PROMOTING
GROWTH AND
SHARED PROSPERITY
IN THE UK

DISCUSSION PAPER

THE CASE FOR AUSTERITY AMONG THE RICH

Danny Dorling

March 2012

Institute for Public Policy Research

ABOUT THE AUTHOR

Danny Dorling is a professor of human geography at the University of Sheffield. His book *The no-nonsense guide to equality* has just been published by New Internationalist.

ABOUT IPPR

IPPR, the Institute for Public Policy Research, is the UK's leading progressive thinktank. We produce rigorous research and innovative policy ideas for a fair, democratic and sustainable world.

We are open and independent in how we work, and with offices in London and the North of England, IPPR spans a full range of local and national policy debates. Our international partnerships extend IPPR's influence and reputation across the world.

IPPR
4th Floor
14 Buckingham Street
London WC2N 6DF
T: +44 (0)20 7470 6100
E: info@ippr.org
www.ippr.org
Registered charity no. 800065

BOLD IDEAS for CHANGE

ABOUT PROMOTING GROWTH AND SHARED PROSPERITY

This major programme of work aims to identify public policies that will promote the economic growth needed to return the UK to full employment and ensure that the benefits of future prosperity are more equally shared.

For more information, see:
http://www.ippr.org/research-projects/44/7144/promoting-growth-and-shared-prosperity-in-the-uk

Many people, no matter how well-off they are, think they are hard done by, or at least that they are deserving of their income and wealth. Beliefs such as this may have contributed to the cut in the 50p tax rate announced in the budget in March 2012.

In November 2011, the High Pay Commission reported that the pay of the chief executives of the 100 largest companies on the London stock exchange had risen by 49 per cent during the previous year, compared with average increases of less than 3 per cent for their employees. As 2012 began, each chief executive could, on average, expect to receive around £4.2 million, 145 times the average pay of their employees and some 162 times the British average wage.

Because pay distributions are almost always skewed, the majority of these chief executives will have received less than the average of £4.2 million, in some cases much less. If they only compare themselves with those they consider their peers, and don't look down, they may well think they are badly-off and deserving of more. But if they ever did look down, they would see a different picture.

In January 2012, BBC reporter Michael Robertson used the World Top Income database to report how rapidly income inequalities between all households in Britain have been rising. The rise in inequality during the Tony Blair years was rapid. As Blair came to power, the best-off one-thousandth (0.1 per cent) of the population received an income 61 times what the 90 per cent at the bottom received; by 2007 this ratio had risen to 95 times.

Table 1
Income of UK households, 1997–2007

	Average income: Bottom 90%	Average income: Top 1%	Multiple: 1% vs 90%	Average income: Top 0.5%	Multiple: 0.5% vs 90%	Average income: Top 0.1%	Multiple: 0.1% vs 90%
1997	£10,567	£187,989	18	£271,626	26	£646,358	61
2007	£12,430	£301,325	24	£452,476	36	£1,176,947	95
Increase: 1997–2007	**18%**	**60%**		**67%**		**83%**	

Source: BBC *The Wealth Gap* (broadcast 17 January 2012), analysis from World Top Income database. Data provided direct to author.

This paper suggests there is some merit in producing estimates of the alternatives to continued income polarisation of the kind revealed in table 1. Would a little more austerity at the top and a little less at the bottom of the income distribution cancel each other out in terms of cost, or even save a huge amount of money? Might it result in greater overall spending on the necessities of life and less spending on luxuries (or spending overseas)? This paper does largely ignore stores of wealth in the UK – these are very high and are a further possibility for alternative austerity and making great national savings. In early March 2012, business secretary Vince Cable raised again the idea of a 'mansion tax' on just a small part of that stored wealth, so this debate is ongoing – but here I concentrate on excessive incomes, not wealth.

The general case against austerity has been well made: the economy moves into a cycle of decline. A sensible government, even a right-wing one, would act to stimulate the economy. However '… if there are also strong ideological pressures towards immediate austerity, then this change of direction may not occur' (Wren-Lewis 2011). And there are such ideological pressures: 'The longer-term goal is to shrink the state, free up the market and set British political economy on a new course' (Taylor-Gooby 2012).

