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Wellbeing and Inequality

How using subjective measurement helps quantify the case for equality

The Challenge of Economic Inequality

June 2014

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4.4%

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- Redistribution is good for wellbeing
- Growth is sometimes good for wellbeing
- *If* redistribution reduces growth, how much growth is it worth sacrificing to get it?

Standard economic theory posits an optimum level of inequality

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- There is declining marginal utility of income
- Therefore other things being equal, utility is maximised when incomes are equal
- But other things are not equal
  - Incentives needed to stimulate the economy and make it grow
  - A growing economy needed to generate rising income and jobs
  - Rising income and enough jobs increase utility
- So optimum level of inequality: the marginal gain from incentives (growth) equals the marginal gain from redistribution

But where is this optimum level?

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- The numbers are disputed…
- …creating space for the following assumptions
  - We need to maximise GDP growth
  - The existing level of inequality is justified since it is needed to achieve this
- The subjective wellbeing evidence helps counter this
- *In principle* we can say: *this* level of inequality is only justified if it produces *that* increase in GDP
- Or *this* level of redistribution is worth it even if we have to lose *that* amount of GDP

What the evidence tells us – and doesn't tell us

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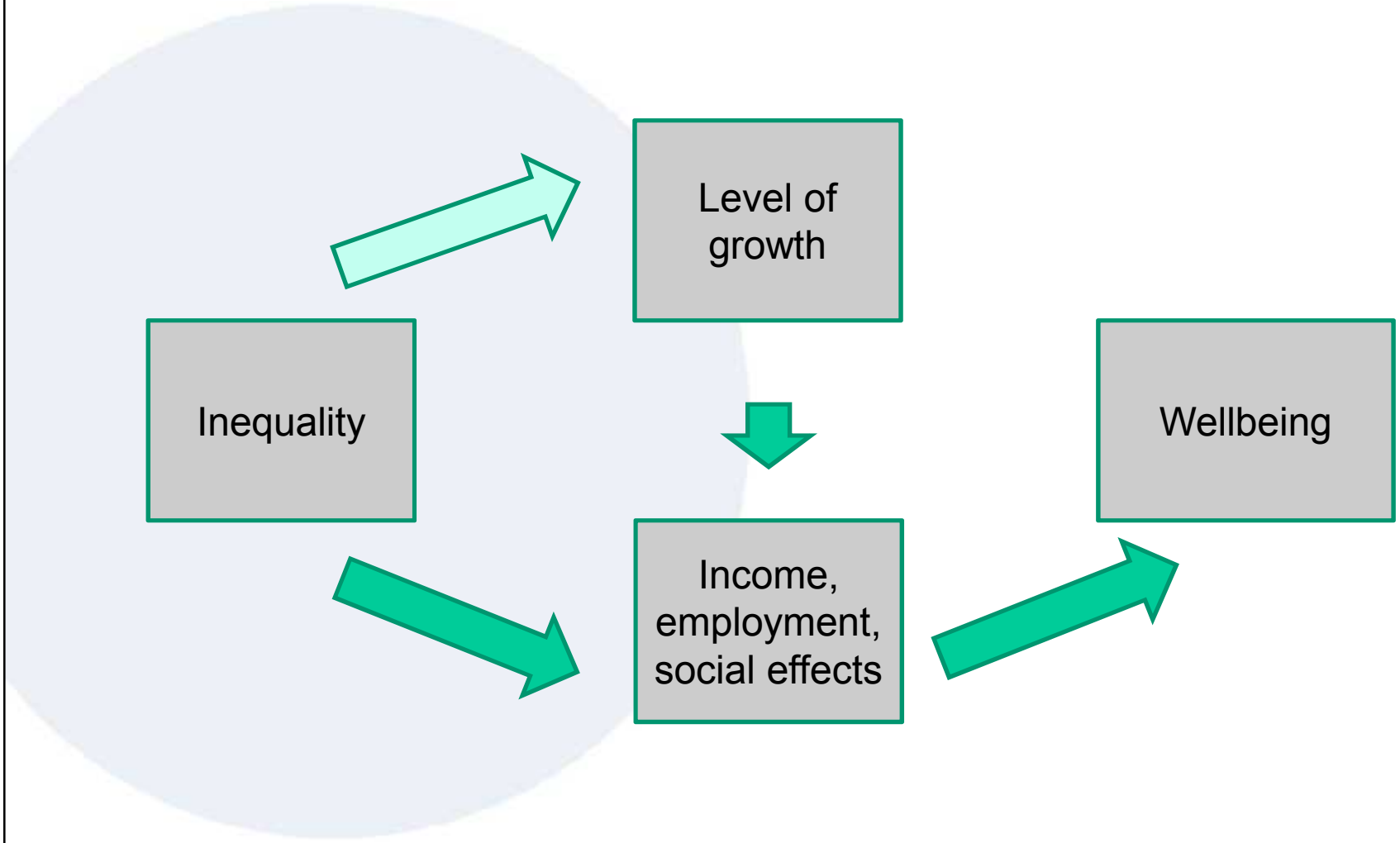
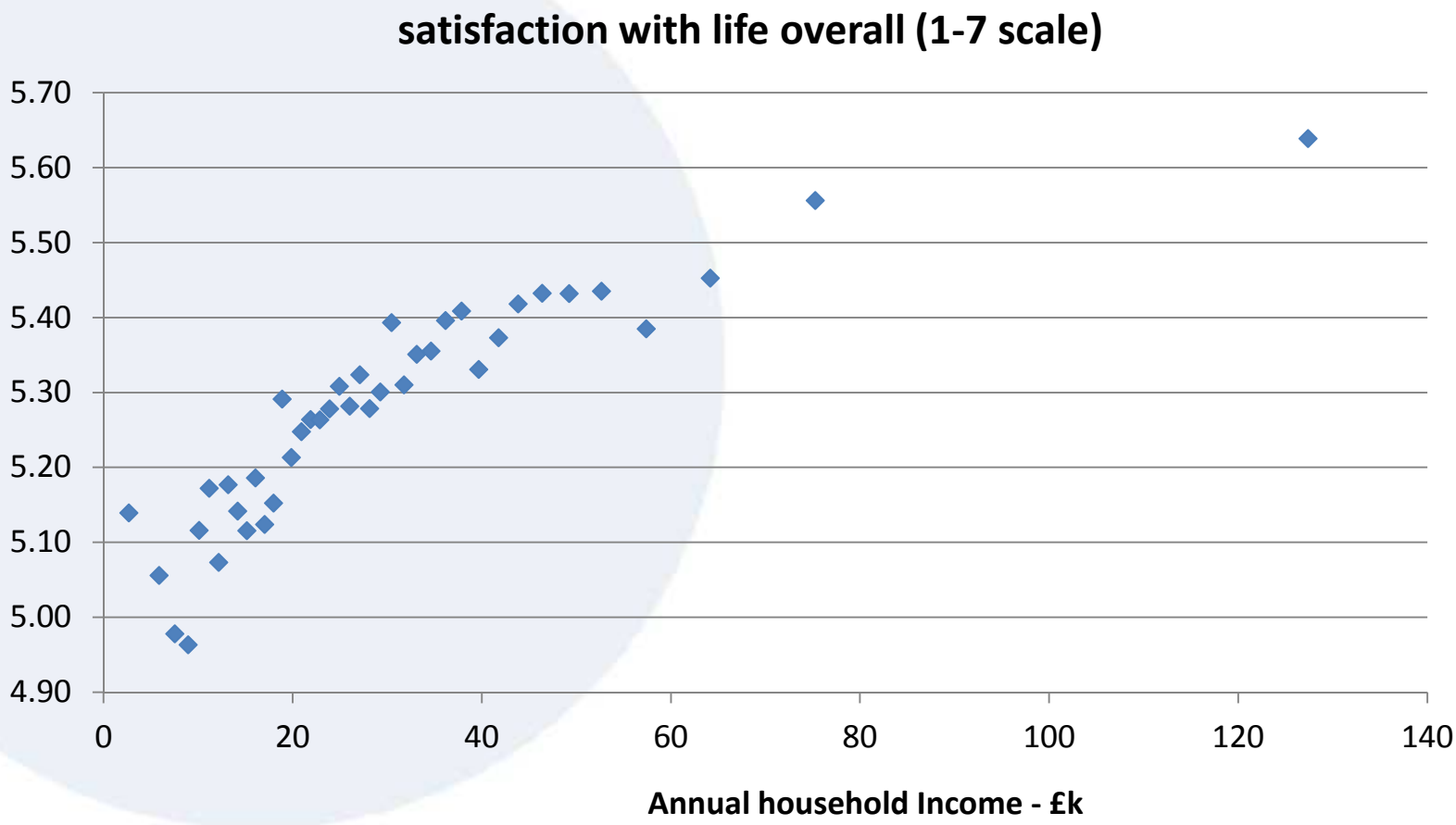


