



## UvA-DARE (Digital Academic Repository)

### Income and inequality

Keune, M.

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## 4. INCOME AND INEQUALITY

The Lisbon Strategy includes among its overall objectives the fight against poverty and for greater social cohesion in Europe. Indeed, heads of state committed themselves under the Lisbon umbrella to make a decisive impact on the eradication of poverty and social exclusion by the year 2010. Key policy areas for achievement of these objectives are social, labour market and wage policy. Traditionally, these policy areas fell largely outside the scope of European-level policymaking, remaining predominantly subject to national decision-making powers. Over time, however, the competences of the Community in the social area have been gradually expanded, especially – initially – with regard to issues like equal treatment, health and safety and the free movement of workers and – more recently – in relation also to the portability of certain welfare entitlements (Goetschy 2006; Keune 2008a). While a large number of directives have by now established European regulations in these areas, these do not cover traditional core social policy areas (income redistribution and social protection) or employment or wage policies. Since 1997, however, an increasing number of such areas have indeed been tackled at the European level, not through legislation but by means of the Open Method of Coordination (OMC), a multi-level process entailing bench-

marking, multilateral surveillance, peer review, exchange of information, cooperation and consultation. This new approach started with the introduction of the European Employment Strategy in 1997 (see Chapter 3) and, in subsequent years, under the Lisbon Strategy, the OMC was also introduced into other areas including social inclusion (as well as health care, pensions and education and training). Though actual policymaking in these areas continues to take place at the national level, the European level in general, and the Lisbon Strategy in particular, increasingly play a ‘soft’ role in terms of coordination, benchmarking and the dissemination of best practices.

At the same time, in the economic field, the deepening of the Internal Market and EMU have been advancing under the Lisbon Strategy. Here the process has included numerous and frequent instances of hard regulation, and much sovereignty in this field has been transferred from the member states to the European level. This has substantially limited the range of policy instruments available to national policymakers, particularly where monetary and budgetary policies are concerned, and has restricted their control not only over their economies, but – more importantly for this chapter – also over their welfare states and labour markets (Scharpf

2002). Pressure is now being exerted, for example, on welfare state expenditure and in favour of wage moderation, the latter being further strengthened as a result of increased capital mobility and regime competition.

The Lisbon Strategy has, accordingly, been of importance for developments in poverty and inequality but its impact has been indirect and difficult to pinpoint. Indeed, no clear or single causal relationship exists between the two, and whatever relationship does exist must be expected to differ from one country to another. The ambition of this chapter is therefore rather more modest. We will examine the development of a number of income, poverty and wage indicators to see whether or not they have improved in the Lisbon period and whether the objective of greater social cohesion both within and across countries has been achieved.

### Themes

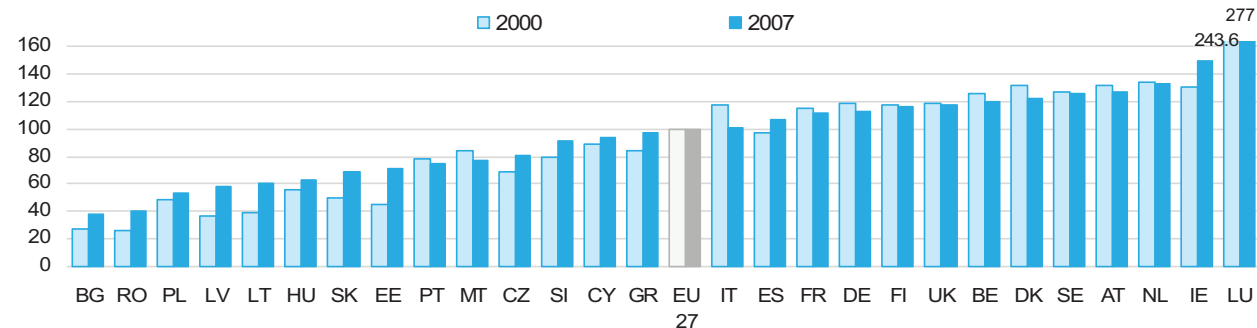
- 4.1. Income differences across Europe
- 4.2. Income inequality and poverty
- 4.3. Working poverty
- 4.4. Wage share and real compensation
- 4.5. Minimum wage
- 4.6. Conclusions

