INEQUALITY

What Can Be Done?

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Chapter 1 ::

Setting the Scene

This book is concerned with ways of reducing the extent of inequality, and we need to be clear at the outset exactly what is, and what is not, meant by this goal. Let me begin by removing one possible misconception. I am not seeking to eliminate all differences in economic outcomes. I am not aiming for total equality. Indeed, certain differences in economic rewards may be quite justifiable. Rather, the goal is to *reduce* inequality below its current level, in the belief that the present level of inequality is excessive. I have stated this proposition deliberately in terms of the direction of movement, not of the ultimate destination. Readers may well disagree as to how much inequality is acceptable while agreeing that the present level is intolerable or unsustainable.

In this chapter, I explore the reasons we should be concerned about inequality and its relation with underlying social values. I then take a first look at the empirical evidence. Just how unequal are our societies? By how much has inequality increased? Once we have seen the broad patterns, however, it is necessary to probe more deeply. Just what is being included in the statistics and what is missing? Who is where in the distribution?

Inequality of Opportunity and Inequality of Outcome

On hearing the term "inequality," many people think in terms of achieving "equality of opportunity." This phrase occurs frequently in political speeches, party manifestos, and campaign rhetoric. It is a powerful rallying call with long roots in history. In his classic essay *Equality*, Richard Tawney argued that all people should be "equally enabled to make the best of such powers as they possess." In the recent economics literature, following the work of John Roemer, the determinants of economic outcomes are separated into those due to "circumstances" that are beyond personal control, such as family background, and "effort," for which an individual can be held responsible. Equality of opportunity is achieved when the former variables—circumstances—do not play any role in the resulting outcome. If some people work harder at school, pass their exams, and get into medical school, then at least part (but not necessarily all) of their higher salary as a doctor can be attributed to effort. If, on the other hand, their place at medical school is secured through parental influence (for example, preference being given to the children of alumni), then there is inequality of opportunity.[1]

The concept of equality of opportunity is an attractive one. However, does it mean that inequality of outcome is irrelevant? In my view, the answer to this question is "no." Inequality of outcome is still important, even for those who start from concern for a "level playing field." To see why, we need to start by noting the difference between the two concepts. Inequality of opportunity is essentially an ex ante concept—everyone should have an equal starting point—whereas much redistributional activity is concerned with the ex post outcomes. Those who think inequality of outcome is irrelevant regard concern for ex post outcomes as illegitimate and believe that, once a level playing field for the race of life has been established, we should not enquire into the outcomes. To me this is wrong for three reasons.

First, most people would find it unacceptable to ignore completely what happens after the starting gun is fired. Individuals may exert effort but have bad luck. Suppose that some people trip and fall into poverty. In any humane society help will be provided to them. Moreover, many believe that this help should be offered without enquiring into the reasons the person fell on hard times. As the economists Ravi Kanbur and Adam Wagstaff note, it would be morally repugnant to "condition the doling out of soup on an assessment of whether it was circumstance or effort which led to the outcome of the individual . . . to be in the soup line."[2] The first reason, then, that outcomes matter is that we cannot ignore those for whom the outcome is hardship—even if ex ante equality of opportunity were to exist.

But the significance of outcomes goes much deeper than this, leading to the second reason that inequality of outcome matters. We need to distinguish between competitive and noncompetitive equality of opportunity. The latter ensures that all people have an equal chance to fulfill their *independent* life projects. To pursue the athletic analogy, all can have the opportunity to acquire swimming certificates. In contrast, competitive equality of opportunity means only that we all have an equal chance to take part in a race—a swimming competition—where there are unequal prizes. In this, more typical case, there are ex post unequal rewards, and this is where inequality of outcome enters the picture. It is the existence of a highly unequal distribution of prizes that leads us to attach so much weight to ensuring that the race is a fair one. And the prize structure is largely socially constructed. Our economic and social arrangements determine whether the winner gets a garland or $3 million (the top prize in the U.S. Open Tennis tournament in 2014). The determination of the prize structure is the principal concern of this book.

Finally, the third reason for concern about inequality of outcome is that it directly affects equality of opportunity—for the next generation. Today's ex-post outcomes shape tomorrow's ex ante playing field: the beneficiaries of inequality of outcome today can transmit an unfair advantage to their children tomorrow. Concern about unequal opportunity, and about limited social mobility, has intensified as the distributions of income and wealth have become more unequal. This is because the impact of family background on outcome depends both on the strength of the relationship between background and outcome and on the extent of inequality among family backgrounds. Inequality of outcome among today's generation is the source of the unfair advantage received by the next generation. If we are concerned about equality of opportunity tomorrow, we need to be concerned about inequality of outcome today.

Instrumental and Intrinsic Concerns for Inequality

Reducing inequality of outcome matters, therefore, even to those for whom equality of opportunity is the ultimate objective. It is a means to an end. In the same way, influential books such as *The Price of Inequality* by Joseph Stiglitz and *The Spirit Level* by Kate Pickett and Richard Wilkinson have identified other instrumental reasons we should be concerned about inequality of outcome.[3] They argue that we should reduce inequality of outcome because it has bad consequences for today's society; they blame increased inequality for lack of social cohesion, increased crime, ill-health, teenage pregnancy, obesity, and a whole range of social problems. Political scientists have identified a two-way relationship between income inequality and the role of money in determining the outcome of democratic elections, characterised by the "dance of ideology and unequal riches."[4] Economists have placed worsening economic performance at the door of increased inequality. In her speech to the 2012 Annual Meetings of the IMF and the World Bank, Christine Lagarde spoke of her "third milestone: inequality and the quality of growth in our future world." She went on to say that "recent IMF research tells us that less inequality is associated with greater macroeconomic stability and more sustainable growth." The extent of consequential benefits from reducing inequality can be much debated, and I return to the relation between inequality and economic performance in Chapter 9.

The case for reducing inequality does not, however, depend solely on its having adverse consequences of the kind described above. There are *intrinsic* reasons for believing that the current degree of inequality is excessive. These reasons may be framed in terms of a broader theory of justice. For economists writing on these issues a hundred years ago, it was natural to think in utilitarian terms. Summarising individual well-being in terms of the utility level attributed to each person, they argued that excessive inequality reduced the sum of total utility, since the value of an additional unit of income (or economic resources more generally) was lower for the well-off. As it was put by Hugh Dalton, British economist and postwar Labour Chancellor of the Exchequer, transferring £1 from a rich person to a less well-off person would, other things the same, reduce inequality and raise the sum of utility for society as a whole.[5]

Utilitarianism has been much criticised, not least for being concerned solely with the sum of individual utilities, and being, in the words of Am-artya Sen, "supremely unconcerned with the inter-personal distribution of that sum. This should make it a particularly unsuitable approach to use for measuring or judging inequality."[6] It is for this reason that distribu-tional weights are applied when measuring inequality, with more weigh[t] attached to those who are less well-placed. These distributional weight[s] incorporate our social values regarding redistribution and provide an in-trinsic basis for concern about inequality. Just what these weights shoul[d] be is a matter over which people differ, as may be seen from the "leak[y] bucket experiment" described by the economist Arthur Okun. He asked what would happen if some of Dalton's £1 transfer were to be lost on the way. From the answer given, Okun deduced how much more weight would have to be attached to the income of the recipient, compared with that of the donor, in order to justify the transfer. If half of the transfer leaked out of the bucket, then we would need to give twice the weight to the income of the recipient compared with that of the donor. People giving greater weight to poorer recipients would favour more redistribution; they would go further towards reducing inequality. In the limit, all the weight would be given to the least well-off, a position often associated with *A Theory of Justice* by John Rawls, although there is much more to his theory than is captured by this limiting case.[7]

The "Rawlsian" position of favouring the least advantaged may sound quite radical. However, it is not far removed from the statements of politicians who argue for income tax cuts on the basis that these would stimulate economic activity and hence increase revenue that could be used to raise the incomes of the poorest among us. As this argument illustrates, there is nothing intrinsically egalitarian about the Rawlsian objective. Maximising the well-being of the least advantaged may lead to a quite unequal distribution. More radical in this sense than Rawls was Plato, who expressed the view that no one should be more than four times richer than the poorest member of the society.[8] On this egalitarian view, inequality matters on account of the distance between rich and poor, and there may be a case for action even where there is no gain to the poorest.

A Theory of Justice by Rawls initiated a wide debate among moral philosophers about the nature of social justice. Of particular relevance here is Rawls's framing of the principles of justice in terms of access to "primary goods": "things which it is supposed a rational man wants whatever else he wants," listed in broad categories as "rights and opportunities and powers, income and wealth."[9] As Sen has argued, this takes us well beyond utilitarianism but stops short of considering the "wide variations [people] have in being able to *convert* primary goods into good living."[10] Sen has proposed that we should move on from primary goods to "capabilities," defining social justice in terms of the opportunities open to people according to their functioning. The capability approach differs from Rawls's approach in two respects. It focuses on what goods can do for people in their particular circumstances, taking into consideration, for example, that people with disabilities may have higher travel-to-work costs than able-bodied people. It is concerned not just with the achieved outcomes, but also with the range of opportunities, which Sen regards as an essential element of personal freedom (hence the title of Sen's book, *Development as Freedom*).[11] In practical terms, the capability approach has broadened the dimensions of social and economic performance under examination, notably influencing the Human Development Index launched twenty-five years ago by Mahbub ul Haq (the index ranks countries according to their level of development, looking at education and life expectancy, as well as income).[12] In the present context, the capability approach brings us back to instrumental reasons for concern about the inequality of economic resources, but now within a coherent set of principles of justice.[13] Within such a framework, income is only one dimension, and differences in income should be interpreted in the light of differing circumstances and of the underlying opportunities. But it remains the case that achieved economic resources are a major source of injustice. That is my reason for concentrating here on the economic dimension of inequality.

But what do economists have to say about inequality?

Economists and Income Inequality

Some two decades ago, I gave my presidential address to the Royal Economic Society titled "Bringing Income Distribution in from the Cold."[14] The title was chosen to underscore the way the subject of income inequality had become marginalised in economics. For much of the twentieth century the topic had been ignored, whereas I believed that it should be central to the study of economics. I started that address by quoting the same concern expressed earlier in the century by Dalton, who said that as a student he had been especially interested in the distribution of income: "I gradually noticed, however, that most 'theories of distribution' were almost wholly concerned with distribution as between 'factors of production.'" He went on to say that "distribution as between persons, a problem of more direct and obvious interest, was either left out of textbooks altogether, or treated so briefly, as to suggest that it raised no question, which could not be answered either by generalizations about the factors of production, or by plodding statistical investigations, which professors of economic theory were content to leave to lesser men."[15] The same remained true when I reviewed the economics literature in the 1990s. In his account of the history of economic thought on income distribution, Agnar Sandmo observes that "the connection between resource allocation and the distribution of income was not given much attention in modern general equilibrium theory; in the influential presentation of the theory by Gerard Debreu [Nobel Prize–winning economist], the term 'distribution' does not even appear in the index." Later he notes that economic theory has begun "to catch up on its neglect of the determination of income distribution. But this neglect is still visible in the allocation of space in introductory textbooks and books on microeconomic theory."[16] A glance at today's best-selling textbooks shows that the structure has remained much the same as in the past, with discussion of inequality kept separate from the central chapters on production and the macroeconomy. For example, the *Principles of Microeconomics* by Harvard professor Greg Mankiw has an excellent chapter titled "Income Inequality and Poverty," but it is separate from the earlier chapters (and from the companion *Principles of Macroeconomics*). Perhaps more telling is the fact that, when it comes to compressing the book into the *Essentials of Economics*, the inequality chapter does not make the cut, the criterion for which is, to quote the author, "to emphasize the material that students should and do find interesting about the study of the economy."[17] Apparently, inequality does not qualify.[18]

The implication is that distributional issues are not of central interest to economists. Indeed some economists hold the view that the economics profession should not concern itself at all with inequality. This has been expressed forcefully by the Nobel Prize–winner Robert Lucas of the University of Chicago: "Of the tendencies that are harmful to sound economics, the most seductive, and in my opinion the most poisonous, is to focus on questions of distribution. . . . The potential for improving the lives of poor people by finding different ways of distributing current production is nothing compared to the apparently limitless potential of increasing production."[19]

Lucas is right to emphasise the great contribution of economic growth to improving the lives of many poor people all around the world. If cast in sustainable form (an important "if"), then future growth offers the prospect both of reducing international inequality and of helping the least advantaged within countries. But I disagree with him in two respects. First, distribution and redistribution of the current total of income *do* matter to individuals. The extent of differences has a profound effect on the nature of our societies. It does matter that some people can buy tickets for space travel when others are queuing for food banks. A society in which no one could afford to travel privately into space, and in which everyone could afford to buy their food from ordinary shops, would be more cohesive and have a greater sense of shared interests. Second, total production is influenced by distribution. Understanding the distribution of income is necessary to understanding the working of the economy. As we have learned from the recent economic crisis, it is not enough to look simply at macroeconomic aggregates. Economic differences among people are of first-order importance. As the Nobel Prize–winner Robert Solow of the Massachusetts Institute of Technology (MIT) says in his critique of the models that have dominated modern macroeconomics: "heterogeneity is the essence of a modern economy. In real life we worry about the relations between managers and shareowners, between banks and their borrowers, between workers and employers, between venture capitalists and entrepreneurs, you name it. . . . We know for a fact that heterogeneous agents have different and sometimes conflicting goals, different information, different capacities to process it, different expectations, different beliefs about how the economy works. [The] models exclude all this landscape."[20] Questions of distribution and differences in outcomes for individuals are not the sole part of economics—to suggest that would be unwarranted—but they *are* an essential part.

