

Round Table on Income Inequality: Measurement, Causes, and Policy Response Policies to address Inequality Concerns

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GRID Conference on Global Trends in Inequality: Myths vs Facts

Barcelona

June 26th 2024

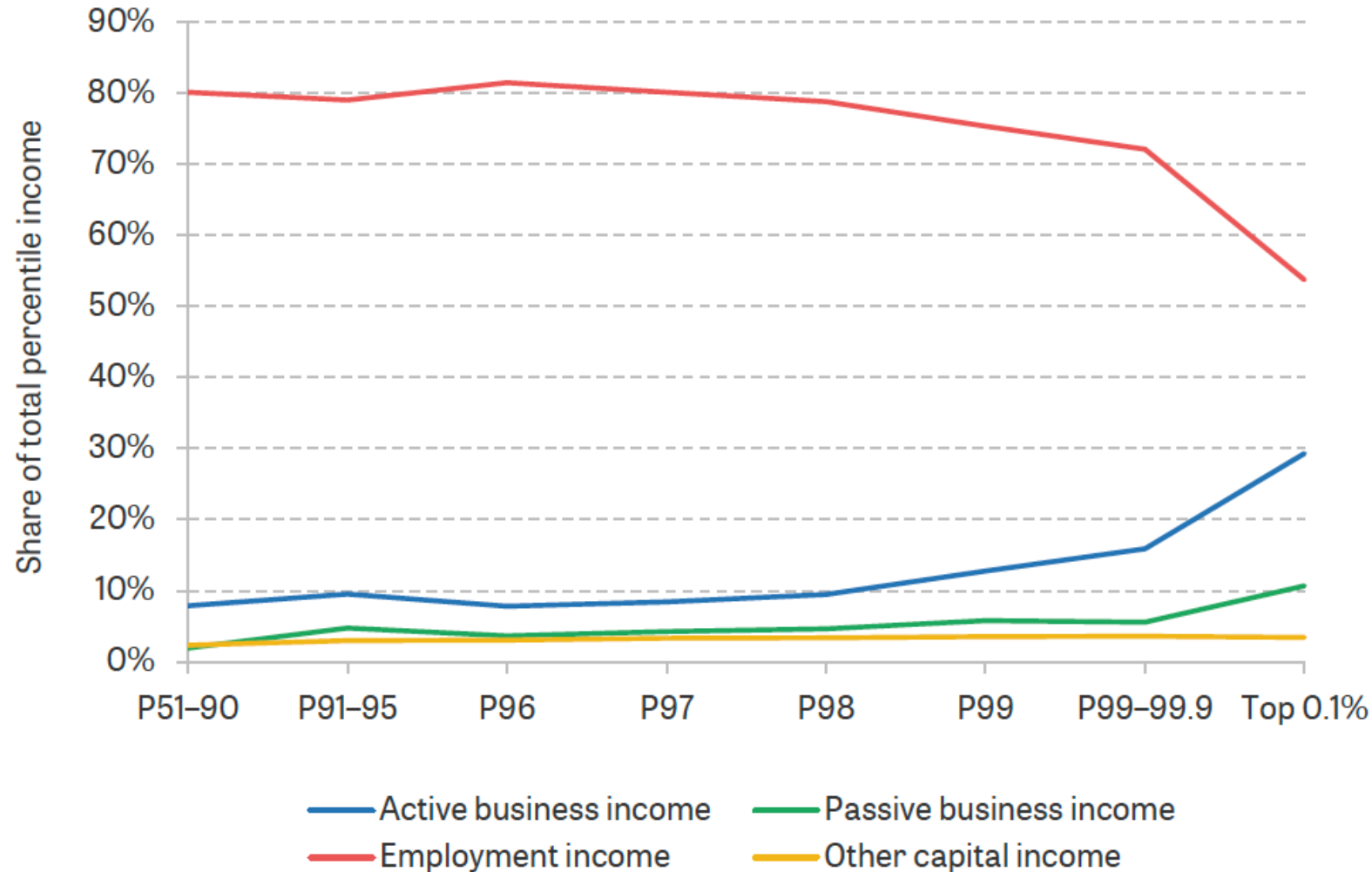
Drawing on the IFS-Deaton Review: Inequalities in the 21st Century