## 4.1. Income differences across Europe

### Limited convergence

Where social cohesion across Europe is concerned, the situation can, to a significant extent, be expressed by means of income differences between countries. Figure 4.1 provides income figures, expressed in GDP per capita in purchasing power standards (PPS) related to the EU27 average for 2000 and 2007. The figure clearly shows that income differences across countries have decreased in this period, signifying an improvement in cross-country social cohesion. Of the 14 countries with an income level below the EU27 average in 2007, 12 had improved their average position since 2000, while only two (Portugal and Malta) were further below the average at the end than at the beginning of this seven-year period. Particularly strong 'catching up' took place in the Baltic countries, as well as Slovakia, the Czech Republic and Greece. At the same time, 10 of the 13 countries with income levels above the EU27 average saw their relative position worsen in these seven years. The biggest relative declines were experienced by Italy (-15.7 percentage points) and Denmark (-9.2 percentage points). In the case of the richest two EU countries, Ireland and Luxembourg, the gap between themselves and the rest of the EU has – counter to the general trend towards income convergence – widened during this period. It should be noted, however, that, in spite of this overall trend towards convergence, income differences within the EU are still wide and will no doubt remain substantial for decades to come.

Figure 4.1: GDP per capita in PPS, 2000-2007 (EU27=100)



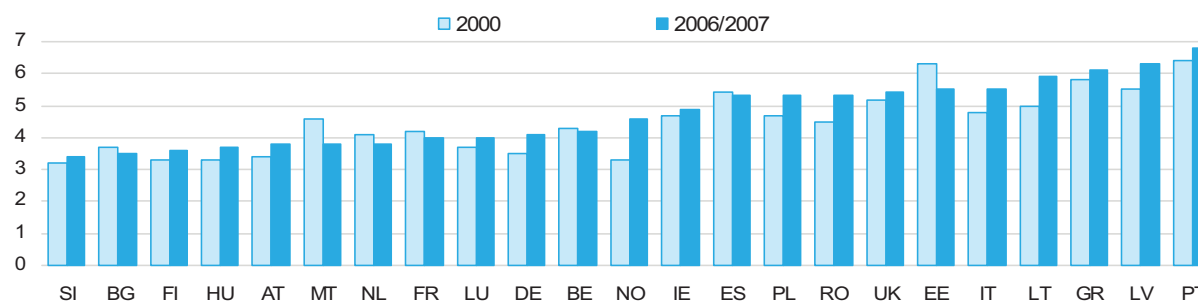
Data source: Eurostat (2008c). Note: The volume index of GDP per capita in Purchasing Power Standards (PPS) is expressed in relation to the European Union (EU-27) average set to equal 100. If the index of a country is higher than 100, this country's level of GDP per head is higher than the EU average and vice versa. Basic figures are expressed in PPS, i.e. a common currency that eliminates the differences in price levels between countries.

## 4.2. Income inequality and poverty

### Increasing inequality

Whereas income differences among EU countries at large have been (slowly) decreasing in the Lisbon era, the picture concerning income differences within each country taken separately is much more diverse. Figure 4.2 shows that, when the income of the richest 20% of the population is compared with that of the poorest 20%, in the majority of countries (16 of the 23 countries represented in the figure) the income difference between the richest and the poorest increased between 2000-2006/07, while decreasing in only seven countries. Substantial decreases in inequality (more than 0.5) can be observed only in Malta and Estonia (0.8 in both cases) while substantial increases have taken place in Germany (0.6), Poland (0.6), Italy (0.7), Latvia (0.8), Romania (0.8) and Lithuania (0.9). Hence, in the majority of countries, intra-country social cohesion, as measured by income inequality, is worsening rather than improving.

Figure 4.2: Inequality of income distribution (80/20 income quintile share ratio), 2000-2006/07



Data source: Eurostat (2008c). Note: The S80/S20 income quintile share ratio is the ratio of equivalised total disposable income received by the 20 % of the country's population with the highest income (top quintile) to that received by the 20 % of the country's population with the lowest income (lowest quintile). The higher the ratio, the wider is the gap between the most (top 20 % quintile) and least well-off (bottom 20 % quintile). Note: LV, LT, LU, HU, MT, AT, and PL are 2007; all others are 2006. Note: Eurostat does not provide data for the early 2000s on this indicator for CY, CZ, DK, SE and SK.

