

INEQUALITY UNDER THE LABOUR GOVERNMENT

Andrew Shephard

Income Inequality under the Labour Government

Andrew Shephard

a.shephard@ifs.org.uk

Institute for Fiscal Studies
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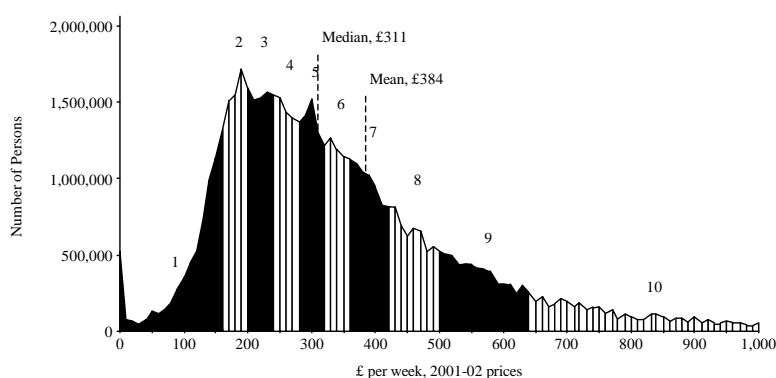
Summary

This Briefing Note will provide a brief analysis of changes to income inequality since the Labour government came to power in 1997.¹ The most recent data from 2001-02 show that there has been little change in income inequality since 2000-01. An implication of this is that there has been little impact upon the slight upward trend in inequality that has been experienced over Labour's term in government.

The Income Distribution

A picture of the income distribution today is presented in Figure 1.² The horizontal axis gives the weekly household income grouped in bands of £10 and adjusted for family size, while the vertical axis gives the number of individuals observed at each level of income. The alternately shaded sections show the income decile groups. Each of these groups contains 10 per cent of the population.

Figure 1: The Income Distribution, 2001-02



Notes: Distribution has been truncated at incomes above £1,000. Incomes are measured before housing costs and adjusted for family size using McClements equivalence scales (see appendix 2 of the government's HBAI publication).

Source: Author's calculations using Family Resources Survey.

¹For a more detailed assessment of the trends in income inequality in Great Britain up to 2000-01, see A. Goodman and A. Shephard, *Inequality and Living Standards in Great Britain: Some Facts*, Briefing Note no. 19, Institute for Fiscal Studies, London, 2002 (www.ifs.org.uk/inequality/bn19.pdf).

²Throughout this Briefing Note, methodology consistent with the government's Households Below Average Income (HBAI) publication is used. See Department for Work and Pensions, *Households Below Average Income 1994/95 - 2001/02*, CDS, Leeds, 2003.

The figure shows that the current distribution of income is highly skewed, with approximately two-thirds of individuals having incomes below the national average. The distribution is concentrated within a fairly narrow range of income in decile groups 2 to 6. However, as we move further up the income distribution, there is a widening of the decile group income bands. While the distribution shown in Figure 1 has been truncated at income levels in excess of £1,000 per week, almost 3 per cent of individuals have incomes above this amount.

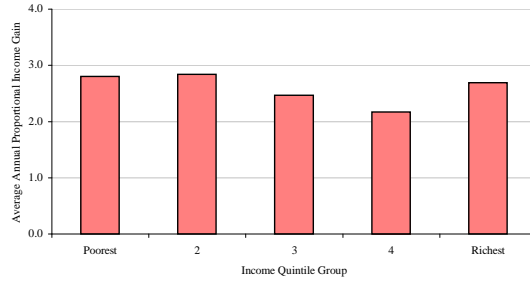
Real Income Growth

How have incomes changed across the distribution over the first five years of the Labour government, and how do these changes compare with experiences under previous governments? In Figure 2, we show the average annualised real income growth by quintile group. Each quintile group contains 20 per cent of the population.

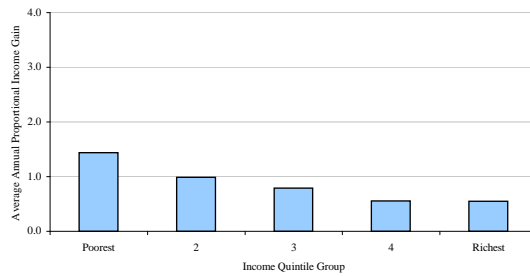
Under the present Labour government, the greatest proportional income gains were experienced in the bottom two quintile groups, followed by the richest group. On average, these groups experienced real gains of a little under 3 per cent per year. Compared with the previous Conservative governments, these gains are actually relatively equally distributed over the income distribution. Although the magnitude of the gains under John Major is lower, the poorest groups gained most. This is in stark contrast to the changes that occurred when Margaret Thatcher was in power, during which time the poorest group gained just 0.4 per cent on average per year, compared with the 3.8 per cent gain of the richest group.

