

## IRELAND'S INCOME DISTRIBUTION IN COMPARATIVE PERSPECTIVE

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There are concerns that the unprecedented economic boom which Ireland experienced in the second half of the 1990s has raised only some living standards and has widened income gaps. This paper analyzes Ireland's income distribution in comparative perspective, to understand how Ireland's distribution changed and how it compares to other rich countries. We begin with OECD (Organization for Economic Cooperation and Development) and the Luxembourg Income Study (LIS) data to compare Ireland's degree of well-being and inequality with other advanced countries. We also look in some detail at alternative sources of Irish income and their implications for the trends in income inequality in Ireland from 1994 to 2000. For instance, we examine the top of the distribution using data from the administration of the income tax system. We conclude that the spectacular economic growth in the past decade has seen the gap in average income between Ireland and the richer OECD countries narrow dramatically. However, this growth has not greatly affected the Irish ranking in terms of income inequality. Ireland remains an outlier among rich European nations in its high degree of income inequality, though still falling well short of the level seen in the United States. In the end, we find that Ireland's new-found prosperity provides a "social dividend," and choices about how it is used will fundamentally affect whether the current high level of income inequality persists into the future.

### 1. INTRODUCTION

One of the most frequently expressed concerns about the unprecedented economic boom that Ireland experienced in the second half of the 1990s has been that the benefits were not shared evenly, that rising living standards were accompanied by widening gaps leaving Ireland with a particularly unequal distribution of income. This paper examines Ireland's income distribution in comparative perspective, and seeks to shed some empirical light on what happened during the boom and how Ireland compares to other rich countries. It begins by using the

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data from the OECD and the Luxembourg Income Study to compare Ireland's degree of income inequality with other advanced countries. It then looks in some detail at what alternative sources of survey data suggest about key trends in income inequality in Ireland from 1994 to 2000. Since there is a particular interest in what happened right at the top of the distribution, this is then examined using data from the administration of the income tax system. Finally, we conclude with some reflections on the implications of the results presented.

### *The "Irish Miracle"*

One very important fact to keep in mind in analyzing income inequality in Ireland is the exceptionally rapid rate of economic growth seen in the last decade. Table 1 shows Ireland in comparison with eight other OECD nations. In 1980 Ireland had an (OECD) PPP (Purchasing Power Parities) adjusted GDP (Gross Domestic Product) per capita of \$10,926 (in 2000 United States dollars), which was only 48 percent that of the United States and 77 percent of the (unweighted overall) average for the countries shown. The United Kingdom had 70 percent of the United States level. By 1990, the Ireland to United States ratio was up to 53, still far below both the simple average (77) and the United Kingdom (72). By 2000, however, Ireland had a GDP per person that was 81 percent that of the United States, just behind Canada, while the United Kingdom remained at 73 percent of the United States level. Obviously Ireland's advance over the 1990s was unmatched by these nations. By 2003, the latest OECD figures (not shown here) have Ireland at 90 percent of the United States GDP per capita.

These figures overstate the rise in living standards in Ireland compared with these other countries, because Ireland is notable among OECD countries for the size of gap between its GDP and Gross National Product (GNP). Due to the scale of repatriation of profits accruing to foreign companies operating in Ireland, this gap increased from 4 percent of GDP in 1980 to 11 percent in 1990, 15 percent in 2000 and 20 percent in 2002. The problem is that much of these profits reflect high measured margins in sectors such as information technology, pharmaceuticals and soft drink concentrates. However, low corporation tax in Ireland provides an incentive to book large profits in Ireland, so the figures may exaggerate how much of these firms' net value added is actually taking place in Ireland. For example, as the OECD (2003b) has pointed out, multinationals dominate the chemicals sector which accounts for a large proportion of overall value added and is characterized by a relatively low labor share, with only a small proportion of gross value added distributed to the domestic workforce, so their high levels of output are not reflected in Irish incomes.

This means that the lower GNP figure is closer to a measure of the income that is domestically available in Ireland. When we focus on GNP rather than GDP per head—which makes virtually no difference for the other countries being considered—Ireland achieves a position broadly similar to Germany in average income per capita in PPP terms by 2000, slightly below the United Kingdom. While this is less dramatic, it still represents a very rapid catch-up in a very short time, from 46 percent of the United States' average in 1980 to over 70 percent by 2000, with the gap closed further in subsequent years. So Ireland's income

TABLE 1  
GROSS DOMESTIC PRODUCT PER HEAD AT THE PRICE LEVELS AND PPPs OF 2000 (IN 2000 US DOLLARS)

Nation	1980	Index <sup>1</sup>	1990	Index <sup>1</sup>	2000	Index <sup>1</sup>	Percent Change		
							1980 to 1990	1990 to 2000	1980 to 2000
Belgium	\$ 17,870	78	21,512	76	25,916	75	16.9	17.0	31.0
Canada	20,349	89	23,631	83	28,367	82	13.9	16.7	28.3
Finland	16,892	74	21,860	77	25,359	73	22.7	13.8	33.4
Germany	17,175	75	21,271	75	24,851	72	19.3	14.4	30.9
<b>Ireland</b>	<b>10,926</b>	<b>48</b>	<b>15,128</b>	<b>53</b>	<b>28,035</b>	<b>81</b>	<b>27.8</b>	<b>46.0</b>	<b>61.0</b>
Netherlands	18,272	80	21,580	76	26,982	78	15.3	20.0	32.3
Sweden	18,763	82	22,635	80	26,567	77	17.1	14.8	29.4
United Kingdom	16,034	70	20,473	72	25,322	73	21.7	19.1	36.7
United States	22,849	100	28,420	100	34,575	100	19.6	17.8	33.9
Overall Average	\$ 17,681	77	21,834	77	27,331	79	19.4	20.0	35.2

Source: OECD, 2003. *Annual National Accounts for OECD Member Countries*, Gross Domestic Product and Household Final Consumption Expenditure Comparative Tables (B1–B12) ([http://www.oecd.org/document/28/0,2340,en\\_2649\\_34259\\_2750044\\_1\\_1\\_1\\_00.html](http://www.oecd.org/document/28/0,2340,en_2649_34259_2750044_1_1_1_00.html)).

Note: <sup>1</sup>United States = 100.

distribution must be seen in the context of this remarkable convergence towards the richest OECD countries. Conversely, the average level of income per capita must be seen in the light of how it is distributed. Using the abbreviated social welfare function suggested by Sen, for example, which weights average income per capita by  $(1-G)$  where  $G$  is the Gini measure of income inequality, it turns out that Ireland and the U.K. would rank well below the other countries in Table 1. So it is to the distribution of income that we now turn.

## 2. INCOME INEQUALITY AND POVERTY IN IRELAND IN COMPARATIVE PERSPECTIVE

### *Introduction*

This section compares recent economic inequality in industrialized nations, largely those belonging to the Organization for Economic Cooperation and Development (OECD),<sup>1</sup> with inequality in Ireland. We find that Ireland has a rather high overall level of inequality, though below that found in the United States. In real income terms, the gap between Ireland's poor and rich is also wider than in the rich European countries we examine, though again less than in the United States. Next we examine the effects of government policies and social spending efforts on poverty and inequality, finding that direct tax and transfers have a rather limited impact in reducing income inequality and the numbers below relative income poverty thresholds in Ireland.

