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Globalisation, Inequality and Populism

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1. INTRODUCTION

Inequality in the distribution of income and wealth among individuals has now come to the fore as a core concern across the industrialised world. In 2013 then President of the United States Barack Obama identified rising income inequality as *"the defining challenge of our times"*. The Managing Director of the International Monetary Fund Christine Lagarde has stated that *"reducing excessive inequality is not just morally and politically correct, but it is good economics*." Secretary-General of the OECD Angel Gurría has emphasized that "*Inequality can no longer be treated as an afterthought. We need to focus the debate on how the benefits of growth are distributed"*. This reflects the fact that inequality has been rising in many rich countries, and that this is seen as undermining economic growth, 'squeezing' middle and lower income households, exacerbating social 'bads' such as health inequalities, and undermining social solidarity and trust. Most recently, in light of political developments, it has also been held responsible for fuelling the rise of populism.

To explore this line of argument, we first examine what has happened to income inequality across the rich countries in recent decades and through the Great Recession, also referring to what is known about the distribution of wealth. We discuss the range of factors that appear to be driving inequality upwards, including the role that globalisation may play. Finally, we look at the robustness of the claim that is responsible for the 'revolt of the angry' and rise of populism, directly or indirectly.

2. INCOME INEQUALITIES IN OECD COUNTRIES: PATTERNS AND TRENDS

We draw here on data from a variety of sources to capture patterns and trends in income inequality over recent decades, going back as close to 1980 as the data allow in order to see the longer-run trends up to the onset of the financial and economic crisis in 2007-08, and then focusing on what happened during and after the Great Recession. Income inequality is captured first by the most commonly-used summary measure, the Gini coefficient, which reflects income differences across the distribution and ranges from 0, indicating no inequality, up to 1 which indicates maximum inequality. Different data sources and databases on income distribution (notably those brought together by the OECD and the Luxembourg Income Study) cover different periods and do not always show the same picture over time for a given country. Here a judgement has been made about the most suitable source to draw on for current purposes for each country. The income concept employed, as is usual, is equivalised disposable income – in other words, income from the market plus cash transfers minus direct taxes (including employee social insurance contributions), adjusted for differences in household size to take the greater needs of larger households into account.

Table 1 shows the direction and extent of movement in the Gini coefficient inequality measure from around 1980 (or as close as possible) to about 2007 for OECD countries. The most common pattern is rising inequality. However, there are countries where inequality was stable (such as France and Ireland) and ones where it declined (such as Greece and Portugal). Furthermore, among those where inequality rose, the scale of that increase varied widely: for some it was relatively modest, whereas for others the Gini coefficient rose markedly. The most substantial increases were for Finland, Sweden and the UK; the USA was in the group with the next-highest rise, but from a particularly high initial level. As pointed out in the overview presented in Förster and Tóth (2015), there was some tendency for inequality to fall or remain stable where it was initially relatively high, while some of the larger increases were in countries which has relatively low levels at the outset of the period such as some of the Nordic and Baltic countries. This meant that some degree of convergence in inequality levels was observed. In some countries inequality rose in a reasonably consistent fashion, but for others it was more concentrated in discrete 'episodes'.

Table 1: Income Inequality from About 1980 to Before the Crisis: Change in Gini Coefficient Summary Indicator

Fall	No Change	Modest Rise	Substantial Rise	Pronounced Rise
Estonia	Austria	Belgium	Australia	Finland
Greece	France	Canada	Germany	Latvia
Portugal	Ireland	Czech Republic	Luxembourg	Lithuania
Switzerland	Italy	Denmark	New Zealand	Sweden
	Japan	Netherlands	Poland	UK
	Slovenia	Norway	Slovak Republic	
	Spain		USA	

Source: OECD Income Distribution Database, Luxembourg Income Study, GINI FP7 Project Database, Chartbook of Economic Inequality