The evidence tells us about the impact of income on wellbeing



Understanding Society Survey, 2009-10

…and thus the impact of inequality and growth on wellbeing

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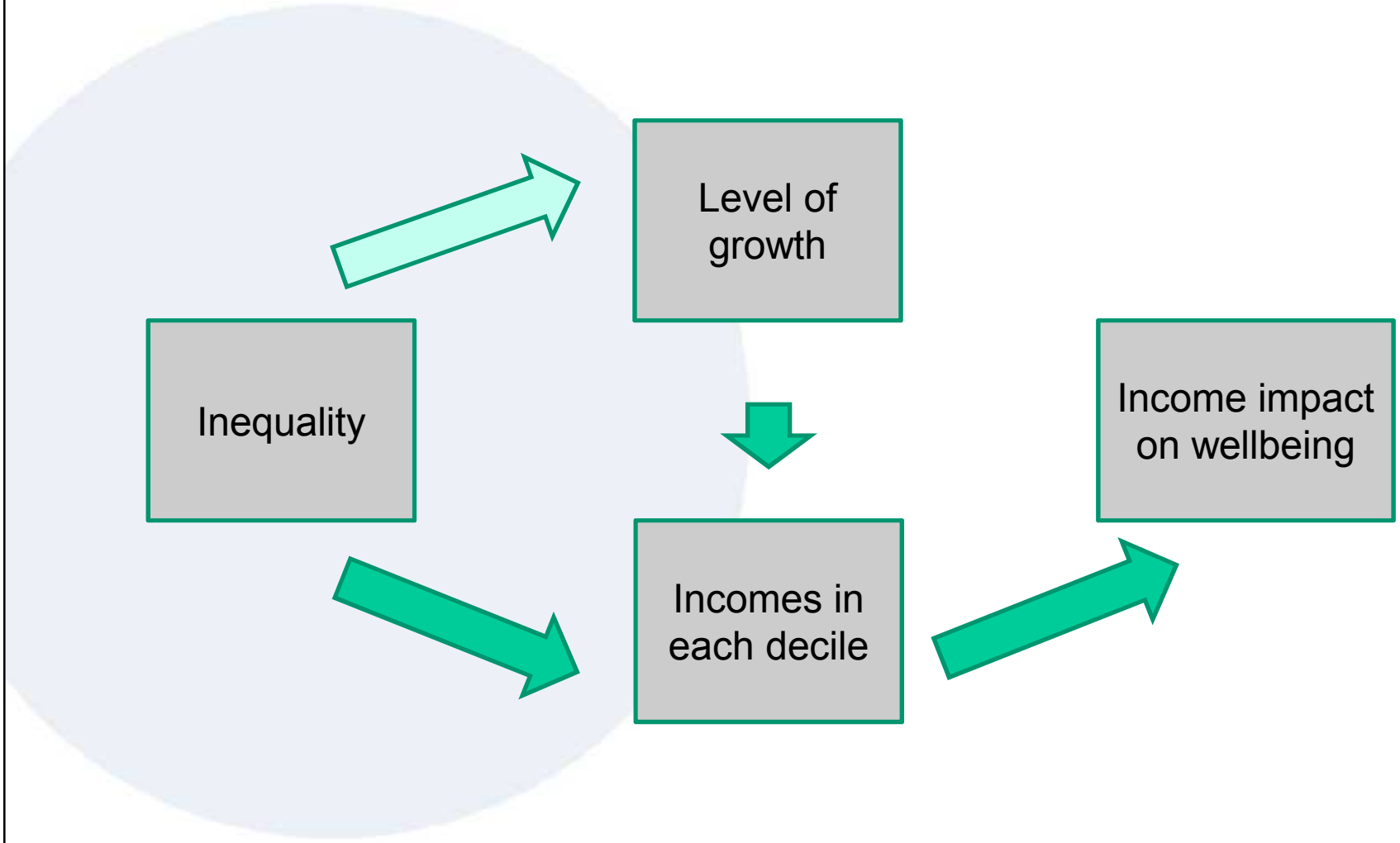