### *Methodological Details*

First, we provide some details on our approach to capturing income inequality. Many pitfalls must be avoided in comparing income inequality across countries and over time, in terms of the comparability of the underlying data and measures of not only income but also income recipient unit and unit of analysis (see, for example, Atkinson and Brandolini, 2001). Our analysis concentrates on income inequality among households (including one person households) and does not directly address the issue of individual earnings inequality. Granted that earnings are generally the largest part of income, nevertheless, these are very different phenomena. Earnings refer to persons, and income to households. Income pools the earnings of household members, taxes, transfers, pensions, and capital income, each of which is liable to make the distribution of household income very different from the distribution of individual or household earnings.

We measure disposable money income. For most families, the primary income source is market income, which includes earned income from wages, salaries, and self-employment and other cash income from private sources—from property, from pensions, from alimony or child support. To reach disposable income, governments add public transfer payments (retirement, family allowances, unemployment compensation, and welfare benefits) and deduct income tax and social security contributions from market income. This cross-nationally comparable

<sup>1</sup>The research that we summarize, expand upon and update here is reported more fully in Smeeding (1998, 2004) and Gottschalk and Smeeding (1997, 2000).

definition of income is hardly comprehensive, typically excluding much of capital gains, imputed rents, home production, and in-kind income. We take no account of indirect taxes or of the benefits from public spending on such social goods as health care, education, or most housing subsidies.<sup>2</sup> We also measure income on an annual basis in our comparative analysis (looking at alternatives in our analysis of Irish trends later on). This may be too long an accounting period for families that are severely credit constrained, too short for those that can smooth consumption over multiple years—but almost all the available surveys report income for the calendar year.

The answer to the question “distribution among whom?” is “among individuals.” Some surveys focus on the individual as the unit of analysis, some on the household as the unit of income sharing. The most common unit of analysis is the household, defined as all persons sharing the same housing unit and living facilities, regardless of any familial relationship.<sup>3</sup> We therefore estimate individual disposable income by aggregating the income of all household members and using an equivalence scale to arrive at individual equivalent income.<sup>4</sup> When examining poverty we count the number of persons with incomes below half of the national median income, using these same market and disposable income definitions.

#### *Differences in Inequality Across Nations: Relative and Absolute Income Differences*

Figure 1 compares the distribution of disposable income in 30 nations for various years around the turn of the century (2000). Within each country we focus on the relative differences between those at the bottom and those at the top of the income distribution. To do so we first measure, in each country, the ratio of the income of a household at the 10th percentile ( $P_{10}$ , in Figure 1) and a household at the 90th percentile ( $P_{90}$ ) to median income. This gives us some indication of how far below or above the middle of the distribution the poor and the rich are located on the continuum of income. Second, we measure the ratio between the incomes of those at the 90th and 10th percentiles (the “decile ratio”). This gives us the size of the gap between the richest and the poorest in each country. These measures—measures of socio-economic distance, if one will—are easy to understand but focus on only a few points in the distribution of income. An alternative measure of inequality across the entire distribution is the Gini coefficient, much used by economists in studies of inequality.<sup>5</sup> We include this number also in Figure 1. Note that countries in Figure 1 are ranked by the  $P_{10}$  ratio. Ranking by  $P_{10}$ , the  $P_{90}/10$  or

<sup>2</sup>In general, countries which spend more for cash benefits also tend to spend more for non-cash benefits, so that the distribution of housing, education and health care benefits reinforces differences in income distribution for at least some western European nations. This is not necessarily so, however, for other countries or other methods of accounting.

<sup>3</sup>Some countries use more restrictive definitions; Sweden, for example, uses the nuclear family as the accounting unit. Otherwise, households are of similar size across the rich countries examined here. A household excludes boarders, but does include and pool the incomes of unrelated persons sharing the same living facilities.

<sup>4</sup>We use the square root of household size to obtain equivalent income.

<sup>5</sup>The Gini coefficient uses a scale from 0, perfect equality, to 1, perfect inequality. Thus, in Figure 1, Denmark, with a Gini coefficient of 0.236, has the least inequality and the U.S., with a Gini coefficient of 0.368, has the highest level of inequality.

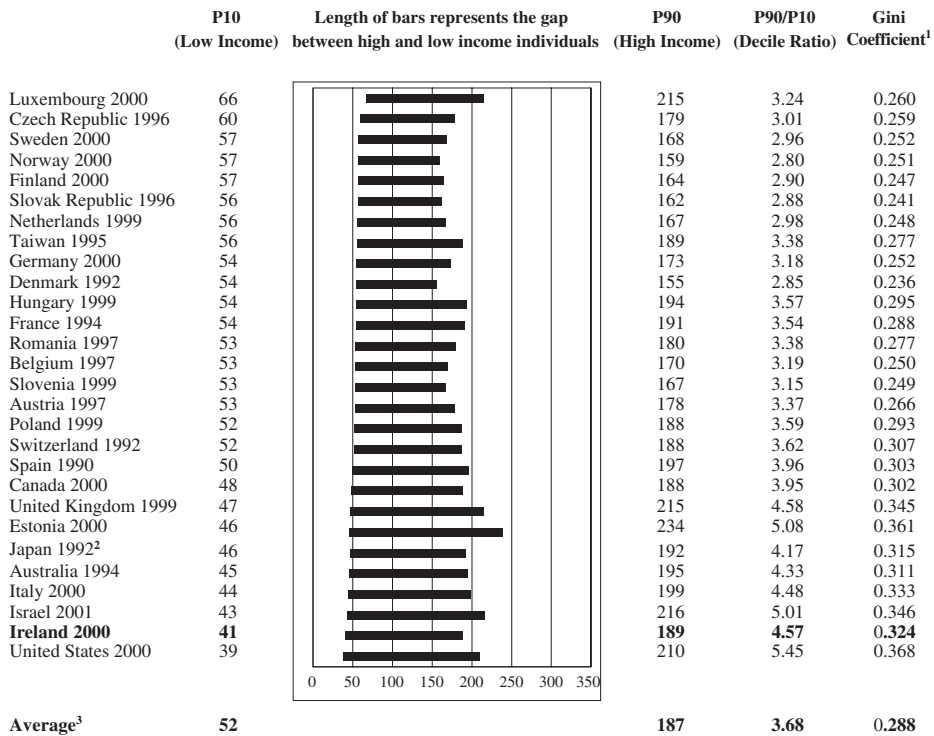


Figure 1. Social Distance and Social Exclusion (numbers given are percent of median in each nation and Gini coefficient)

Source: Author's calculations from Luxembourg Income Study.

Notes: <sup>1</sup>Gini coefficients are based on incomes which are bottom coded at 1 percent of disposable income and top coded at 10 times the median disposable income.

<sup>2</sup>Japanese gini coefficient as calculated in Gottschalk and Smeeding (2000) from 1993 Japanese Survey of Income Redistribution.

<sup>3</sup>Simple average.

the Gini would give different rankings. This point should be well noted by those who prefer a single coefficient inequality measure to rank nations.

