)

Labour income share, 1991-2013

Wage share of GDP adjusted for the income of the self-employed

(compensation per employee as a percentage of GDP at market prices per person employed).

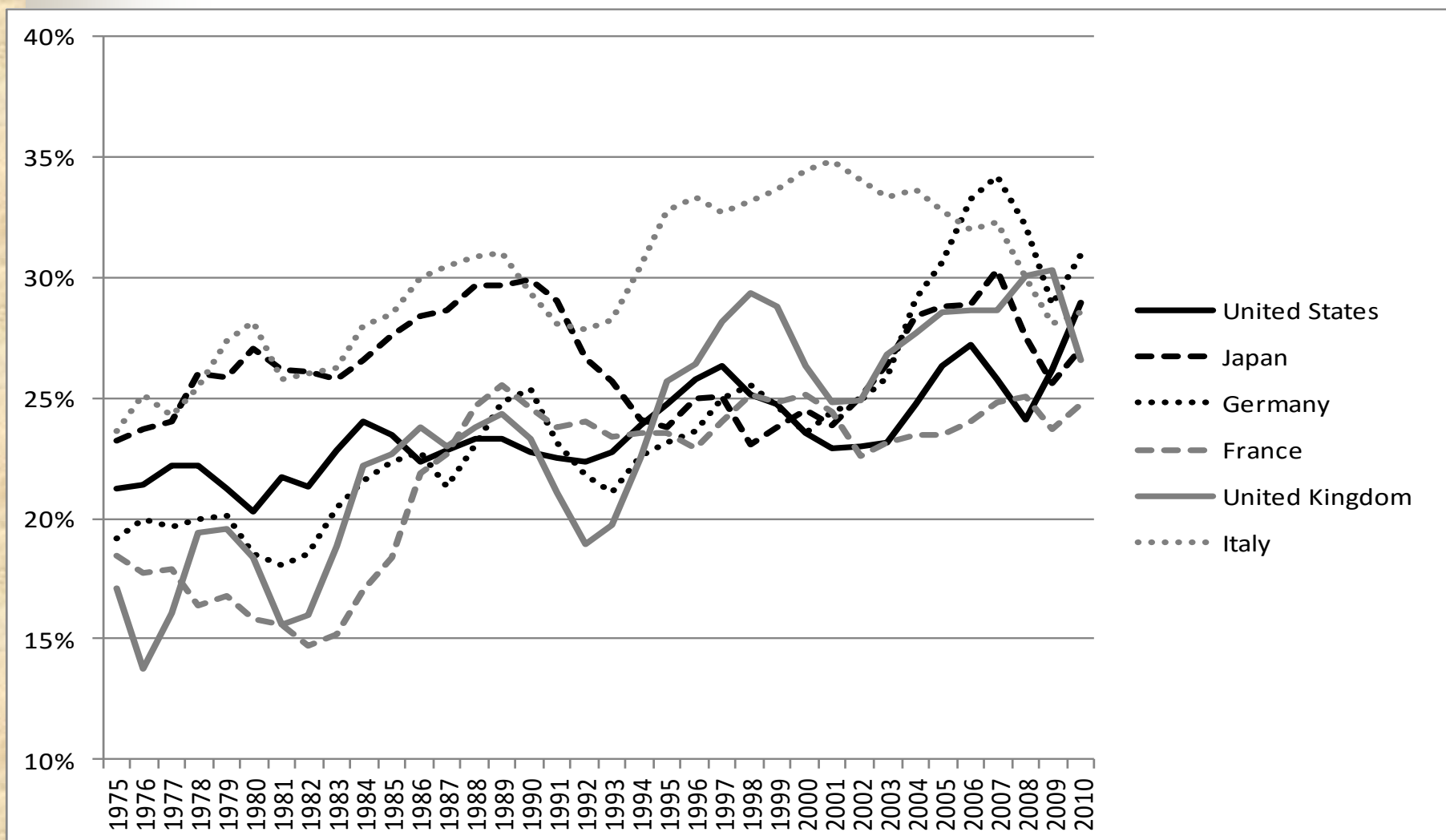
Data from European Commission AMECO database, from: ILO Global Wage Report 2014/15, p.11



The capital share in advanced countries, 1975-2010

Adapted from Piketty (2013), Figure 6.5, p.351.

For sources and data see piketty.pse.ens.fr/capital21c





Profits and wages

- **Profits** are higher when more capital is invested, new technologies used, with oligopolistic power, finance with greater role (profits pay financial rents), tax elusion and evasion is possible
- **Wages** are higher with high skill jobs, lower when jobs are moved abroad, replaced by machinery, when workers lose union protection, national labour contracts and permanent employment, when precarious, low wage jobs expand.



Capital vs labour

- In advanced countries labour share is 55-70% of income; increased in 1970s, fallen since the 1980s, shifting to capital 10-15% of income. (Different calculations)
- In US, UK: income of the top 1% of wage earners – top managers – should be excluded from labour income.
- 1991 to 2013: In Spain labour share from 62 to 54%, In Greece from 57 to 48%

Growth of labour productivity and average wages

Wage growth is calculated as a weighted average of year-on-year growth in average monthly real wages in 36 economies. Index is based to 1999 because of data availability.

Data from ILO Global Wage Database; ILO Trends Econometric Model.

From: ILO Global Wage Report 2014/15, p.8.