Growth, unemployment and wellbeing are also related

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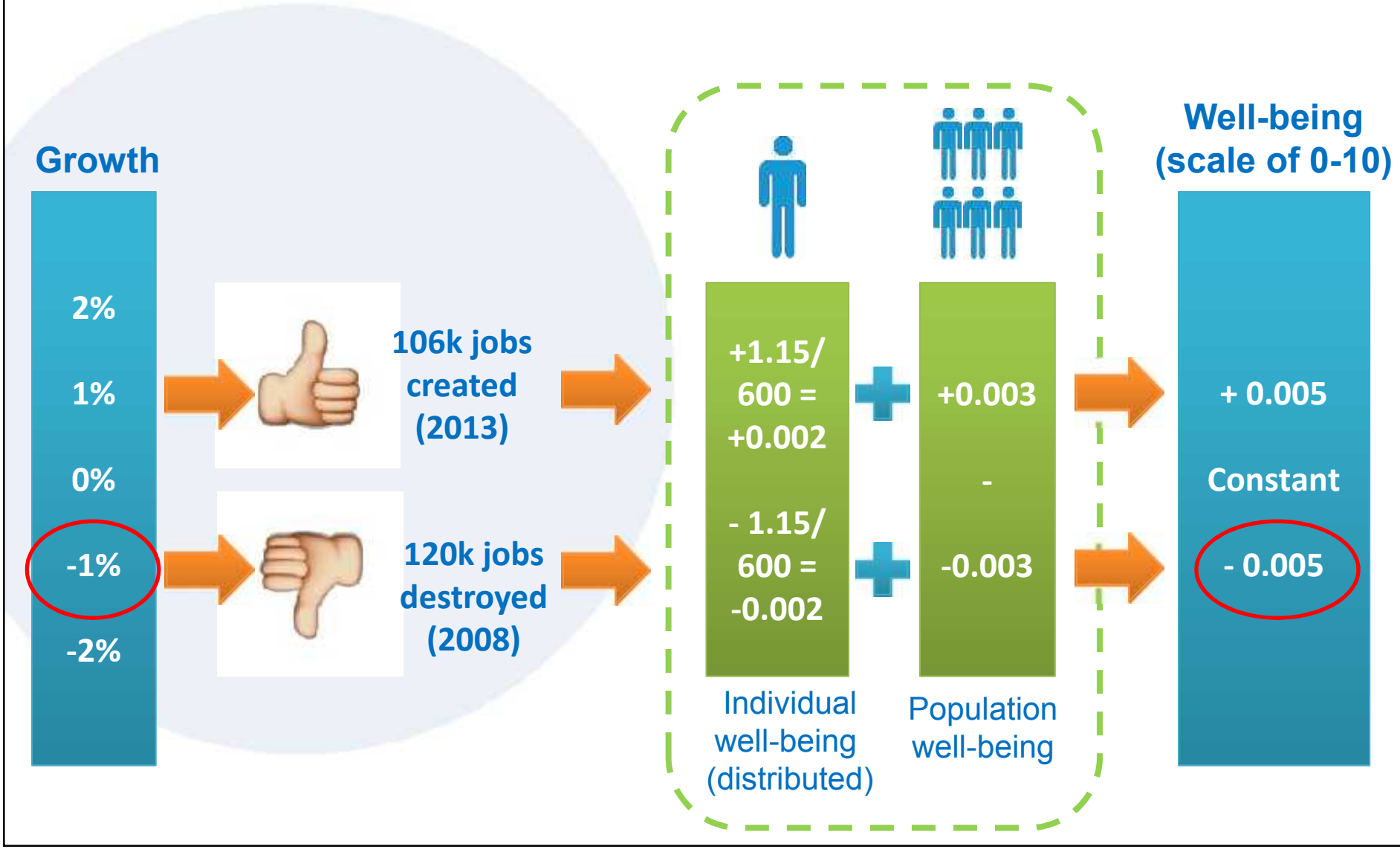