Turning to what happening from the onset of the Crisis to 2014, which is as far as the comparative data allows one to go at present, Table 2 brings out that income inequality then went down or was stable as often as it increased. Even among the countries worst hit by the crisis in terms of GDP per head and average household income, some saw inequality rise markedly but others (for example Ireland and Portugal) did not. In-depth studies of the impact of recession on income inequality (for example Jenkins et al, 2013) highlight the complex channels through which incomes from different sources (notably earnings, self-employment income and social protection transfers) are affected. This brings out that the impact on overall inequality depends on how profits are affected, on how much unemployment rises and how that affects households across the income distribution, and on the response of the tax and transfer system, both in terms of automatic ‘stabilisers’ and discretionary policy choices in response to increasing demands on the system and fiscal deficits. The effects of the Great Recession on absolute income levels, deprivation, poverty and social exclusion can be captured by a variety of other indicators: focusing purely on the distribution rather than the level of incomes, though, the recession has had varying effects rather than simply or consistently reinforced previous trends towards increasing inequality.

Table 2: Income Inequality Through the Crisis: Change in Gini Coefficient 2007-2014

Fall	No Change	Rise
Belgium	Australia	Denmark
Finland	Austria	Estonia
Iceland	Canada	Greece
Latvia	Czech Republic	Hungary
Netherlands	France	Italy
Poland	Germany	Lithuania
Portugal	Ireland	Slovak Republic
Romania	Luxembourg	Slovenia
UK	Norway	Spain
	Switzerland	Sweden
		USA

Source: OECD Income Distribution Database

So far we have been concerned with inequality across the entire distribution. However, in the debate about rising inequality a great deal of attention has focused on what has been happening at the very top of the distribution, in terms of the growing share of total income going to the top 1% or even the top 0.1%. This is most pronounced in the case of the USA, where the share of gross (i.e. pre-tax) income going to the top 1% of tax units rose from around 1980 to before the crisis; after dipping in the first few years of the crisis it has since recovered and appears to be on the rise again. The data revealing these trends in top incomes come from analysis of tax data rather than the household surveys that are (mostly) used to track inequality across the entire distribution, and such estimates are available only for some countries. The available estimates show that while top income shares rose markedly from around 1980 to before the Crisis in some OECD countries, notably Australia, Canada, Germany, Finland, Ireland, Sweden, the UK, and the USA, they were relatively stable in some others such as Denmark, France and Spain. Estimates are only available for some of these showing what happened through the crisis. These generally show either stability or – especially in the UK – some decline in top income shares, reflecting the impact on profits, top executive reimbursement, and the financial sector in particular; in the USA, however, growth in top shares soon returned.

Alongside inequality in income, increasing attention has also been paid to the distribution of wealth among households and whether that has been increasing – especially following the publication in English of Thomas Piketty's *Capital in the 21st. Century*, which highlighted what he sees as the return of 'patrimonial capitalism'. The evidence about the distribution of wealth among persons is more limited than for income, but has been improving in recent years, including via new households surveys of assets and debts coordinated by the European Central Bank, and compilations brought together by the OECD and the Luxembourg Wealth Study. This has allowed for more meaningful comparisons across rich countries, highlighting that the distribution is substantially more unequal for wealth than income. The extent to which change over time in wealth inequality can be measured consistently is more limited. The available evidence does not suggest, however, that the pronounced increase in wealth inequality seen over recent decades in the USA, and much-commented on there, has been the general experience. There appears to have been some increase in share of wealth going to top since the late 1980s in Finland, Italy and the UK, but not for Germany, the Netherlands, Norway or Sweden. As far as the impact of the crisis and recession is concerned, these would be expected to have a marked immediate effect on the value of different assets, including housing and shares, but the pattern across countries appears quite varied, with some increase in inequality in the distribution of wealth in for example Italy and the Netherlands but little or none in the UK.