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

Beyond static measures and static policy responses – towards a broader agenda

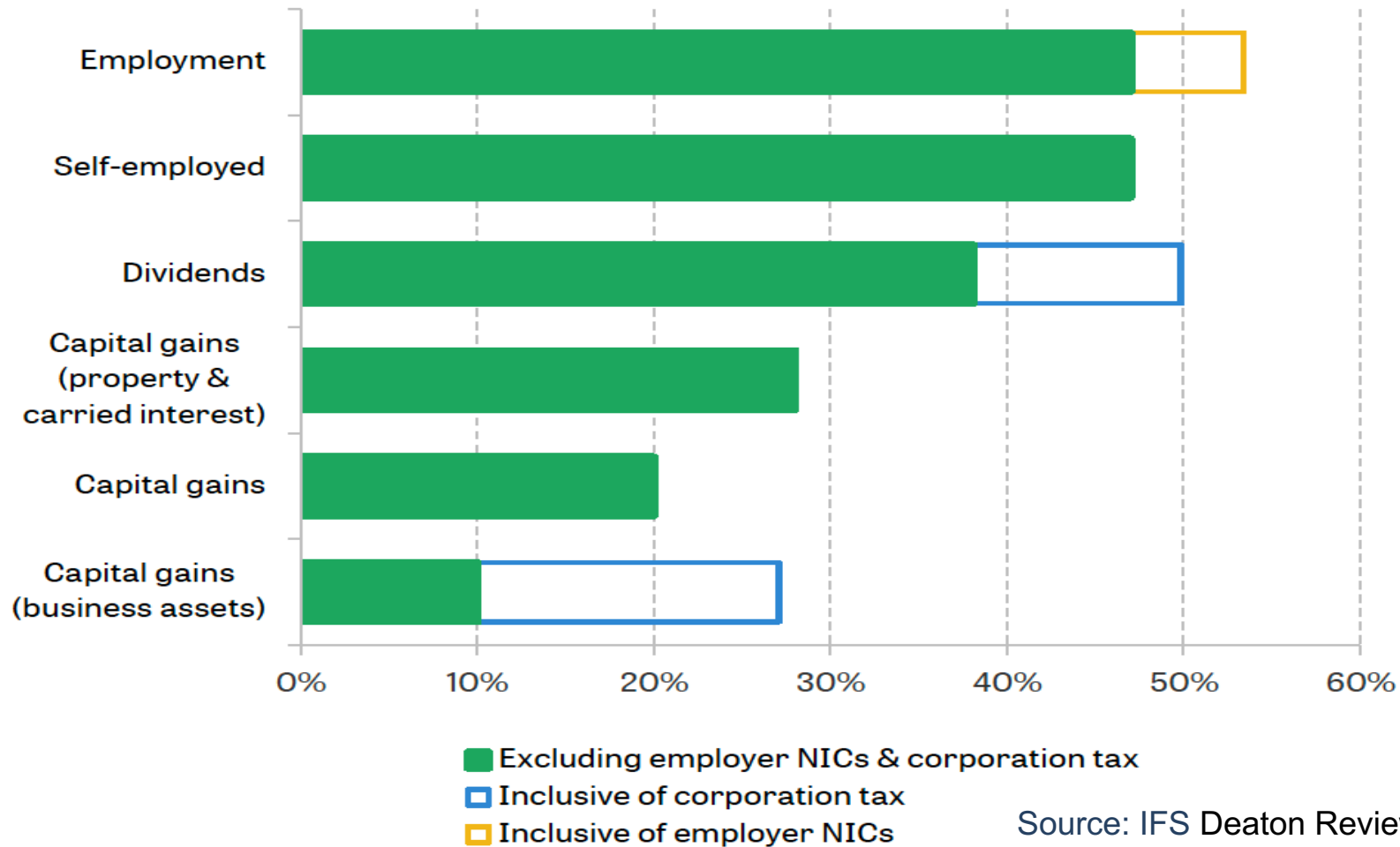
- To design policy responses, need to dig deeper into the key drivers of income inequality
 - Gini and top income shares provide little understanding of drivers or help with policy design
 - GRID is motivated by the key role of income dynamics, human capital, mobility, firms and innovation
- Persistence of income inequality matters – new linked data allows new insights
 - At the top – persistence of ‘rents’ with innovators capturing their position and restricting entry
 - At the bottom – persistent low wages with little prospect for earnings progression or good firm match
- Looking for policies that address inequality concerns and enhance innovation and social mobility
 - need a balance of tax policy with social insurance, human capital policy and competition policy
- At the top
 - policies toward productive investment, innovation, and social mobility
 - > mix of tax rates, tax base and competition policy
- At the bottom
 - policies toward individual earnings progression and net family income
 - > mix of benefits, in-work tax credits, min wage, human capital, and regulation
- A couple of illustrations at the top and for the rest, then some broader policy directions.....

Sources of top incomes for UK adults, 2018–19



- **Shifting:** rates vary widely by income source -> 'inefficient' changes in organisational form and shifting of labour income to capital gain and shifting of other forms of business income.
- Similar for US and many other economies.