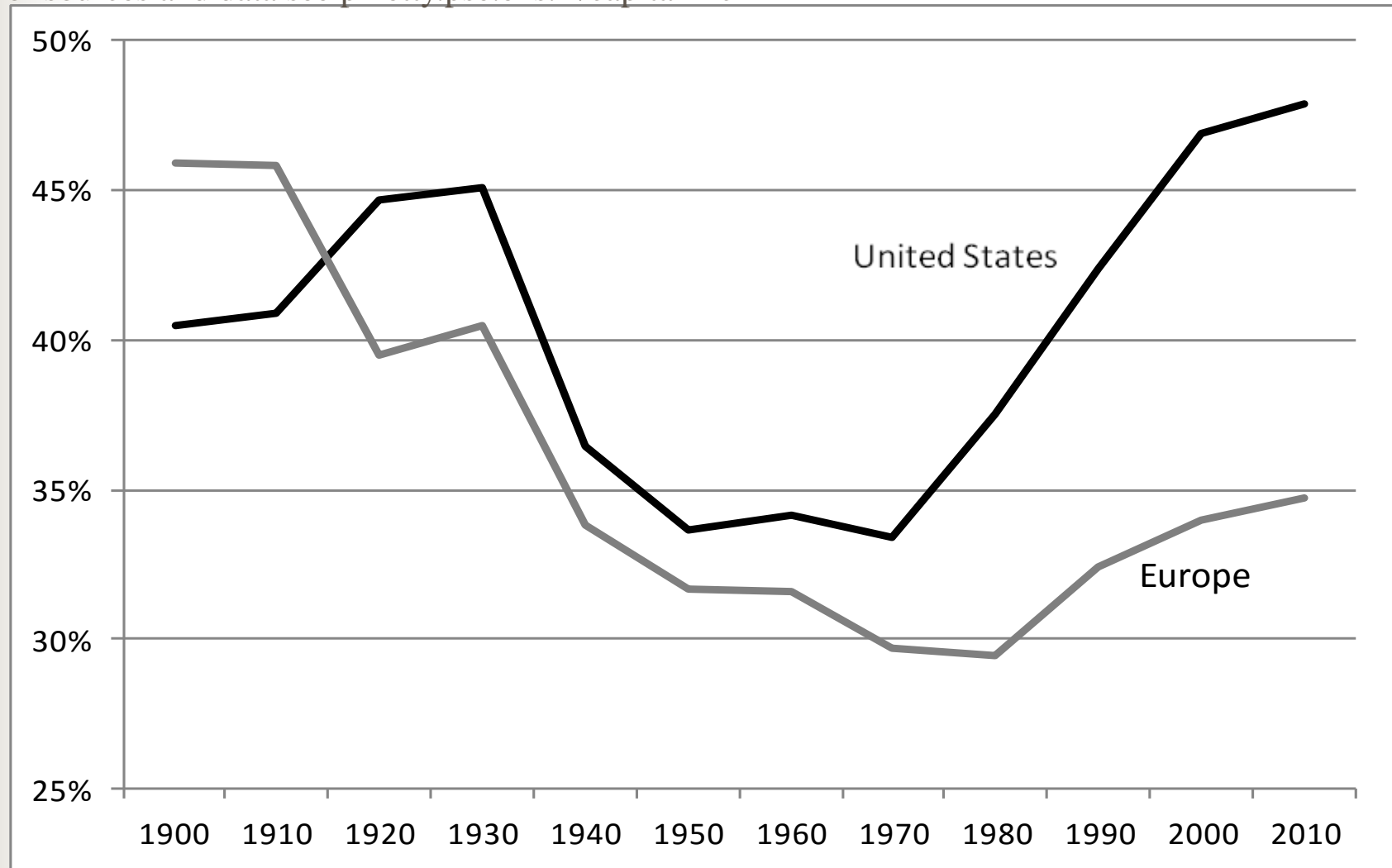
The top 10%

- Piketty's work on tax returns in the US and France, extended to many countries (gross incomes)
- Focus on the top 10%, 1%
- Info on median vs mean income

The share of income of the richest 10% in the US and Europe

Adapted from Piketty (2013), Figure 9.8, p.514.

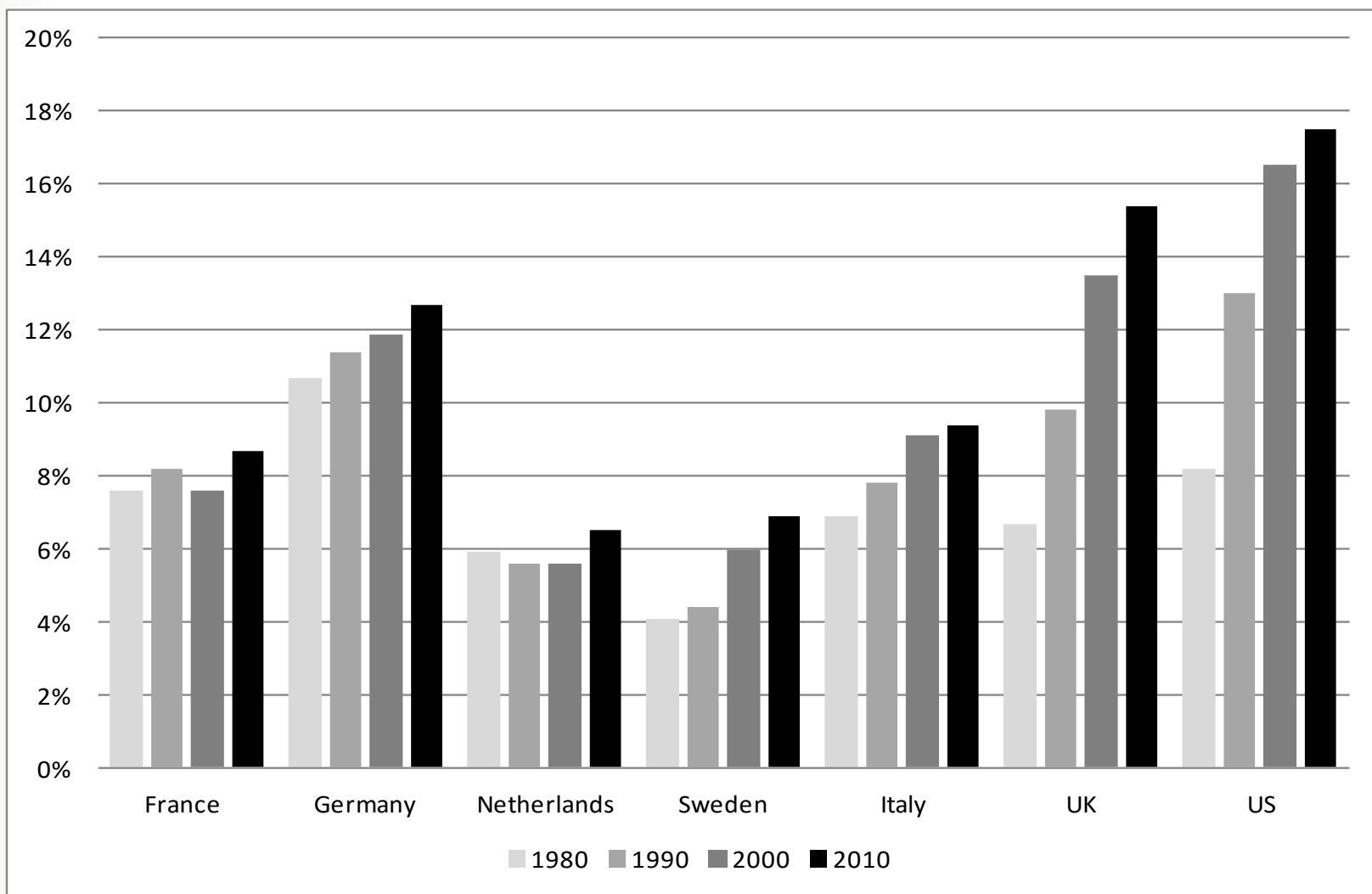
For sources and data see piketty.pse.ens.fr/capital21c



The top 1% income share in advanced countries, 1980-2010

Calculations on data from the World Top Income Database

<http://topincomes.parisschoolofeconomics.eu/>





The 1% and the rest, US

- "1% of the richest Americans in the seventies counted for 9% of the income; in 2007 their share had risen to 23%, the value of 1928. Median income has declined in real terms over the last 30 years "
(Robert Reich)
- **Finance** has compensated lower incomes through real estate debt



Where does the 1% get its money?

- US, Top 0.1%: 45% is “labour income”
- Lazonick (2015, p.28-31): this includes compensation from the realised gains on stock options and stock awards
- Look at 500 highest paid executives (ExecuComp data) in 2013 avg total compensation of \$24.4 million;
- 84% was from gains on stock options and stock awards, salaries and bonuses were just 5%.
- Money comes from rents and privileged info.