## 4.2. Income inequality and poverty

### No improvement in poverty

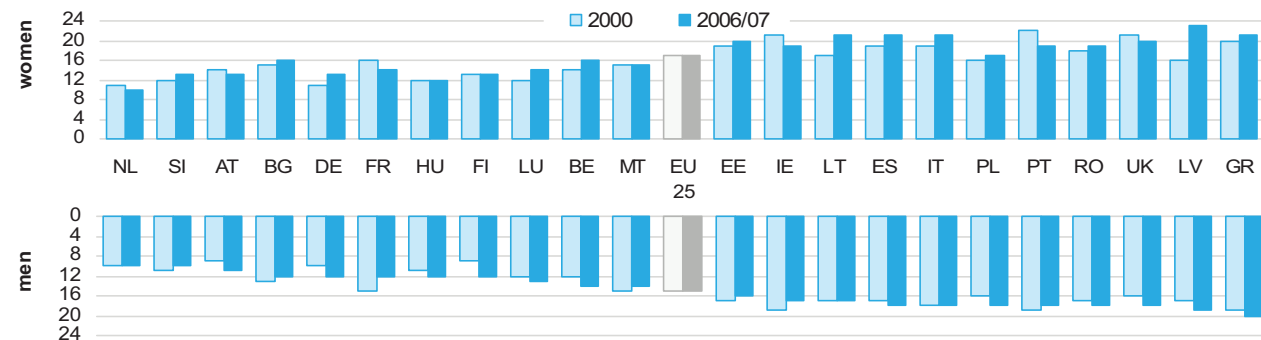
A different way of considering inequality is by looking at poverty data which indicate the percentage of the population with an income lower than 60% of the national median. Figure 4.3 provides these data by gender. One finding that is evident from this figure is that between 2000 and 2006/07, on average, the poverty levels for men and those for women have, in both cases, remained stable. This means, on the one hand, that no improvement in overall poverty levels has been achieved and, on the other, that women have preserved their disadvantage, as compared to men, in relation to poverty, since, in overall terms, female poverty is still 2 percentage points higher than male poverty. In other words, no progress is being made, under the Lisbon Strategy, in relation to the objectives of reducing poverty and strengthening (gender) equality.

In this respect there exist, however, major differences between countries. First of all, in some countries, which include the Netherlands, Slovenia, Germany and Finland, overall poverty levels are comparatively low, whereas in Latvia, Lithuania, Greece, Italy and Spain they are high. Secondly, there are important changes over time. For example, during the period expressed in the figure, while overall poverty

declined substantially in France and Portugal (-3 percentage points in both cases), it increased substantially in Germany and Latvia (+3 and +5 percentage points respectively). In another eight countries, the level of poverty changed, whether upwards or downwards, by as much as two percentage points in this relatively short period. Thirdly, poverty developments of men and women are the same, or at least similar, in most countries, but not everywhere, since in Lithuania and Latvia female poverty is increasing much faster than male poverty, while in Austria, Finland and the UK male poverty is on the rise and female

poverty is either declining or stable, thus reducing the gender gap in relation to poverty.

Figure 4.3: At-risk-of-poverty rate by gender, 2000-2006/07



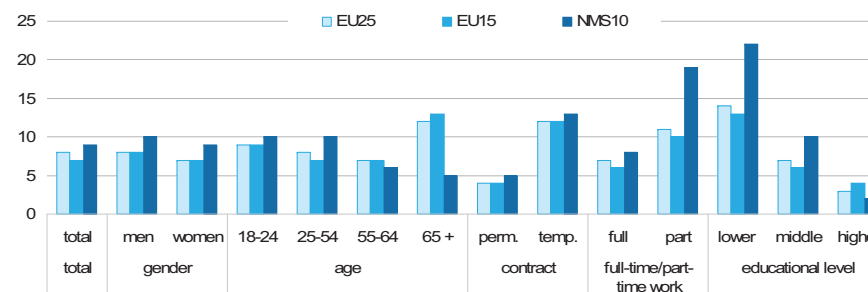
Data source: Eurostat (2008c). Note: The cut-off point for the at-risk-of-poverty rate is 60% of median equivalised income after social transfers. Note: LV, LT, LU, HU, MT, AT and PL are 2007; all others are 2006. Note: Eurostat does not provide data for the early 2000s on this indicator for CY, CZ, DK, SE and SK.

## 4.3. Working poverty

### Wages are not always enough

One of the reasons why poverty is not diminishing in Europe is that wages and salaries are not always adequate to raise working people and their households above the poverty threshold (cf. Marx and Salverda 2005). In the EU25, 8% of working people are also poor; in the EU15 working poverty affects 7% of the employed population, and in the NMS10 this figure is slightly higher at 9% (Figure 4.4). Not all employed populations are affected by working poverty to the same extent, however. In the EU15 working poverty is slightly higher among men than among women. It is higher than average among young workers and the difference is even more pronounced among the population aged 65 and over. Working poverty also disproportionately affects those employed on temporary and part-time contracts, and it is much higher for employed persons with lower educational levels than for the rest of the employed population, especially in the NMS10 (Peña-Casas and Latta 2004 for a detailed study of working poverty).