Distributional issues are central to this book, and I seek to show how they relate to our understanding of how the economy works. But first we need to consider the results of the "plodding statistical investigations" in which I and my colleagues have been engaged. Just how unequal are our societies? How much has inequality risen in recent decades?

A First Look at the Evidence

The broad picture with regard to economic inequality in the UK and the US over the past 100 years is summarised in Figures 1.1 (US) and 1.2 (UK).

I start with the evolution over time of overall inequality in the distribution of household incomes. The definition of household income is described in more detail in the next section; for the present it can be thought of, in the US case, as the number a person would enter on their income tax return. Inequality is measured by the Gini coefficient, which is a single-number summary index of inequality ranging from 0 to 100 per cent, popularised by the Italian statistician Corrado Gini.[21] Implicit in using such an index are distributional weights, as discussed above, but these may not be evident to the countless researchers who use the Gini coefficient. In fact, by employing the Gini coefficient, they are implicitly weighting an extra £1 to a person a quarter of the way up from the bottom at three times the weight of an extra £1 given to a person a quarter of the way down from the top.[22] In terms of the leaky bucket experiment, one could lose two-thirds of the transfer and still regard the transfer as worthwhile. I take the Gini index here, since it is widely used and the available statistics are presented in this form, but we need to remember that the index converts a whole distribution to a single number and that there are many different ways in which such a conversion can be made.[23]

The graph for overall inequality in Figure 1.1 provides a long-run perspective, from which we can see that the distribution of income in the US has gone through a sea change. At mid-century, it looked as though incomes were over time becoming more evenly distributed. Herman Miller of the US Census Bureau said in 1966 that "this view is held by prominent economists and is shared by influential writers and editors," quoting the statement by *Fortune* magazine that there had been a distributional revolution "though not a head has been raised aloft on a pikestaff, nor a railway station seized."[24] The Gini coefficient had fallen by some 10 percentage points from its peak in 1929. From the end of the Second World War to the late 1970s, there followed a period of little change in overall inequality, prompting the US economist Henry Aaron to famously joke that following the income distribution statistics in the US "was like watching the grass grow." Then, in the 1980s, the grass shot up. This was the "Inequality Turn" in the US. Between 1977 and 1992, the Gini coefficient rose by some 4.5 percentage points; and since 1992 it has increased by a further 3 points. Overall inequality is not back to the levels reached in the Jazz Age, but it is more than halfway there.

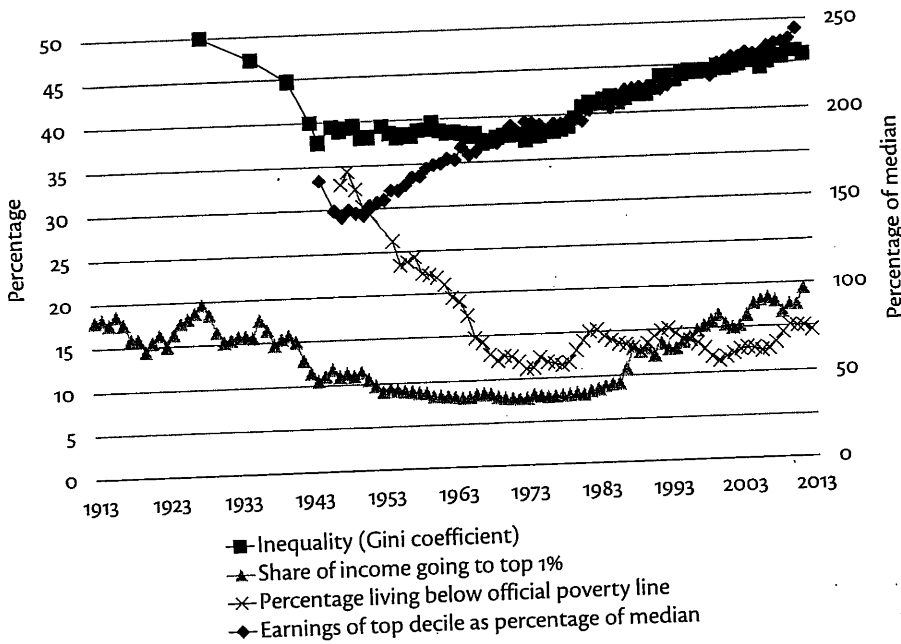


FIGURE 1.1: Inequality in the US, 1913–2013

Overall inequality (squares) is measured by the Gini coefficient, based on household gross income equivalised (adjusted) for household size. The percentage of total gross in-come (excluding capital gains) that goes to the top 1% is shown by triangles. The percent-age of the population living below the official poverty line is represented by X's. Using the scale on the right-hand side, the diamonds show the earnings of the top decile (the per-son 10% from the top) relative to the median (the person in the middle of the earnings distribution) of full-time workers.

At the top of the distribution, the share in total gross income of the top 1 per cent increased by one-half between 1979 and 1992, and by 2012 it was more than double its 1979 share. Even allowing for the effect of changes in income tax (the Tax Reform Act of 1986 led to income shift-ing between the corporate sector and individual tax returns), this is a re-markable increase. For the top shares, we can go back in time before the Second World War to see an overall decline for the first fifty years. The fall initially took place during the First World War, although the decline in the share was recouped by the end of the roaring 1920s, and then again after the Great Crash of 1929 and during the Second World War. Today

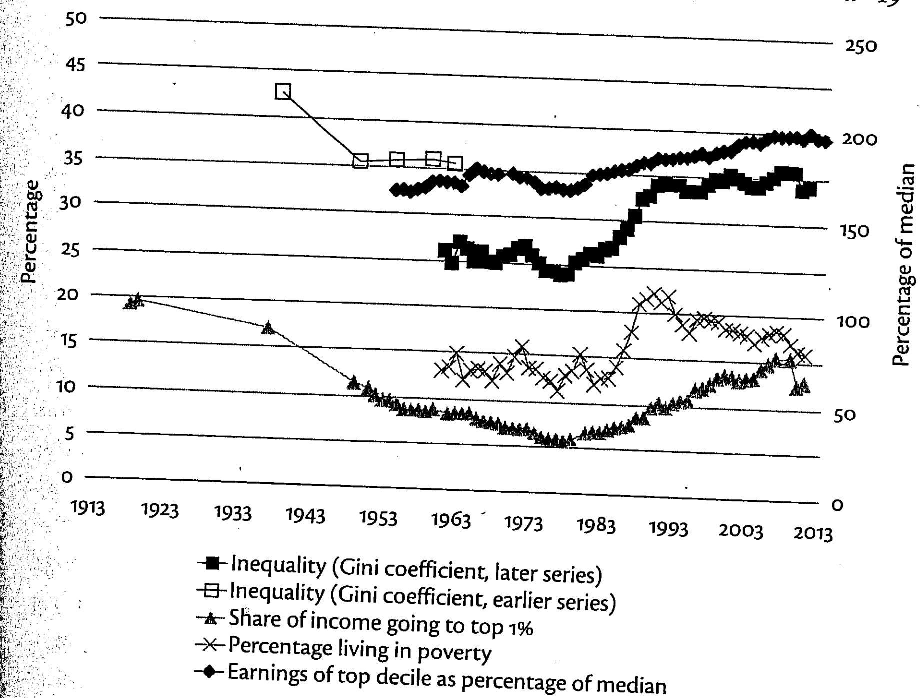


FIGURE 1.2: Inequality in the UK, 1913–2013

Overall inequality, measured by the Gini coefficient, is shown by squares. In the earlier series (open squares), the Gini is based on after-tax income, not adjusted for tax unit size. In the later series (solid squares), Gini coefficients are lower because they are based on disposable household income equivalised (adjusted) for household size. The percentage of total gross income going to the top 1% (triangles) shows an increase between the 1980s and 1990s. This increase may be due in part to a change in the taxation system in 1990, from treating couples as a tax unit to an individual base. The percentage living in poverty (X's) is the percentage of individuals who live in households with equivalised disposable income below 60% of the UK median. Using the scale on the right-hand side, the diamonds show the earnings of the top decile (person 10% from the top) as a percentage of the earnings of the median (the person in the middle of the distribution) of full-time adult workers.

the share of the top 1 per cent has returned to its value of 100 years ago. The top 1 per cent in the US now receives close to one-fifth of total gross income—meaning that, on average, they have twenty times their propor-tionate share. Within the top 1 per cent, too, there is considerable in-equality: the share of the top 1 per cent of those within the top 1 per cent (that is, the top 0.01 per cent) is also around one-fifth of the total income of this group. This means that 1/10,000 of the population receives 1/25 of the total income. The upper tail of the distribution has some resemblance to a Russian matryoshka nested doll: wherever we slice the distribution we find the same inequality being reproduced within the remaining top part.[25]

Trends in the US and the UK Compared

How does the experience of the UK compare with the changes in inequal- ity that have taken place in the US? It is often suggested that the situation in the UK is a pale imitation of what is happening in the US, and that the UK chart can be obtained by simply replacing "S" by "K" in the heading. There is some truth in this. As shown in Figure 1.2, the UK overall in- equality series, which begins in 1938, showed a fall of some 7 percentage points when the series restarted after the Second World War. (In looking at these charts, the reader should focus on the *changes over time*; the lev- els of inequality are not fully comparable across the two countries, as in- come is measured differently in the US and the UK.) Overall inequality then rose in the 1980s. There was a similar post-1979 "Inequality Turn" in the UK. The top shares fell up to the late 1970s and then started rising. The share of the top 1 per cent in gross income was 19 per cent in 1919 and fell to some 6 per cent by 1979; it has since more than doubled. The share of the top 1 per cent in the UK is lower than that in the US, but this group still receives one-eighth of total gross income.

