Social Europe in the Crisis

MICHAEL DAUDERSTÄDT AND CEM KELTEK

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At a Glance

In 2013, Europe's burgeoning inequality, ever underestimated by the EU, remained at a high level. The catch-up process of the poorer countries that had been observed until 2009 was scarcely making headway any longer due to austerity policy and weak growth. Even though domestic inequality had worsened in only a few countries – including Germany – since 2012, Social Europe's pledge of cohesion remained largely unfulfilled. Only growth based primarily on rising incomes among poorer population groups can provide sustainable prosperity for all.

Up to the threefold crisis of the years 2008–2010 – financial market crisis, great recession and public debt panic – Social Europe was able to point to solid progress.[1] Unemployment was falling; life expectancy was rising; and income inequality, although increasing in some countries, was declining in the European Union (EU) as a whole thanks to growth in the poorer member states. The development of European inequality is the focus of the present analysis. To that end it considers the income disparities between the richest and poorest quintiles of the EU population (quintile ratio S80/S20).

Inequality in Europe

Although the EU Statistical Office (Eurostat) publishes data on national quintile ratios, for the EU as a whole it provides only the weighted average of national ratios. This EU figure makes no methodological sense, however, and deviates from the actual S80/S20 ratio for the EU as a whole because Eurostat abstracts from the high income differences between the member states and their dynamics.[2] Inequality in Europe in fact has two dimensions: (i) differences between the average per capita incomes of EU member states and (ii) differences between per capita incomes within countries. In order to link the two – which is necessary for a realistic estimation of inequality in the EU – one has to construct the richest and the poorest European quintiles, which can be compiled from a certain number of the richest and poorest national quintiles in the member states, with the poorest states contributing more than the richest.[3] Tables 1a and 1b present the relevant composition for 2013, which differs slightly depending on whether one compares incomes in terms of exchange rates or purchasing power standards (PPS).

If one sums the incomes of the red and green national quintiles one obtains approximately the incomes of the poorest and richest quintiles in the EU, each comprising just under 100 million people. The ratio between these two incomes is the S80/S20 ratio for the EU as a whole, which in 2013 was 9.5 in euros and 6.2 in PPS. The richest quintile – calculated in terms of exchange rates – thus earns almost ten times as much as the poorest. This means that inequality is more or less as high as in China and higher than in the United States, India or Russia.[4] Eurostat's incorrect average value is only five.

1. See Michael Dauderstädt, »Convergence in Crisis. European Integration in Jeopardy «, Berlin 2014 (http://library.fes.de/pdf-files/id/ipa/11001.pdf)

2. For more detail on the issue of appropriate calculation, see Michael Dauderstädt, »Ungleichheit und sozialer Ausgleich in der erweiterten Europäischen Union«, Wirtschaftsdienst, Vol. 88, 4, April 2008, 261–269, as well as Michael Dauderstädt and Cem Keltek, »Immeasurable Inequality in the European Union«, Intereconomics 2/2011.

3. The procedure is described in detail in Michael Dauderstädt and Cem Keltek, »Krise, Austerität und Kohäsion: Europas stagnierende Ungleichheit«, Bonn 2014 (http://library.fes.de/pdf-files/wiso/10578.pdf)

4. According to the UN's Human Development Report the values are 4.9 (India), 7.3 (Russia), 8.4 (USA) and 9.6 (China) (http://hdr.undp.org/sites/default/files/reports/14/hdr2013-en-complete.pdf)

Table 1a: The poorest (light grey) and richest (dark grey) quintiles in the EU (euros)