Figure 1 shows us that Ireland (bold) is indeed an outlier among rich nations. Only in the United States does P<sub>10</sub>, the income level cutting off the bottom decile, represent a lower proportion of the median. A low-income Irishman (or woman) at the 10th percentile in 2000 had an income that is only 41 percent of median income, whereas a high-income Ireland resident in the 90th percentile had an income that is 189 percent of the median. The income of the high-income Irish is roughly four and a half times the income of the low-income Irish, even after we have adjusted for taxes, transfers, and family size (the decile ratio is 4.57). In contrast, across all the countries in Figure 1 the income of the poor averages 52 percent of the income of middle-income persons; that of high-income persons averages 187 percent of the median income. The average rich person has about 3.7 times the income of the average poor person. The rich Irish are a bit above average in relative terms (P<sub>90</sub> of 189 vs. 187 for all) but the poor Irish are among the least well off, with incomes at P<sub>10</sub> of 41 compared to an average of 52.

The countries in Figure 1 fall into clusters despite the fact that different measures of inequality give different rankings. Inequality is least in Northern Europe (the Scandinavian countries, Belgium, the Netherlands), where the income of those at the 10th percentile is 57 percent of the median. Central Europe comes next (Switzerland, Germany, and France). They are followed by an eclectic mix. Canada and Australia are at roughly at the same level, but still more equal than Ireland and Italy; the U.K. is in a similar range with its precise ranking depending on the measure employed, but the United States displays the highest inequality with most of the measures ( $P_{90}$  being the exception). In some rich countries, for example, Luxembourg, Israel, Estonia, and the United Kingdom, the incomes of the richest (those at the 90th percentile) are all more than 200 percent of median income—a little above the relative level of the Irish rich. In summary, Ireland is distinctive, above all, in the relative disadvantage of its poorest residents. These persons have incomes only 41 percent of the median—in other rich nations (other than the United States) they are much higher—e.g. 47 percent in the United Kingdom, 48 percent in Canada.

#### *Absolute Differences in Income Inequality Across Nations*

At the outset of this paper we drew attention to the fact that average income for Ireland has been converging rapidly with countries such as Germany and the United Kingdom, and the gap with the United States has been narrowing (although not as rapidly as GDP per head might suggest). We now ask where this leaves the incomes of those at different points in the Irish income distribution in real terms compared with people at the same point in the distribution in other rich countries. We examined this question by converting the incomes of a set of rich nations (from Figure 2) into real 2000 United States dollars, using the standard OECD measure of purchasing power parity (PPP). We then recomputed low-, median-, and high-incomes in these countries as a fraction of the United States median, creating “real incomes,” and then present them in Figure 2. Because conversion of real income across countries is sensitive to the PPP index used and to other factors, these comparisons should be taken as only rough indicators of “real living” standards. (Note however that because we are now focusing on incomes reported in household surveys, the Irish figures can be compared directly with others without the problems which arise with GDP per head.)

Those on the 10th percentile, whose incomes average about 50 percent of median income in their own countries, are now seen to have real incomes of only 40 percent of the United States median. The real incomes of Germans at the 10th percentile are on average 4 percentage points higher than the real incomes of the Irish at the 10th percentile. Low-income Canadians are even better off, with incomes 9 percentage points higher than the low-income Irish, while having about the same overall equivalent income per person as Ireland. Only in Great Britain were the living standards of low-income households a bit lower than in Ireland (35 vs. 37 percent). Overall, lower-income Irish are worse off than the low-income persons in all other nations, save Britain. But it is at the high end that Ireland stands out: real income at the 90th percentile in Ireland exceeds all the other countries except for Canada and the United States, and is far above the other country

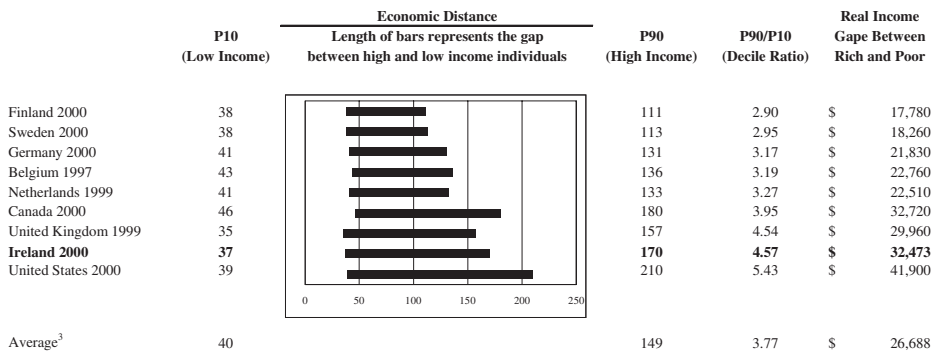


Figure 2. Real Income Well-being of All Persons in Eight Countries<sup>1</sup> (as percentage of overall US 2000 median equivalent income in PPP terms)<sup>2</sup>

Source: Author's calculations from Luxembourg Income Study.

Notes: <sup>1</sup>Figures given are adjusted dollars per equivalent person (child) in own currency as a percent of own overall national median income (P50), weighted for the number of persons in each unit.

<sup>2</sup>Figures given are adjusted dollars per equivalent person 2000 U.S. dollars, weighted for the number of persons in each unit size, and relative to the overall U.S. median of \$24,416.

<sup>3</sup>Simple average.

average. The average “rich” Irish is 21 percentage points above the average rich person and 13 points above the average rich British person.

We can also measure the income distance between top and bottom, all in United States 2000 PPP adjusted dollars now. The gap in Ireland is \$32,473 per person—the lower-income person has resources of about \$9,000 per person, while the rich person has about \$41,500 per person. That gap is much higher than in most nations—higher than the UK, the same as Canada, but below the United States.

These real income measures are admittedly crude. They should be seen as measures of net spendable income rather than of total consumption. Total consumption would also include goods and services such as health care, education and child care that are provided at different prices and under different financing schemes in different nations. To the extent that low-income citizens elsewhere need to spend less out of pocket for such goods as these than do low-income Irish, the latter are at an even greater real income disadvantage. The northern European welfare states that have the most generous cash transfers also seem to provide such social goods most comprehensively, though they may be a larger fraction of lower incomes in Anglo-Saxon nations (see, for example, Smeeding *et al.*, 1993; Garfinkel *et al.*, 2004), and differential access between rich and poor to, for example, hospital care is of particular concern in Ireland (see, for example, Nolan, 2005). Furthermore, wealth as well as current income is a key determinant of what a household can spend, but once again we have no systematic information on the relative position of those towards the top versus those towards the bottom of the income distribution in different countries that would allow us to incorporate household assets and liabilities into the distance measure.<sup>6</sup>

<sup>6</sup>The new Luxembourg Wealth Study (LWS) will provide such information for a set of rich countries by the end of 2006. For more on LWS, see <http://www.lisproject.org/lws.htm>.