Let us suppose that current policy fails, that it becomes clear that the freed-up market is not bringing growth within the current parliament, and so even more money needs to be saved. One possible path to follow is greater austerity for the rich.

Seen from Westminster, this scenario might appear fanciful, but viewed from the Midlands, from the north of England, from Wales, Scotland or Northern Ireland, it is much more palatable. It is also more palatable for people who are not well-off but are living in south-east England. For the majority of the population of the UK who are or will be badly affected by the current austerity programme, and in areas where very few of the top 1 per cent of income earners live. Austerity for the rich could prove popular.

In October 2011, the Institute for Fiscal Studies (IFS) and Joseph Rowntree Foundation (JRF) published a key report (Brewer et al 2011). It is worth reading the summary points again, while remembering, in each case, that this will mostly occur outside of the south-east of England and outside all but the poorest parts of London:

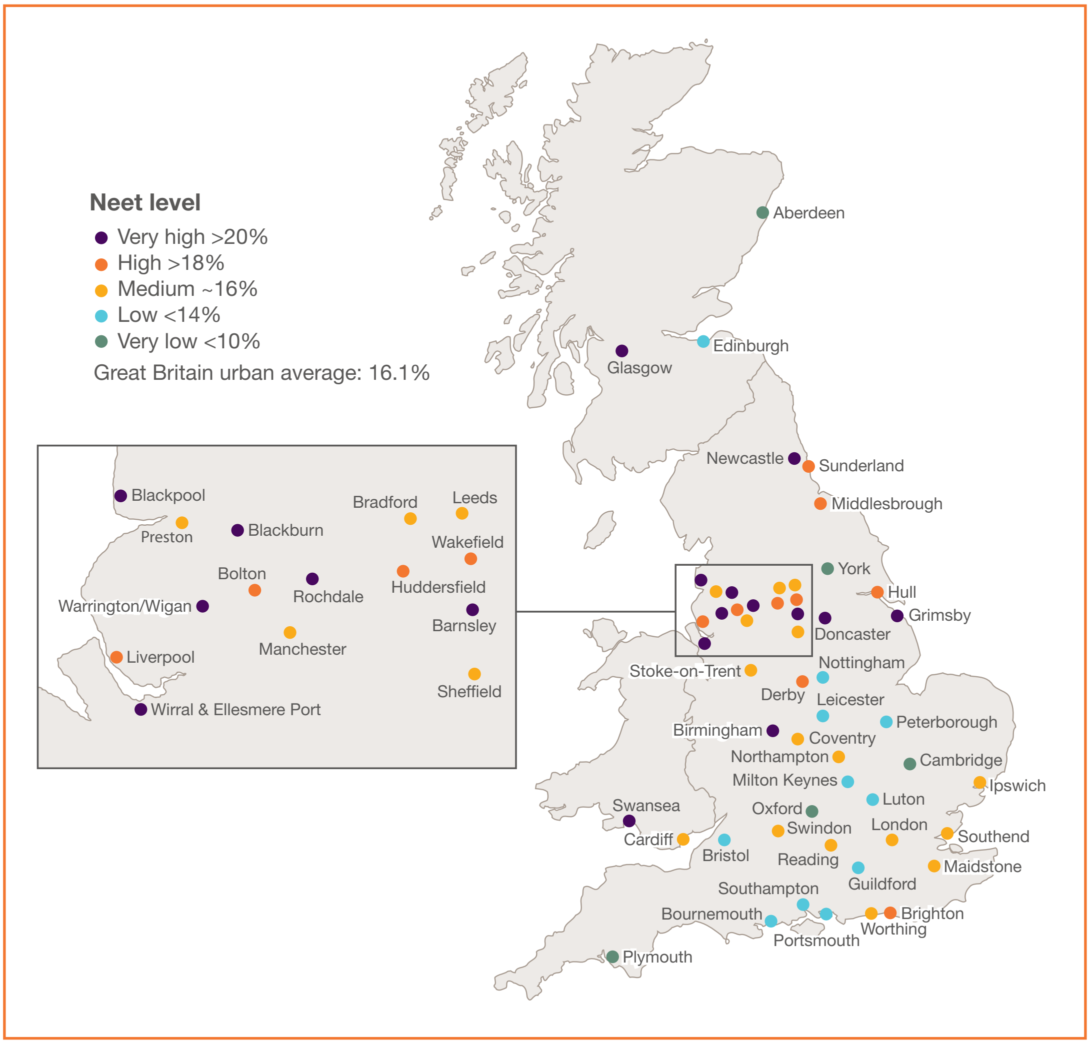
1. The number of children in relative poverty is forecast to rise from 2.6 million in 2009/10 to 3.3 million by 2020/21(before housing costs), and that of working-age adults from 5.7 million to 7.5 million by 2020/21.
2. Relative child poverty will rise from 20 per cent currently to 24 per cent by 2020/21, the highest rate since 1999/2000 and considerably higher than the 10 per cent target in the Child Poverty Act.
3. The proportion of children in absolute poverty is forecast to rise to 23 per cent by 2020/21, compared with the 5 per cent target.
4. Absolute poverty will rise considerably in the next few years as earnings growth is forecast to be weak but inflation high.
5. Universal Credit should reduce poverty substantially, but the effect of other government changes to personal taxes and state benefits will more than offset this.