2013	Per capita income in euros				
Member state	Q1	Q2	Q3	Q4	Q5
Bulgaria	1123	2129	2942	3960	7389
Romania	727	1450	2071	2828	4759
Latvia	1902	3386	4696	6648	12017
Lithuania	1953	3398	4676	6419	11785
Poland	2380	3923	5184	6782	11602
Estonia	2859	4847	6595	9100	15824
Hungary	2271	3585	4542	5724	9511
Slovakia	3415	5506	6765	8409	12231
Czech Republic	4503	6406	7708	9544	15308
Portugal	3425	6177	8222	11095	20568
Greece	2873	5716	8212	10846	18846
Malta	5998	9099	12045	15371	24664
Spain	4986	9765	13590	18472	31358
Slovenia	6020	9476	11865	14536	21616
Italy	6167	11558	15737	20590	35264
Cyprus	8113	12117	15874	21233	39754
Germany	9324	15176	19607	25355	42890
France	10905	16618	21039	26675	48604
Belgium	10662	16520	21511	27121	40548
United Kingdom	8982	14078	18691	24934	41573
Austria	10642	17519	22128	27803	43723
Finland	12704	18590	23376	29248	45581
Netherlands	11342	16929	20882	25859	40606
Sweden	12832	20860	26425	32387	47861
Ireland	9633	14916	19893	27511	50416
Denmark	12518	21343	26910	33360	53015
Luxembourg	16239	24987	33147	43275	74516

Table 1b: The poorest (light grey) and richest (dark grey) quintiles in the EU (PPS)

2013	Per capita income in PPS				
Member state	Q1	Q2	Q3	Q4	Q5
Bulgaria	2292	4345	6003	8081	15081
Romania	1346	2685	3834	5237	8813
Latvia	2671	4756	6596	9337	16877
Lithuania	3075	5350	7364	10109	18559
Poland	4265	7031	9291	12154	20792
Estonia	3661	6206	8445	11652	20262
Hungary	3804	6006	7608	9588	15932
Slovakia	4921	7933	9748	12117	17624
Czech Republic	6555	9325	11220	13893	22282
Portugal	4213	7598	10113	13647	25299
Greece	3221	6409	9206	12159	21128
Malta	7271	11029	14600	18631	29896
Spain	5333	10444	14534	19756	33538
Slovenia	7244	11403	14278	17493	26012
Italy	5976	11200	15249	19951	34170
Cyprus	8876	13257	17367	23231	43495
Germany	9114	14835	19166	24785	41926
France	9932	15134	19162	24295	44266
Belgium	9622	14910	19414	24478	36595
United Kingdom	7838	12285	16310	21757	36276
Austria	9927	16342	20642	25936	40786
Finland	10320	15101	18989	23760	37028
Netherlands	10209	15238	18796	23276	36549
Sweden	9750	15851	20080	24610	36368
Ireland	9633	14916	19893	27511	50416
Denmark	8980	15310	19304	23931	38031
Luxembourg	13376	20583	27304	35647	61380

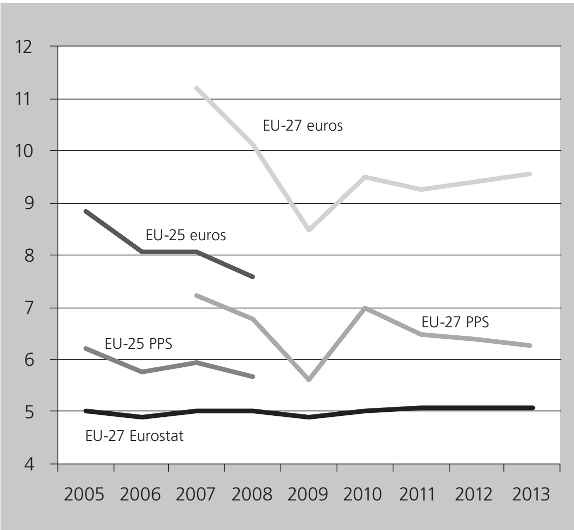
Source: Eurostat and authors' calculations.

Note: The lightly shaded quintiles are only partially represented in the corresponding EU quintile.