Top marginal statutory tax rates, UK 2021–22

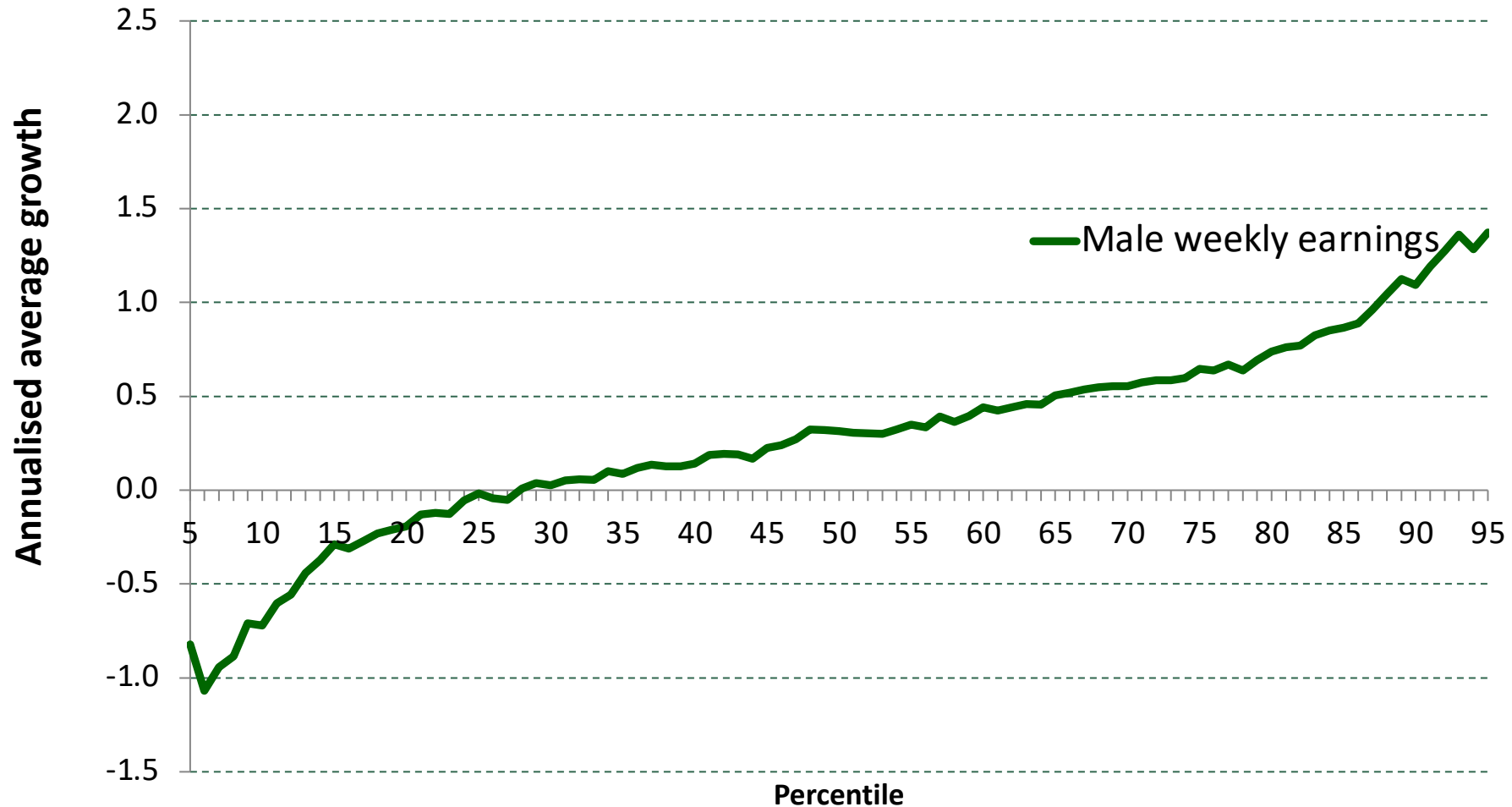


Source: IFS Deaton Review, 2024.

- At the top capital gains becomes a key area for reform...
- capital gains rate is zero if gains are deferred until death,
- concentration of capital gains in the UK among the top 1% is similar to the US, see Zidar (IFS Inequality Review, 2024)
- combined base and rate reform can increase productive investment and raise revenue.

Unpacking overall inequality for the rest.....