Figure 4.4: In work at-risk-of-poverty rate after social transfers, 2006



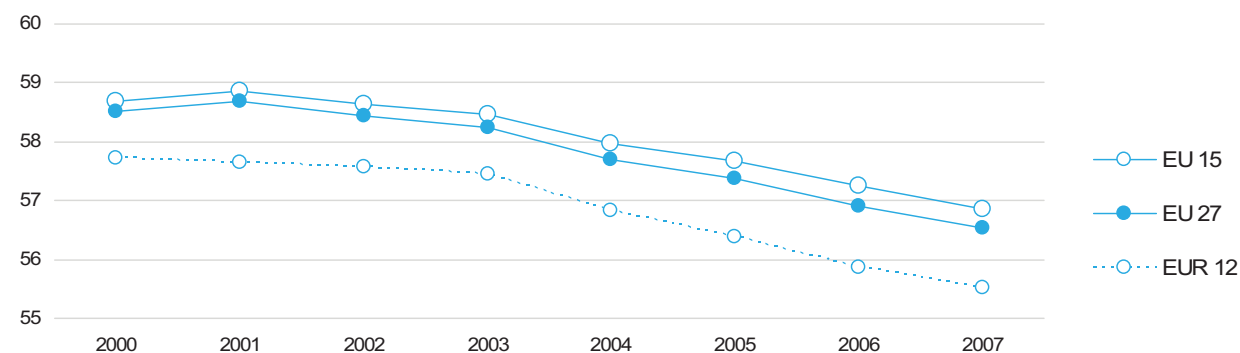
Data source: Eurostat (2008c). Note: The cut-off point for the at-risk-of-poverty rate is 60% of median equivalised income after social transfers.

## 4.4. Wage share and real compensation

### Wage share shows steady decline

Important developments have also taken place in the distribution of income between labour and capital in the Lisbon era. This is shown by the developments in the wage share, i.e. the share of GDP represented by wages and employers' social contributions. Between 2000 and 2007, the adjusted wage share in the EU27 declined by 2 percentage points, from 58.5% to 56.5% (Figure 4.5). For the Euro area this decline was slightly stronger and amounted to 2.2 percentage points. These developments are not, however, specific to the Lisbon period but are the continuation of a longer-term trend. The level and the development of the wage share depend, first of all, on the extent to which productivity improvements are reflected in wage growth. Hence, the decline of the wage share reflects, to a major extent, the fact that wage growth in the EU lags structurally behind productivity growth (Keune 2008b). It is also influenced, however, by other factors, including job creation and the types of job created, the incidence of part-time work, the extent of the informal sector and informal payments, regulations on social contributions, and so forth.

Figure 4.5: Adjusted wage share 2000-2007



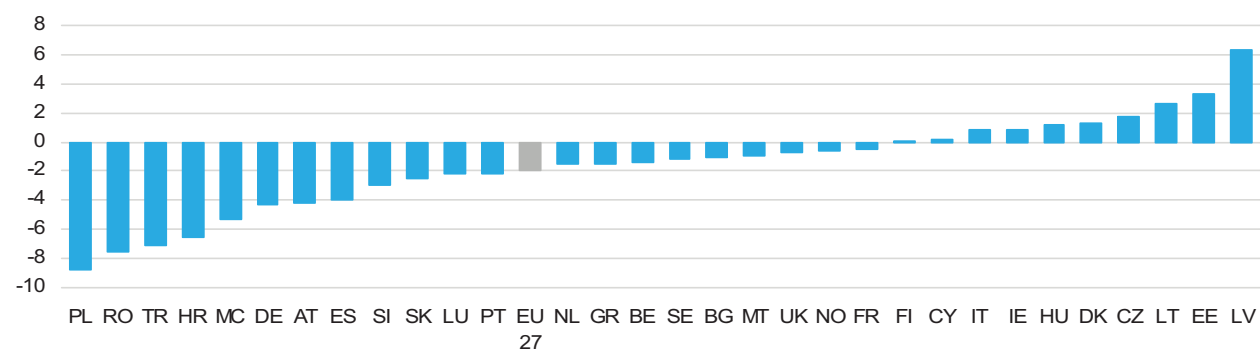
Source: AMECO. Note: Data refer to compensation (i.e. wages and employers' social contributions) per employee as percentage of GDP at market prices per person employed.