It is not surprising, therefore, that Robert Solow, writing in 1960 abou the distribution of income, drew attention to "the similarity of British and American experience in the twentieth century."[26] But differences have emerged since then. In the 1980s the rise in overall inequality in the UK was much larger than in the US. Between 1979 and 1992, the rise in the Gini coefficient in the UK was some 9 points, twice that in the US. In contrast, after 1992 there was little increase: the coefficient in 2011 was es sentially the same as it had been twenty years earlier. The differing time pattern, as well as the total overall increase, shows that the UK and the US were not following identical paths, and the differences provide us with valuable information about the underlying forces. Studying "diffe

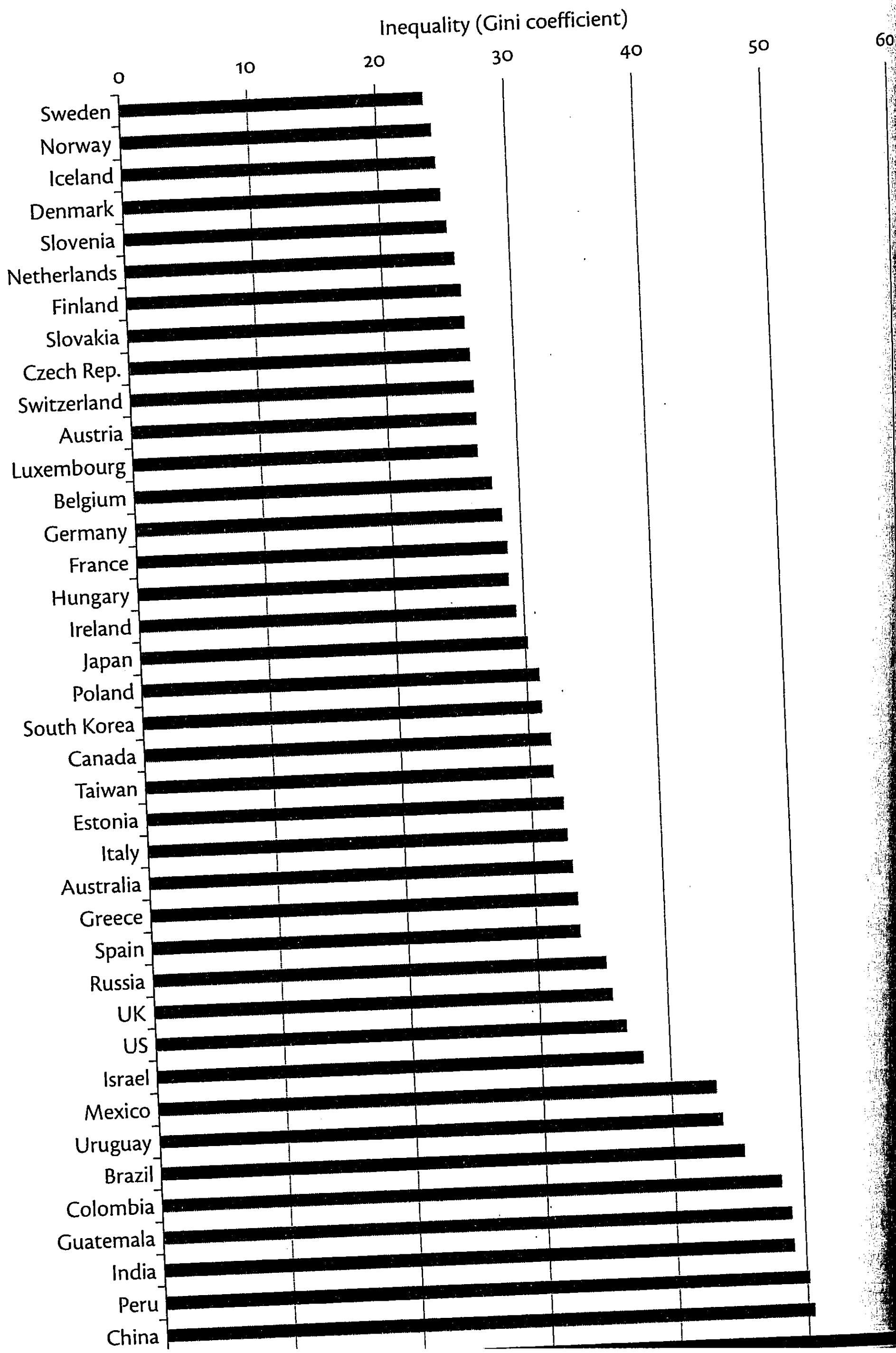
ences in differences"—the *differences* across countries in the *changes over time*—is a valuable source of insight in our search for explanations of ris- ing inequality.

Readers concerned about the UK may draw some consolation from the fact that the last twenty years have seen no increase in overall income inequality as measured by the Gini coefficient. It is the case, however, that the level of inequality remains stubbornly above its level in the 1960s and 1970s. To get back to where we were when the Beatles were playing, we have to reduce the Gini coefficient by some 10 percentage points. What does this mean? To get some idea, suppose that we seek to achieve such a reduction through taxes and transfers alone. Based on reasonable as- sumptions about tax rates and government spending, the tax rate increase required to reduce the Gini coefficient for disposable income from 35 to 25 per cent would be 16 percentage points of income.[27] The magnitude of the required increase in the tax rate points to the fact that reduced in- equality cannot be achieved solely through fiscal measures, a conclusion that is reinforced once we take account of the likely impact of such a tax hike on incentives. This is why many of the policy measures proposed in this book are directed at making the distribution of market incomes less unequal. It is also why a radical policy to reduce inequality has to engage the whole of government. But for the moment, we can see that we are fac- ing a major challenge.

Inequality around the World

The extent of the challenge becomes clear when we compare income in- equality across a range of countries. Figure 1.3 shows the Gini coefficient for equivalised disposable household income for countries ranging al- phabetically from Australia to Uruguay and in terms of their overall income per head from India to the United States. Making such com- parisons is not easy, and in the next chapter the sources of the data are discussed in greater detail.

In China and India, the Gini coefficient shown in Figure 1.3 is close to 50 per cent, or around double the values found in the Nordic countries at the top of the graph. (In South Africa, it is close to 60 per cent.) The coefficient is also high—above 40 per cent—in the Latin



American countries shown, such as Brazil and Mexico. Next (after Israel) comes the US and then the UK. (The value shown for the US is lower than that in Figure 1.1 since the latter measured income before deduction of taxes.) These Anglo-Saxon countries have much higher overall income inequality than Continental Europe and still higher than the Nordic countries.[28]

The cross-country comparison shows what is implied by the challenge of reversing the rise in income inequality that has taken place since the 1970s. For the UK, the challenge of reducing the Gini coefficient by 10 percentage points means making the UK like the Netherlands. For the US, a reduction in the Gini of 7.5 percentage points would mean making the US like France. For other countries in the Organisation for Economic Co-operation and Development (OECD), the distance is smaller. In Australia, the Gini coefficient has risen since 1980 by 4 percentage points, and France would again be the target.

Should We Just Focus on Poverty?

So far, I have discussed the evidence about income inequality. Martin Feldstein, the Harvard economist who has pioneered research on the economics of social security, argues strongly that "the emphasis should be on eliminating poverty and not on the overall distribution of income or the general extent of inequality," and this is a widely held view.[29] I share this concern with what is happening at the bottom of the income scale. It was the rediscovery of poverty in Britain in the 1960s—specifically, the publication on Christmas Eve 1965 of *The Poor and the Poorest* by Brian Abel-Smith and Peter Townsend—that led to my research on poverty and my first book, *Poverty in Britain and the Reform of Social Security.*[30] Fifty years later, the fight against poverty is now firmly on the political agenda, with national governments setting explicit goals. Following the 1995 United Nations (UN) Social Summit in Copenhagen, the Irish govern-

FIGURE 1.3: Inequality in selected world countries, 2010

Inequality is measured by Gini coefficients based on equivalised household disposable income (income after taxes and transfers). The coefficient in Sweden is 23.7%, which may be compared with 59.4% in South Africa.

ment set a national poverty-reduction target as part of its 1997 National Anti-Poverty Strategy. In 1999 under Tony Blair the UK government adopted an official target for the abolition of child poverty, with the aim of eradicating child poverty by 2020; Blair's successor, Gordon Brown, enshrined this ambition in law in the Child Poverty Act 2010. The European Union (EU) in its Europe 2020 Agenda set the goal of reducing by at least 20 million the number of people who are either at-risk-of-poverty, severely materially deprived, or living in "jobless households" (the current EU total population is approximately 500 million).[31]

Despite these good intentions, progress towards reducing poverty in rich countries has been slow. The evolution of poverty over time in the US and the UK is shown in Figures 1.1 and 1.2. In the US, the poverty threshold has been held constant in terms of purchasing power, contrasting in this respect with the threshold in the UK and the EU.[32] It is not therefore surprising that the official poverty rate in the US fell from 33 per cent in 1948 to 19 per cent at the time President Lyndon Johnson launched the War on Poverty in 1964. Poverty continued to fall until the late 1960s, but since then there has been little overall improvement in the poverty rate, and the absolute number has increased as the population has grown: today some 45 million Americans live below the official poverty line.

In the UK (Figure 1.2) the poverty rate, measured according to a threshold expressed as a proportion of median income, was reduced from 22 per cent to 16 per cent between 1992 and 2011. This decline, which began under the Conservative government of John Major, is a substantial one. It demonstrates that poverty can be reduced. Does this then justify the "focus on poverty" strategy? The decline in poverty in the UK was accompanied by a marked rise in top income shares. The New Labour government was "intensely relaxed" (a contradiction in terms?) about people getting rich. However, the fall achieved in the past twenty years—for which credit must be given—still leaves the current UK poverty rate above the level of the 1960s and 1970s, a level that was regarded at the time as profoundly shocking. The Child Poverty Action Group was founded in 1965 when the poverty rate was 3 per cent lower than it is today.

In the EU, the at-risk-of-poverty rate has risen in recent years.[33] The

Social Protection Committee reported in 2014 that "the latest figures on living and income conditions in the EU show that the EU is not making any progress towards achieving its Europe 2020 poverty and social exclusion target." Quite the reverse: "There are 6.7 million more people living in poverty or social exclusion since 2008, a total of 124.2 million people for the EU28 or close to 1 in 4 Europeans in 2012. Poverty and social exclusion has increased in more than 1/3 of the Member States in both 2011 and 2012."[34]

There is still a long way to go. In my judgement, the eradication of poverty in rich countries requires us to think more ambitiously, beyond the strategies employed to date. We have to view our societies as a whole and to recognise that there are important interconnections: economics tends to assume away or downplay any interdependency between the economic fortunes of individuals (or households), but John Donne was right when he wrote that "no man is an Iland, intire of it selfe." What happens at the top of the distribution affects those at the bottom. As Tawney wrote a century ago, "what thoughtful rich people call the problem of poverty, thoughtful poor people call with equal justice a problem of riches."[35]

Put more pragmatically, we can ask whether countries can achieve low rates of poverty at the same time as having high top income shares. To examine whether this is the case, I have assembled in Figure 1.4 the evidence for fifteen OECD countries. The lines in the graph divide the countries into groups according to whether they are above or below the median country. Eleven of the fifteen countries are found in the top right-hand or the bottom left-hand boxes. Only Switzerland appears to have achieved below-median poverty while having above-median top income shares. Higher poverty tends to go together with larger top shares.

Rising Earnings Dispersion

The title of this section refers to "dispersion" to underline the obvious—but often overlooked—fact that not all differences in economic outcome represent unjustified *inequality*. Some people are paid more than others for perfectly justifiable reasons, such as working longer hours or doing unpleasant jobs or taking on more responsibility. Among the most im-

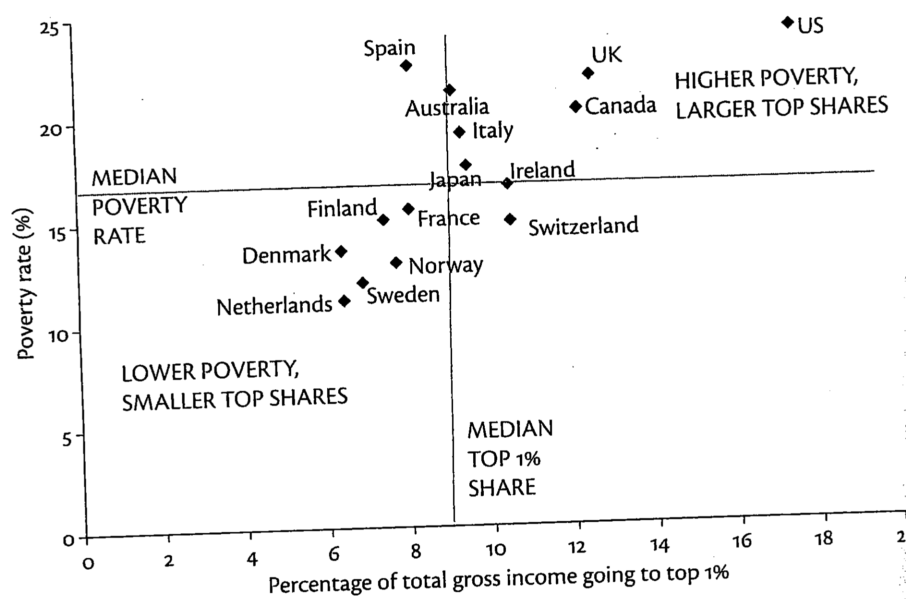


FIGURE 1.4: Poverty and top income shares in selected countries, c. 2010

In the US in 2010 the relative poverty rate (percentage living on incomes below 60 per cent of the median) was 24.7%, and the share of total gross income going to the top 1% (excluding capital gains) was 17.5%.

