Michael Dauderstädt and Cem Keltek

No Progress on Social Cohesion in Europe

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AT A GLANCE

The crisis afflicting Social Europe that has been evident for several years continues unabated. Inequality within countries increased in most member states in 2014, especially in Germany. Cohesion across the EU has made no progress, even if growth in the poorest countries has been somewhat above the EU average. The better off social strata benefit most from rather weak growth overall. Social development remains dire in the Mediterranean countries, where the poorest strata are particularly hard hit by austerity policy.

The latest data for 2014 confirm the worrying trend that has been discernible in the European Union since 2011: income inequality remains stubbornly at the same level it had reached by 2010. It had attained its nadir in 2009, after clear progress in previous years. The S80/S20 ratio, which indicates the ratio between incomes in the richest quintile (fifth) and those in the poorest quintile, was then around 8.5 measured in euros at current exchange rates and 5.6 in terms of purchasing power standard (PPS). Since 2011 the figure has varied between 9 and 10 in euros and between 6 and 7 in PPS (see Figure 1). A minimal rise on 2013 is discernible.

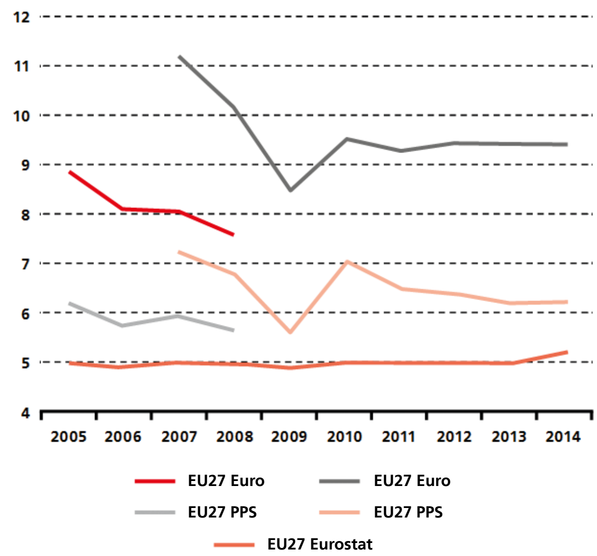
This is markedly higher than the value given by Eurostat for the EU as a whole – around 5 (lowest curve in Figure 1) – in its official statistics. The latter is the average of the S80/S20 ratios of all EU member states without taking into account the enormous income differences between them. It thus considerably underestimates the real income ratio between the richest and the poorest quintile in the EU as a whole. Also with regard to longer term development trends of income inequality (relatively constant since 2005) the EU is thus often wrong. The recent rise from 5 to 5.2 recorded in its official statistics only reflects the growing income inequality within many member states, which, however, tends to be compensated across the EU by the higher growth in the poorer member states.

In order to estimate real inequality across Europe both dimensions have to be taken into account: inequality between and inequality within countries. This is done with the methods used here, which calculates the pan-European quintiles (each of around 100 million people) and their incomes, and comes up with the ratio between them (cf. Table 1).[1]

MULTIDIMENSIONAL INEQUALITY IN EUROPE

For the period for which the latest Eurostat data are available (2014) it is – in contrast to 2013 – primarily income inequality within most countries that has risen.

Figure 1
Development of income inequality in the EU (S80/S20 income quintile ratio)



Source: Eurostat, authors' calculations; PPS = purchasing power standard; for the sake of comparability Croatia was excluded.

Germany – alongside Estonia, Slovakia and the United Kingdom – is among the frontrunners in this respect; the S80/S20 ratio rose by more than 10 per cent (the Gini coefficient rose by 3.4 per cent). On EU average the increases were of 4 and 1.3 per cent, respectively. Because 2014 was the last year before the introduction of a statutory minimum wage in Germany, these poor values may have improved again in 2015. It should also be noted that, despite this above-average rise, the level of inequality in Germany is still slightly below the EU average (Germany: 5.1; EU: 5.2), which is pushed up by the high inequality in southern and eastern Europe, where the S80/S20 values tend to be over 6.