## 4.4. Wage share and real compensation

### Major differences between countries

At the country level, the picture is again extremely mixed (Figure 4.6). While the wage share declined in a majority of European countries, in nine countries, including, in particular, the Baltic states, it showed an increase. All of the nine countries in question, with the single exception of Italy, are small countries. The largest declines in this respect were to be seen in Poland, Romania and Turkey, where they amounted, on average, to one percentage point per year or more. In Europe's biggest economy, Germany, as well as in Spain and Austria, the decline exceeded, on average, 0.5 percentage points per year.

Figure 4.6: Change in wage share, 2000-2007 (percentage points)



Source: AMECO. Note: Data refer to compensation (i.e. wages and employers' social contributions) per employee as percentage of GDP at market prices per person employed.

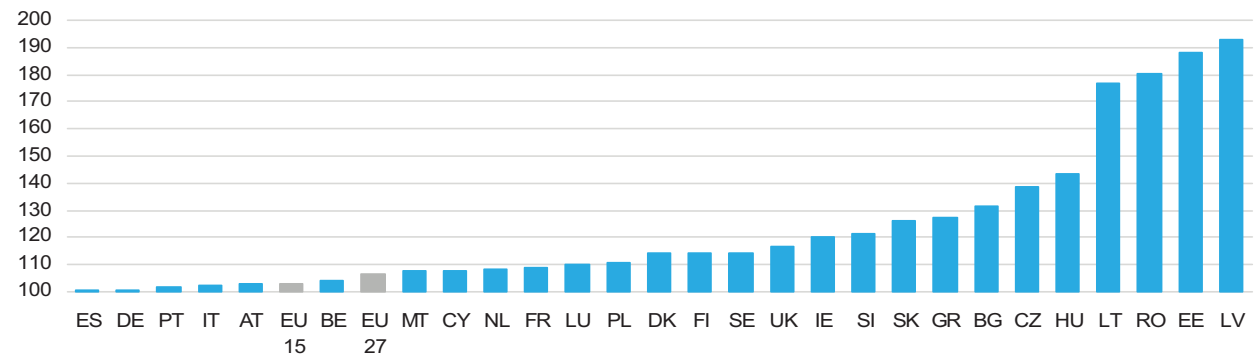


## 4.4. Wage share and real compensation

### Wage moderation is the norm

The declining wage share is, as mentioned above, significantly related to wage moderation. In the 2000-2007 period, real growth of compensation (i.e. wages and employers' social contributions) was 6.5% for the EU27, less than 1% per year (Figure 4.7). Real growth in compensation was highest in the new member states and Greece, and in particular in the Baltic States and Romania where it was above 175%. Growth in real compensation has been particularly slow in most of the Euro countries (exceptions being Greece, Slovenia, Slovakia and Ireland) and particularly low in both Spain and Germany where, in these seven years, it has increased by less than 1%. These diverging developments in real compensation growth are one important explanatory factor for the only limited convergence in general income levels across Europe discussed earlier in this chapter. At the same time, little improvement can be seen in the gender wage gap, which remains at 15% in 2006 for the EU27, down only one percentage point compared to the start of the Lisbon era.

Figure 4.7: Real compensation 2000-2007 (2000=100)



Source: AMECO. Note: compensation refers to wages and employers' social contributions.

## 4.5. Minimum wage

### Limited convergence again

A final indication of limited convergence across Europe comes from data on the minimum wage (Figure 4.8). In general terms, it can be observed that the minimum wage, expressed in purchasing power standards (PPS), has been increasing between 2000 and 2008 in those countries where it was lowest in the starting year. The minimum wage (in PPS) in the NMS increased between 1.5- and 4.3-fold during this period, while among the EU15 countries only in Spain did it increase by as much as 1.5-fold, all other countries having experienced lower growth in this respect. Still, in 2008, the differences between countries remain striking. In the Czech Republic or Poland, for example, the figures are double that for Romania, while in six EU15 countries the value of the minimum wage is more than twice what it is in the Czech Republic and Poland. Moreover, as discussed above, the fact that a minimum wage exists does not prevent a substantial percentage of the employed population from living in poverty (for a discussion of the minimum wage in Europe see Schulten *et al.* 2006).