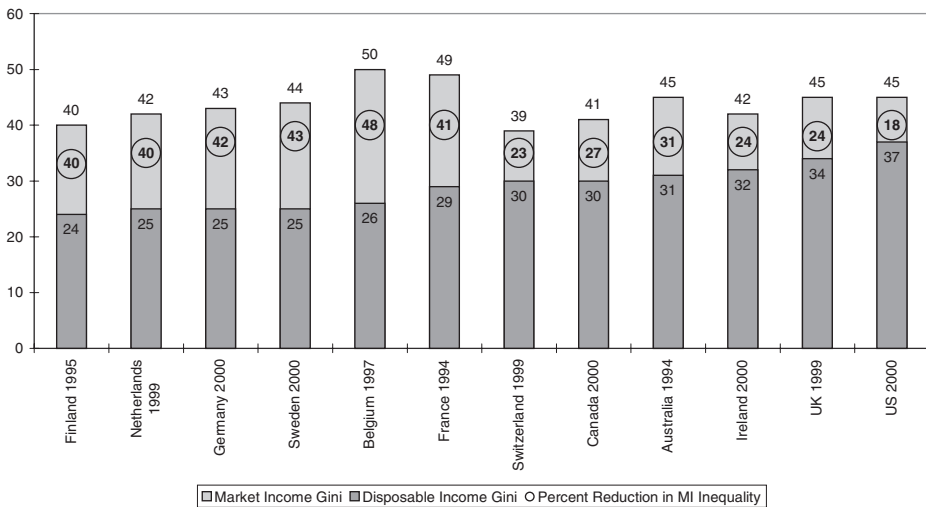


Figure 3. Inequality of Market Income<sup>1</sup> and Net Disposable Income in OECD Countries: Gini Coefficients before and after Taxes and Benefits

Source: Author's calculations from the Luxembourg Income Study.

Note: <sup>1</sup>Estimate based on communication with Sutherland (2004). LIS does not contain market income estimate for Ireland.

The claim that Ireland enjoys the most rapidly rising living standards in the OECD must be evaluated alongside the equally valid claim that Ireland has a relatively high level of real income inequality compared to the other countries we study. And the social costs of low absolute incomes may be quite high, especially for families with children. From other research, we know that young children living in households with incomes at 75 percent of the official United States poverty line—that is, households at roughly the 10th percentile in the income distribution in Ireland or the United Kingdom or the United States are at severe risk of poor health, subsequent poor educational performance, and diminished achievement.<sup>7</sup>

### *Patterns of Redistribution*

Every nation's tax and benefit system reduces market income inequality, but not all are equally effective in doing so. Figure 3 uses the Luxembourg Income Study to demonstrate both market income inequality and disposable income inequality among a set of 14 nations using the Gini coefficient (rounded to two digits and multiplied by 100). In all nations disposable income inequality is less than market income inequality, suggesting that the tax and benefit system reduces overall inequality. We see that the market generates similar patterns of income inequality in all rich nations. The Gini for market incomes varies only from 39 to 50 across these 12 rich nations and Ireland at 42 is at the lower end of these nations

<sup>7</sup>Duncan *et al.* (1998).

(owing mainly to its strong economy, see Appendix Table A1). After tax and transfers disposable income inequality measures range from 24 to 37 and Ireland has an intermediate level of inequality at 32 (consistent with Figure 1 earlier in the article). The percentage reduction in before tax and benefit inequality in Ireland is 24 percent, roughly the same reduction as the United Kingdom and Switzerland, less than Canada (27) or Australia (31), but more than the United States (18). These reductions are less than those found in Central and Northern Europe and in Scandinavia (e.g. France, Belgium, Sweden, Germany, Netherlands). For instance, the Netherlands, which begins with the same MI Gini (42), achieves a 40 percent reduction in inequality by means of its tax transfer system compared to 24 percent in Ireland.<sup>8</sup>

Before tax and benefit inequality in Finland, Netherlands, Germany, and Sweden are less than those found in Ireland. These are all relatively large and generous welfare states, compared to Ireland or the Anglo-Saxon nations. Those that redistribute the most are therefore not the ones who have indirectly created the greatest degree of market income inequality via their tax and benefit systems.

### *The Antipoverty Effect of Taxes and Transfers*

As well as overall redistribution, it is also of interest to look at how taxes and transfers affect poverty and the lowest part of the income distribution. In every nation, benefits from governments, net of taxes, reduce income poverty as we see from Figure 4 (adapted from Smeeding (2004), adding Ireland and updating the Canadian figure to 2000). It shows the percent of persons with market and then with disposable incomes less than half of the median disposable income, in Ireland and eight other nations. As with the inequality measures in Figure 3, poverty rates computed using before-tax-and-transfer household income do not differ among countries as much as do those calculated after taxes and transfers in Figure 4. (The figures based on market income are not properly “poverty” rates, in that poverty properly refers to living standards and they clearly depend on tax and transfers as well as income from the market, but we use the term for convenience.)

Here we find that the Irish before-tax-and-transfer poverty rate is actually below average, owing mainly to its strong economy. As one might expect based on the previous analyses, the United States shows the least antipoverty effect of any nation analyzed. It reduces poverty by 28 percent compared to the average reduction of 62 percent in Figure 4. The nation closest to the United States in terms of overall net poverty is Ireland at 16.6 percent. Here government programs reduce market income-based poverty by 33 percent. In all other nations, the effects of programs on poverty are much higher than in the United States and Ireland.

This finding implies that different levels and mixes of government spending on the poor have sizable effects on national poverty rates (Burtless *et al.*, 2001). In fact, detailed analysis shows that higher levels of government spending (as in Scandinavia and Northern Europe) and more careful targeting of government transfers on the poor (as in Canada, Sweden, and Finland) produce lower poverty

<sup>8</sup>Note that the same conclusion applies if one measures “redistributive effort” in terms of the decline in the Gini coefficient in percentage point, rather than percentage, terms—i.e. independent of the base level of inequality in market income.

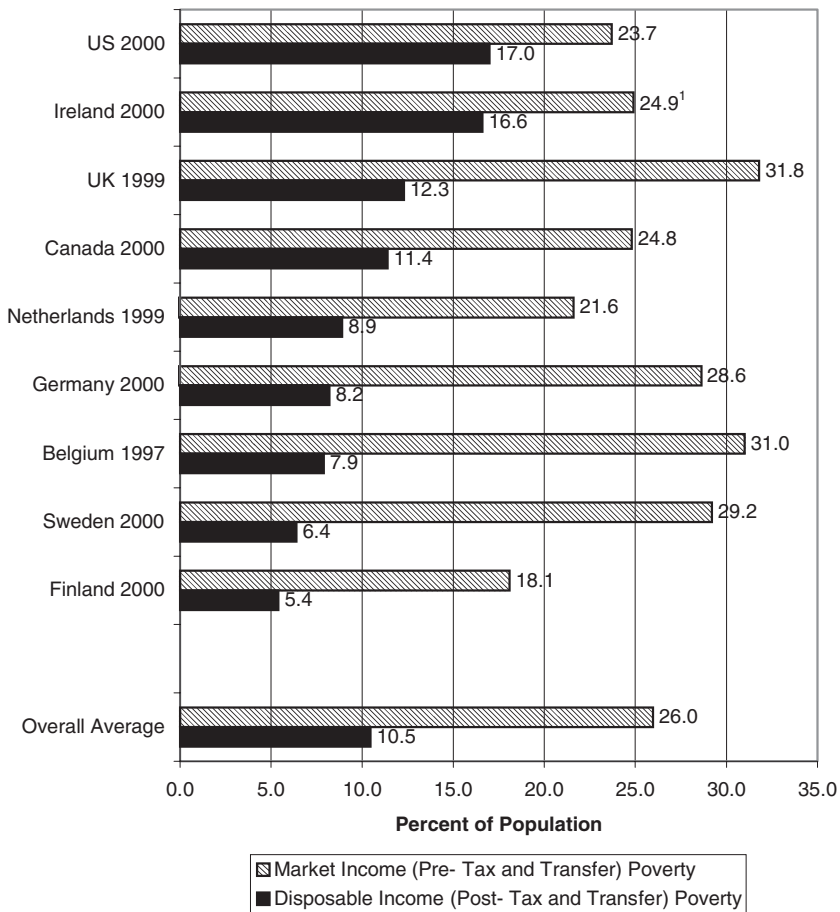


Figure 4. Relative Poverty Rates and Antipoverty Effects in Eight Rich Nations at the Turn of the Century (Percent of Persons with Market Income and Disposable Income Less than Half of Adjusted National Disposable Median Income)

Source: Author's calculations from Luxembourg Income Study.

