2012 Downing Lecture

The Great Recession and the Distribution of Household Income

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The Great Recession and the Distribution of Household Income

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Summary

Subject:
• impact of the downturn that began end-2007
• total & average incomes, inequality, and poverty for 21 rich industrialised countries

Findings: for most countries,
• in short-term, little/modest change
• In medium-term, greater change likely
‘The Great Recession’

Slowdown in OECD area late 2007,

Lehman Bros collapse in Sept 2008, ... banking crises, housing busts, international trade collapse...

→ first shrinking in world economy since WWII

... the worst recession in the OECD area since the Great Depression
shades of the 1930s?

George Orwell
The Road to Wigan Pier

John Steinbeck
The Grapes of Wrath
But much has changed..
Features of our study

1. Comparison across countries
   - Australia, Austria, Belgium, Canada, Denmark, Germany, Greece, Finland, France, Ireland, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, UK, USA

2. Household net income
   - not just earnings
   - not consumption expenditure nor wealth

3. Analyse all individuals
   - young, old, working or not working
   - sum incomes within households
What we do

1. review analytical models and evidence from past recessions [ch 1]
2. what has happened to the distrib. of household income in 21 countries [ch 2]
3. country case studies: 6 countries (DE, IE, IT, SE, UK, US) [chs. 3-8]
4. summarise & conclude [ch. 9]

NB no formal ‘evaluation’ against a counterfactual
“It’s too early to tell”..?

• GR not over everywhere + fear of double-dip

• consequences for many years
  – e.g. scarring impact of unemployment
  – impact of ‘fiscal consolidation’

• lags in data availability
What should we expect?

• analytic frameworks
  – Dynamic Stochastic General Equilibrium models
  – tax-benefit simulation models
  – decomposition by sub-group or income source

• evidence from past recessions
  – time-series studies of quantile group shares (Blinder-Esaki)
  – top incomes literature (Atkinson-Piketty)
  – case studies e.g. the US in the 1930s, NZ in late 1980s, Nordic countries in the late 1980s, UK since 1970s

• NB is this time different?
Mendershausen: incomes in US cities in 1929 and 1933

- average real income ↓; absolute poverty ↑
- inequality: Gini index ↑ 5 per cent pts. on average

Graph showing:
- unemployment
- number of people
- fall in income from capital

Income level
The Great Recession: how big?

• OECD area:
  – GDP fell by 5%, 2008q1-2009q2
• large range among our 21 countries, 2007-9
  – no fall in Australia, only 2% fall in NZ
  – falls of 9% in Finland and 13% in Ireland
  – median fall 5% (USA 4%)
• speed of recovery has varied greatly too
Heterogeneity in fall in real GDP, and in recovery

Quarterly changes in GDP: 6 countries 2007-2011 (2007q1=100)
National Accounts show total household income cushioned across in the Eurozone.
18 countries, 2007-9; household income typically ↑ as GDP ↓
Changes in income sources

total household net income = labour earnings + capital income + state benefits + other income − direct taxes

• labour earnings:
  - employment and hours among individuals
  - employment among households (% with no work)
  - earnings among individuals (average and distribution)

• other income sources (but fewer data)
Employment falls larger for men than women for women in 10 of our 21 countries, 2007-9 (annual rates)

... and much larger for the young (15-24) than middle aged (25-54); rises for 55+ in 12 countries
More adults in households with no workers in most EU countries

% of 18–59 year olds in workless households, 2009

% of 18–59 year olds in workless households, 2007
Average earnings increased in most countries when employment rates fell.

Changes in annual average earnings (%) and in employment rates (percent points), 2007–9
Earnings inequality: little change in ‘Anglo’ countries
gross earnings of FT employees:
ratio of 90th percentile to 10th percentile, 2000–9

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Graph showing earnings inequality trends from 2000 to 2009 for different countries.
Short-term changes over 2007-9 in the distribution of household income

• Eurostat figures for EU countries (harmonised surveys ‘Statistics on Income and Living Conditions’ - SILC)

• Census Bureau figures for the USA (2007-10)

• median incomes: story similar to total income in National Accounts (*modest change, often +ve*)
Little change in inequality of household incomes in Europe

Gini coefficient (%)
...or in the USA
Gini coefficient (%)

Elderly fared relatively well 2007-9 in Europe: median income of persons 60+ as % of median for persons aged <60

Nordics

W. Europe

Anglo

S. Europe
... and in the US: % of persons with ‘money incomes’ below the official US poverty line
Government balances worsened almost everywhere

general government balance as % of GDP, 2007 and 2009
Fiscal consolidation plans
Survey of 30 OECD member states, Autumn 2010: most frequently cited ‘areas’

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<th>Expenditure Area</th>
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<td>Tax on financial sector</td>
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**Distributional consequences?**

- cuts in cash benefits hit bottom of distrib → poverty up
- impact on inequality – depends on measures
Conclusions and Caveats

1. *short-term* changes modest
   - the elderly have done relatively well

2. distributional impacts will differ between short-, medium-, and longer-term

3. need to go beyond cash incomes

4. case study countries exclude GR, PT, and ES
Policy lessons

1. stabilisation of incomes achievable in the short-term (cf. 1930s)

2. stronger welfare states provide greater ‘automatic stabilisation’

3. timely monitoring of distributional outcomes essential