Growth in male weekly earnings: UK 1994/95 – 2018/19



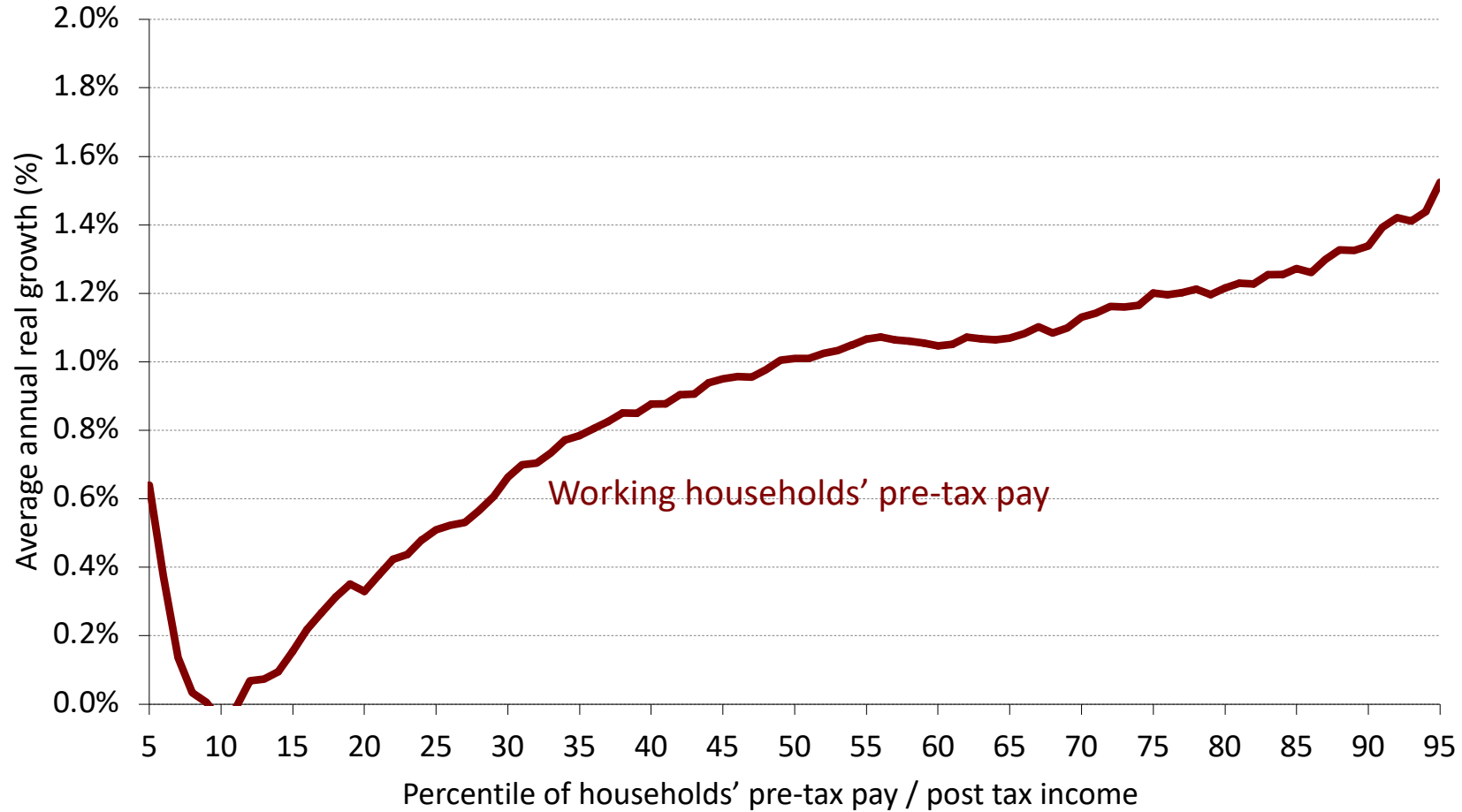
- Similar figures for other European countries, US and Canada: 17 Country Studies in IFS Deaton Review

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

Data used is UK FRS 1994-95 and 2016-17, not in full time education and aged <64

Unpacking overall inequality for the rest.....