portant justifications for differences in earnings is that some people have invested in training for occupations that require more skill. Such a "human capital" explanation of pay differences is of ancient vintage. In *The Wealth of Nations*, Adam Smith stated this clearly: "A man educated at the expense of much labour or time . . . must be expected to earn over and above the usual wages . . . the whole expenses of his education, with at least the ordinary profits of an equally valuable capital." This simple statement of what underlies the college-wage premium explains both why differences do not necessarily imply inequality *and* why it is not necessarily the case that all of the observed difference can be explained in this way. It is quite possible that the investment in human capital by a higher-educated worker earns more (or less) than the ordinary profit on capital. A pioneering study by Nobel Prize–winners Milton Friedman and Simon Kuznets of professional earnings in the 1930s in the US con

cluded that "the actual difference between the incomes of professional and non-professional workers seems decidedly larger than the difference that would compensate for the extra capital investment required." To this extent, the difference *did* constitute inequality.[36]

The long-run evolution of the earnings distribution in the US and the UK is depicted in Figures 1.1 and 1.2 (earnings at top decile). The graphs are best understood by imagining all those with earnings being lined up in a parade in order of how much they earn. The statistician then divides them into tenths and asks the person at the start of each tenth to step forward. The person at the start of the sixth tenth is the *median*—the person in the middle—and the person at the start of the top tenth is the *top decile*. What the graphs show for each year is the ratio of the earnings of the top decile to the earnings of the median. So in the US in 1952 the top decile earned some 150 per cent of the median. This graph extends further back in time than is commonly the case in studies of wage dispersion, which tend to focus on what has happened since the 1970s. It is, however, important to set the experience of recent decades in historical context. We can see that, in the US, the rise in top earnings began long before 1970. Between 1952 and 1972, the relative advantage of the top decile rose from 150 per cent to 194 per cent of the median, a rise as large as that which took place between 1972 and 2012. The experience of the UK was different. In the 1950s and early 1960s, earnings dispersion was widening, but from the mid-1960s to 1979 the top decile fell relative to the median. How this was brought about is discussed further in the next chapter. Not only is the time-path different, but also the overall increase is smaller in the UK than in the US—in contrast to what we have seen to be the case for overall income inequality. In the UK, earnings dispersion increased less, but overall income inequality more, than in the US.

We are therefore telling a more nuanced story than simply "rising inequality." As summarised in Table 1.1, there are differences between periods, between countries, and between individual earnings and household incomes. These differences help us understand the determinants of inequality. We can learn from the episodes circled in Table 1. How did the US maintain a broadly stable level of household income inequality in the 1950s and 1960s, despite widening earnings dispersion? How did the UK reduce earnings dispersion from 1965 to 1979? Why did income inequal-

TABLE 1.1. *A brief postwar history of inequality in the UK and the US*

	1950 to mid-1960s	Mid-1960s to end of 1970s	1980s	1990 to today
Individual earnings dispersion	Rise in UK Rise in US	Fall in UK Rise in US	Rise in UK Rise in US	Rise in UK Rise in US
Household income inequality	Stable in US Stable in UK	Stable in US Fall in UK	Rise in US Large rise in UK	Rise in US Stable in UK

ity rise much more sharply in the UK in the 1980s? These questions, together with the experiences of other OECD countries, are taken up in the next chapter.

The Dimensions of Inequality

We have taken a first look at the evidence about inequality; before going further we need to take a step back and clarify the concepts underlying the statistics. There are many dimensions to inequality, and some important ones have so far been missing. Indeed, even within the field covered, the reader may well have been wondering just what is or is not included. Graphs such as Figures 1.1 and 1.2 lead one to ask, inequality of what among whom?

Inequality among Whom?

So far I have talked about households and, when discussing earnings, about individuals. But there are other possible units of analysis. Within the household there may be distinct families, and within the family there may be distinct generations. Which of these should be used? The answer depends in part on the extent to which members of the household share equally in its resources. If there is full sharing, then the calculations described above, based on total household income, would be appropriate. Where sharing is incomplete, we can make a case for considering the different spending units, or nuclear families, that constitute the household. On a family basis, we would treat separately grown-up children still living at home, and elderly parents living with their children would constilearn about the distribution of income, earnings, and wealth. If you appear in the statistics that follow, it may be because you have taken part in a household survey; it may be because your employer made a return as part of a survey; your income tax records or your social security tax records may have been an input into the estimates; or you may appear in the Rich List! The important point to take away from this account of the sources underlying the evidence is that all data are imperfect, and that we have to make the best use we can of these flawed materials. I like the image of economic data described by the Harvard economist Zvi Griliches: "The available economic statistics are our main window on economic behavior. In spite of the scratches and persistent fogging, we cannot stop peering through it and trying to understand what is happening."[14]

When Has Inequality Fallen in the Past?

In this chapter, I am seeking lessons from periods when there has been a salient reduction in inequality. What do I mean by this? What constitutes a "salient" change in inequality? We know that the summary measures of inequality, such as the Gini coefficient, vary from year to year. How much does the figure have to fall for us to say that there has been a salient reduction? The standard answer people give to this question is in terms of the sampling error, or the variation that can be expected from collecting information on only a sample as opposed to the whole population. Statistics Canada, for example, suggests that, with a sample of some 35,000 households, a change in the Gini coefficient of 1 percentage point or more can be considered statistically significant.[15] It is, however, the policy salience that concerns me here. Making the same kind of calculation as that in the previous chapter, linking changes in the overall tax rate to changes in the Gini coefficient, we can see that a 5 percentage point rise in the tax rate would bring about a fall of 3 percentage points in the Gini coefficient.[16] Since a 5 percentage point rise in the tax rate would be a major step for any minister of finance, a 3 percentage point reduction in the Gini coefficient does not seem unreasonable as a criterion of salience, and it is employed here—although it is, of course, only an indication. Referring back to the country comparisons of Gini coefficients in Figure 1.3, we can see that a 3 percentage point reduction would render the UK less unequal than Australia, and France and Germany less unequal than Finland.

What about the other inequality indicators? For the poverty rate, we may note that the Europe 2020 target for combating poverty and social exclusion over the present decade aims, in round numbers, at a reduction of one-sixth. Applied to the at-risk-of-poverty rate (rather than the extended measure of poverty and social exclusion), this too would imply in rounded terms a reduction of 3 percentage points. For top income shares, there is no obvious metric, and I take the same figure of 3 percentage points. Finally, for the top decile of earnings, expressed as a percentage of the median, I take a 5 per cent change as salient, which would mean that a fall from, say, 200 per cent to 190 per cent of median earnings would register. In each case the change is measured over a period when the indicator was proceeding in a clear direction, but without regard to the length of the period. I am seeking periods of change, not speed of change.

Changing Inequality from 1914 to 1945 and the Role of War

In *Capital in the Twenty-First Century,* Thomas Piketty says of his native France that "it is striking to see the extent to which the compression of income inequality is concentrated in one highly distinctive period: 1914–1945. . . . To a large extent, it was the chaos of war, with its attendant economic and political shocks, that reduced inequality in the twentieth century. There was no gradual, consensual, conflict-free evolution towards greater equality. In the twentieth century, it was war, not harmonious democratic or economic rationality, that erased the past."[17] The evidence about France on which Piketty draws for this period is that on top income shares. There are eight other countries for which we have evidence on top shares for 1914 and 1945, and for all but two (Norway and South Africa) the share of the top 1 per cent in total gross income was by 1945 at least 3 percentage points lower than in 1914.[18] In Japan, the share of the top 1 per cent fell from 18.6 per cent to 7.4 per cent, numbers virtually identical to those for France (where the share fell from 18.3 per cent to 7.5 per cent). What is more, in these two countries the fall between 1914 and 1945 accounted for almost all of the total fall in the twentieth century. A difference begins to emerge, however, between France and Japan, on one side, and the other seven countries for which we have data covering the period. In Denmark, the Netherlands, Norway, South Africa, Sweden, the UK, and the US, there were salient declines in top income shares after 1945. The reduction in inequality was not confined to the period 1914 to 1945.

To understand more clearly the role of the world wars, we need to examine in more detail what happened in the period 1914 to 1945. Beginning with the First World War (1914 to 1918), we can see that top income shares in the UK were lower after the war, reflecting among other things the loss of overseas assets: the share of the top 0.1 per cent fell from 10.7 per cent in 1914 to 8.7 per cent in 1918. But there was no salient reduction in the other combatant countries such as Japan or the US. In France, the share of the top 1 per cent was 18.3 per cent in 1915 and 17.9 per cent in 1920. In noncombatants, such as Denmark and the Netherlands, the top income share actually rose during the First World War. As has been shown in the events to mark the centenary of 1914, the war had profound consequences, but these did not include major redistribution away from rich people. There were indeed calls after the war in the UK and other countries for a capital levy to deal with war profiteering. Sir Josiah Stamp remarked in his lectures *The Financial Aftermath of War* that "there was a great clamour for attacks upon *increase* of capital wealth made during the war" (his italics).[19]

For the interwar period, we have evidence for more countries: for the years from 1920 to 1939, the evidence on top income shares now covers fifteen countries, extending to India and Zimbabwe (then Southern Rhodesia). Of the fifteen, nine, including four Anglo-Saxon countries (Australia, Canada, the UK, and the US) and Denmark, Japan, and Sweden, did not exhibit a salient overall change in top shares between 1920 and 1939. In only four was there a salient decrease over the period as a whole: France, the Netherlands, New Zealand, and South Africa. In his discussion of the French experience, Piketty stresses the complexity of the interwar period and the existence of countermovements superimposed on the overall pattern of change. One was the deflation between 1929 and 1935, the distributional consequences of which were offset by the election of the Front Populaire in 1936, with the subsequent tax changes and the

Matignon Agreements on workers' rights.[20] There were considerable differences across countries in the distributional impact of the Great Depression that started in 1929.[21]

In the Second World War (1939 to 1945)—in contrast to the First World War—inequality fell widely. For all except two of the seventeen countries for which we have top income share data, there was a fall in inequality between 1939 and 1945 (the exceptions were South Africa and Southern Rhodesia). In eight of the seventeen countries, the fall was sufficient to qualify as salient. It was not just in occupied or defeated countries that inequality fell. The time paths are shown for a selection of countries in Figure 2.1. As indicated, the shares of the top 1 per cent fell to a similar extent in all countries shown—with the exception of Switzerland. It is also possible to bring to bear evidence about overall inequality, in the form of the Gini coefficient, shown by the solid lines in Figure 2.1. In the UK, the Gini coefficient after the Second World War was a full 7 percentage points lower than in 1938; in the US the difference between 1936 and 1944 is of a similar order of magnitude.

The Second World War was different in that there was a more general reduction in income inequality. In some cases, this was the product of the "chaos" of war and occupation, or of the structural breaks imposed by the postwar settlement. But even in countries where there was continuity of government major changes took place as a result of new social attitudes and a greater sense of social solidarity. In the UK this had already led during the war to the 1944 Education Act, and, more generally, as Richard Titmuss described in his history of social policy during the war, "by the end of the Second World War the Government had . . . assumed and developed a measure of direct concern for the health and well-being of the population which, by contrast with the role of the Government in the nineteen-thirties, was a little short of remarkable."[22] The year 1945 saw the election of the postwar Labour government, which created the National Health Service and a unified system of National Insurance along the lines proposed by Beveridge. In the US, Claudia Goldin and Robert Margo, who characterise the reduction in wage dispersion as the "Great Compression," highlight the role of labour -market intervention in the form of the National War Labor Board.[23] More generally, Paul Krugman has cited

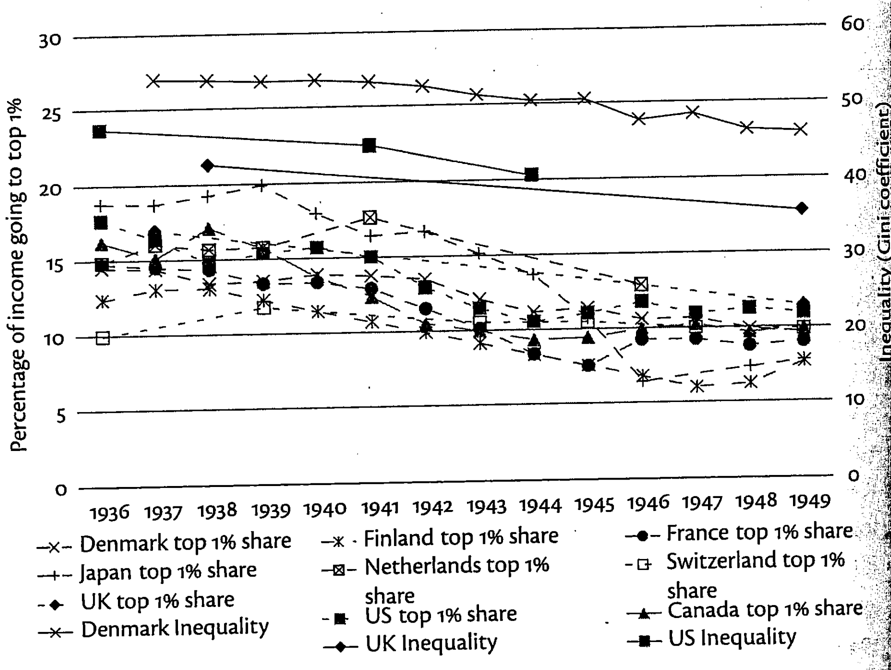


FIGURE 2.1: Inequality and the Second World War, selected world countries

The share of total gross income going to the top 1% (left axis) and overall inequality (as measured by the Gini coefficient; percentage on right axis) fell in most countries during the Second World War.

the other New Deal and Second World War policies of President Roosevelt, and the strengthening of trade unions.[24] But the question then arises, how long did this last?