Income inequality *between* countries, by contrast, has been on a downward trend in the EU for years because growth in the poorer new member states from central and eastern Europe was usually stronger than in the richer north-west of the old EU. Although this convergence was not consistent and clearly discernible, the trend was unequivocal. For example, the ratio between the average per capita income in the richest member state (Luxembourg) and that in the poorest (Bulgaria) fell relatively constantly.[2] With regard to the comparison between countries one also has to distinguish between a comparison in terms of current exchange rates and one based on the purchasing power standard (PPS). The purchasing power of a euro varies from country to country and is higher in poorer countries because housing and services there are usually cheaper. Thus inequality between countries is lower measured in PPS.

1 For more details on the question of appropriate calculation see Michael Dauderstädt and Cem Keltek: Immeasurable Inequality in the European Union, in: Intereconomics 46, 1 (2011), pp. 44–51. The procedure is described in more detail in Michael Dauderstädt and Cem Keltek: Crisis, austerity and cohesion: Europe's stagnating inequality Friedrich-Ebert-Stiftung Berlin 2014, http://library.fes.de/pdf-files/id/ipa/10672.pdf (4.6.2016).

2 See Michael Dauderstädt: Convergence in crisis. Europe's integration in jeopardy, Internationale Politikanalyse, Friedrich-Ebert-Stiftung, Berlin 2014, http://library.fes.de/pdf-files/id/ipa/11001.pdf (4.6.2016)

If one compares growth of national quintiles from 2013 to 2014 (see Table 2) it transpires that on EU average incomes increased more quickly the higher they already were. The incomes of the poorest quintile (Q1) grew by only 0.2 per cent, that of the second poorest (Q2) by 1.6 per cent, that of Q3 by 2.1 per cent, that of Q4 by 2.5 per cent and that of the richest quintile (Q5) by 3.5 per cent (see Table 2, last row). Thus the richest benefitted most from the overall rather weaker growth.

This unequal distribution of growth is even more marked in the poorer member states, which includes all countries that lie above Germany in Table 2. There average growth rates rose from zero for the poorest households (Q1) to 4.3 per cent for the richest households (Q5) (see Table 2, penultimate row). Individual national developments should be highlighted: in Germany incomes fell in the lowest quintile by almost 10 per cent, while in all other quintiles they rose. In countries with generally falling incomes (EU programme countries Spain, Greece, Portugal and Cyprus, but also the Czech Republic), as a rule (Greece being the exception) the incomes of the poorest fell most. By contrast, in Austria, Denmark and Malta the poorest quintile did surprisingly well.

PAN-EUROPEAN INEQUALITY STAGNATING DESPITE RISING INEQUALITY AT NATIONAL LEVEL

Despite rising income inequality at national level the figure for the EU as a whole has barely changed, due to the convergence of per capita incomes between the member states. In order to understand this development better it is worth taking a closer look at the composition of European quintiles (see Table 1). Their structure has hardly changed over the years. The poorest European quintile includes above all many national quintiles from eastern Europe (for example, almost the whole of Romania), while the richest EU quintile includes mainly the richest national quintiles (Q5) of the more prosperous EU countries. Some countries contribute both to the poorest and the richest EU quintiles (for example, Italy and Spain). Because of its higher inequality Germany's poorest quintile (Q1 in PPS) also belongs proportionally to the poorest EU quintile.

The composition of EU quintiles also differs in accordance with whether income is calculated in terms of euros or PPS. In euros (the first five columns in Table 1) more national quintiles in the poorer countries are in the lowest EU quintile (for example, four instead of three from

Table 1
The poorest (red) and richest (grey) quintiles in the EU, 2014 (in euros and PPS)