Family earnings: UK 1994/95 – 2018/19

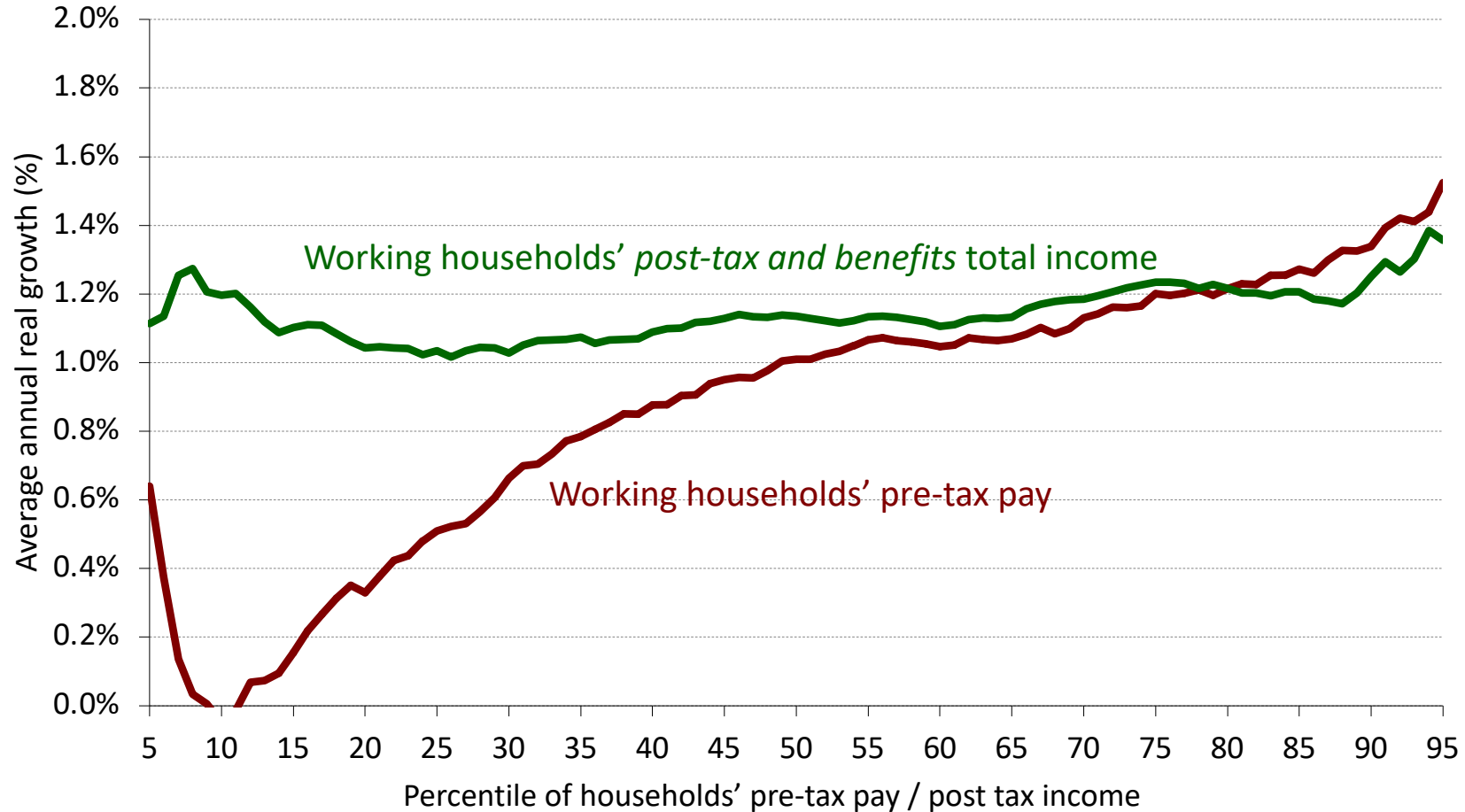


Notes: Family Resources Survey. All income measures are equivalised.

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

Unpacking overall inequality for the rest.....