Note: <sup>1</sup>Market income unavailable for Ireland in LIS. Ireland's Market income poverty rate was estimated based on private communications with M. Corak (2004) and H. Sutherland (2004).

rates (Smeeding, 2004). Unemployment (Appendix Table A1) is not well correlated with either market income poverty or disposable income poverty. Rather, earnings and wage disparities are important in determining both market income and disposable income poverty rates, especially among families with children (Bradbury and Jäntti, 1999; Jäntti and Danziger, 2000). Countries with an egalitarian wage structure tend to have lower child poverty rates, in part because the relative poverty rate among working-age adults is lower when wage disparities are small.

Other nations get a much larger poverty reduction from social insurance. In heavily insured countries like Sweden, Belgium, and Germany, social insurance

(unemployment and workers' compensation, disability benefits, paid family leave) reduces poverty by over 70 percent. In the case of social assistance, large effects of targeted programs are found in Finland and the United Kingdom, while relatively lower ones are observed in the more socially insured nations where the heavy lifting has already been done by these benefits (e.g. in Germany, Belgium, the Netherlands, and Canada). It should be apparent that different nations use different instruments and different "income packages" to achieve their antipoverty effects. There is no one program or one type of policy instrument that is universally generous and common across these eight nations.

### 3. TRENDS IN INCOME INEQUALITY DURING THE ECONOMIC BOOM

#### *How to Lie with Statistics?*

Capturing trends in income inequality requires both reliable data and appropriate methods, and there are many pitfalls and challenges as already noted. To illustrate the sorts of difficulties that can arise, we begin our analysis of recent trends in Ireland by presenting three sets of figures. Each relates to disposable income and has been used elsewhere to represent what has been happening to income inequality over the period.

Table 2 shows results from the Household Budget Surveys (HBS) carried out by the Central Statistics Office in 1994–95 and 1999–2000, calculated from figures published in the official reports. The share of each decile in total disposable household income in each year is given, and a clear pattern is seen. The share of the bottom two deciles has declined from the mid-1990s to the end of the decade, by about half a percentage point in total, but the more pronounced shift has been towards the top, where the share of the top decile has risen by one and a half percentage points. So this has been taken as constituting clear evidence of substantially "widening gaps."

Table 3 shows figures taken from the authoritative EU (European Union) source in this context, the *Joint Report by the Commission and the Council on Social*

TABLE 2  
DECILE SHARES IRELAND 1994–2000, HOUSEHOLD BUDGET SURVEYS

Decile	1994–95 %	1999–2000 %
Bottom	2.2	1.9
2	3.5	3.3
3	4.7	4.5
4	6	5.9
5	7.6	7.5
6	9.2	9.2
7	11.3	11.1
8	13.6	13.4
9	16.7	16.6
Top	25.2	26.7
All	100	100

Source: Derived from *Household Budget Survey Reports*, 1994–95 and 1999–2000.

TABLE 3  
DECILE SHARES IRELAND 1994–2000, LIVING IN IRELAND SURVEYS

	1995	1997	1999	2001
Top/bottom quintile ratio	5.1	5	4.9	4.5

Source: *Joint Report by the Commission and the Council on Social Inclusion* (2004), Statistical Annex Table 6, p. 13.

TABLE 4  
DECILE SHARES IRELAND 1994–2000, LIVING IN IRELAND SURVEYS

Decile	1994 (%)	2000 (%)
Bottom	3.8	3.2
2	4.9	4.5
3	5.6	5.5
4	6.4	6.9
5	7.5	8
6	8.9	9.3
7	10.6	10.8
8	12.6	12.7
9	15.3	15.6
Top	24.4	23.6
All	100	100

Source: Nolan (2003).

*Inclusion* (2004). This time a summary inequality measure, the ratio of the share of the top to the bottom quintile, is used to capture trends in the distribution, based on figures from the European Community Household Panel Survey (ECHP). We see that this ratio was considerably lower at the end of the decade than in the middle: inequality seems to have fallen sharply, gaps have narrowed!

The third set of income distribution results is shown in Table 4, taken from a paper published by one of us in 2003. The figures relate to decile shares once again and are now from the Living in Ireland Survey (LII) carried out by the Economic and Social Research Institute between 1994 and 2001. The share of the bottom two deciles is now seen to have fallen sharply—by a total of 1 percentage point in all. However, the top decile has not been the gainer, indeed its share has also fallen, by not much less than 1 percentage point. It is the middle and upper parts of the distribution—deciles 4 to 9—that have gained, at the expense of both top and bottom. Unlike the figures from the Household Budget Survey, these results fail to confirm the widespread belief that the economic boom saw the top of the distribution do exceptionally well and pull away from the rest—as, indeed, might be expected given the growth in profits which was a feature of the Irish boom.

#### *Teasing Out the Differences*

By teasing out exactly what these figures represent and where they come from, we can go some way towards reconciling these results, though we will still be left with some critical areas of uncertainty. This involves focusing on issues that have

become familiar in income distribution analysis, namely how differences not only in data sources but also in the precise way income and its distribution are defined and measured can have major implications for measured income inequality levels and trends.

The first point about the three sets of figures we have presented is that they come from different sources. Those familiar with the Irish data will immediately object that the Living in Ireland Survey is in fact the Irish component of the ECHP. However, differences between the two could well arise. The main income concept used in the ECHP refers to income received in the previous calendar year, so the figures labeled “1995” and “2001” in Table 3 actually refer to 1994 and 2000 incomes respectively. With the survey concentrated in the latter part of each year, respondents were often reporting on income for a period ending 9–12 months earlier. In the Living in Ireland Survey, on the other hand, income is generally that received in the previous week or month—depending on the pay period—with only capital and self-employment income the weekly average of that received over a year. Another difference between the ECHP and LII figures quoted is that the former make use of the “modified OECD” equivalence scale which assigns a value of 1 to the first adult in the household, 0.5 to each other adult, and 0.3 to each child, whereas the latter employ a scale based on the relativities implicit in Irish social assistance rates, giving a value of 0.66 to the second and subsequent adults in the household and 0.33 to each child.

