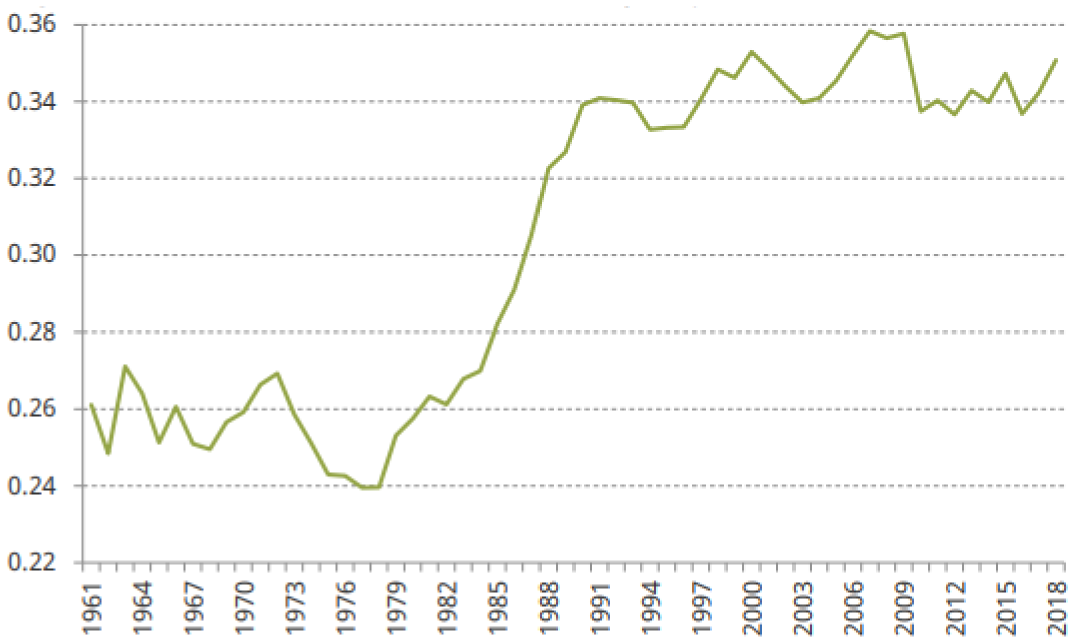
Inequality of Income: How bad is it?

In the latest financial year Sainsbury's chief executive was paid £3.8million. This amounts to a 31% increase over the year and compares with the 5.3% pay increases for the staff who work in the supermarket stores. The chief executive's increase means his new salary is 183 times larger than the annual salary of the median worker at Sainsbury's. [1]



Inequality of income refers to the difference in the way income is shared out across the population. The most widely used method of measuring this difference is by means of the Gini coefficient. [2] The Gini coefficient can have any value between 0 and 1. Zero indicates a perfectly equal distribution of income, while 1 represents complete inequality with one household receiving all the income available.

The chart shows the Gini coefficient for the UK from 1961.[3] The lowest values were between 1961 and 1978. In the 1980s during the Conservative years inequality increased dramatically with the Gini coefficient rising from around 0.24 in 1978 to around 0.34 in 1991, an increase of almost 50%. "*The scale of this rise in inequality* (is) *………..unparalleled both historically and compared with the changes taking place at the same time in most other developed countries*." [4] Out of 38 member countries in the OECD the UK ranks 33 on inequality. France and Germany, with similar populations, rank 13 and 14, significantly lower than the UK.[5]

During the 1990s the Gini coefficient remained largely unchanged, but it increased towards the end of the decade to reach 0.35 in 2000 and 0.36 in 2009. This means that during Labour's period in office there was " *a small increase in overall measures of income inequality*……." [6] At the end of the financial year 2021 the Gini coefficient stood at 34.3%.[7] Income inequality therefore is much the same as it was in the late 1980s, but much higher than it was in the 1960s and 1970s.

According to the High Pay Centre, the rapid growth of pay for executives and other high-earning professionals over the last 40 years is one of the reasons why the UK has such a high level of income inequality.[8] The share of income which went to the top 1% of richest individuals in the UK fell considerably during the First and Second World Wars. In 1919 for example the share of income going to the top 1% was 19% - by 1979 it had fallen to 6%.[9] It then went into reverse and by 1989 the top 1% was receiving 8.7% of all income, increasing to 12.5% in 1998, 14.8% in 2006 and 17% in 2009.[10] Today the top 1%, which is made up of the 524,000 people with incomes above £128,000, receive 15% of income. The top 0.1%, the 52,400 people with incomes above £515,000, receive 6% of income.[11] The top 1% clearly gained between 1979 and 2010 during the periods of Conservative and Labour governments. The bottom 10% and especially the bottom 5% however fared particularly badly, and *"the vast majority of the population ....also lost out significantly*." [12]

A second reason for the steep rise in inequality during the 1980s relates to the changes which were applied to taxes and benefits after 1979. "*Overall, tax and benefit changes contributed half of the total increase in inequality during these years*".[13] The most significant tax change pushing up inequality was the reduction in the top rate of income tax from 83% to 40% between 1979 and 1988. Alongside the reductions in direct taxes, indirect taxes, particularly VAT was increased from 8% to 15%. The Institute for Fiscal Studies estimated that as a result of the increase, the poorest 10% of the population would have ended up spending nearly 20% of their income on indirect taxes while the top 10% would only have spent 8%.[14]

In relation to benefits, the yearly increase in the state retirement pension was changed in 1980 so that it went up in line with prices rather than earnings. Because earnings usually went up faster than prices, this resulted in pension payments falling relative to average earnings. From being 26% of average earnings in 1979 the basic pension was just 15% of average earnings by the mid-2000s.[15] With the introduction of the new pension in 2016, pensions as a percentage of average earnings have recovered and now stand at 25%. This compares with Ireland at 26%, Netherlands 31% and Denmark 36%.[16] Unemployment benefit, which represented 20% of the median wage in 1984, also fell. It dropped to 15% of the median wage by the middle of the 1990s and 12.6% by 2008. It now stands at around 12.8%.[17]

A third reason relates to trade unions. A study, which analysed the extent of inequality during the 1980s and 1990s across a range of countries, found that falls in trade union membership were associated with growing inequality. The evidence pointed to the fact that "*in countries in which inequality increased, this was primarily the result of the decline in the importance and bargaining power of organized labour*." [18] Higher unemployment and the rise in self-employment also contributed to inequality. [19]

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