Family earnings and household income: UK 1994/95 – 2018/19

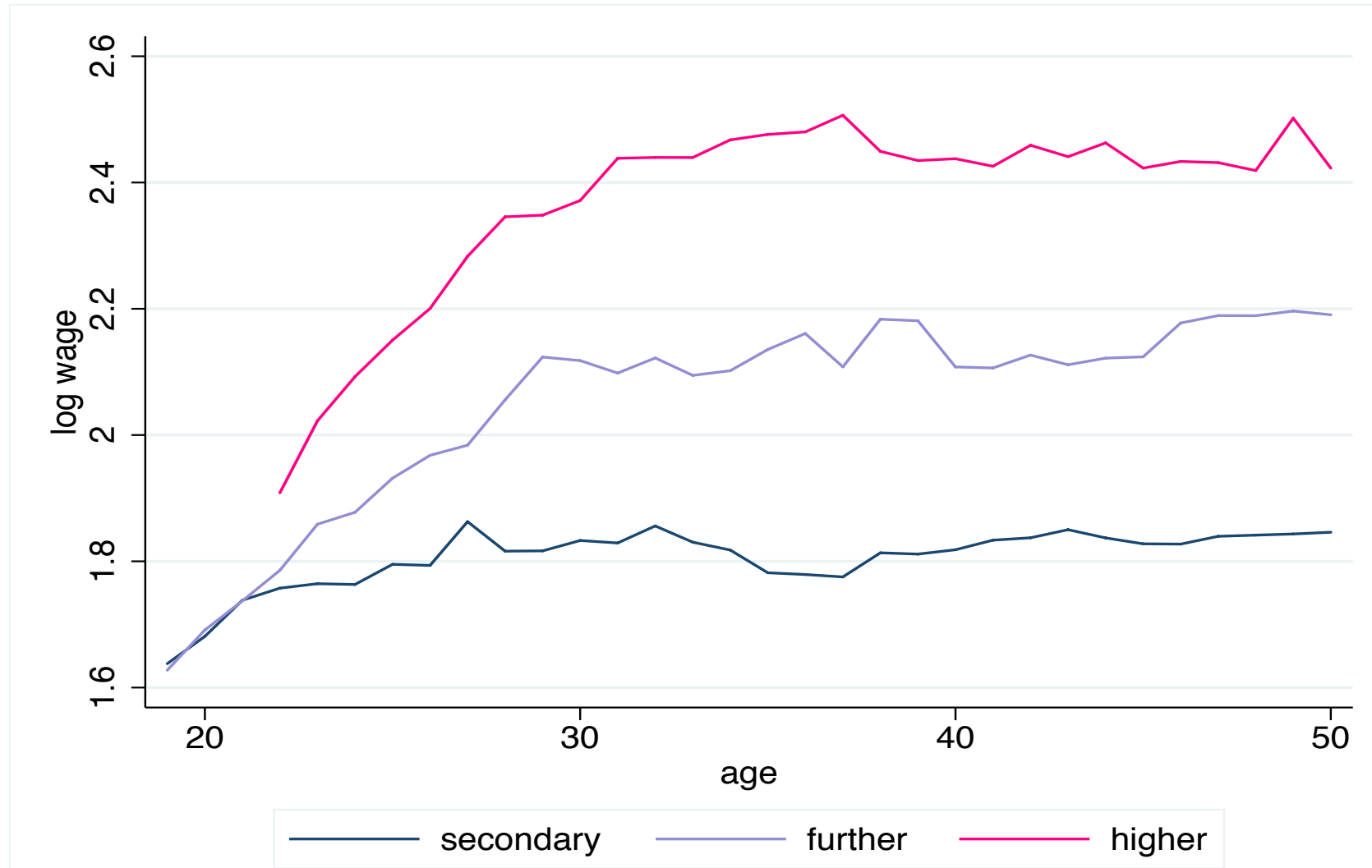


Notes: Family Resources Survey. All income measures are equivalised.

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

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

- progression (or lack of it) is key for many of the concerns about labour market inequality

