Where Do We Draw the Line?
Suggesting a Threshold for Extreme Inequality

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London July 3rd 2015

Presentation SASE, Mini-Conference:
Inequality of What?: Social Monitoring and the Difficult Choice of Analytical Concepts and an Implementable Metric
Three main points

- Improving the distribution starts with measuring it appropriately first, with an indicator fit for purpose: to detect changes in the tails (esp. top).

- We then need to fix an objective (threshold), the “too much”, below which we want to remain, and formulate policy accordingly.

- The indicators proposed here (Palma ratios) could help us getting there: to “the inequality level we want”.
➢ The experience of the poverty line
➢ (GDP)

➢ Choosing a threshold
  ➢ The indicator
  ➢ The level
Every indicator encapsulates an **implicit value-statement**: do we care mostly about changes in the middle of the distribution, or in the extremes, transfers between which groups of the population?

The generic usage of the Gini indicator as inequality measure not only makes **interpretation** difficult without training, it also **obscures developments in the high and low ends** of the income distributions, where most of these changes occur.

How does the distribution **actually** look like?
Graph 2: Income Distribution in 116 countries, by population share (2008)

Panel A: The tails define the inequality level while the middle remains "stable"

Panel B: The diversity of the top ventile contrasts with the homogeneity of the 19th ventile

Source: constructed with data from Milanovic 2014.
Inequality in the Emerging Countries, 2002-2011

Figure 7: Income Shares by Population Group, 2002-2011

Source: author's elaboration with data from Milanovic (2015)
Even within top decile distribution is highly unequal, skewed towards top percentiles (D10 has highest Gini coefficient compared to all other deciles)

**Graph 3: The Top of the Income Distribution for 116 countries (2008)**

(Income shares held by the 10th decile and the 19th and 20th percentiles)

Source: constructed with data from Milanovic (2014).
“Gini vs. Palma” shows: if we care about concentration, indicators must be sensitive to changes in the extremes.

So is the 10/40 ratio the solution?
Extending the Palma Ratio

Graph 6: Comparing the original Palma with the Palma v.2 and v.3
(41 countries, latest year)

- Palma v.2: ratio of top 5% to bottom 40%
- Palma v.3: ratio of top 1% to bottom 40%

World average Palma v.2 = 1

Source: constructed with LIS (2014) data.
➢ Income concentration at the very top is higher than expected from the information provided by “standard” inequality indicators.

➢ Such levels are unlikely to be in the (best) interest of the majority of people.

➢ Improving the distribution starts with measuring it appropriately first, with an indicator fit for purpose: to detect changes in the tails (esp. top).

➢ We then need to fix an objective (threshold), the “too much”, below which we want to remain, and formulate policy accordingly. For that: We lack a concrete objective to aspire.

➢ The indicators proposed here (Palma v.2 and v.3) could help us getting there: to “the inequality level we want”.

➢ The increased discussion space about inequality in public discourse currently opens up an unprecedented policy space.

➢ Fill this vacuum with a concrete and achievable goal to reach
Thank you!
Comments?