After the Second World War in the US

What happened next? Quite soon, in the US, the earnings distribution began to widen. As we saw in Chapter 1, the rise in top US earnings can be traced back to 1951. This had nothing to do with globalisation or new computer technologies. The pay distribution began to widen before there was a single commercial computer in operation: the first were delivered in that year (Ferranti Mark 1 in the UK, followed by UNIVAC 1 in the

US). But what is striking is that this widening of the pay distribution was not accompanied by a rise in the inequality of household incomes. It was much later—in the 1980s—that household inequality began to increase. We tend to talk as though wider pay differentials must automatically lead to greater income inequality, but this US experience of the immediate postwar decades tells us that the link can be broken.

How was this achieved? It is useful to go back to the Guide to household income (Figure 1.5). From this, we can see that several different elements intervened to ensure that rising dispersion of individual earnings did not lead to an increase in the Gini coefficient for overall incomes. The first stage is the move from individual earnings to total household earnings. Here, the postwar period saw major developments. The 1980 study by the National Bureau of Economic Research titled *The American Economy in Transition* found that in the labour market "the most important change was the influx of women into the job market, particularly of married women with children." In 1947, one-fifth (22 per cent) of married women (living with their husbands) were in the paid labour force; thirty years later, the figure was close to one-half (47 per cent).[25] The composition of household income was therefore changing. How did this affect inequality? The distribution of the sum of household earnings depends on the degree to which the earnings of husbands and wives are correlated. By the same token, the impact of increased labour-market participation depends on who was entering the labour force. Inequality could be moderated or enhanced. In the immediate postwar period, it appears that increased participation enhanced the earnings of households in the lower part of the distribution. Summarising the postwar US experience, Nan Maxwell writes that "for husband-wife families prior to 1970, equalizing impacts stem from relatively high participation rates of women married to low-earning men." However, after 1970, "increased participation came mainly from women with above-average earnings growth who were married to high-earning men. Hence, continued increased female labor force participation may increase inequality for dual-earning husband-wife families."[26] Lynn Karoly and Gary Burtless have documented how the correlation between male and female earnings was negative in 1959 but by 1989 had become positive. It was then the case that "the growing correlation between husbands' and wives' earnings tends to boost overall income inequality."[27] What had been an equalising force began to work in the opposite direction. This trend has not continued, however. According to Jeff Larrimore, changes in the correlation of the earnings of husbands and wives are no longer operating to increase inequality.[28]

In the immediate postwar period in the US, then, the labour-market changes worked to reduce household income inequality (similar forces were operating in other OECD countries). The next step in the Guide to household income is to add nonlabour income, which consists of three major components: capital income, private transfers, and state transfers. In the case of capital income, there has been much discussion of the trends in wealth distribution in the US, not least on account of the different sources: some data relate to individuals, such as the estate-based estimates, other data relate to tax units (investment-income–based estimates), or to households (survey-based estimates), and still others to wider family units (as in the rich lists). It seems clear, however, that after the Second World War wealth in the US was less unequally distributed than it had been in the 1920s: according to the estate-based estimates, the share of the top 1 per cent in the 1920s was in excess of one-third (36 per cent averaged from 1920 to 1929), whereas in the 1950s it was under one quarter (24 per cent averaged over the 1950s).[29] But there was little apparent further downward trend in the top wealth share over the postwar decades, and to this degree capital income did not contribute to offsetting the rise in earnings dispersion.

What prevented a rise in overall inequality in the immediate postwar decades in the US? Government transfers, which grew rapidly, played a major role. Federal expenditure on payments to individuals doubled as a proportion of national income between 1955 and 1970.[30] The growth of transfers, including the maturing of the New Deal (1935) programme for Old-Age, Survivors, and Disability (the last being added in 1954) Insurance, worked to reduce the inequality of household incomes. Karoly and Burtless refer to the "extraordinary growth in unearned income, primarily government transfers." This increase in transfers, coupled with strong growth of average incomes in the earlier postwar decades, contributed to the impressive reduction in the proportion of the population living below the official poverty line, as shown in Figure 1.1. Karoly and Burtless go on

to say, however, that after 1969 "gains in nonlabor income were tilted in favor of the well-to-do. Capital income and benefits from private pension plans have climbed faster than cash government transfers targeted to the poor."[31] In this case, the change in the course of events was due, not to social or economic change, but to policy choices.

The final step in the journey from individual earnings to household disposable income involves the other side of the government account: taxation. In the postwar decades, the tax rates continued at a high level in the period 1950 to 1979: the top US tax rate on earned income averaged 75 per cent (whereas that for the next thirty years, 1980 to 2009, averaged 39 per cent). The figures for the Gini coefficient in Figure 1.1 relate to income before tax (as do the top share figures), and therefore do not reflect the impact of the high rates of income tax. Their impact was much debated at the time. According to Joseph Schumpeter, through redistributive taxation "the New Deal was able to expropriate the upper income brackets even before the war" and had effected "a tremendous transfer." On the other hand, Irving Kravis summarised his statistical findings by saying that the "increase in the progressivity of the tax structure has played little if any part in making the income distribution more equal [after 1929]." An intermediate position is that taken by Richard Goode in his review of the income tax for the Brookings Institution, which "neither corroborates the opinion that the income tax is a Draconian measure for redistribution nor justifies writing-off its equalizing effects as inconsequential."[32]

In considering the impact of progressive taxation, it is important to bear in mind that the tax base is as important as the tax rates, and that one reason for the limited effectiveness of high rates is that the base had been eroded. As a result, the "effective tax rate" in the US at this time was considerably less progressive than the nominal tax rate.[33] (The nominal rate is the percentage of total income paid in taxes according to the tax schedule; the effective tax rate expresses the taxes actually paid, allowing for reduced rates on certain items of income, as a proportion of an extended definition of income, including tax-exempt income, such as interest on state and local government securities.) Moreover, we should note that the impact can be evaluated only by comparing the disposable incomes with the gross incomes that would have obtained if there had been no income tax in existence. This counterfactual is not easy to establish, since it requires us to predict the changes in behaviour that are induced by the tax. Opponents of high rates of income tax argue that gross incomes would have been larger in the absence of the high top tax rates, since people would have worked longer and harder. This is an issue that I take up later.

The end result of this process was that, while the top decile of earnings in the US rose steadily relative to the median during the immediate postwar decades, this increase in earnings dispersion was not translated into increased overall income inequality, as measured by the Gini coefficient. There was also a salient fall in the share of the top 1 per cent. More unequal rewards in the labour market did not translate into greater inequality of incomes. That this did not happen was due in part to the expansion of social transfers and in part to the increased labour-market participation of women acting in an equalising direction. These forces counteracting the rise in wage dispersion did not apply in the final quarter of the twentieth century.

Lowering Inequality in Postwar Europe

In the US, as we have just seen, overall income inequality as measured by the Gini coefficient was much the same at the end of the 1970s as in the late 1940s; in contrast, a number of European countries saw a major decline in overall inequality in the immediate postwar decades. In this section, I describe this reduction in inequality and how it was achieved. Circumstances at that time were different, but the postwar experience provides valuable lessons for us today.

The Postwar Decades in Europe: Two Questions

In the UK, overall inequality measured by the Gini coefficient fell by some 3 percentage points in the 1970s (from 1972 to 1977), meeting the criterion for salience, but the reductions were more marked, and of longer duration, in other European countries. Figure 2.2 shows the time paths of overall inequality and the top income shares for three countries in Scandinavia. We should focus on the time paths, not the levels, since

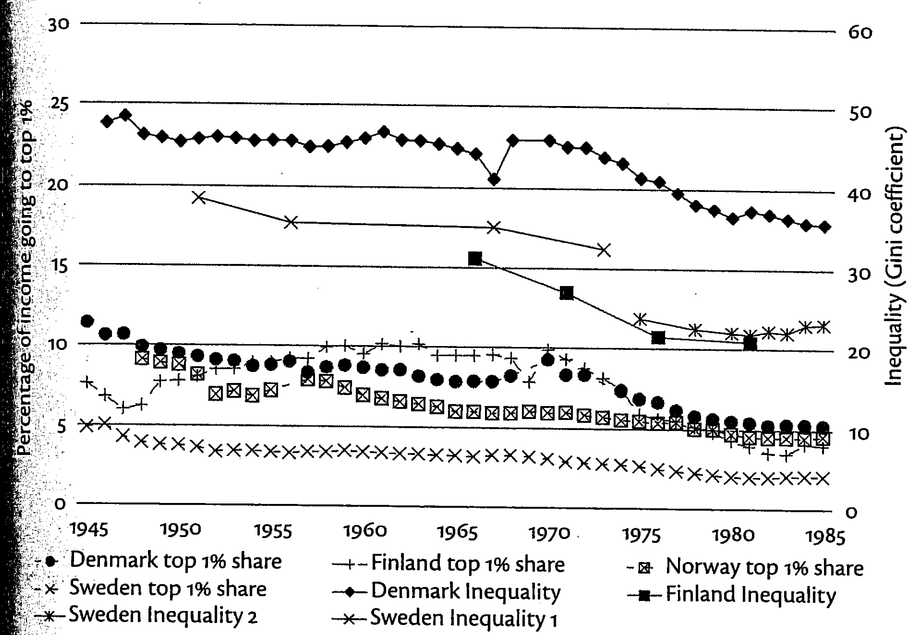


FIGURE 2.2: Inequality in Scandinavia in the post–Second World War decades
Share of gross income going to top 1% (left axis) and inequality (right axis), in post–Second World War period.

the estimates are not necessarily comparable across countries (we cannot conclude that Denmark is more unequal than the other countries). The time paths all show marked reductions from the mid-1960s to the end of the 1980s, typified by Finland, where the Gini coefficient fell from 31 per cent in 1966 to 21 per cent in 1980. In Denmark, the fall was similarly of the order of 10 percentage points. In Sweden, piecing together the two series, the total fall since the 1950s was 8 percentage points. The experience of Continental Europe is illustrated in Figure 2.3. In Germany, the fall was smaller—4 percentage points—and confined to the 1960s. In France and the Netherlands, there was a fall of 8 percentage points in the 1960s and 1970s. In Italy the total fall was 10 percentage points. In the UK, the fall was more limited, but there was a decline of 3 percentage point from 1972 to 1977.