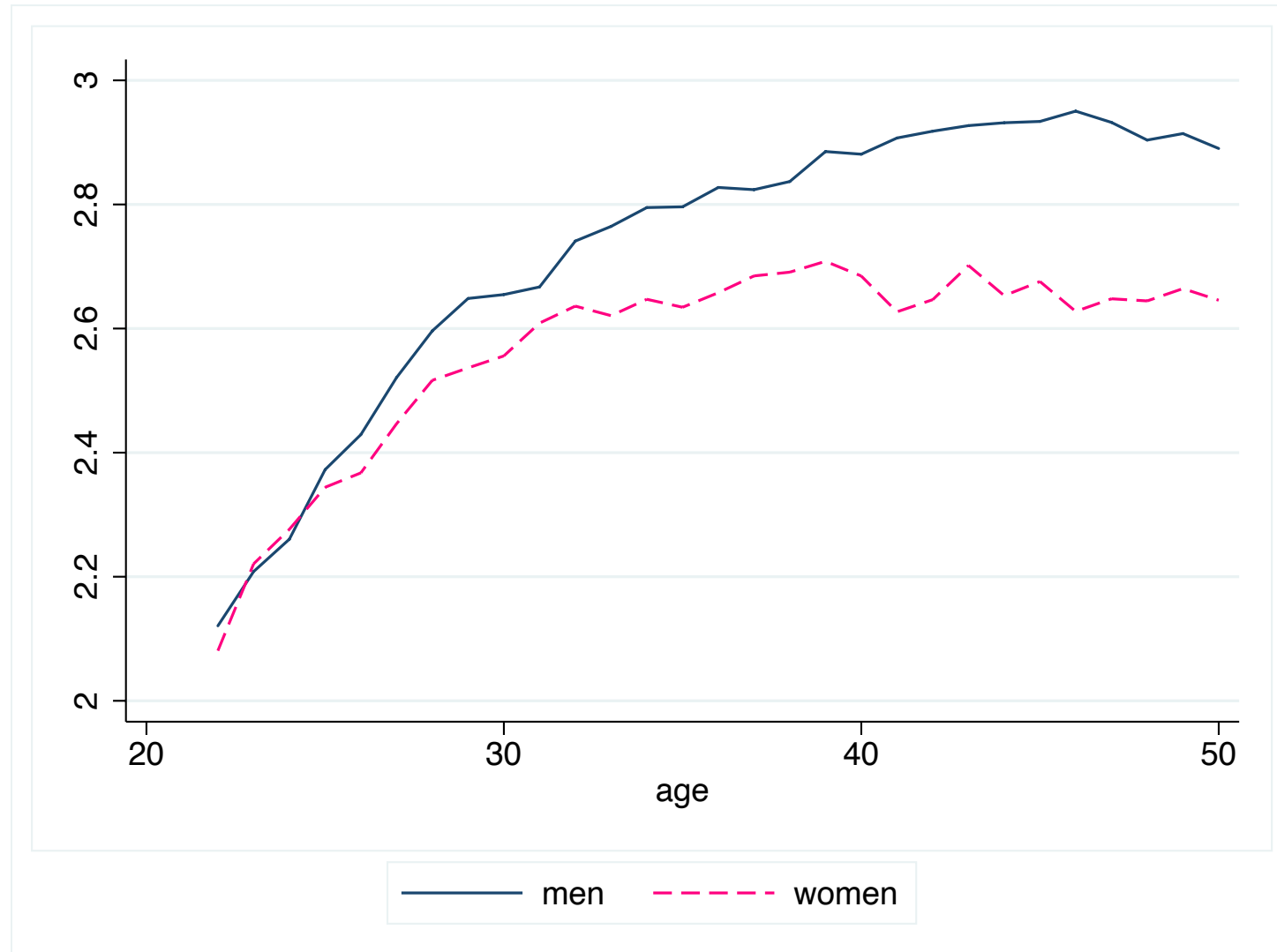


A finding common across many economies, US, France, etc., and for men and women,

Source: Blundell, Dias, Meghir and Shaw (2016, updated), Notes: Women, UK BHPS

Wage-age profiles by for university graduates by gender

- progression is key for understanding the gender gap

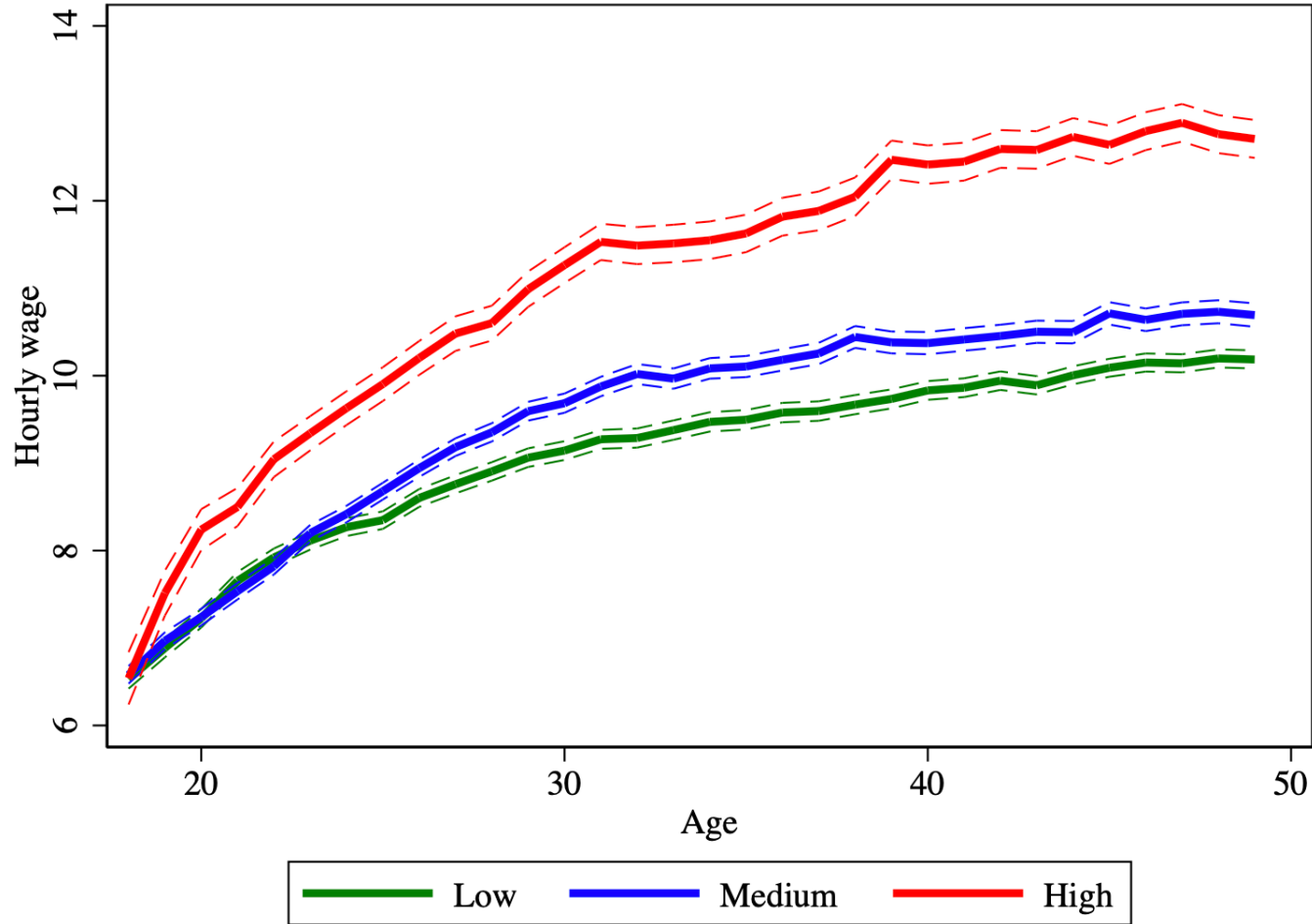


Source: Blundell, Costa-Dias, Meghir and Shaw (2016, updated).

Notes: Log hourly wage, College graduates, UK HLS, 1991- .

Progression is very poor for low educated but there are 'successes'

Wage progression for workers according to social skill intensity,
Premium is higher in firms with higher proportion of educated workers.



Notes: Data from Annual Survey of Hours and Employment (ASHE) 2004-2019. Figure shows average hourly wage at each age for male workers in private sector firms in occupations with low-educational requirements categorised by the measure of the importance of social-skills.

Source: Aghion, Bergeaud, Blundell and Griffith (2023)

Towards a balance of policies

At the bottom: beyond tax credits and the minimum wage

- **Earned income tax credits** - increase employment, well targeted but do little for wage progression – remove part-time incentives and condition eligibility on human capital investments and progression.
- **Minimum wages** - raise hourly wages, less targeted to poor families, no progression or job quality.
- **Human capital/training** - focus on firm-based accredited training for lower educated, emphasis on firm match and ‘social skills’, more likely to see wage progression, attract training, less outsourcing, and AI?
- **Solo self-employment** - line up effective tax rates, social insurance and benefit eligibility..

At the top: not just rates rates, but base and beyond

- **Alignment of rates:** moving toward the alignment marginal rates across labour income and different sources of capital income, including capital gains and expand base to allowance for new equity.
- **Wealth tax:** property tax and capital gains alignment with wealth transfers tax makes sense – a la Mirrlees; a one-off wealth tax and tax alignment - or a (book value) wealth tax to move resources from less productive wealthy to more productive agents?
- **Beyond tax and base:** balance with competition and education policies to nurture new innovators.