Entrenched Inequality in Europe

These values for 2013 mean that inequality in Europe had barely changed since 2012 (see Figure 1). The national average reported by Eurostat also remained constant. However, this conceals diverging national developments. In some countries inequality increased on 2012, for example, in Lithuania, Germany, Bulgaria and Luxembourg. In other countries it decreased, for example, in the United Kingdom. With regard to the indicator selected here – the European S80/S20 ratio – a sideward shift can be observed since 2010. The relevant national quintiles also largely stayed put. In exchange rate terms inequality increased slightly, while in terms of purchasing power it fell slightly.

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



Note: PPS = purchasing power standards.

Source: Eurostat, authors' calculations.

After falling substantially up to the great recession of 2009, inequality within the EU suffered a setback in 2010, but then appeared to resume its long-term trajectory of income convergence. Since 2011, however, this process has practically ground to a halt, especially in euro terms (rather than in PPS).

The main cause is not the diverging development of domestic inequality, but the end of strong catch-up growth in many poorer EU member states. After the crisis of 2008/2009 many poorer countries – especially in central and eastern Europe – were able to resume their growth path. It was the countries affected by the public debt panic and austerity policy (GIPS) and Cyprus that fell back. Because they do not figure among the poorest countries in the EU, however, their deep crisis scarcely increased inequality, but only retarded its reduction.

This effect continues to be felt, but now – between 2012 and 2013 – some of the new member states (Bulgaria, Czech Republic, Slovenia) have experienced a slump, while two large, wealthy countries – Germany and the United Kingdom – exhibited weak, but above average growth. The economies of some richer countries – such as Finland, Italy, Belgium and Denmark – shrank, while many poorer new member states continued to grow strongly (Baltic states, Poland, Romania, Hungary, Slovakia).

The Purchasing Power Riddle

Measured in terms of purchasing power standards (PPS) inequality has still fallen, albeit very slowly. If one considers the changes in the income of the richest and poorest quintiles in the EU between 2011 and 2013 one sees an opposite development, depending on how one measures it. In exchange rate terms the income of the richest quintile increased by 5.1 per cent between 2011 and 2013, while in terms of PPS it rose by only 2.4 per cent. In the case of the poorest quintile it was the other way round: income in exchange rate terms rose by only 2.3 per cent, while in terms of PPS it increased by 6.6 per cent.

What underlies this discrepancy? Basically, the different development of exchange rates and inflation. Especially in poorer countries and in countries compelled to pursue austerity policies, the tendency between 2011 and 2013 was deflationary development or below average inflation. This applies in particular to Greece, Ireland, Portugal and Spain (GIPS), but also to many of the new member states.

The Weaknesses of Social Europe

The key finding with regard to recent years is the stagnation of inequality. Social Europe's promise to reduce income differences in the EU is no longer really being kept. Without vigorous growth in the poorer countries inequality remains high. But where is growth supposed to come from? Germany and important EU bodies continue to rely on structural reforms and austerity policy, whose effects on growth are scarcely discernible. In the meantime, at least, the new European Commission has come to recognise that other policies are needed.

However, the planned investment programme is on too small a scale and depends on a somewhat questionable willingness on the part of private investors to leverage the meagre public resources on a massive scale (by a factor of 15). But what will be their effect on inequality? In order to reduce disparities between countries investment should be concentrated in poorer member states. Within countries the build-up of wealth resulting from investment will primarily benefit richer households. This holds in particular when EU funds are used to reduce risks for private investors and policies to improve the investment climate are aimed exclusively at lower wages, more flexible labor markets and weaker social protection. But the most important obstacle to investment remains the lack of demand. Only stronger demand based on widespread income growth will lead to sustainable growth. In order to achieve this, investment must create jobs that deserve the label »decent work«.

About the authors

Dr Michael Dauderstädt was director of the division for Economic and Social Policy of the FES until 2013.

Cem Keltek is a student of economic science and mathematics and holds an FES scholarship.

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Friedrich-Ebert-Stiftung | International Dialogue
Hiroshimastr. 28 | 10785 Berlin | Germany | Tel.: ++49-30-269-35-7745 | Fax: ++49-30-269-35-9248
E-Mail: info.ipa@fes.de | www.fes.de/ipa

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