We will investigate the role of these differences in the measure of equivalized income shortly, but the ECHP and LII datasets also differ for other reasons. Eurostat developed its own internal procedures for imputation of missing values, for dealing with outliers, and for weighting the responses, applied in a uniform way across all the participating countries, but not identical to those employed in preparing the Living in Ireland survey for domestic analysis. Furthermore, the sample used for domestic purposes was supplemented substantially in 2000 and 2001, in the light of the attrition that had taken place since the initiation of the survey in 1994; Eurostat did not include these additional cases in the ECHP data for Ireland.

While there are, thus, potentially significant differences between them, the results from the ECHP and the LII surveys in Tables 3 and 4 respectively employ the same unit of analysis: the household is taken to be the underlying income recipient unit and equal sharing among household members is assumed, so each has the same living standard, as reflected in equivalized income of the household, and the individual is the unit analyzed. The results from the HBS shown in Table 2, by contrast, employ the household both as the income recipient unit and the unit of analysis, and household income is not equivalized. As we shall see, this can make a big difference to the measured income distribution. The HBS is also different in nature to the ECHP and LII in being a cross-section survey obtaining results from a different set of households, whereas the ECHP and LII are longitudinal surveys seeking to go back to the same set of people each year—though with the addition of a substantial supplement of new cases to the LII in 2000 as already described. All three seek to represent the underlying population and are weighted for analysis for that purpose, but their differing designs—and in particular the impact that attrition might have in panel surveys—need to be kept in mind.

*Harmonizing the Analysis*

So we have pin-pointed a variety of factors which might explain why the results in the public domain from these three sources convey differing pictures of trends in income inequality over Ireland’s boom. What we now want to do is tease out which factors actually do have a substantial impact on the results and, crucially, whether these sources still tell a different story when we harmonize the methods employed in the analysis. We do so by re-analyzing the LII, by analyzing the ECHP micro-data directly rather than relying on published results, and by exploring further the HBS with the help of the CSO (Central Statistical Office).<sup>9</sup>

So we now look at decile shares from the LII, the HBS and the ECHP, but focus first simply on the household as unit of analysis and on disposable income without any equalization—in other words, align with the basis for the figures from the HBS in Table 2. These results are shown in Table 5 (where we also add in results for the LII from 2001 which have not previously been published). The pattern from the HBS is of course as before, but on this basis the trend in the ECHP is now falling shares for the bottom 3 deciles, increases for deciles 6–9, but a fall in the top decile’s share. In the LII results by contrast we see some fall in shares throughout bottom half of distribution, and increases for most of the top half but not the top decile. So all three sources now show some decline towards the bottom over the period, but very different patterns at the top—the HBS has the share of the top decile going up by 1.5 percentage points, the ECHP has it falling by over half a percentage point, and the LII shows it to be stable.

So what happens when we shift to persons rather than households as the unit of analysis, and to equalized rather than unequalized income? To facilitate this

TABLE 5  
DECILE SHARES IN DISPOSABLE INCOME AMONG HOUSEHOLDS, IRELAND 1994–2001

Decile	Share in Total Disposable Income (%)						
	Household Budget Surveys		ECHP		Living in Ireland Surveys		
	1994–95	1999–2000	1994	2001	1994	2000	2001
Bottom	2.2	1.9	2.3	1.8	2.3	1.8	1.8
2	3.5	3.3	3.3	2.9	3.3	2.9	3.1
3	4.7	4.5	4.8	4.3	4.6	4.1	4.4
4	6	5.9	6	6.2	6	5.5	5.8
5	7.6	7.5	7.6	7.5	7.5	7.6	7.6
6	9.2	9.2	9.1	9.3	9.1	9.4	9.4
7	11.3	11.1	11	11.4	11.1	11.6	11.2
8	13.6	13.4	13.2	13.7	13.5	13.7	13.6
9	16.7	16.6	16.2	17.1	16.5	16.7	16.9
Top	25.2	26.7	26.6	26	26.4	26.8	26.4
All	100	100	100	100	100	100	100

Source: HBS as in Table 2; LII, ECHP calculated from microdata.

<sup>9</sup>Micro-data from the HBS have been lodged in the Irish Social Science Data Archive and are available for analysis, but significant numbers of high incomes have been “top-coded” so this public use dataset is not suitable for analysis of the overall distribution of income.

TABLE 6  
DECILE SHARES IN EQUIVALIZED DISPOSABLE INCOME AMONG PERSONS, IRELAND 1994–2001  
("OECD EQUIVALENCE SCALE" 1/0.7/0.5)

Decile	Share in Total Equivalized Disposable Income (%)						
	Household Budget Surveys*		ECHP		Living in Ireland Surveys		
	1994–95	1999–2000	1994	2001	1994	2000	2001
	%	%	%	%	%	%	%
Bottom	3.6	3.2	3.5	3.4	3.5	3.3	3.3
2	4.8	4.7	4.6	4.9	4.6	4.7	4.7
3	5.7	5.6	5.6	6	5.6	5.7	5.7
4	6.6	6.7	6.4	7.2	6.4	6.9	6.9
5	7.6	8	7.4	8.5	7.5	8.1	8.3
6	9	9.2	8.7	9.7	8.9	9.2	9.4
7	10.6	10.6	10.4	10.8	10.6	10.9	10.6
8	12.5	12.5	12.4	12.3	12.6	12.5	12.5
9	15.5	15	15.3	14.7	15.5	15.2	15
Top	24.1	24.4	25.7	22.6	24.8	23.4	23.6
All	100	100	100	100	100	100	100

\*The assistance of the CSO in producing these figures is gratefully acknowledged.

analysis the CSO kindly produced figures for us from the HBS using person-weighting and equivalizing income using the equivalence scale they (like many others) have employed in the past, namely the so-called "OECD scale." This assigns a value of 1 to the first adult, 0.7 to each other adult, and 0.5 to each child in the household. Table 6 shows decile shares from the three sources among persons with disposable income equivalized using that scale.

The patterns this reveals are different in many respects to those in Table 5. First, the shift makes a big difference to the trends shown by the HBS. In particular, the share of the top decile now increases rather modestly, by only 0.3 rather than 1.5 percentage points. This increase is also offset by a decline for the 9th decile, so the top quintile sees no increase in share. So there is not a marked overall shift towards the top, though the bottom does lose out and the middle gain. Turning to the ECHP, the trend it displays is now very different to Table 5: there is no decline in share for the bottom decile, and the top decile loses share dramatically—falling by 3 percent of total income.

Finally in the LII we also no longer see declines in shares for the bottom three deciles, although the share of the bottom decile does still fall slightly. Rather than deciles 6–9 it is now deciles 4 and 5 that gain substantially. At the top, the share of the top decile is no longer stable but now falls by over 1 percent.