**Figure 4.8: Monthly minimum wages in purchasing power parities**

|    | 2000 (first half) | 2008 (second half) | change |
|----|-------------------|--------------------|--------|
| RO | 54.0              | 231.8              | 4.3    |
| BG | 101.9             | 245.0              | 2.4    |
| LV | 155.5             | 351.3              | 2.3    |
| SK | 258.3             | 381.0              | 1.5    |
| LT | 225.3             | 388.0              | 1.7    |
| EE | 190.4             | 390.0              | 2.0    |
| HU | 202.7             | 417.8              | 2.1    |
| CZ | 238.0             | 460.3              | 1.9    |
| PL | 296.9             | 469.3              | 1.6    |
| PT | 505.4             | 588.0              | 1.2    |
| SI | 491.5             | 736.4              | 1.5    |
| ES | 499.8             | 752.7              | 1.5    |
| GR | 634.1             | 768.0              | 1.2    |
| MT | 688.3             | 837.0              | 1.2    |
| IE | 846.6             | 1159.9             | 1.4    |
| UK | 850.7             | 1182.9             | 1.4    |
| FR | 980.5             | 1238.6             | 1.3    |
| BE | 1035.5            | 1267.8             | 1.2    |
| NL | 1048.3            | 1316.1             | 1.3    |
| LU | 1180.4            | 1531.9             | 1.3    |

Source: Eurostat (2008d). Note: EE and SK: 2000=2002

## 4.6. Conclusions

### The Lisbon Strategy has not achieved its objectives

The fight against poverty and for greater social cohesion in Europe is one of the key objectives of the Lisbon Strategy. From the data presented in this chapter it emerges that, when average data for countries are compared, there is limited convergence across Europe; in other words, differences between countries, in terms of income, wages and the minimum wage, although they have been decreasing, remain high. Nor is it possible to report much progress within individual countries. In most cases the income differences between the richest and the poorest 20% of the population have increased, poverty has on average remained stable, gender differences in poverty and pay remain significant, having declined only slightly or not at all, and there is a continuing shift of income from labour to capital, expressed in a declining wage share. The limited convergence among European countries can be explained, to a considerable extent, by differing growth rates. The lack of progress in terms of intra-country income differences points rather to the absence of solidaristic social policy, which is indeed conspicuously absent from the Lisbon Strategy, and from policies stemming from European integration in general. Social and wage policies remain nationally dominated but do not work

towards the Lisbon goals, and the OMC type of exercise seems to have exerted little positive influence in this field. What is more, the economic criteria and policies resulting from European integration rather hamper any efforts on the part of national welfare states to make progress in combatting poverty and inequality because they restrict the range of policy instruments available to national policymakers and set serious limits on permissible levels of public debt and budget deficits. The Lisbon Strategy operates along these same lines and has not compensated for this loss of national social policy capacity, either by providing national policymakers with new instruments or by introducing significant social policies at the European level.

# The Benchmarking Group

## Introduction

John Monks, ETUC, General Secretary

Philippe Pochet, ETUI, General Director

Maria Jepsen, ETUI, Director of Research Department

### Chapter 1: Close to ten years of the Lisbon Strategy

Ronald Janssen (ETUC)

ETUI documentation centre

Kathleen Llanwarne, language editor and translation of Chapter 8

### Chapter 2: Has the Lisbon Strategy equipped Europe to become more resilient to the economic crisis?

Béla Galgóczi (ETUI)

Irmgard Pas, ETUI, data-processing manager

Eric Van Heymbeeck, ETUI, layouter

### Chapter 3: Has the Lisbon Strategy contributed to more and better jobs?

Janine Leschke (ETUI)

Janine Leschke, ETUI, senior researcher, coordinator

### Chapter 4: Income and inequality

Maarten Keune (ETUI)

### Chapter 5: Worker participation and the Lisbon Agenda

Bruno Cattero (University of Piemonte Orientale),

Romuald Jagodzinski (ETUI), Norbert Kluge (ETUI),

Isabelle Schömann (ETUI), Michael Stollt (ETUI),

Kurt Vandaele (ETUI), Sigurt Vitols (WZB)

### Chapter 6: Has European social dialogue and social legislation supported the Lisbon Strategy?

Stefan Clauwaert (ETUI), Anne Peeters (OSE),

Isabelle Schömann (ETUI), Wiebke Warneck (ETUI)

### Chapter 7: Does work impact health and how much?

Roland Gauthy (ETUI)

### Chapter 8: What's in the Sustainable Development Strategy for workers?

Christophe Degryse (OSE)

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