Policy mix at the bottom - beyond tax credits and the minimum wage.....

- **Earned income tax credits** - increase employment, well targeted to low earning families, but do little for wage progression and job quality – low educated spend working life in UK on tax credits
- **Minimum wages** - raise hourly wages, less well targeted to poor families, complement to in-work benefits; no incentive for progression or job quality or insurance to lay-off shocks.

Cannot continue to rely on these as the main policy leavers

- **Tax credits** – remove part-time incentives and condition eligibility on human capital investments
- **Training** - focus on firm-based accredited qualifications that align with job quality.. with social skills and productive firm match to enhance pay progression and career opportunities..
- **Solo self-employment** - line up effective tax rates, social insurance and benefit eligibility..
- **Local productivity and progression** – local policies to attract productive firms and retain educated...
- **Regulation and competition** - policies that improve competition and/or bargaining power of workers.

Key is to use models of self-insurance for households and innovation for firms to find policies that address inequality concerns while enhancing innovation and social mobility.

A balance of policies at the top

- Rates and base:
 - Alignment of rates: moving toward the alignment marginal rates across labour income and capital income, including capital gains is a key policy recommendation.
 - Base and death: need base reform too and removal of capital gains tax uplift at death.
 - Specific policy: Scrap preferential CGT rate for business assets and introduce new allowance for (equity) investment into a company – increases investment and reduces top inequality
- Wealth tax:
 - Property tax and capital gains alignment with wealth transfers/inheritance tax makes sense – a la Mirrlees,
 - A one-off wealth tax and tax alignment - or an annual wealth tax?
- Cannot address all concerns through tax alone:
 - The top 1% reflect rents to innovation and productive investment - but these rents can be too high, increasing top inequality and encouraging low productivity investment.
 - Balance tax policy at the top with competition policy and policies to nurture new entrants and the 'lost Einsteins'
- What about the rest of the distribution?