So the shift in focus from household unequivalized income to person-weighted equivalized income certainly makes a substantial difference to measured inequality trends—and both first principles and conventional practice now suggest that the latter is the more relevant in trying to capture personal living standards. However, even after harmonization in terms of the unit of analysis and equivalization, we are left with substantially different trends being shown by the different sources. This is the case towards the bottom, where the HBS shows the share of the bottom quartile falling, the LII surveys show stability, and the ECHP shows



TABLE 7  
 DECILE SHARES IN EQUIVALIZED DISPOSABLE INCOME AMONG PERSONS USING ALTERNATIVE INCOME  
 MEASURES, ECHP (EQUIVALENCE SCALE 1/0.7/0.5)

Decile	Share in Total Equivalized Disposable Income (%)			
	Annual		Current	
	1994	2001	1994	2001
	%	%	%	%
Bottom	3.5	3.4	3.6	3.5
2	4.6	4.9	4.7	5.1
3	5.6	6	5.7	6.1
4	6.4	7.2	6.6	7.1
5	7.4	8.5	7.5	8.3
6	8.7	9.7	8.5	9.4
7	10.4	10.8	10	10.7
8	12.4	12.3	12	12.2
9	15.3	14.7	15.3	15
Top	25.7	22.6	26.1	22.6
All	100	100	100	100

an increase. However, this is dwarfed by the differences at the top, which range from stability to a drop of 3 percentage points. Clearly we have more work to do in trying to understand these measured differences.

One remaining potential source of difference is in the income measure itself. While all three sets of results in Table 6 relate to equivalized income among persons, the income concept used in the ECHP is still annual income in the previous calendar year rather than current as in both the LII and HBS. To see how much difference this makes we can compare those ECHP figures with decile shares for an alternative income measure also available in the ECHP database which relates mostly to income in the previous month. (This is much closer to but not identical with the current income measure employed in the LII and HBS.) Table 7 makes this comparison for income equivalized again with the 1/0.7/0.5 scale and distributed across persons, and reveals little difference between the annual and “current” income distributions in either 1994 or 2001, except that the share of the top decile is slightly higher with current than with annual income in 1994.

*Explaining the Remaining Differences?*

Why then is the decline in the share of the top decile much larger in the ECHP than the LII, having harmonized on equivalized income among persons—the share of the top decile was 1 percentage point higher in the ECHP than in the LII in 1994, whereas in 2000/01 it was 1 percentage point lower. Several factors may be at work, though it is difficult to identify their effects precisely. First, a very small number of cases right at the top of the income distribution can make a substantial difference to the share of the top decile. A handful of high-income households and the way they are weighted largely account for the gap observed in 1994 between the share of that decile in the ECHP versus the LII. Second, attrition in

panel data over time may then have a substantial impact if a number of these households are “lost” to the sample. This can be amply demonstrated by reference to the LII survey for 2001, when the initial sample had been substantially supplemented by additional cases because of the scale of attrition. (Overall, by 2000 a total of 5,500 individuals had been followed since 1994, representing only about 40 percent of all the adults in the first wave; a new sample of 5,200 persons was then added.<sup>10</sup>) If we compare the share of the top decile for the full 2001 sample after supplementation with the corresponding figure for the “continuing” sample only, we find that the latter is about 1.5 percentage points higher. So this suggests that the supplementation of the sample has indeed had a substantial impact—but these additional cases were not included in the ECHP.

This suggests that in assessing trends in the distribution over this period, greater weight should be placed on the LII and HBS. Focusing on them, the broad pattern is similar in suggesting relatively modest declines in shares towards the bottom, but the picture at the top is still something of a contrast, a small increase (in the HBS) versus a fall of about 1 percentage point (in the LII). The LII may still be affected by its panel nature despite sample supplementation and appropriate reweighting, and the HBS has a sample size that is about twice as large, so perhaps most weight might be placed on the latter. The difference in overall trend in inequality between them should not in any case be exaggerated: the Gini coefficient in the HBS is roughly stable at about 0.31, whereas from the LII one would see a fall from just above that figure to just below it—0.32 to 0.30. What is striking is that neither source suggests the substantial increase in income inequality that many domestic commentators have seen to be accompanying Ireland’s economic convergence with its higher-income EU partners.

### *“Widening Gaps”?*

Much of that commentary has been in terms of “widening gaps” between the rich and the poor. While our primary focus here is on income inequality rather than poverty, it is worth noting that the numbers falling below relative income thresholds derived as proportions of mean or median incomes have certainly risen over the course of Ireland’s economic boom. Taking the commonly-used threshold of 60 percent of median equivalized income, for example, about 16 percent of persons were below that level in 1994 but the 2001 the corresponding figure was 22 percent (see Whelan *et al.*, 2003 for details). This reflects the fact that social security support rates, though increased a good deal more rapidly than consumer prices, lagged significantly behind the very rapid rise in incomes from work and property. This meant that the impact of the boom in bringing very substantial numbers from unemployment into work was more than offset by the numbers of long-term pension recipients (notably the elderly) who fell below such relative thresholds.

It is important, however, to emphasize that this was taking place in a context where real incomes and living standards were improving throughout the distribution, though at a varying pace. This is highlighted by the very different picture

<sup>10</sup>See Whelan *et al.* (2003, Table 2.1, p. 6).

conveyed by income thresholds held constant in purchasing power terms rather than indexed to average incomes. Suppose, for example, we take the 60 percent of median threshold in 1997, the middle of the period of very rapid growth, when about 18 percent fell below that threshold. A threshold with the same purchasing power would have had 36 percent falling below it as recently as 1994 and by 2001 only 3 percent are to be found below the corresponding “real” threshold. So over a period of such unprecedented growth, the benchmark used in measuring poverty makes all the difference to the picture one sees. Questions certainly need to be asked about relying on purely relative thresholds to capture trends in poverty in such circumstances, and much of the focus in analyzing poverty in Ireland over the period has been on levels of deprivation as reflected in a range of non-monetary indicators, and on “consistent poverty”—those both falling below relative thresholds and reporting enforced deprivation of a quite basic kind (see, for example, Nolan, 2003; Whelan *et al.*, 2003).

The perception of “widening gaps” depends not only on what is happening to the poor, but also what is happening to the rich—and it would not be surprising if they did particularly well in a boom. The difficulty is that general household surveys may not be best placed to capture trends right at the top of the distribution, both because it is difficult to represent any small group with limited sample size, and because those at the top may be particularly elusive. For this reason we now go on to look at an alternative source of data which has information about that group, namely administrative records from the tax system—which as we shall see also faces particular problems, but is worth investigating.

#### 4. TOP INCOMES IN IRELAND DURING THE BOOM

Income tax data was used in the past to study the income distribution in many countries, a notable example being Kuznets’ mid-century study of United States data on which he based his hypothesis about a long-term tendency for inequality to rise and then fall as development occurs. There has recently been a resurgence of interest in exploiting such data following the influential study by Piketty (2001, 2003) of long-term trends in the shares of top income groups in France. This study used data from income tax records over the 20th century to produce some fascinating and indeed dramatic findings. Together with the depth and sophistication of the analysis, this has encouraged others to look again at data from this source to examine long-run trends in top incomes in various countries—notably Atkinson (2001) for the United Kingdom, Piketty and Saez (2003) for the United States, and Saez and Veall (2005) for Canada. In the same spirit Nolan (2004) uses this type of information to look for the first time at long-run trends in top income groups in Ireland from the 1930s up to the end of the 20th century. Here we employ the methods described in that paper but extend the analysis to produce more detailed results for the period on which this paper is focused, namely the 1990s.