2. Personal distribution of income

- Data from household surveys, sources: OECD, the World Bank, WIDER, Luxembourg Income Study, etc
- **gross incomes** reach individuals as market outcomes;
- they become **disposable income** (in cash) after taxes and benefits;
- they become **extended disposable income** if we add the value of non-cash, in-kind services



Extended concepts of income

Gross income = Gross earnings + Gross self-employment + Other capital income

Disposable income = Gross income - Personal income tax – Social security contributions + Tax reliefs – Self-employment taxes – Capital income taxes + Cash benefits (pensions, unempl. benefits)

Extended disposable income = Disposable income (cash) + in-kind benefits (e.g. health, education and social housing) + in-kind income (e.g. imputed rents) – Consumption taxes

(Bogliacino and Maestri 2014, p.27)



Household income

- Individual incomes can be turned into household income by adding all the incomes of family members and “equivalising” for numbers of household (economies of scale in joint consumption) equivalence scales: if we compare a household with one person and a household with two persons having the same total monetary income, the benefits obtained by each individual of the latter household are more than half that of the former.

Lorenz curve

Deciles of population

Share of total income

Gini index

= 0 no inequality

= 1 max ineq

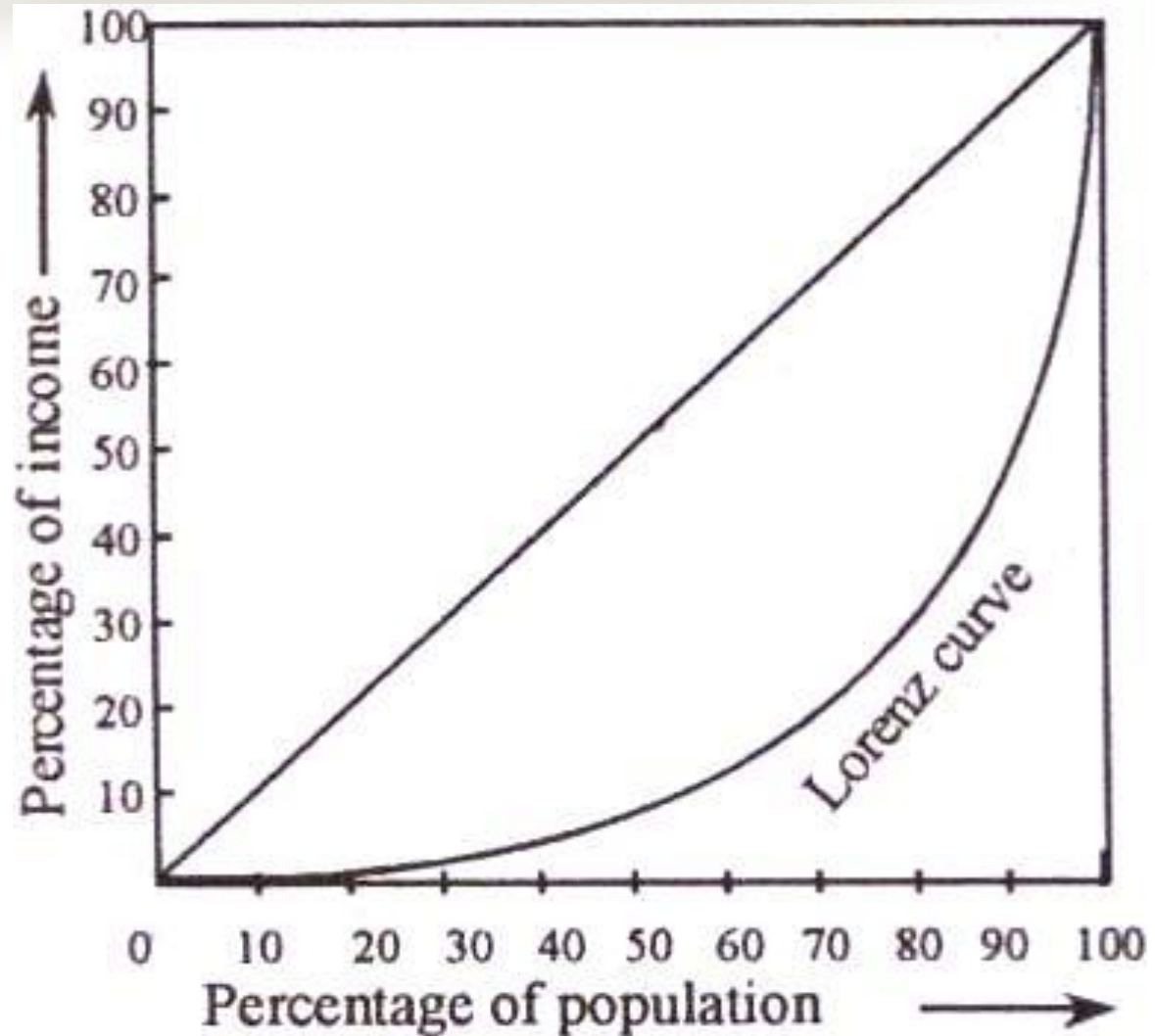
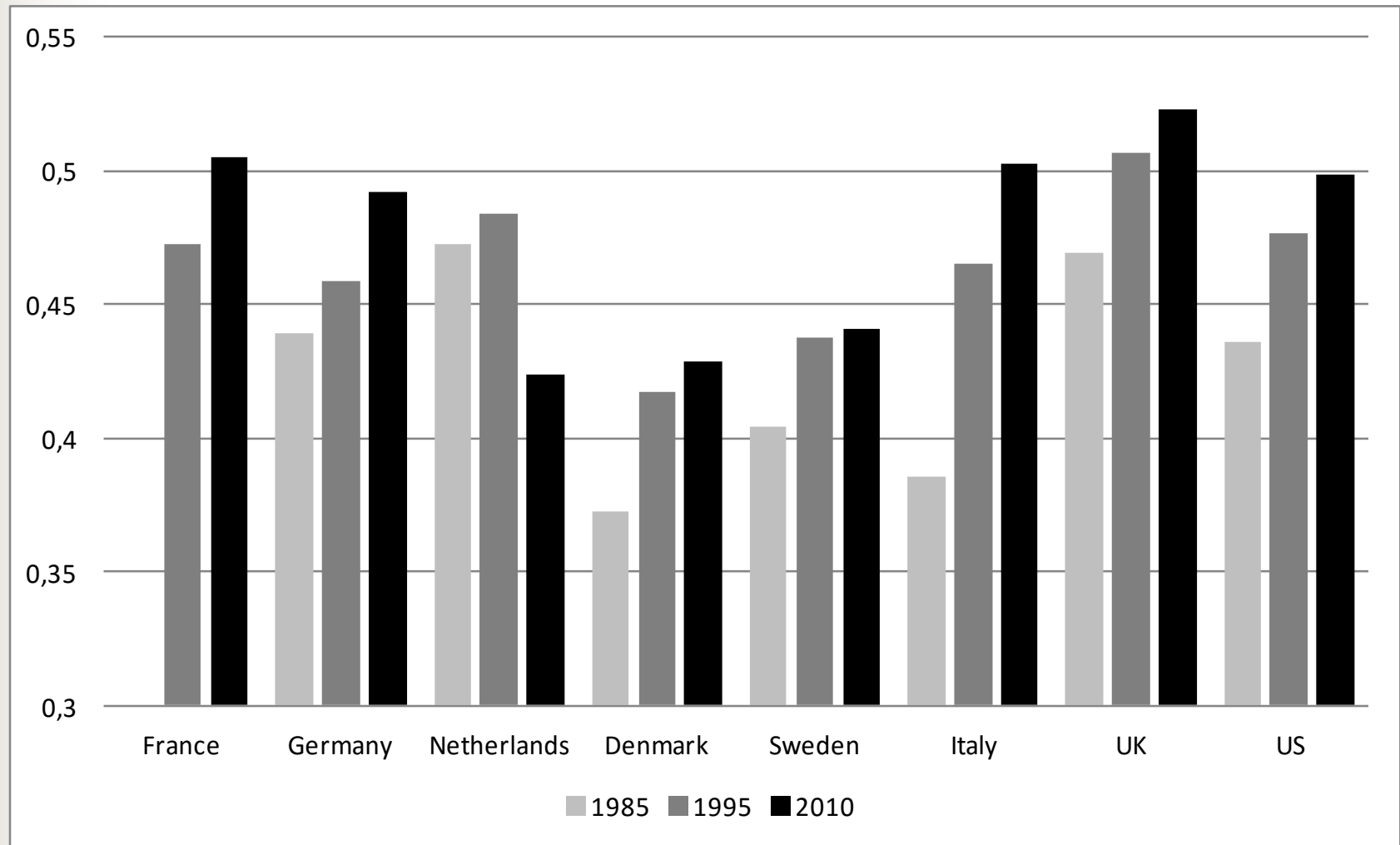