Who was gaining and who was losing? Some countries demonstrated

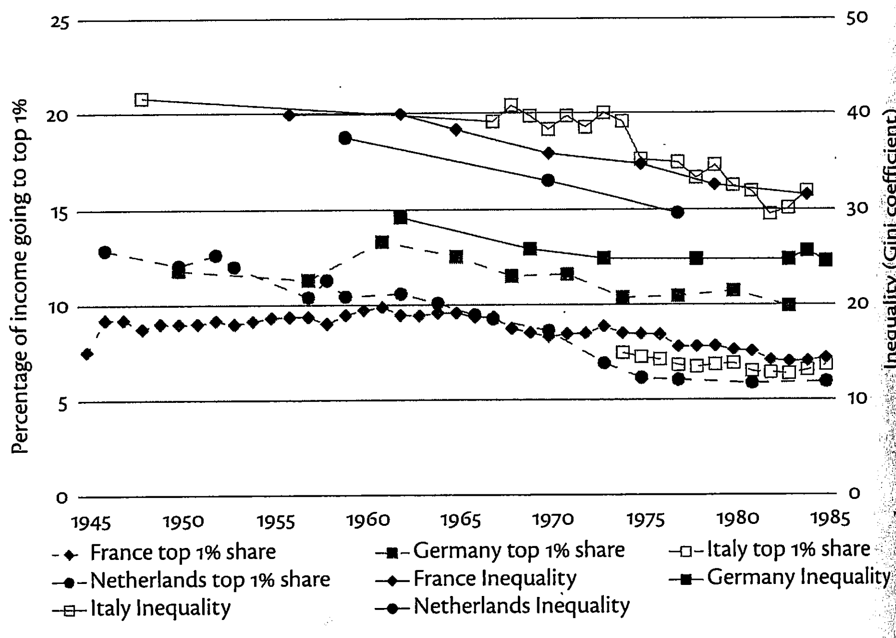


FIGURE 2.3: Inequality in Continental Europe in the post–Second World War decades
Share of gross income going to top 1% (left axis) and inequality (right axis), in post–Second World War period.

an evident improvement in terms of helping those with the lowest incomes. In France, the proportion of the population living in households with incomes below 60 per cent of the median (the current EU indicator of financial poverty) fell from 18 per cent in 1970 to 14 per cent in 1990. In Finland, the proportion fell from 21 per cent in 1971 to 13 per cent in 1985.[34] In Germany and Italy, however, there was little sign of declining poverty, and for a number of other countries the necessary evidence is not available. For top incomes we know more, and the shares of the top 1 per cent are shown in Figures 2.2 and 2.3 (in each case the dashed lines in the lower part of the graph). In the case of Scandinavia, we can see that the top shares fell from being in a range of 7–9 per cent in the early 1950s to closer to 4–5 per cent in the early 1980s. In Norway and Sweden, the fall was relatively gradual, whereas in Denmark and Finland, the fall was

concentrated in the 1970s, in the latter case coming after a rise in the 1950s. In France, the share of the top 1 per cent is described by Piketty as "fairly stable," and the decline does indeed fall just short of the salience criterion: from 9.9 per cent in 1961 to 7.0 per cent in 1983.[35] The fall in Germany is of a similar order of magnitude. In the Netherlands, the fall was larger, the share being halved between the early 1950s and the 1980s. Equally, in the UK the share of the top 1 per cent halved: from 12 per cent in 1949 to 6 per cent at the end of the 1970s.

Thus in the immediate postwar decades income inequality fell in a number of European countries. Two questions follow from this fact. How was the reduction in inequality from 1945 to the 1970s achieved? Why did the process of equalisation end in the 1980s? To provide answers, we can again follow the steps set out in the Guide to household income (Figure 1.5), in this case working in reverse order.

Reducing Inequality: The Welfare State and Progressive Taxation

The first, obvious factor in explaining the fall in inequality in postwar Europe is that this was a period during which the welfare state and social provision expanded, financed at least in part by progressive income taxation. The maturing of state pensions reduced the extent of poverty among older people, and the extension of social transfers to other groups, such as people with disabilities, widened the effectiveness of the social safety net. At the same time, demographic developments, notably the ageing of the population, were increasing the need for social protection. As the size of the dependent population increased, so the distribution of market incomes (earnings, self-employment income, rent, dividends, interest, and private pensions and other private transfers) became more unequal. More people had zero earnings because they had left the labour force. There was, in effect, a race between expanding provision and burgeoning need.

The evidence from household surveys in different European countries suggests that, in this race, the welfare state held its own for a significant period, but then it was unable to keep up. The regular official studies in the UK of the impact of taxes and benefits show a steady rise from 1961 onwards in the inequality of incomes from market sources: the Gini coefficient for market income by the end of the 1970s was some 5 percentage points higher. In contrast, the Gini coefficient for final income, arrived at by adding cash transfers and benefits in kind and subtracting direct and indirect taxes, shows no upward trend from 1961 to the mid-1980s. The "difference," or the arithmetic contribution of taxes and transfers, rose to offset the rise in market inequality; in the 1970s post-tax inequality fell. (This is, again, a purely arithmetic calculation; the market incomes could well have been different in the absence of the state transfers and taxes.) Taxes, and particularly cash transfers, allowed the welfare state to more than hold its own.[36]

So why did it end? After 1984, the UK story is quite different. Inequality in market income continued to rise, but the contribution from taxes and transfers moved in the opposite direction, causing inequality in post-tax income to rise more sharply. Figure 1.2 showed how sharply inequality rose in the UK in the second half of the 1980s. Between 1984 and 1990, the redistributive contribution of taxes and transfers towards reducing the Gini coefficient fell by 8 percentage points. This reflected policy decisions such as the change in up-rating for state pensions, which meant that the basic pension for a single person fell by nearly one-fifth relative to average take-home pay in the second half of the 1980s, and the scaling back of unemployment insurance. Although some of the ground was later made up, it remains the case that the redistributive "difference" is 6 percentage points below the amount that would be required, given the evolution of market income, to return the Gini coefficient for disposable income to its pre-1984 level.

Evidence from West Germany similarly shows that initially the inequality of market income widened substantially but that this development was not accompanied by an equivalent rise in inequality of disposable income. To quote Richard Hauser, "The German tax and transfer system reduces the inequality of market income quite considerably . . . the German social security system, despite the increasingly unfavourable conditions, largely reached its goals from 1973 to 1993."[37] In Finland, the experience was different in that market income inequality fell in the 1960s and the first half of the 1970s, but similar in that the "difference" was rising. As a result, inequality in disposable income fell by twice the amount of the fall in market income Gini coefficient. This trend continued through the 1980s, but in Finland, as in the other countries, there was then a reversal: "During the deepest recession . . . in the 1990s, income inequality did not change, since redistribution of cash transfers compensated the growing inequality of factor incomes. After the recession . . . income inequality has increased, because redistribution of cash transfers has declined, while factor income inequality has continued to grow."[38]

These country case studies illustrate the role played by the welfare state in reducing income inequality and in preventing any rise in market income inequality from feeding into inequality in disposable income. The immediate postwar decades were a success for the European welfare states. But in each case, too, the race was eventually lost, and more generally there has been an unwinding of redistributive policies in OECD countries, with serious adverse distributional consequences. The OECD Secretary-General in his introduction to the 2011 report *Divided We Stand* spelled out that "from the mid-1990s to 2005, the reduced redistributive capacity of tax-benefit systems was sometimes the main source of widening household-income gaps."[39] Michael Förster and István Tóth summarised the position as follows: "The redistributive power of the welfare state was weakened in the period between the mid-1990s to mid-2000s. While in the period between mid-1980s and mid-1990s the share of increased market income inequality offset by taxes and transfers was measured at the level of almost 60%, this share has declined to around 20% by the mid-2000s."[40] The OECD report stresses the role of cash transfers and "the importance of spending levels for inequality outcomes." The key element is less the level of benefits than the proportion of people eligible for transfers. The coverage of unemployment benefits, for example, fell between 1995 and 2005 in Austria, Belgium, the Czech Republic, Denmark, Estonia, Finland, Hungary, Italy, the Netherlands, Poland, Slovakia, Switzerland, Sweden, the UK, and the US. In causing the fall in coverage, "tighter eligibility rules played a role, as did the sizeable increase in the proportion of non-standard workers."[41]

So we have an answer to the two questions posed earlier. In the immediate postwar decades, the welfare state was ahead in the race to keep up with widening inequality of market incomes, but since the 1980s it has failed to do so—often as a result of explicit policy decisions to cut back on benefits and on coverage.

Reducing Inequality and the Share of Wages

The postwar reduction in inequality in Europe was not, however, solely achieved by redistribution. Both wage and capital incomes were—at times—becoming less unequally distributed. Our investigation into how this happened considers the following ways in which these components of income might contribute to reduced inequality:

» the share of wages in total income increases;
» capital income becomes less unequally distributed;
» wage income becomes less unequally distributed

In each case, we need to bear in mind that these three different elements are inter-related and that the effect of a change in one element depends on the others: for example, the impact of a rise in the share of wages depends on how unequally wages are distributed. (There is also a fourth element: the extent to which the same people do well on both wages and capital income. I return to this in the next chapter.)

For many years the share of wages in national income was regarded as one of the core variables in economics. Economists held strong views on the subject, many regarding the share of wages as one of life's constants. One of my teachers at Cambridge, Nicholas Kaldor, observed in 1957 that "the share of wages and the share of profits in the national income has shown a remarkable constancy in 'developed' capitalist economies of the United States and the United Kingdom since the second half of the nineteenth century," and this was later labelled a "stylized fact."[42] In the postwar period, however, there was evidence that the wage share was *increasing*. In his 1969 study of seventeen countries, Klaus Heidensohn found that over the period 1948 to 1963 there had been a "rising trend of labour's relative share in a large number of countries."[43] The labour share rose in Austria, Canada, and Denmark (all by 5 percentage points), in Finland

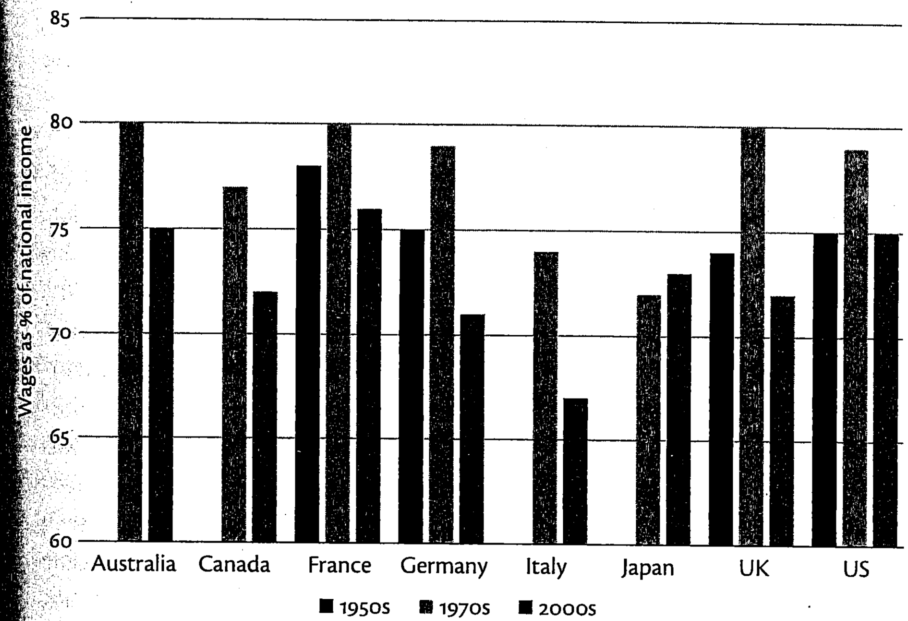


FIGURE 2.4: Share of wages (ten-year averages), selected world countries, 1950s to 2000s
The share of wages in national income was 80% in Australia when averaged over the ten years 1970 to 1979.

and Ireland (both by 6 points), in Belgium and the Netherlands (by 7 points), and by more than 10 percentage points in Norway and Sweden. Figure 2.4 shows the ten-year averages for 1950 and 1970 assembled by Thomas Piketty and Gabriel Zucman. It allows us to compare the average labour shares for 1950–1959 with those of 1970–1979. The increases are smaller, but they show the labour share as rising by 4 percentage points or more in West Germany, the UK, and the US. The Piketty-Zucman data equally show that the rise was subsequently reversed: in all cases apart from Japan there was a fall in the wage share from the 1970s to the 2000s. As summarised by Piketty, "the available data indicate that capital's share of income increased in most rich countries between 1970 and 2010."[44] The rise is not limited to rich countries. Loukas Karabarbounis and Brent Neiman find that, out of fifty-nine countries for which they have adequate data for years between 1975 and 2012, forty-two countries showed a downward trend in the share of labour. Their estimate of the global share of labour in corporate income exhibited a fall over that period of 5 percentage points.[45]