3. WHAT HAS BEEN DRIVING INEQUALITY UPWARDS?

The upward trend in income inequality in many OECD countries over recent decades has given rise to a substantial research literature seeking to understand the underlying driving forces. Research by the OECD has been particularly influential in providing a comparative perspective (see OECD 2008, 2011, 2015), and there has been a substantial number of other comparative (e.g. Salverda et al, and Nolan et al, 2014) and national studies These show, in summary, that increasing inequality in market incomes accruing to households has played the central role – that is, income from employment, self-employment, investments and private pensions, before transfers or taxes are taken into account. This in turn reflects in the first instance increases in the dispersion in individual earnings among employees, seen in a substantial number of countries. A widening in the economic returns to education and skills, notably between those with some third-level education and those who did no progress beyond school, has been widespread. At the same time a 'hollowing-out' of the occupational structure, with some routine jobs around the middle of the earnings distribution shrinking or disappearing, has been seen in a number of countries.

These changes in the shape of the individual earnings distribution are widely seen to have been very significantly affected by the combination of globalisation and technology. Globalisation, and in particular the entry of China into the global trading sytem, has opened up rich country manufacturing in particular to intense competition from emerging economies with more lower labour costs, while also making capital much more mobile across borders. Firms are much more 'footloose', willing and able to shift production to where costs are lower, and outsourcing of production has proceeded apace. At the same time, technological advances, notably in information and communication technology, both meant that some jobs could be dispensed with entirely and that global supply chains could be organised in such a way that other jobs formerly embedded in the rich countries could be outsourced much more easily. Studies differ in the weight assigned to globalisation versus technological change, and views in the research literature have fluctuated over time about which has been more important. Given the extent to which they interact, with one enabling and reinforcing the other, it is not surprising that their effects have proved very difficult to disentangle.

It is also important to stress that neither globalisation nor technological change are properly to be understood as external, exogenous drivers unrelated to the institutional and policy context in which they occur. Globalisation itself was enabled by a set of changes in global trading 'rules of the game', as well as in the way finance and capital flows were regulated; technology change, as Atkinson (2015) and Mazucatto (2015) emphasise, does not occur in a vacuum, but instead is fundamentally influenced by state action both directly and indirectly. In a similar vein, globalisation and technology were often accompanied by de-regulation in the labour market, and served to reinforce other factors shifting the balance from labour to capital, including declining union power. Policies with respect to minimum wages together with changes in employment protection etc., sometimes help to explain why low earnings became more prevalent. At the same time, the way top executives are rewarded also changed markedly, with a much greater emphasis on performance-related pay and share options, resulting in a remarkable ballooning of the ratio of top to median or average pay – spreading more rapidly across countries in a context where labour mobility had increased. The expanded role of finance both facilitated those trends and contributed directly to the growth in top incomes, with a substantial proportion of top earners working in that sector.

The increasing role of women in the paid labour force has been a major trend over the period in many countries, and for the most part this has served to cushion household incomes from the effects of increasing dispersion among individuals. While much less important than earnings, income from self-employment and from capital (in the form of rent, interest and dividends) constitute a significant share of total household income. These have also contributed to increasing inequality, having grown in importance over time and become more unequally distributed acosss households.

Finally, and crucially, the redistributive capacity of the state through cash transfers and direct taxes also often declined over the decades preceding the crisis, and direct redistribution not been able to fully offset the increases in market income inequality. This reflects on the one hand the ways in which social protection systems evolved, often privileging pensioners at the expense of working-age recipients while struggling to adapt to increasing levels of low pay and in-work poverty and with social safety-nets sometimes weakening. As far as direct taxes are concerned, top income tax rates were generally reduced from the late 1970s and in some cases taxes on income from capital were reduced even more, both because this was seen as encouraging economic activity and because of the competiive pressures this wave created across countries.