Fig. 3: A relatively unequal distribution

Gini index of inequality in household market incomes, 1985-2010

Gini index on equivalised household market incomes.

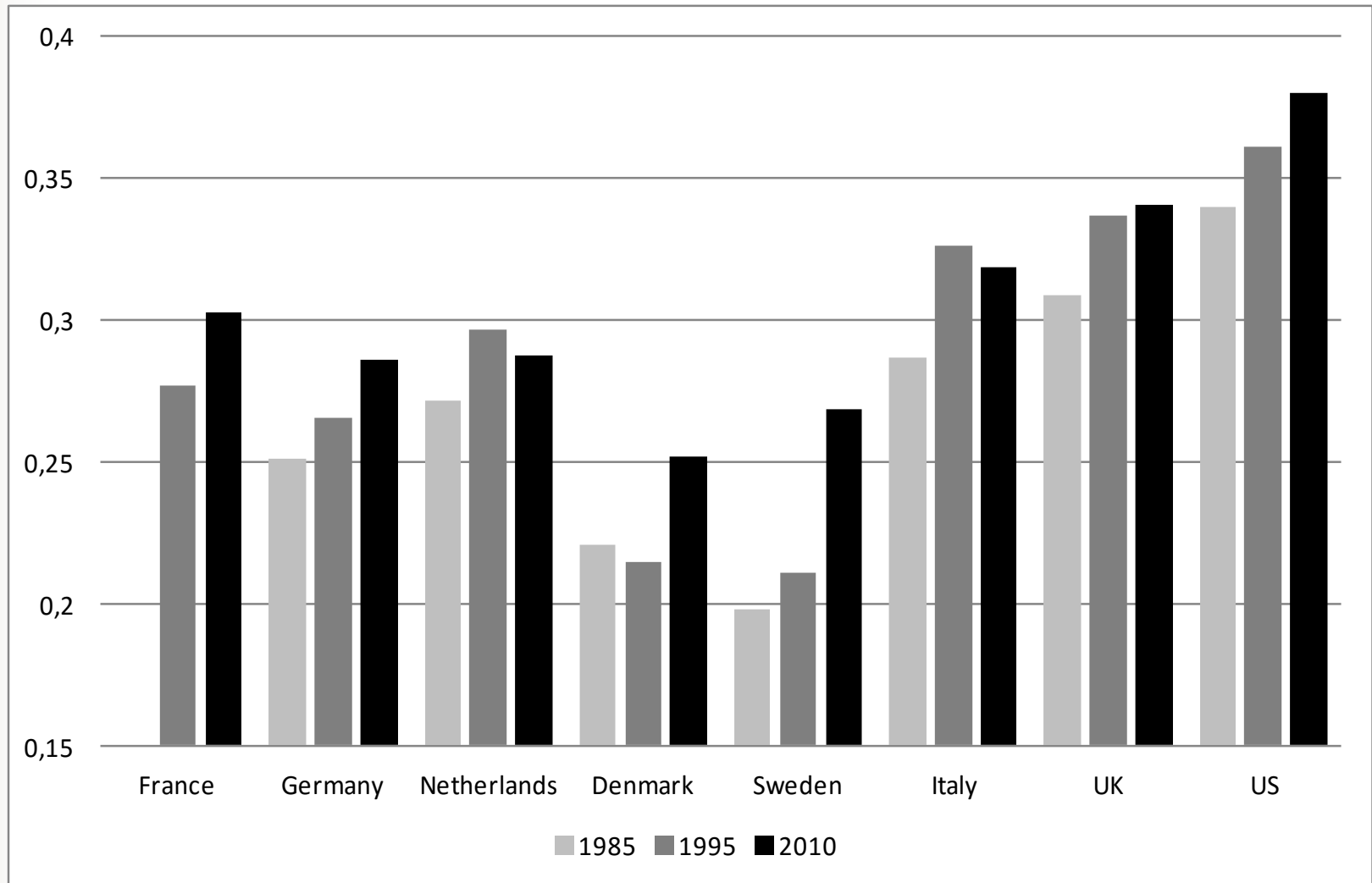
Calculations on OECD data, <http://www.oecd.org/social/income-distribution-database.htm>



Gini index of inequality in household disposable incomes

Gini index on equivalised household disposable incomes, after taxes and monetary transfers.