2014	Euro					PPS				
Member state	Q1	Q2	Q3	Q4	Q5	Q1	Q2	Q3	Q4	Q5
Bulgaria	1.205	2.391	3.317	4.417	8.203	2.458	4.878	6.766	9.010	16.733
Romania	694	1.500	2.197	2.981	4.980	1.284	2.777	4.068	5.519	9.218
Latvia	2.070	3.705	5.198	7.282	13.353	2.912	5.213	7.314	10.245	18.787
Lithuania	2.071	3.563	4.859	6.787	12.586	3.262	5.611	7.652	10.688	19.821
Poland	2.445	4.042	5.329	7.006	11.992	4.380	7.241	9.547	12.550	21.484
Estonia	2.866	5.092	7.245	10.337	18.546	3.670	6.520	9.277	13.237	23.749
Hungary	2.225	3.526	4.515	5.732	9.616	3.727	5.906	7.564	9.602	16.108
Slovakia	3.380	5.537	6.804	8.442	13.245	4.868	7.974	9.798	12.156	19.072
Czech Republic	4.377	6.309	7.615	9.365	15.326	6.369	9.180	11.080	13.626	22.300
Portugal	3.302	6.050	8.270	11.126	20.514	4.063	7.445	10.175	13.690	25.241
Greece	2.825	5.454	7.638	10.252	18.214	3.168	6.115	8.563	11.494	20.421
Malta	6.499	9.628	12.740	16.292	26.278	7.878	11.671	15.443	19.750	31.854
Spain	4.597	9.376	13.291	18.443	31.307	4.918	10.031	14.219	19.731	33.492
Slovenia	5.981	9.481	11.925	14.721	22.103	7.196	11.406	14.347	17.710	26.592
Italia	6.091	11.674	15.793	20.807	35.201	5.903	11.315	15.308	20.168	34.120
Cyprus	7.384	10.933	14.521	19.615	39.593	8.082	11.967	15.895	21.470	43.338
Germany	8.430	15.268	19.872	25.940	43.170	8.245	14.932	19.435	25.370	42.221
France	11.105	16.683	21.175	26.720	47.351	10.114	15.194	19.285	24.335	43.126
Belgium	10.706	16.507	21.680	27.531	40.703	9.664	14.899	19.569	24.850	36.738
United Kingdom	10.706	16.507	21.680	27.531	40.703	9.664	14.899	19.569	24.850	36.738
Austria	11.615	18.411	23.248	29.179	47.934	10.840	17.182	21.696	27.231	44.735
Finland	12.747	18.599	23.659	29.555	46.079	10.352	15.105	19.214	24.003	37.423
Netherlands	10.814	16.778	20.884	26.104	41.364	9.734	15.103	18.799	23.497	37.234
Sweden	12.902	21.315	27.059	33.476	49.659	9.752	16.111	20.452	25.303	37.534
Ireland	9.411	14.999	19.516	25.751	44.986	7.729	12.319	16.029	21.150	36.949
Denmark	13.815	22.185	27.907	34.683	56.907	9.910	15.915	20.019	24.880	40.823
Luxembourg	16.173	26.268	34.279	44.749	71.272	13.322	21.638	28.237	36.861	58.709

Notes: The grey shaded quintiles are only included in the relevant EU quintile on a pro rata basis; because of the lack of data for the United Kingdom for 2014 the previous year's values were used.
Source: Eurostat and authors' calculations.

Bulgaria, five instead of four from Romania) because their incomes have fallen in terms of euros. In the upper EU quintile in euros the national quintiles of the richer countries are more strongly represented (for example, three instead of two from Sweden and Denmark), while Portugal's richest quintile (Q5) no longer manages to get in, although in terms of PPS it belongs to the richest EU quintile. In PPS (the right-hand five columns in Table 1) things are reversed: in the poorest EU quintile we now find also the poorest national quintile (Q1) of richer member states (for example, Germany) and in the richest EU quintile national quintiles of poorer countries such as Portugal and Slovenia.

Since 2011 EU-wide income inequality has scarcely changed in either euros or PPS (see Figure 1). In the most recent period of observation presented here, 2013 to 2014, EU-wide inequality in PPS rose minimally to 6.25 and in euros to 9.41. But why do the higher growth rates of the poorer countries not reduce it EU-wide, as they did before 2010? In a nutshell, because incomes in the poorest EU quintile did not grow faster than incomes in the richest. In fact, both hardly changed (less than half a percentage point), which in itself limits the scope for progress. In PPS the figure for the poorest EU quintile even fell slightly in comparison with 2013.