…so there is another impact of growth on wellbeing

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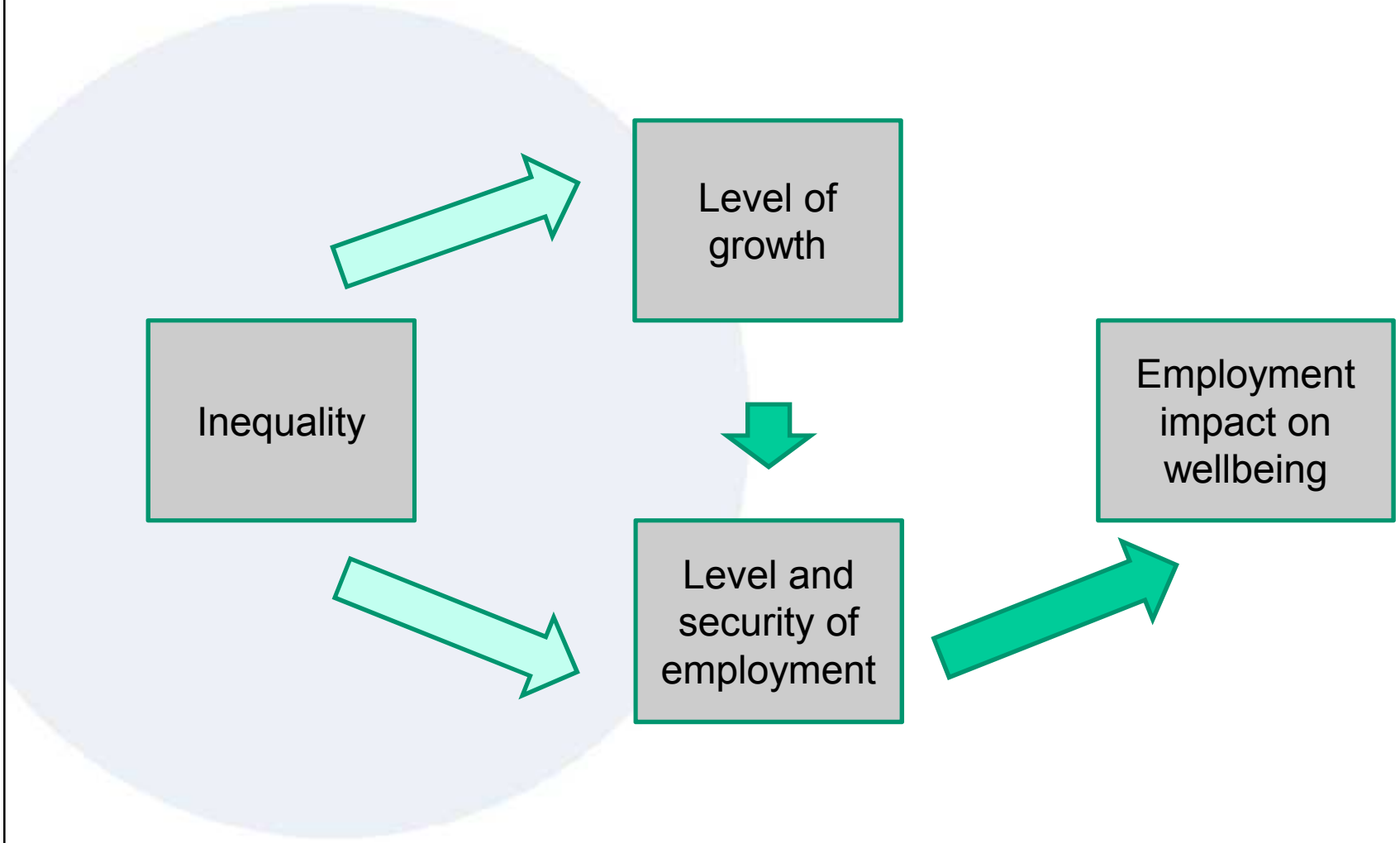