4. INEQUALITY, SOCIAL COHESION AND POLITICS

We now turn to the impact rising inequality may have on politics and on the rise of populism in particular. The first channel through which this might operate is if rising inequality itself serves to undermine economic growth. The potential negative effects of inequality on economic growth been highlighted by for example Stiglitz, (2012, 2015), Ostry et al, (2014), and Dabla-Norris et al (2015) for the IMF, and OECD, (2014). A widely-cited study carried out by the International Monetary Fund in 2014 concluded that "An increase in the income share of the top 20% drags down growth" (Ostry et al, 2014). Another much-quoted study by the OECD (Cingano, 2014) concluded that if inequality had not grown from 1980 onwards in many OECD countries, real GDP growth would have been considerably greater. Thewissen, Kenworthy, Nolan, Roser and Smeeding (2015) found that increasing inequality was statistically associated with slower growth in middle and lower incomes (although not accounting for much of the variation in those incomes).

Another potential channel is if rising inequality is seen to be choking off opportunities and mobility from one generation to the next. The idea that intergenerational mobility in earnings is lower in countries with high inequality was highlighted in the so-called 'Great Gatsby curve' popularised by Alan Krueger. This captures what appears to be a common-sense notion that, as Andrews and Leigh (2009) put it, "Moving from rags to riches is harder in more unequal countries". However, much of the evidence put forward to support it in practice (including the Great Gatsby curve itself) is based on comparing countries at a point in time, to see whether low inequality and high mobility go together and vice versa. Since countries also differ in many other respects than their inequality levels, in ways that could also affect mobility, drawing strong conclusions from such a comparison is problematic. Seeing what happens to mobility as inequality increases markedly is a more promising route to identifying its distinct effects, but so far evidence of that sort is scarce, and findings also depend on whether mobility is being assessed in terms of earnings/incomes or class position.

Another concern about increasing inequality of particular relevance here is that it erodes trust in institutions and in others, with serious consequences for community life and for politics as solidarity is undermined. While the evidence suggests that declining levels of trust have indeed been observed for many countries, this does not appear to be robustly related to increasing inequality (e.g. Stein and Lancee, 2011, Olivera, 2012). Solidarity, in the sense of concern for and willingness to help others, has been seen in some studies as negatively related to inequality, though that relationship is not strong and a variety of other factors appear to be at work (e.g. Paskov and Dewilde,

2012). increasing inequality is strongly related to trends in poverty measured vis-à-vis relative income thresholds, but much less so when poverty is thought of in 'absolute' terms. Similarly, the extent and patterning of deprivation is much more strongly related to how average household income varies than to summary measures of inequality, though in some countries where mean income fell sharply in the economic crisis the impact on the poor was exacerbated by rising inequality.

As far as political processes are concerned, higher inequality is commonly associated with lower civic participation and lower voting turnout among poor. It is also reasonable to expect that increasing concentration of income and wealth enhances the political influence of the rich, though the ways in which this makes itself felt are often hard to observe. On reactions to increasing inequality itself in the political domain, survey evidence suggests that the extent of discontent with inequality has increased as inequality rose, but only moderately - at least until recently. This is because the extent of increasing inequality may not be not fully recognized by voters, because there is some increase in the acceptability of higher inequality, and because inequality may be less 'salient' for voters than other issues.

Inequality has been seen in commentary as a central driving force in the UK referendum vote to leave the EU, in the rise of 'populist' or protest parties across Europe, and in the election of Donald Trump as US president. In-depth research to examine these claims is emerging, but suggests a more nuanced picture. In the UK case, income inequality has not in fact risen markedly in the last 15 years, having increased very sharply in the Thatcher era. The long-term effects of the de-industrialisation this involved, a slowdown in income growth from the early 2000's, the impact of the crisis and post-crisis austerity measures on living standards, and the scale of immigration from 2004 may all have played a role. Localities more exposed to trade with China voted more strongly in favor of leaving EU It is striking that education level appears the most consistent single predictor of how people voted in the Brexit referendum, straddling economics, demographics and culture.