Does a rise (fall) in the wage share mean that the distribution of income becomes less (more) unequal? In the world envisaged by classical economists, the answer was "yes." They assumed that most of the population—the workers—had no income from wealth, and that the rest—the capitalists and landlords—lived off their income from rents, dividends, and profits. When the nineteenth-century English economist (and Member of Parliament) David Ricardo said that "the principal problem in Political Economy" was to determine how "the produce of the earth" was divided among rent, profit, and wages, he envisioned three separate social classes, each with its specific source of income.[46] Today, in contrast, we can make no such clear identification. People may receive income from all three sources. A person may have wages but also receive interest on savings and benefit from owning a house. Indeed, housing has seen dramatic changes. A hundred years ago many people were tenants and houses were typically owned by landlords. In England and Wales in 1918, 77 per cent of households rented their accommodations; by 1981 the proportion had fallen to 42 per cent, and, with the rise of social housing, the proportion renting from private landlords was only 11 per cent.[47]

In a class society, as in Ricardian England, an increase of 1 percentage point in the share of wages would have reduced the Gini coefficient by 1 percentage point.[48] Today, when the links between classes of income and the distribution among persons are less clear-cut, the expected reduction in the Gini coefficient is smaller. Nonetheless, the impact of a change in the wage share may still be substantial. Daniele Checchi and Cecilia García Peñalosa, in a study of sixteen OECD countries over the period 1970 to 1996, estimated that a 1 percentage point rise in the wage share is associated with a 0.7 percentage point reduction in the Gini coefficient.[49] On this basis, a 5 percentage point increase in the labour share would be associated with a salient 3.5 percentage point reduction in the Gini coefficient. One mechanism that reduced inequality in the postwar decades appears, therefore, to have been the rising share of wages in national income, a rise that was subsequently reversed.

Reducing Inequality: Sharing Capital

At the same time, the distribution of capital income was becoming less unequal. Evidence on the personal distribution of wealth (both capital and land) is less readily available on an internationally comparable basis than is the case for income, but Jesper Roine and Daniel Waldenström have assembled a long-run series for the share of the top 1 per cent in ten countries.[50] Their figures show large reductions in top wealth shares. In France, the share of the top 1 per cent in total personal wealth fell between 1950 and 1980 by one-third, from 33 per cent to 22 per cent. In Denmark, the share fell by the same proportion between 1945 and 1975. In Sweden, the fall was even larger: from 38 per cent in 1945 to 17 per cent in 1975, and in the UK the fall between 1950 and 1975 was 17 percentage points.[51]

This decline in top wealth shares has reduced the share of capital income accruing to the top income groups and increased the share received by the bottom 99 per cent. But this has not been a simple transfer. Wealthy people have not simply handed over share certificates. In the UK, one major explanation for the rising share of the bottom 99 per cent has been the rise in owner-occupation. When politicians talk of Britain becoming a "property-owning democracy," they often mean property in the sense of housing. This is, however, a rather special asset, generating a return in the form of imputed income. Other forms of popular wealth, such as savings and bank accounts or pension funds, are held via financial institutions. The latter hold the share certificates. One consequence is that part of the capital income now accrues to the financial-services sector that manages these funds. There is a wedge between the rate of return to capital and the income received by savers. The growth of popular wealth has contributed to the increased "financialization" of the economy. (This in turn has implications for the separation of beneficial ownership and control, to which I will return.)

Has the downward trend in top wealth shares continued or has it been subsequently reversed? The series assembled by Roine and Waldenström show that the share of the top 1 per cent in total personal wealth between the early 1980s and the 2000s rose from 22 per cent to 24.4 per cent in France and increased by 2 percentage points in the UK and by 1.1 per cent in Sweden. These are small changes by the standards of the previous decades, and we need to be cautious in drawing conclusions about any upturn in wealth concentration.[52] Rather, we can conclude that the trend to less wealth concentration came to an end—which is still, of course, a significant departure from what happened in the immediate postwar decades.

Reducing Inequality: Wages and Labour-Market Institutions

Widening of the wage distribution dates back in the US to the 1950s, and the same is true in the UK and in France. The top decile rose in both countries from the mid-1950s to the mid-1960s. This is the period to the left of the first vertical line in Figure 2.5. However, in Europe but not in the US, earnings dispersion began to narrow after the mid-1960s—shown in the middle section of Figure 2.5.

The late 1960s and 1970s were a tumultuous period for European labour markets. After the widespread civil unrest in France in May 1968, earnings differences were narrowed in that country, but the May 1968 effect was not limited to France. According to Christopher Erickson and Andrea Ichino, "during the 1970s, Italy experienced an impressive compression of wage differentials." A major element in this compression was the Scala Mobile (SM), a negotiated agreement between workers and employers to link wages to increases in the cost of living. Writing in 1979, Ignacio Visco, now governor of the Bank of Italy, noted that there was a "marked tendency for the range of earnings to become narrower." The role of collective bargaining was important in the Nordic countries. The data assembled for Sweden by Magnus Gustavsson show the quintile ratio for men as falling from 1968 to 1976. As he notes, the period coincided with the heyday of the "solidarity wage policy" followed by the major trade union confederation, Landsorganisationen (LO). Tor Eriksson and Markus Jäntti found in Finland that "earnings inequality dropped dramatically between 1971 and 1975, and continued to decrease until 1985."[53] In the UK, as Figure 2.5 shows, the top decile fell. At the same time, the bottom decile rose by one-fifth relative to the median between 1968 and 1977, and together these developments narrowed the ratio of the top decile to the bottom decile to an extent that, applying the estimates of the relation of this variable to the Gini coefficient in the study by Checchi

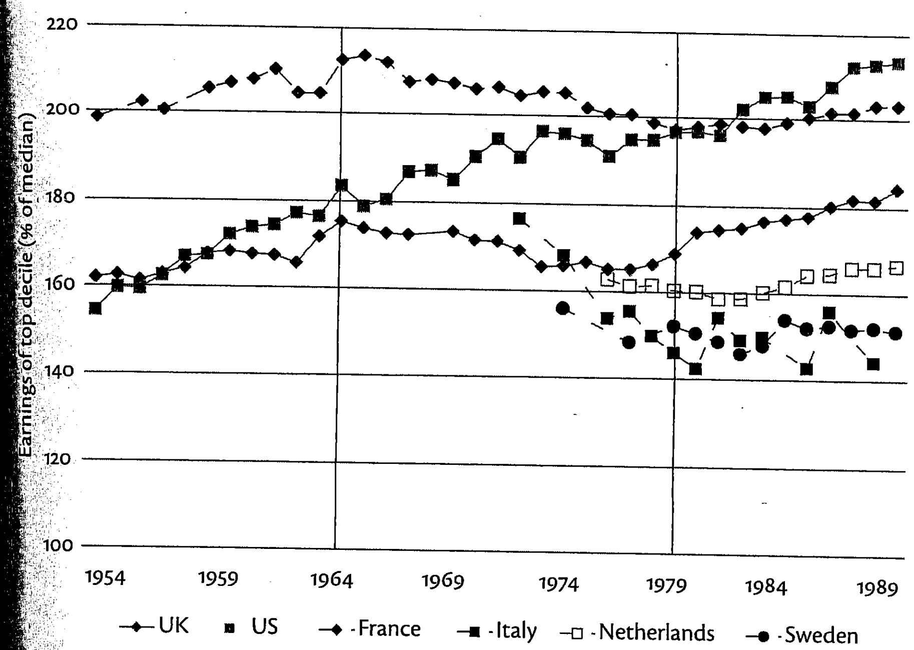


FIGURE 2.5: Earnings dispersion in US and Europe, 1954–1990

This graph shows the earnings of the top decile (the person 10% from the top) relative to the median (the person in the middle) of the earnings distribution for full-time workers.

and Garcia Peñalosa cited earlier, they could account for a fall in the Gini coefficient for overall income inequality of between 4 and 7 percentage points.[54]

An important factor in securing the reduction in earnings dispersion was collective bargaining by trade unions on behalf of their members and government intervention in the labour market. Government influenced the wage distribution via minimum wage legislation (although not in all countries: a national minimum wage was not introduced in the UK until 1999). Piketty says that the change in direction in France was "the result of breaks in the wages policy of the state, and notably in policy towards the minimum wage."[55] In the Netherlands, the minimum wage was raised substantially in 1974, and the government followed a policy of narrowing differentials.[56] To this we must add the contribution made to reducing overall inequality by the reduction in earnings differentials by gender. In a number of countries, equal pay legislation took effect during this period, and we sometimes lose sight of what has been achieved: in the UK, the gender wage gap was more than halved. There was also regulation of wages by collective action. A striking example in the UK is the case of soccer, where until 1961 there was a maximum weekly wage of £20 (which was around average earnings in the country). This is a far cry from today's free market, where footballers in the UK can earn more than 500 times average earnings.

Reduction in earnings dispersion from the mid-1960s to the late 1970s was also the goal of another instrument, now largely forgotten in Anglo-Saxon countries: national incomes policies. These were in origin macroeconomic policies, but negotiations between the social partners (employers and trade unions) meant that they came to have distinct distributional elements. In Norway in 1989, the agreement negotiated between the trade union federation and the employer organisation allowed for a uniform increase of 3 kronor per hour (with a supplement in export industries). In the United Kingdom, the 1973 Stage Two incomes policy under the Conservative government had a progressive formula for pay increases of £1 plus 4 per cent and an absolute limit on individual pay increases. Under Labour's "Attack on Inflation" in 1975, the pay rise allowed under incomes policy legislation was a flat £6 per week, with no increases for those earning above a certain amount. Incomes policy is now typically regarded as an anachronism. The Wikipedia entry introduces a distinctly dramatic historical note: "Incomes policies have often been resorted to during wartime. During the French Revolution, 'The Law of the Maximum' imposed price controls (by penalty of death) in an unsuccessful attempt to curb inflation."[57] But these policies have a contemporary relevance. As discussed in later chapters, I believe that we need to hold a "national conversation" about the development of incomes, as part of a strengthening of the role of social partners.

The Two Questions Answered

The two questions posed at the beginning of this section were: why did inequality fall in Europe in the immediate postwar decades, and why has there been an upward turn in inequality since 1980? There is much more that could be said, but the main factors identified as candidates for explaining the period of falling European income inequality are—as summarised in the middle column of Table 2.1—the welfare state and the expansion of transfers, the rising share of wages, the reduced concentration of personal wealth, and the reduced dispersion of earnings as a result of government intervention and collective bargaining. And the main reason that equalisation came to an end appears to be—see the final column in Table 2.1—that these factors have gone into reverse (welfare-state cutbacks, declining share of wages, and rising earnings dispersion) or come to an end (the redistribution of wealth).