Inequality has societal effects too

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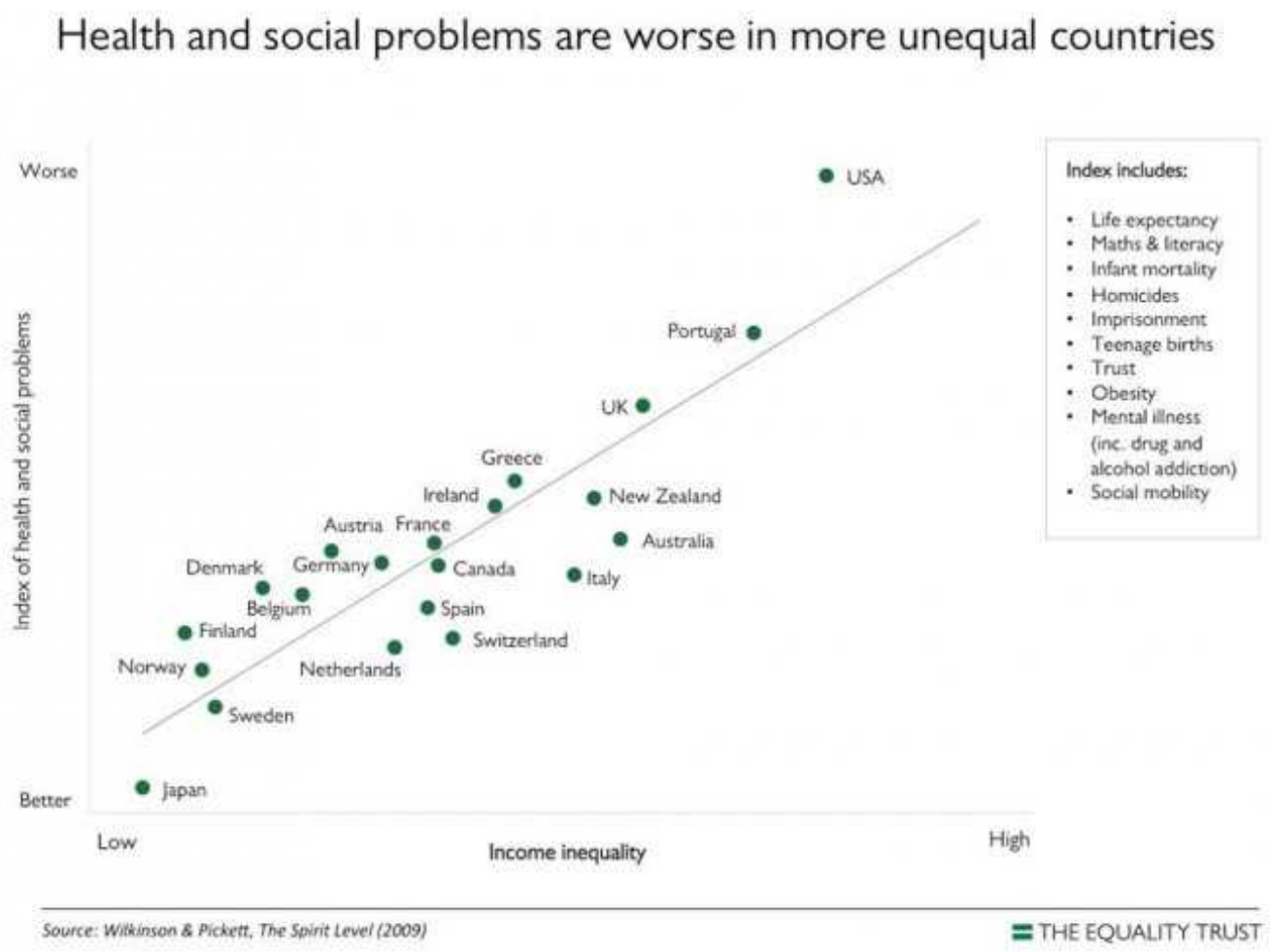
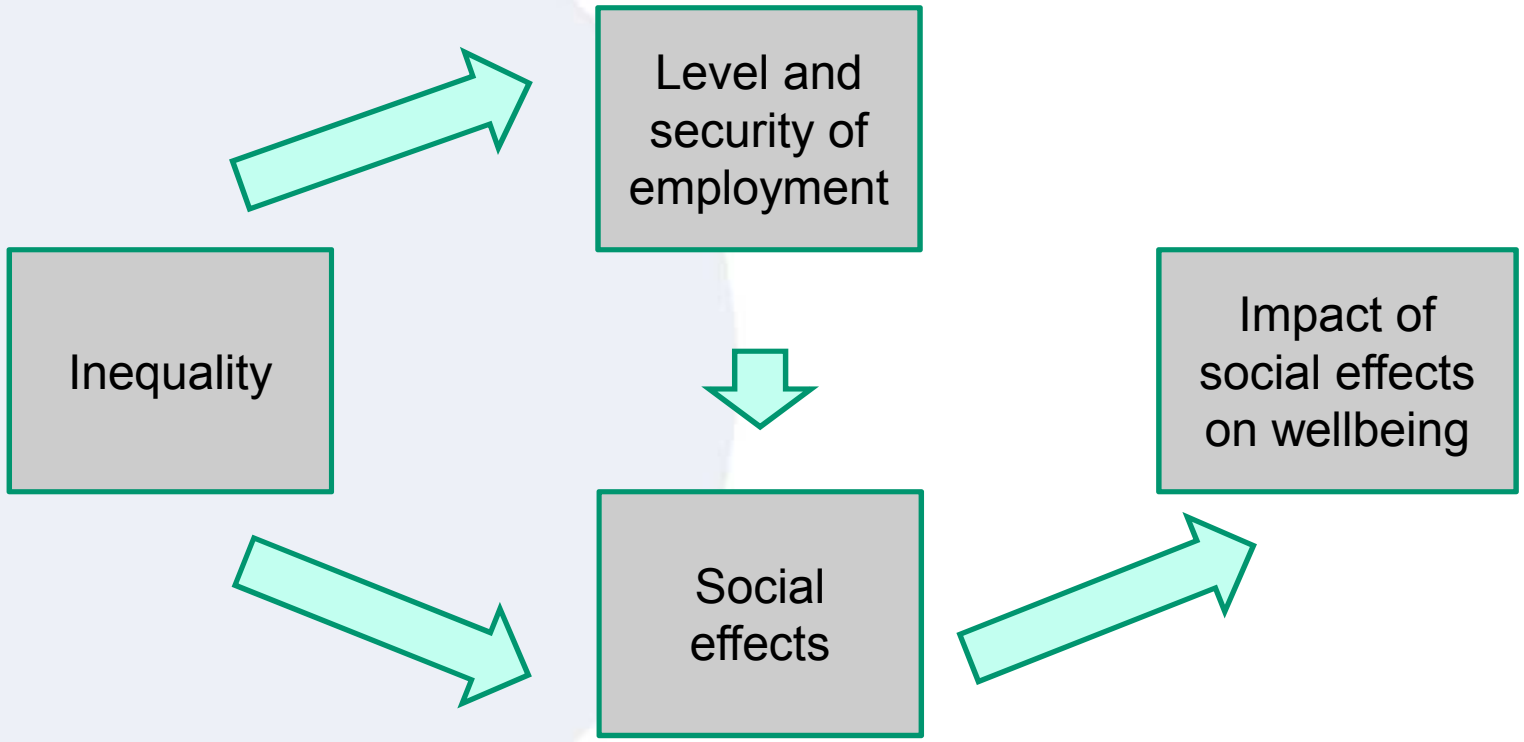