It should be noted that these results can be sensitive to small changes in the start and end dates considered due to variations in incomes over the economic cycle.

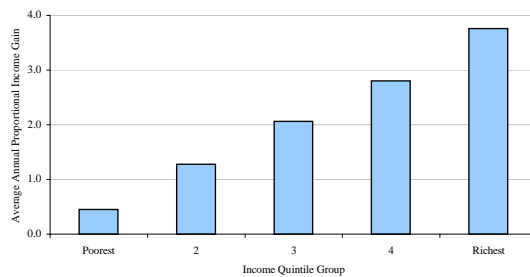
Figure 2: Real Annualised Income Growth



Blair, 1997-98 to 2001-02



Major, 1990 to 1997-98



Thatcher, 1979 to 1990

Note: Incomes are measured before housing costs and adjusted for family size.

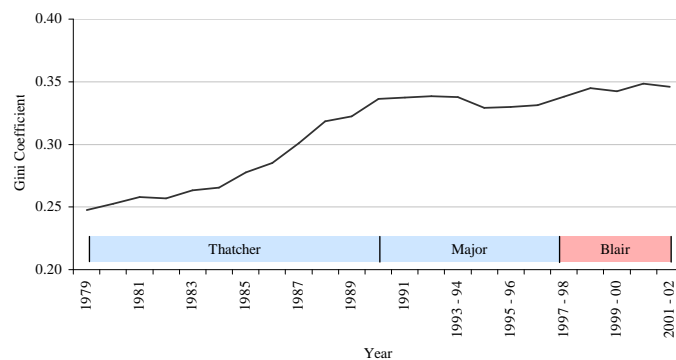
Source: Author's calculations using Family Resources Survey and Family Expenditure Survey.

The Gini Coefficient

While Figure 2 showed changes across broad groups of the population, it is possible that a different picture may emerge once every income point, including those at the tails, is taken into consideration. We are able to do this through use of the Gini coefficient.

The Gini coefficient is a popular measure of income inequality. It collapses the entire income distribution into a single number between zero and one; the higher this number is, the greater is the degree of income inequality. It is a convenient tool for analysing how the observed income changes affect measured inequality. An advantage of such a one-dimensional measure is that it enables unambiguous statements about changes in inequality to be made. Figure 3 shows the evolution of the Gini coefficient from 1979 to 2001-02.

Figure 3: The Gini Coefficient



Note: Incomes are measured before housing costs and adjusted for family size.
Source: Author's calculations using Family Resources Survey and Family Expenditure Survey.

The figure shows that over the 1980s, there was a considerable increase in inequality as measured by the Gini coefficient. It stabilised in the early 1990s, and then fell slightly over the last Conservative government. Since Labour came to power, the Gini coefficient has increased once more. Indeed, despite the slight (statistically insignificant) fall in 2001-02, income inequality over the past two years has been higher than in any other period covered by our data. Although the increase in inequality observed since Labour came to power is statistically significant at the 10 per cent level, it is not so at the 5 per cent level.

Appendix: Where Do You Fit In?

Many people are unaware of their own position in the income distribution. Table 1 gives the monthly income levels of different family types falling into each income decile group. Remember, incomes are measured after subtracting direct taxes (including council tax), and count the income of all the members of your household from all sources, including state benefits.

Table 1: Where Do You Fit In?

	Single person, no children	Couple, no children	Couple with two children (aged 4 and 13)
Bottom decile	£0 to £400	£0 to £700	£0 to £1,000
Decile 2	£400 to £500	£700 to £900	£1,000 to £1,200
Decile 3	£500 to £600	£900 to £1,000	£1,200 to £1,500
Decile 4	£600 to £700	£1,000 to £1,200	£1,500 to £1,700
Decile 5	£700 to £800	£1,200 to £1,400	£1,700 to £2,000
Decile 6	£800 to £900	£1,400 to £1,600	£2,000 to £2,300
Decile 7	£900 to £1,100	£1,600 to £1,800	£2,300 to £2,600
Decile 8	£1,100 to £1,300	£1,800 to £2,100	£2,600 to £3,100
Decile 9	£1,300 to £1,700	£2,100 to £2,800	£3,100 to £4,000
Top decile	£1,700+	£2,800+	£4,000+

Note: Incomes are monthly incomes measured before housing costs and are expressed in 2001-02 prices. The income differences across family types reflect the ‘equivalence scales’ used. Income ranges within each decile group are the same once adjusted for household size and composition.

Source: Author’s calculations using Family Resources Survey.

This table reflects the fact that different family types have different financial requirements to achieve any given standard of living. For example, whereas a couple with two children aged 4 and 13 may require monthly income of £4,000 or above to be placed in the highest decile group, a single-person household would require the lower amount of £1,700 to be in this same group.