An important factor in answering the second question that we have not discussed—indeed some readers may regard it as the elephant in the room—is the rise in unemployment.[58] The single most obvious feature distinguishing the recent decades from those after the Second World War is the level of unemployment. In the early 1960s, it was the US that had a problem of unemployment. The unemployment rate as a percentage of the total labour force averaged 4.8 per cent over the period 1960 to 1973 in the US, compared with 2.0 per cent in France, 1.9 per cent in the UK, and 0.8 per cent in Germany. Indeed, in many OECD countries unemployment was very low. One prime minister of New Zealand claimed to know personally all the unemployed in his country; this may well have been true, since according to International Labour Organisation (ILO) statistics, in 1955 there were only fifty-five unemployed people in his country.[59] All this was to change. By the period 1990 to 1995, the average unemployment rate in the US was 6.4 per cent, compared with 10.7 per cent in France, 8.6 per cent in the UK, and 7.1 per cent in Germany. The US still had a problem of unemployment—or so it seems to someone who began studying economics when UK unemployment was 1.4 per cent—but it had been joined, and indeed overtaken, by Europe.[60]

How large is the elephant? How much has higher unemployment contributed to higher inequality? The relationship is a complex one. We have to trace through the steps from the market incomes of individuals to the disposable income of households—following the Guide to household income. Moving from the distribution of individual wages to the distribution of market incomes including unemployed workers as well as employed workers has the effect of increasing the degree of inequality, and rising unemployment widens the gap.[61] Adding those who are not in the labour force, so that the entire population of working age is covered,

TABLE 2.1. *Mechanisms leading to change in inequality*

Mechanism	Postwar decades up to end of 1970s	Period since 1980s
Dispersion of wages	Dispersion of wages has at times been reduced, reflecting collective bargaining and government intervention in the labour market.	In many OECD countries there has been a widening at the top of the earnings distribution.
Unemployment and population not in the labour force	Rising proportion not in labour force with ageing population led to rising inequality of market income, offset by social transfers.	Persistent high unemployment.
Share of wages in national income	Tendency for the share of wages to rise, leading to reduction in overall income inequality.	Tendency for the share of wages to fall.
Concentration of capital income (profits and rents)	Substantial decline in top wealth shares, but need to take account of the implications of growth of "popular wealth."	Decline in top wealth shares appears to have come to an end.
Share of transfer income	Redistributive social transfers more than offset rising inequality of market income.	Scaling back of redistributive social transfers.
Impact of progressive direct taxation	Progressive income tax moderated impact of rising top earnings.	Top income tax rates have been substantially cut.

means that the extent of inequality depends on the employment rate, which has been increasing and operating in the opposite direction.[62] The next step is that of aggregating individual incomes to arrive at household incomes, where we have to take account of the joint distribution of unemployment within households. If all unemployed men were married to employed professional women, then we would be less concerned about the income consequences of unemployment. It is for this reason that attention has focused on jobless households. In moving from market incomes to disposable incomes, we have to allow for the response of state transfer payments to unemployment. Where there is full coverage of unemployment insurance, and a generous replacement rate, then the rise in inequality may be less. If, as we shall see to be the case in Chapter 8, social protection is much less complete, unemployment may indeed be associated with financial hardship. Finally, we have to bear in mind that the evidence about inequality largely relates to annual incomes, and that people may be unemployed for only part of the year. To this extent the measured effect is attenuated and the degree of hardship understated.

From this account, it is clear that the relationship between unemployment and inequality is an intricate one, requiring careful examination, and that no simple statement can be made about the quantitative contribution of unemployment to the higher income inequality post-1980.[63] Nonetheless, involuntary unemployment is of concern in its own right, and for this reason alone it receives considerable attention in what follows. Unemployment, and attendant job precariousness, are themselves sources of inequality. A person rejected by the labour market is suffering a form of social exclusion, and even if full income replacement were to allow his or her standard of living to be maintained during unemployment, the individual's circumstances would have worsened. Above all, it is a matter of agency and a sense of powerlessness.[64] Nearly twenty years ago, Amartya Sen ended an article with the statement, "It is amazing that so much unemployment is so easily tolerated in contemporary Europe."[65] It remains amazing today.

Latin America in the Twenty-First Century

The postwar decades in Europe were a period of falling inequality, but this was not a unique episode. We should not lose sight of the fact that there have been other—more recent—periods when inequality has declined. An important example is Latin America in the 2000s. Admittedly, the region's decline in overall inequality and poverty came after a period in the 1980s and 1990s of rising inequality, but its experience shows that a reduction in inequality is attainable.

The remarkable decline in seven Latin American countries is illustrated in Figure 2.6, where the solid lines show the path of the Gini coefficient of overall inequality and the dashed lines show the relative poverty rate, defined as the proportion of the population below 50 per cent of median household equivalised income.[66] Between 2001 (2000 in Chile and Mexico) and 2011 (2010 in Mexico), the Gini coefficient fell by 5 percentage points in Chile, 6 points in Brazil, 7 in Mexico, and 9 points in Argentina. In El Salvador the fall was 6 percentage points between 2004 and 2012. There were major changes and they were not confined to the countries shown. Facundo Alvaredo and Leonardo Gasparini in their study of nineteen Latin American countries find that, whereas only around one-quarter of the countries exhibited a fall in the Gini coefficient in the 1990s, there was a reduction in inequality in almost all of these countries in the 2000s.[67] There was considerable commonality of experience among these countries, although Alvaredo and Gasparini qualify the conclusion by pointing out that incomes at the top of the distribution may not be adequately covered in the household surveys. Andrea Cornia notes, in his analysis of recent distributive changes in Latin America, that "given the scarcity of information on capital incomes and the income of the 'working rich' in household surveys [it is not possible] to establish formally whether the distributive changes . . . concern also the top percentiles of the income distribution."[68] Tax data, an alternative source, although one that is also subject to understatement of top incomes, provide a warning. The estimates of Alvaredo and Gasparini for Argentina show the share of the top 1 per cent in total gross income as rising in the first part of the 2000s and then falling, so that by 2007 it is back close to the 2000 figure. The share of the top 1 per cent in Colombia rose from 17 per cent to 21 per cent between 2000 and 2010.

With the qualification that we have insufficient information about incomes at the top, we see in Latin America an episode of falling inequality that extends over a wide range of countries. In seeking to explain the fall in inequality, Nora Lustig, Luis Lopez-Calva, and Eduardo Ortiz-

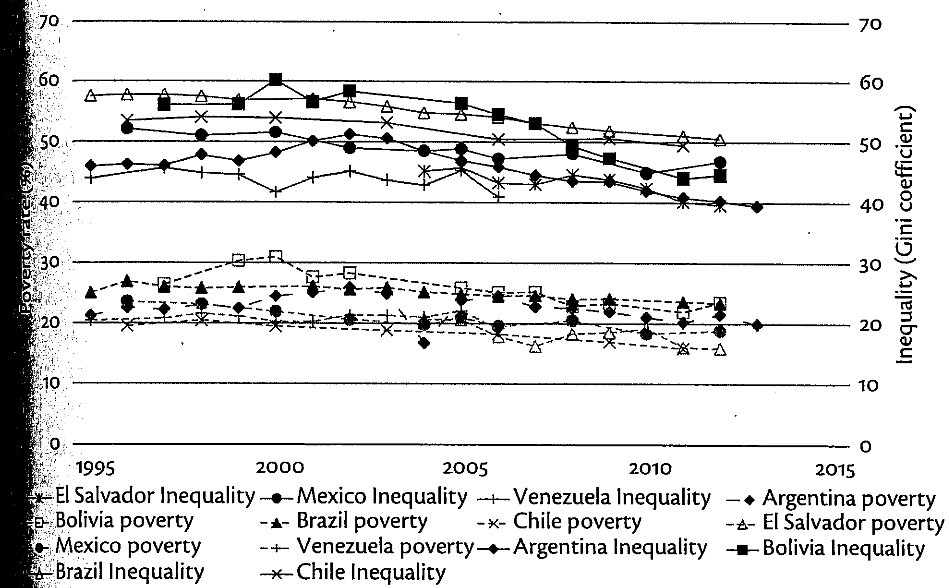


FIGURE 2.6: Recent declines in inequality and poverty in Latin America

This graph shows recent declines in both overall inequality (right axis), measured by the Gini coefficient (per cent), and the percentage of individuals living in poverty (left axis). In 1995 in Brazil the Gini coefficient was 58%, and 25% were living in poverty.

Juarez begin by noting that "there is no clear link between the decline in inequality and economic growth. Inequality has declined in countries which have experienced rapid economic growth, such as Chile, Panama and Peru, and in countries with low-growth spells, such as Brazil and Mexico. Nor is there a link between falling inequality and the orientation of political regimes. Inequality has declined in countries governed by leftist regimes, such as Argentina, Bolivia, Brazil, Chile and Venezuela, and in countries governed by centrist and center-right parties, such as Mexico and Peru."[69] Rather, they suggest, the fall was brought about by a reduction in the wage premium for more educated workers, and by progressive government transfers. Summarising the evidence from studies of Brazil, Alvaredo and Gasparini note in addition that the substantial increase in the minimum wage was an "important force behind the fall in household income inequality, given that the minimum wage sets the floor for both unskilled workers' earnings and for social security benefits." This increase was coupled with "the rapid expansion in the coverage of government cash transfers targeted to the poor, mainly a transfer to the elderly and disabled (Benefício de Prestação Continuada) and Brazil's signature conditional cash transfer program Bolsa Família."[70] In the region as a whole, there was, especially in the upper-middle-income countries, an expansion of social assistance, which—in contrast to the existing social insurance—"worked through the introduction of a set of institutions with a different rationale, institutionalization, and financing." This description is given by Armando Barrientos, who goes on to explain that the "stagnation of social insurance funds in Latin America is associated with the changes in the employment relationship brought about by the new conditions in liberalized labour markets."[71]

To sum up, in Latin America, as in the postwar decades in Europe, inequality reduction was achieved by a combination of changes in market incomes and expanded redistribution.

Where Are We Now?

In the case of Latin America, we have brought the subject up-to-date. Where are we now with respect to the OECD countries discussed earlier in the chapter? As we have seen, the factors that led to the earlier fall in income inequality in Europe have been reversed or come to an end. Where does this leave us?

The short answer is that in many, although not all, OECD countries income inequality is higher today than in 1980. There has been a distinct "turn" towards greater inequality. The rise in inequality has not been confined to the US and the UK, as may be seen from Figure 2.7, which shows the change in the Gini coefficient of overall inequality since 1980.[72] The increases in the UK and the US may have been among the highest, but there are several OECD countries in which the coefficient is higher now than in 1980 by the 3 percentage points that I have taken as a criterion for salience. The graph provides support for the OECD summary of "the big picture: inequality on the rise in most OECD countries."[73] At the same time, it reminds us that there are countries like France where overall inequality was not higher at the end of the 2000s than it had been thirty

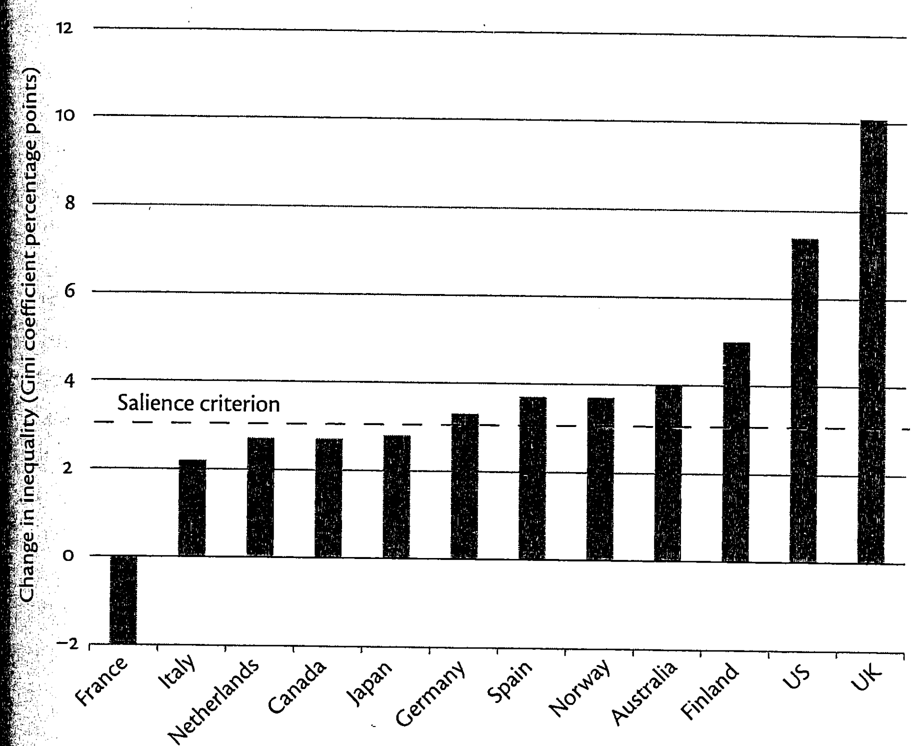


FIGURE 2.7: Change in overall income inequality since 1980 in selected world countries
The graph shows the change in percentage points in the Gini coefficient of overall inequality between 1980 and the end of the 2000s. The Gini coefficient in the UK was higher at the end of the period by just over 10 percentage points.

years earlier: the Gini coefficient has increased from 28.9 per cent in 2004 to 30.6 per cent in 2011, but this still leaves it 2 percentage points below its 1979 value before François Mitterrand came to power.

In seeking to learn from history, we invariably encounter question marks. Of these, the most important concerns the extent to which the world has changed, rendering the conclusions drawn from one period irrelevant today. How far, for example, are the experiences of Europe in the postwar period generalisable to the twenty-first century? In the next chapter, I explore some of the ways in which the economic context has changed and how this affects the design of policies for equality.