…and these have a separate impact on wellbeing



Size of problem varies by decile so regression needed to avoid double counting - ignored for today

So we can use this evidence to answer some questions

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- Imagine half the difference between the income of top 10% and next 10% was redistributed to bottom 30%
- What would the income effect on wellbeing be?
  - Ie the increase in wellbeing for the bottom 30% less the loss of wellbeing for the top 10%
- How much damage to GDP would there have to be to cancel this out?
  - via the income and employment effects
- Is this plausible?

An *illustrative* answer based on UK numbers

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- Excluding social impacts the answer is 4.4% once off
- Note this numbers would be higher if
  - We had included social impacts
  - We had not assumed (incorrectly) that the proceeds of growth are spread evenly across the population
  - We had ignored some of the controls in assessing income effects
  - the money was targeted on factors with more impact on wellbeing than income (eg reducing unemployment, public health, support for the disabled)
  - we had weighted the wellbeing impacts on the least well-off relatively heavily – either because they are least likely to adjust (Easterlin paradox) or for social justice reasons

What does this mean?

- So it would be worth sacrificing at least 4.4% of GDP to achieve this re-distribution, almost certainly more
- If we sacrifice less than this, we are net gainers
- Is it plausible that the level of redistribution described will reduce GDP in this way?
- If not, can we do more in subsequent years?

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Thank you

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