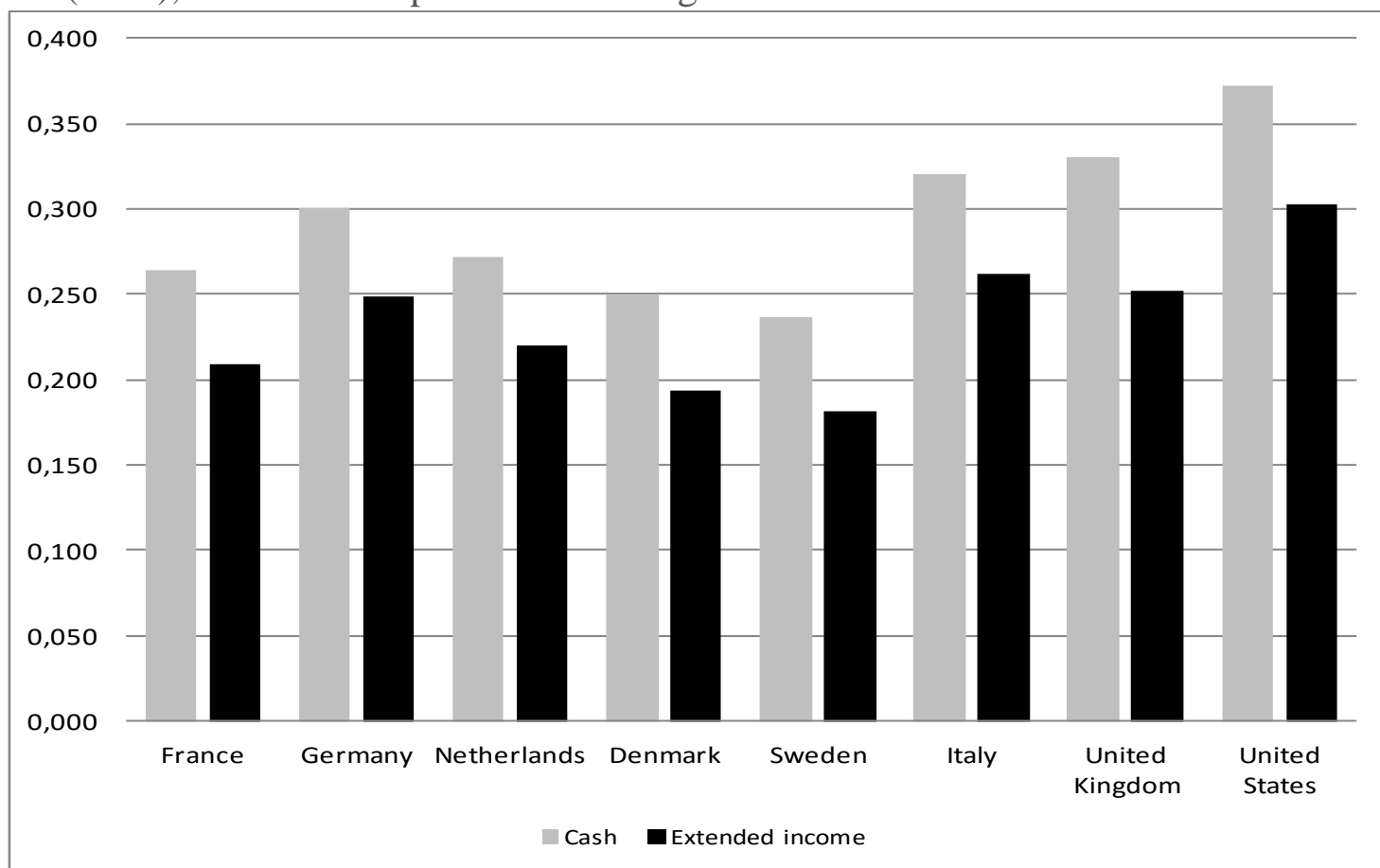
Calculations on OECD data, <http://www.oecd.org/social/income-distribution-database.htm>



Gini index of inequality in cash disposable incomes and in extended income considering public services, 2007

Gini index on equivalised household market incomes (after taxes and monetary transfers)
and on extended income (including the value of public services obtained).

Adapted from OECD (2011), data from <http://www.oecd.org/social/income-distribution-database.htm>