In a similar vein, studies of the rise of support for populist parties across Europe assign differing weights to the role of inequality *per se*, economic insecurity, and cultural factors. The definition of populism itself is rather fluid; as the Economist magazine pointed out in 2016, current usage can encompass militarists, pacifists, admirers of Che Guevara or Ayn Rand; tree-hugging pipeline opponents or drill-baby-drill climate-change deniers. Populism is commonly regarded as combining an anti-establishment perspective with authoritarianism and nativism (see for example Mudde, 2007). It sees common people as exploited by a privileged elite, and seeks to address this, perhaps via a charismatic leader appealing to the masses and sweeping aside existing institutions. This is clearly difficult to implement empirically in studying voting behaviour.

The influential study by Inglehart and Norris (2016) uses 2014 Chapel Hill Expert Survey to identify the ideological location of political parties in 31 European countries. On this basis it finds that votes for populist parties across many countries has roughly doubled in recent decades. It then employs pooled European Social Survey data from 2002-2014 to examine who votes for populist parties. It finds that socio-economic variables have some explanatory power, but much less than cultural attitudes. Economic insecurity plays a role, but explains less of the rise in support for populist parties in Europe than cultural backlash – "retro reaction by once-predominant sectors to progressive value change". The fact that support for populist parties has risen in countries where inequality has been fairly stable over time (such as Austria and France) as well as ones where inequality has risen, and in countries where income growth has been quite robust (such as Poland) as well as ones where median incomes have stagnated, illustrates the complexity of the factors at work. This is highlighted by the differing political reactions to particularly severe crises in the Great Recession in Ireland, Portugal, Greece and Spain.

In the USA, such "retro reaction by once-predominant sectors to progressive value change" has also clearly played an important role alongside rising inequality and stagnating real incomes for much of the distribution over a long period. The white working-class population whose livelihoods have been negatively affected through decades in which US economy shed manufacturing provide the core constituency supporting Donald Trump, but economic dysfunction combines with cultural and demographic factors in a way that makes them very hard to disentangle. There is some recent evidence of specific effects of globalisation on political outcomes in the case of the 'China shock' import penetration. Autor, Doorn, Hansen and Majesi (2016) find that congressional districts exposed to these imports disproportionately removed moderate representatives from office in 2000s and replaced them by more extreme candidates. Their high-profile conclusion is that Hillary Clinton would have been won Michigan and Wisconsin if the trade shock from Chinese imports had been 25% smaller, and would have won Pennsylvania and the presidential election if it had been 50% smaller. While those are striking conclusions, it is not clear what such a counterfactual would have actually looked like, and in such a close election many other – and more marginal – potential differences would have been enough to change the result. More generally, though, in the US

case it does appear that adverse economic conditions drive support for nativist politicians, and opportunistic politicians then employ strategic extremism to spur participation among core supporters. At the same time, rising inequality and changes in campaign financing regulations have served to increase the influence of the wealthy on political campaigns and on the behaviour of those elected.

5. CONCLUSIONS

Rising inequality in income and wealth is now centre-stage, not least due to the impact it is perceived to have on political behaviour and the support for populist parties. The 'grand narrative' that a sustained rise in income inequality is driving a 'revolt against the elites' probably comes closer to reflecting the experience of the USA than many other rich countries, but is not the whole story even there. However, it does provide one of a variety of reasons to focus on policies and strategies to halt or reverse the rise in income and wealth inequality and promote inclusive growth. A central message from analysis of the forces driving rising inequality is that policy matters: "the particular institutions and policies in place in an individual country at a particular point in time have a profound impact on the extent and nature of (those) inequalities and their societal significance" (Salverda et al., 2014, p. 3). As the recent book by the leading economic scholar of inequality over the last half-century puts it, "I do not accept that rising inequality is inevitable: it is not solely the product of forces outside our control. There are steps that can be taken by governments, acting individually or collectively, by firms, by trade unions and consumer organisations, and by us as individuals to reduce the present level of inequality." (Atkinson, 2015, p. 302).

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