For the years from 1990 to 2000, figures were published each year in the Statistical Report of the Revenue Commissioners showing taxpayers categorized by income range and mean income for each category. Two distinct income concepts are used. The first is referred to as “total income,” that is the total income of taxpayers from all sources “as estimated in accordance with the provisions of the

Income Tax Acts.” It is thus net of such items as capital allowances, allowable interest paid, losses, allowable expenses, retirement annuities and superannuation contributions. Figures have also been published for the years from 1989–90 onwards using a concept referred to as “gross income,” which includes all those items except superannuation contributions. The results for the two are similar, and we concentrate on those for “gross income” (whereas Nolan (2004) focuses on “total income” since it is the concept employed in the data published in earlier years).

To use this type of information to derive estimates of top income shares, one needs figures for the total number of tax units in the population and for total household income, in order to convert the tax data into percentages of total income recipients and income. One then needs to interpolate/extrapolate from these to the shares for the specific groups of interest. The unit of tax we take to be the single adult or married couple with dependent children if any. (From the 1980s married persons could submit separate returns if they so wished though their total tax liability would not be affected, but only a relatively small number do so; the more recent move towards separate assessment does not affect the years for which data have been published.) We thus require a control total for the aggregate number of such units in the population as a whole (rather than the total appearing in the tax statistics). We can derive this directly for years in which there was a Census of Population, by taking the total number of adults (aged 18 or over) and subtracting the total number of married women. We then interpolate to produce figures for inter-Censal years, using linear interpolation (though a more sophisticated method of interpolating incorporating the official population estimates for each inter-Censal year could also be employed).

We then require an appropriate aggregate income figure for each year to allow income shares to be computed. For this purpose we simply employ the national accounts personal income aggregate as control total, without adjustment. This is problematic, because that national accounts aggregate includes some income that will not be in the tax data. The most obvious is the income that does not go to households but to non-profit institutions such as charities and life assurance funds. In addition, employers’ social security contributions and imputed rent of owner-occupiers are included in the personal sector aggregate but not in the income tax figures. This is a priority for further investigation, but for the present we have made no such adjustment.

Using these aggregates for the total number of tax units and total income in the population, we then convert the numbers within each income range from the tax statistics and the total income accruing to them into shares, of all tax units and of total income respectively. To move from that point to estimated shares for the groups of interest, we then interpolate assuming a Pareto distribution. We could extrapolate into the open range to produce an estimate for that group, also assuming a Pareto distribution, but that would raise questions which interpolation within closed ranges does not face and here we do not seek to distinguish shares which would require extrapolation into the open-ended range. We concentrate on the share of those at the top of the income distribution, looking at the top 10 percent and the top 1 percent of taxpayers (whereas Nolan (2004) looks only at the top 1 percent or 0.5 percent).

TABLE 8  
ESTIMATED SHARE OF TOP ONE PERCENT IN TOTAL PERSONAL  
INCOME, IRELAND, 1990–2000

Year	Share of Top 10% (%)	Share of Top 1% (%)
1990	21.77	4.84
1991	22.41	5.21
1992	23.4	5.51
1993	21.12	4.78
1994	21.95	4.99
1995	22.23	5.15
1996	22.48	5.36
1997	22.53	5.54
1998	23.03	6.21
1999	24.44	7.16
2000	25.29	7.86

*Source:* Calculated from Annual Reports of the Revenue Commissioners using methods described in Nolan (2004).

The results are shown in Table 8. Looking first at the top 10 percent, a substantial increase in share is seen from 1995, accelerating in 1999 and 2000. Over the decade this meant that the share had risen from under 22 percent to over 25 percent. Turning to the top 1 percent, this also rose sharply in the second half of the decade, from under 5 percent to almost 8 percent—so all the growth in share for the top decile was actually concentrated in the top 1 percent. This meant that by the end of the 1990s the share of the top 1 percent was more than twice the level prevailing through the 1970s and 1980s.

This is very different to the picture suggested by the survey data, and seems to confirm the anecdotal assertions that those at the top did particularly well during the economic boom. However, the obvious issue in relation to data from tax records, for Ireland as elsewhere, is whether we can believe they give a broadly accurate reflection of reality. Some would argue instead that they are so polluted by attempts by the wealthy to evade and avoid tax that they cannot be relied on. In the Irish case, one would certainly be concerned that changes in the reporting of top incomes may have played a significant role in the last decade. The rigor with which income tax was administered has certainly tightened significantly, including some high-profile investigations into tax evasion of various sorts, and the marginal rate of income tax has also come down significantly. Both these factors could lead to a greater proportion of income being reported to the tax man, as evasion is seen to become more risky and avoidance less necessary. It is thus difficult to assess the extent to which the rapid increase in incomes right at the top reflects trends in actual incomes versus reporting behavior: the likelihood is that both contribute to the observed rise in top income shares. In the household surveys, on the other hand, the problem is in all likelihood the difficulty in capturing a sufficient number of those right at the top of the income distribution to properly capture trends in top income shares. (The incomes of those who are at the top and in the sample are not top-coded in the Irish case, as they are in some countries/surveys.)

## 5. CONCLUSIONS

Spectacular economic growth in the past decade has seen the gap in average income between Ireland and the richer OECD countries narrow dramatically. However, this growth has not greatly affected the Irish ranking in terms of income inequality. Ireland remains something of an outlier among rich European nations in its high degree of income inequality, though still falling well short of the level seen in the United States. Capturing the level and trend in income inequality faces researchers with a variety of not only conceptual but also data challenges, some of which have been illustrated by our discussion of the evidence for Ireland, which does not accord with the widespread perception of significantly increasing overall inequality. Ireland has a high degree of economic inequality in comparative terms after the boom, just as it did beforehand and indeed as far back as the early 1970s when nationally representative household survey data first became available. This reflects a variety of factors, but it is noteworthy that it applies to disposable income but much less so to market income in terms of market income—before direct taxes and transfers—Ireland is much less of an outlier compared with other rich EU countries. A lower redistributive “effort” is then a key ingredient in the level of inequality one finds in disposable income. This again is not a new development, but is a long-standing characteristic of Ireland’s welfare state, with its heavy reliance on means-tested programs and on flat-rate rather than earnings-related transfers. (Ireland in this respect has much in common with the U.K., which also has a similar level of disposable income inequality.) Ireland’s new-found prosperity provides a “social dividend”, and choices about how it is used will fundamentally affect whether the current high level of income inequality persists into the future.

## APPENDIX

TABLE A1  
MACROECONOMIC COMPARISON: MOST RECENT YEAR

Nation (year)	Average Standard of Living		OECD Standardized Unemployment Rate	OECD Social Expenditures on Non-elderly <sup>2</sup>
	GDP/Capita (in 2000 US\$) <sup>1</sup>	Index		
United States (00)	34,575	100	4.0	2.8
Canada (00)	28,367	82	6.1	6.0
Ireland (00)	28,035	81	4.2	7.5
Sweden (00)	26,567	77	5.9	12.6
Netherlands (99)	26,517	77	3.4	10.5
Finland (00)	25,359	73	9.7	12.1
Germany (00)	24,851	72	7.9	8.9
United Kingdom (99)	23,723	69	6.1	6.4
Belgium (97)	23,541	68	7.0	8.9

*Source:* OECD (<http://www.oecd.org>); and OECD (2002).

*Notes:* <sup>1</sup>Using 2000 PPPs, price adjusted in each nation to correct year.

<sup>2</sup>Countries with data year 2000 are given the most recent (1999) values available from OECD.

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