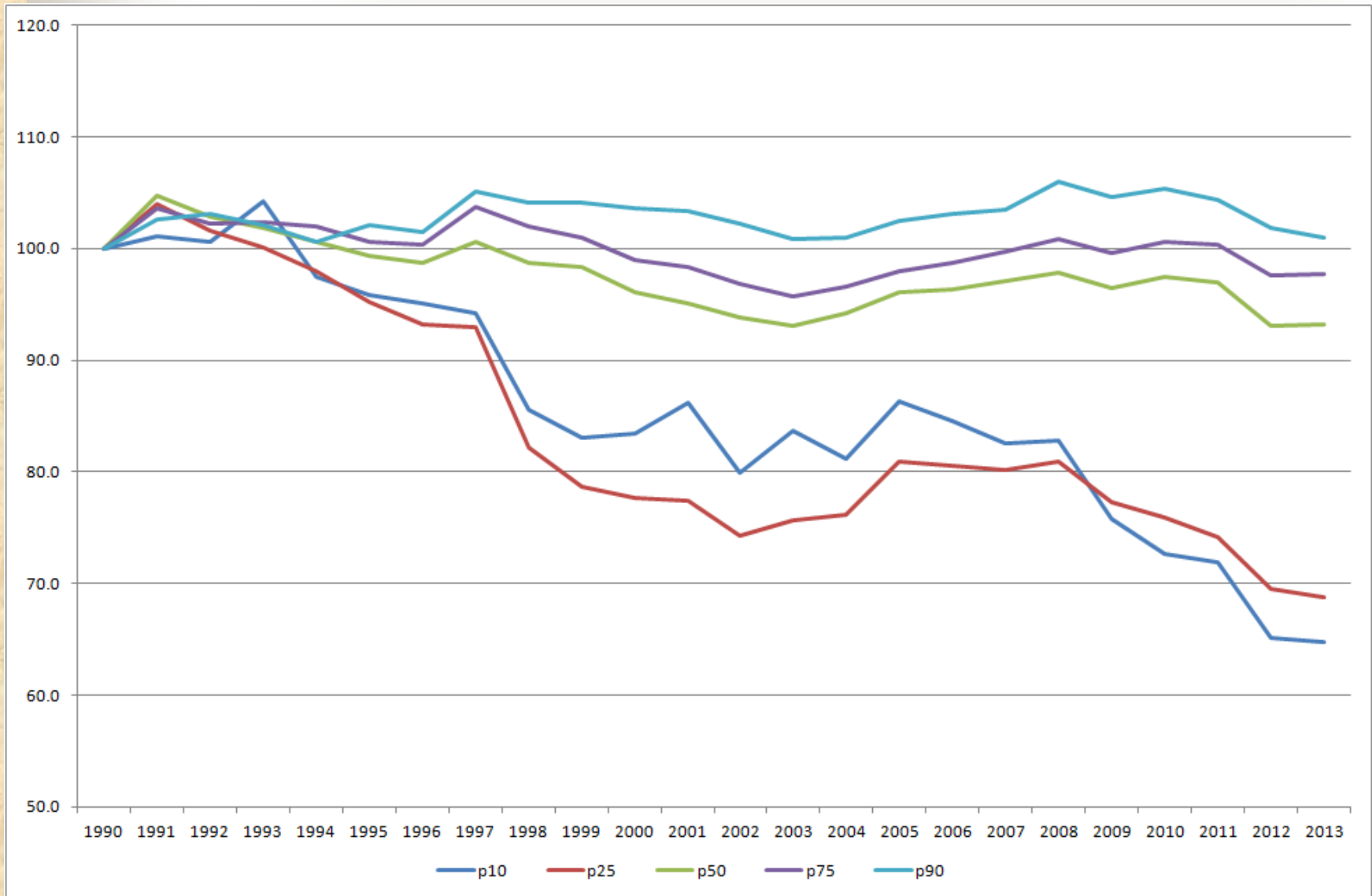




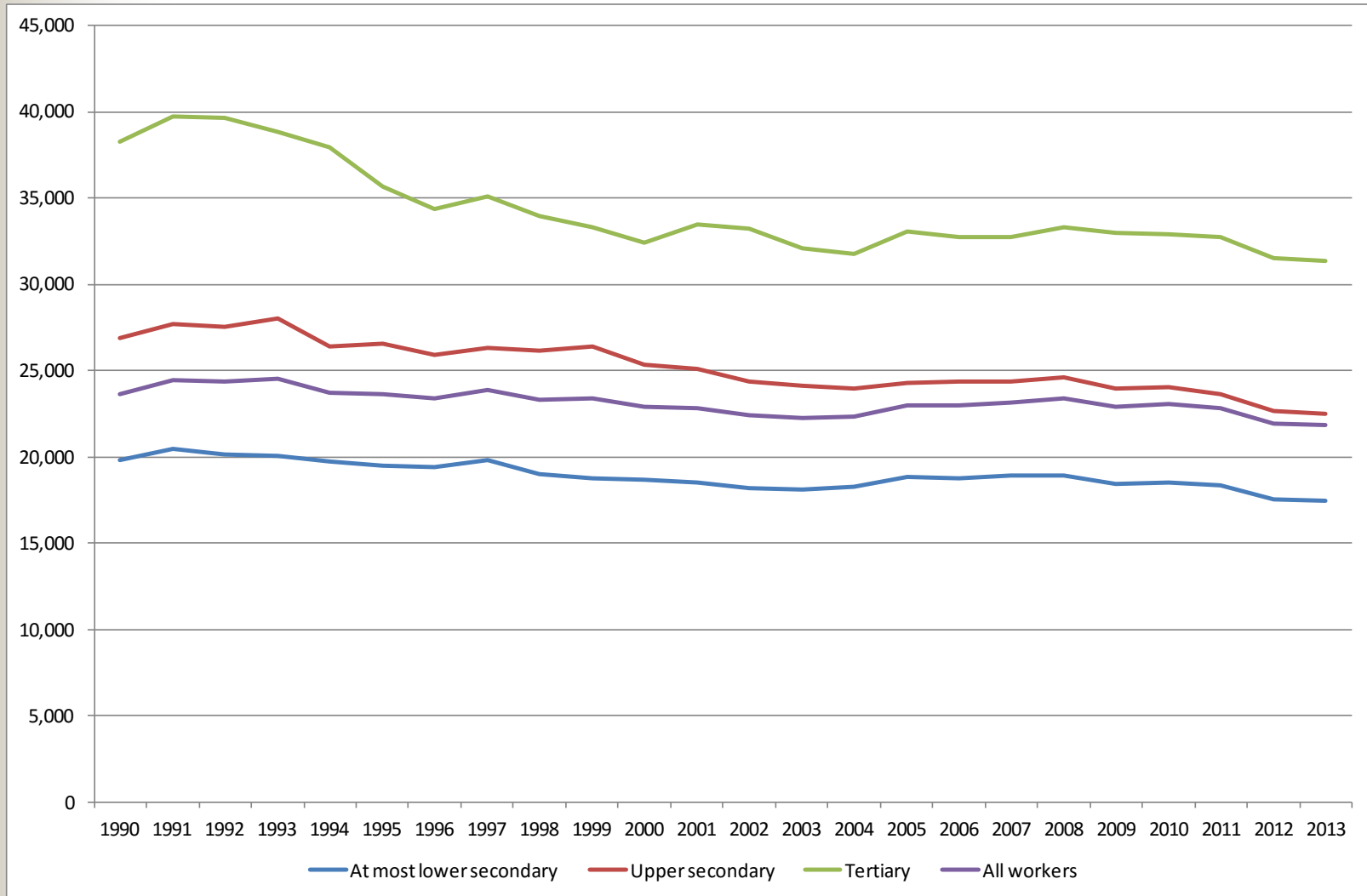
Dati sull'Italia

- **MICHELE RAITANO**
- **L'ANDAMENTO DELLA DISEGUAGLIANZA SALARIALE IN ITALIA: IL RUOLO DELL'ISTRUZIONE**
- **CONVEGNO ISTAT LA SOCIETÀ ITALIANA E LE GRANDI CRISI ECONOMICHE 1929-201**
- Focus on gross earnings of private employees aged 25-54 in 1990-2013
- INPS archives on all individuals interviewed in IT-SILC 2004-2012 => merge variables collected in SILC (at most for 4 years) with longitudinal variables recorded in INPS archives.

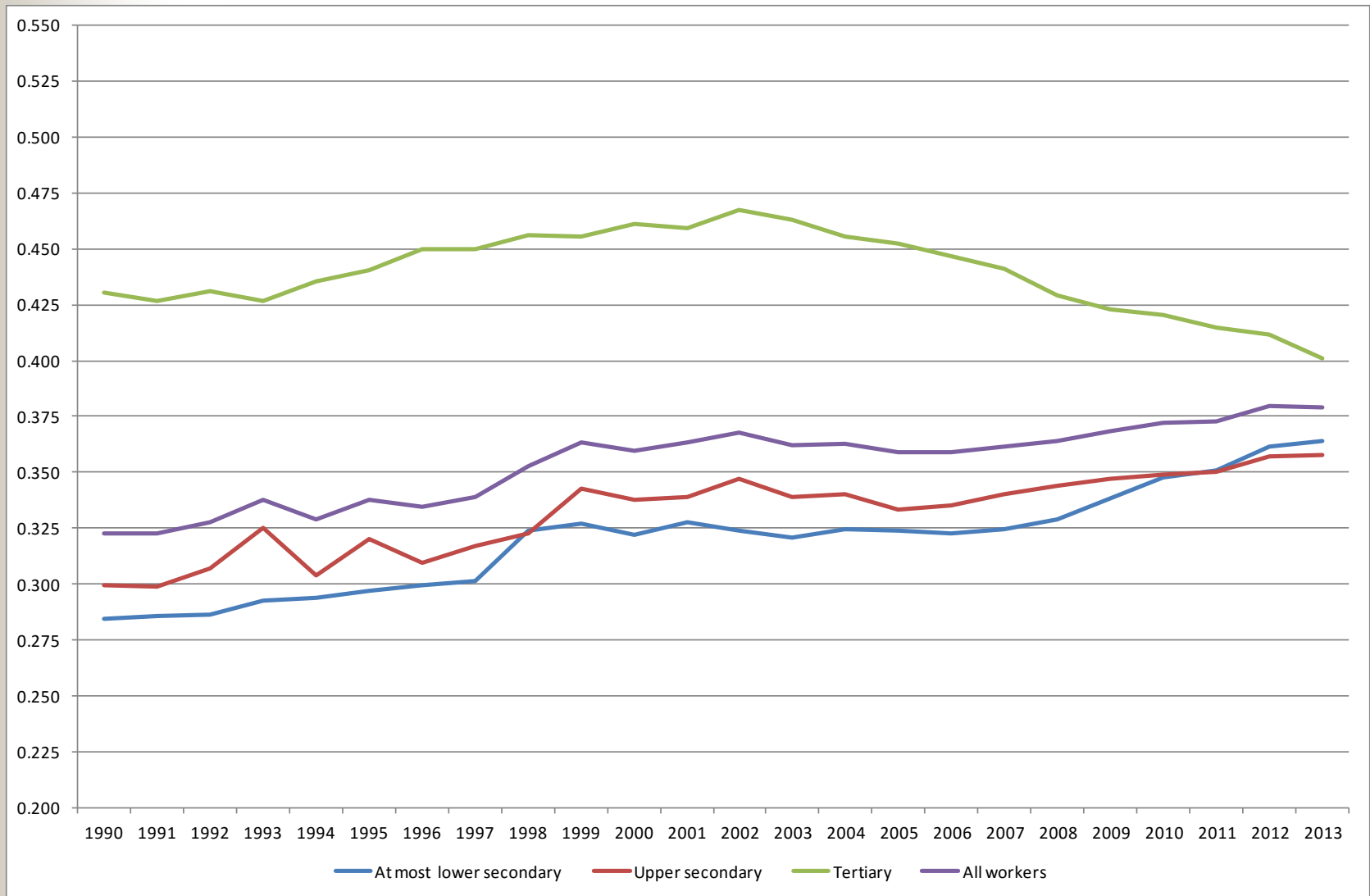
Percentiles of annual earnings: 1990=100