Table 2
Income growth (in euros) by quintile between 2013 and 2014 (%)

Member state	Q1	Q2	Q3	Q4	Q5
Bulgaria	7.3	12.3	12.8	11.6	11.0
Romania	–4.5	3.5	6.1	5.4	4.6
Latvia	8.8	9.4	10.7	9.5	11.1
Lithuania	6.1	4.9	3.9	5.7	6.8
Poland	2.7	3.0	2.8	3.3	3.4
Estonia	0.2	5.0	9.9	13.6	17.2
Hungary	–2.0	–1.7	–0.6	0.1	1.1
Slovakia	–1.0	0.6	0.6	0.4	8.3
Czech Republic	–2.8	–1.5	–1.2	–1.9	0.1
Portugal	–3.6	–2.1	0.6	0.3	–0.3
Greece	–1.7	–4.6	–7.0	–5.5	–3.4
Malta	8.3	5.8	5.8	6.0	6.5
Spain	–7.8	–4.0	–2.2	–0.2	–0.2
Slovenia	–0.6	0.0	0.5	1.3	2.3
Italy	–1.2	1.0	0.4	1.1	–0.2
Cyprus	–9.0	–9.8	–8.5	–7.6	–0.4
Germany	–9.6	0.6	1.4	2.3	0.7
France	1.8	0.4	0.6	0.2	–2.6
Belgium	0.4	–0.1	0.8	1.5	0.4
United Kingdom	NA	NA	NA	NA	NA
Austria	9.1	5.1	5.1	4.9	9.6
Finland	0.3	0.0	1.2	1.1	1.1
Netherlands	–4.7	–0.9	0.0	0.9	1.9
Sweden	0.6	2.2	2.4	3.4	3.8
Ireland	–1.4	1.9	2.0	1.1	4.1
Denmark	10.4	3.9	3.7	4.0	7.3
Luxembourg	–0.4	5.1	3.4	3.4	–4.4
Poorer countries (unweighted average)	**0.0**	**1.4**	**2.2**	**2.7**	**4.3**
EU (unweighted average)	**0.2**	**1.6**	**2.1**	**2.5**	**3.5**

Source: Eurostat and authors' calculations.

THE CRISIS OF SOCIAL COHESION

The picture presented here of an EU marking time in social terms is affected by the selected indicator, the EU-wide quintile ratio (S80/S20 ratio). It obscures developments in the mid-range of the European income pyramid. This mid-range comprises primarily the Mediterranean countries, whose average per capita incomes lie between 15,000 and 25,000 euros. They are thus somewhat poorer than average Europeans (with just under 26,000 euros), but richer than the new member states, whose average lies below 15,000 euros. Their income has shrunk in recent years and, indeed, mainly over all quintiles. Per capita income in an initially somewhat richer Italy has now fallen below the EU average.

The decline of these states since 2009 is in stark contrast to the previous dynamic prosperity, which attracted around 8 million immigrants. Since the crisis they have become emigrant countries with falling incomes, high unemployment, increasing poverty and shrinking social expenditure. In the EU Programme Countries social spending has fallen in absolute terms, despite a rising number of those in need. They have thus contributed to the growing inequality because the incomes we are looking at here are disposal incomes after tax, including transfer payments.

Progress with regard to social cohesion requires a mixed policy approach. Growth must be revived and lower socioeconomic strata must have a larger share of rising incomes. The two are closely linked because if the incomes of poorer households rise aggregate demand rises more strongly because of their lower propensity to save, compared with richer households. Redistribution within countries – for example, through higher taxation of the top incomes, inheritances and wealth – but also between EU member states (by means of a more substantial, autonomously financed and redistributive EU budget) can contribute to this. More efficient taxation of high incomes and profits and capital gains would help to better fund crumbling social protection. But also the distribution of market incomes can and should be improved, for example, by means of adequate minimum wages or a competition policy that reduces excessive income from profits and capital gains.

The EU's weak growth dynamic – especially that of the euro zone – is too dependent on uncertain export surpluses. A large economic area such as Europe should set its own virtuous productive circle in motion, where production for the domestic market gives rise to the employment and incomes from which the necessary domestic purchasing power results. Prosperity does not arise from an increase in claims against other countries through export surpluses, but from investment and consumption at home.

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