A) Mean annual earnings by education



B) Gini of annual earnings by education



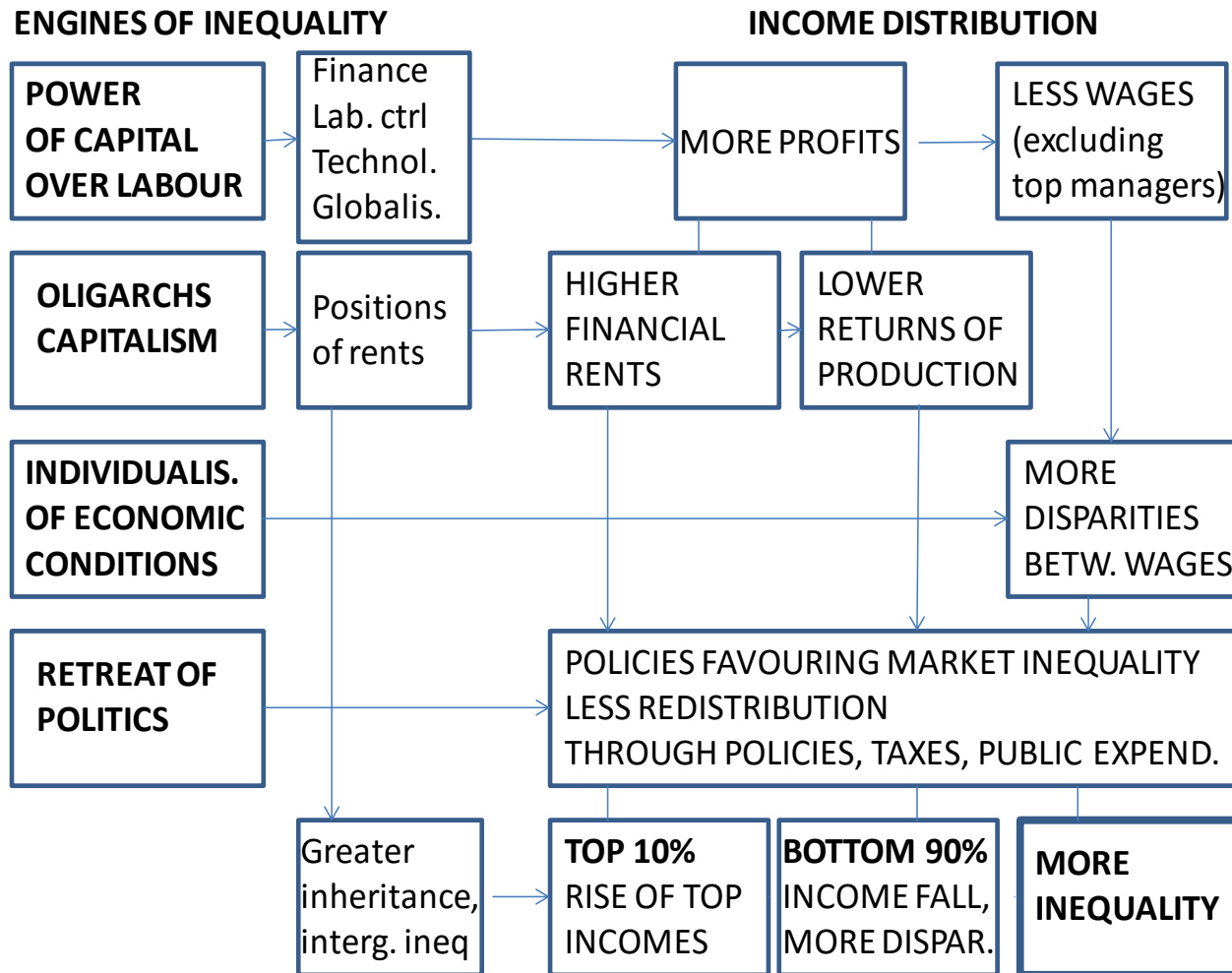


2. Explanations

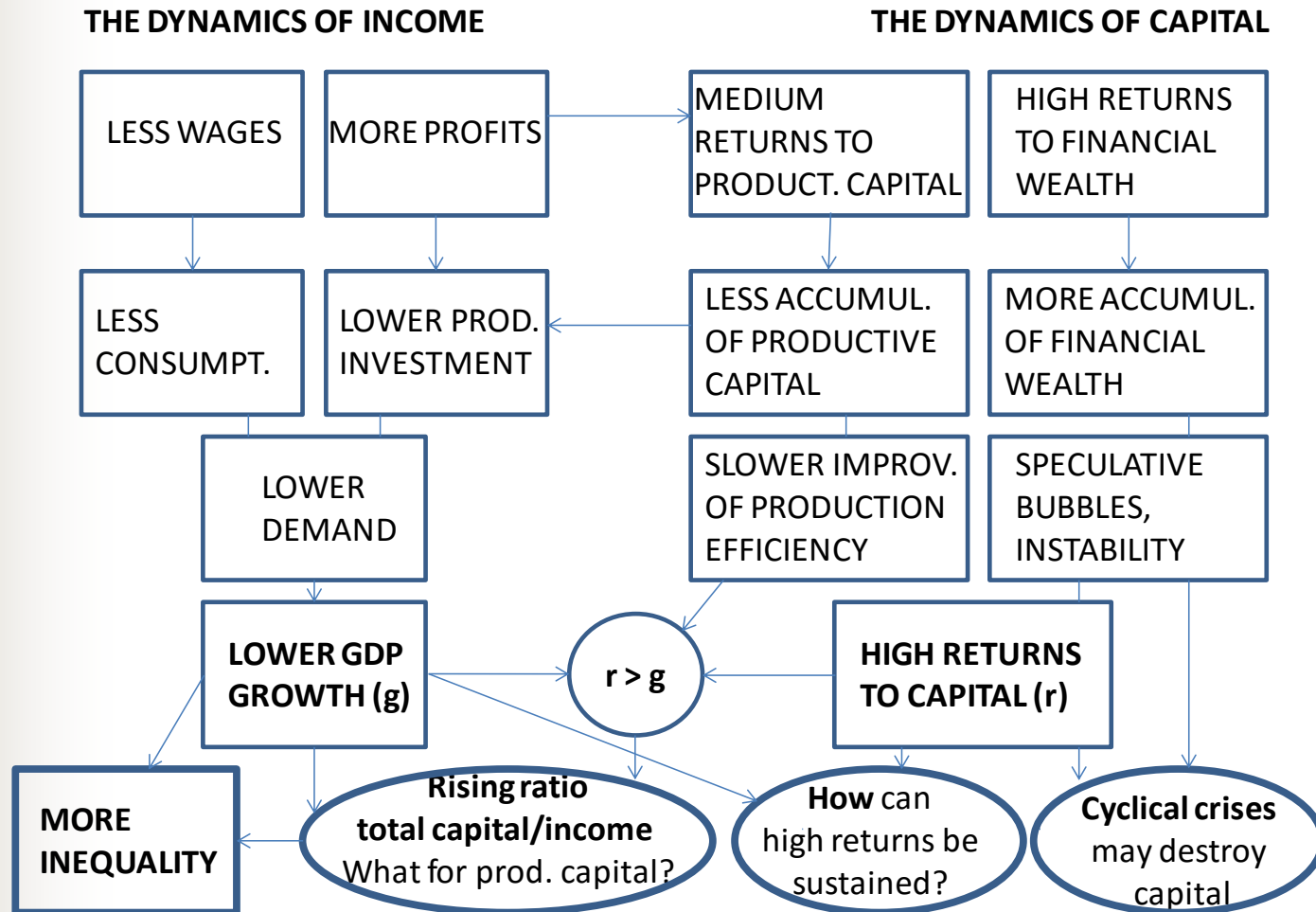
Four engines of inequality

- **The power of capital over labour**
- **Oligarchs capitalism**
- **Individualisation of economic conditions**
- **The retreat of politics**

The four engines of inequality and their impact on income distribution



The dynamics of income and the dynamics of productive and financial capital





1. The power of capital over labour

10-15% of GDP moved from labour to capital

- The power of finance
- Control over labour
- Technological change
- International production



Power of finance

- By 1990 liberalisation of capital movements, surge of capital flows for FDI, financial assets, etc.
- US: ratio of profits of the financial sector to profits of non-financial activities has increased from 20% in the 1970s to 50% after 2000 (Glyn, 2006, ch.3).
- Complex markets for credit, stocks, bonds, real estate, currencies, futures, commodities, derivatives, driven by short-term speculative gains
- Major bubbles, collapse of 2008, instability
- Benefits go to top 1-10%



Piketty on finance

- Financial assets grow much faster than wealth.
- Sum of financial assets and liabilities was equal to 4-5 years of income in the 1970s; in 2010 is between 10 and 15 years in the US, France, Germany and Japan, 20 years in the UK (p.305).
- Ratio between market value and book value of corporations: end of 1970s was 30-50%; in 2010 is close to 120% in the UK, 100% in the US, 80% in France (Germany, Japan 50%) (p.297).



Control over labour

- 2012 OECD Employment Outlook: lower labour share is the result of labour-displacing techn. change, rise of competition, delocalisation and imports, reduction of public ownership. These “*could be partly explained by their effect on workers bargaining power*”(p.111).
- Reduced coverage of collective bargaining systems, lower role and membership of trade unions; All this “*probably explains part of the deterioration of low-skilled workers’ position*” (ibid.).



Wage disparities

- Stronger unions lead to lower inequalities within wages and in the economy as a whole
- OECD “**In it together**” (2015): weaker labour market institutions lead to rise in wage inequality “*declining union coverage has a disequalising effect on the wage distribution*” “*high union density and bargaining coverage, and the centralisation/co-ordination of wage bargaining tend to go hand in hand with lower overall wage inequality*”(p. 42)



Non standard jobs

- OECD: Rise of non-standard jobs that “*can also be associated with precariousness and poorer labour conditions*”, they pay less and lack “*empl. protection, safeguards and fringe benefits*”. “*Earning gaps are especially wide among low-skill, low-paid workers: non-standard workers in the bottom 40% of earners typically suffer wage penalties of 20%*”
- More insecurity risk of job loss, strain



“Labour flexibility benefits the rich”

- IMF study (Dabla-Norris et al., 2015) shows that a decline in organised labour institutions is associated to higher inequality (Gini) *“likely reflecting the fact that labor market flexibility benefits the rich and reduces the bargaining power of lower-income workers”*. *“More lax hiring and firing regulations, lower minimum wages relative to the median wage, and less prevalent collective bargaining and trade unions are associated to higher market inequality”* (p.26).



Technological change

- **Skill biased technological change**
- **ICTs**, greater demand for skills, higher wages for educated workers, lower demand for unskilled workers, more wage inequality
- Associated to **trade and offshoring** effects
- Need for more detailed analysis of **technology** (process vs. product), of its **distribution** effects on profits, wages, of **skills** (professional groups, tasks), different mechanisms for diff. skills, etc.



International production

- Richard Freeman (2009): globalisation doubled the labour force available in the world, lowered the capital/labour ratio, greater (relative) scarcity of capital, resulting in higher profits and lower wages. Increasing trade, greater openness lead to greater inequalities within countries.
- Jobs transferred to emerging countries (with low wages, weak unions, regulation, etc.), lower demand for labour, lower wages, more inequality
- Offshoring and profits (Milberg, Winkler, 2013).



2. Oligarchs capitalism

- Today's inequality is due to the rise of top incomes –1% or 5% of the population
- Low income/social mobility: education has little effect on incomes, incomes and education are affected by parents' conditions
- Strong transmission of inequality from one generation to the next
- Strong importance of inheritance in wealth inequality



3. Individualisation of economic conditions

- Unequal condition among workers
- Education and family background
- Dynamics pointed out above on labour changes
- ILO report: “over 6 out of 10 wage and salaried workers worldwide are in either part-time or temporary work. Women are disproportionately represented (ILO, 2015, p.13). This has lasting effects on lifetime incomes and pensions, expanding disparities at the bottom



Individualism rules?

Deep diffusion of individualism in neoliberalism:

- strong individual identity not linked to collective ones, weak social bonds
- behaviour, work, incentives based on individual attitudes, less room for coll. contracts, solidarity
- disparities become more “acceptable”/justified



4. The retreat of politics

- Less public activities
- More markets producing profits and unequal outcomes
- More liberalisation, more finance
- More deregulation, more profits
- Less taxes, expend. and redistribution