Now consider the map of the worst-affected parts of Britain in terms of young people being out of the labour market or education (known as 'NEETs': not in employment, education or training)(see figure 1 over). Note how clear the divide is north and south of the Severn–Wash line. (The capital is denoted as 'medium' because only one dot is shown, masking wide differences in outcomes in different parts of London.) The status quo – 'austerity for the 90 per cent' – hurts people the most outside of the south east.

This map was drawn up using data gathered before deep austerity began. As the dots nearest the Severn–Wash line turn from blue to yellow to orange, the south east of England will be left as an outlier.

If we were to draw the inverse map, showing relative affluence, then the south east and London would lead the way. Barclays Wealth's report of 2011 showed clearly that it was here where most wealth resides, where house prices are highest and still rising (six times the national average number of properties are valued at more than £1 million here), where luxury car dealerships are most commonly located (three times as many as nationally), where day pupils in private schools are concentrated (twice as many as nationally), and where most Michelin-starred restaurants are (four times as many as elsewhere in the UK, with five times as many Michelin stars). Two-and-a-half times the national average number of charities were set up in this single region of England (Barclays 2011: 24). Setting up charities correlates highly, geographically, with buying expensive cars, consuming gourmet meals and purchasing a privileged education. These are all activities that appear to be increasing in concentration and possibly in total value as Britain, overall, economically contracts.

Figure 1
Cities with highest/ lowest levels of NEET 16 to 24-year-olds



Source: Reproduced from data in Lee and Wright 2011

There will be no easy way out of this conundrum. In a country unlikely to become so rich again quickly, someone will have to pay. It is as if decision-makers in the south east of England read the following words and decided it would not be them or their friends (their social groups) or their neighbourhoods (their geographical groups) that would suffer:

> **'During the past fourteen months the illusion has been sustained that no matter how badly the world economy slumps, there is always a pain-free way out of it. Once the realisation dawns that there is not, and that the pain will be severe, the question is posed that has not really been posed for twenty years: who should feel it?'**
> Mason 2010: 233

However, across most of the rest of the rich world, attitudes appear to differ. Throughout 2011, numerous press stories were released across western Europe of the affluent being asked to pay more tax (Pidd 2011). It was as if in the mainland of Europe the rich could foresee the dire consequences of not permitting some redistribution, the rising social unrest and violence of the alternative. Even in the United States new taxes were being proposed:

> **'Here's how the tax would work. Once a year, the Internal Revenue Service would calculate the Brandeis ratio of the previous year. If the average 1-percenter made more than 36 times the income of the median American household, then the IRS would create a new tax bracket for the highest 1 percent of income and calculate a marginal income tax rate for that bracket sufficient to reduce the after-tax Brandeis ratio to 36.'**
> Ayres and Edlin 2011

The Brandeis ratio – the ratio between the income of the top 1 per cent and the median income – was 36 in 2006. In fact, much greater equality than this is possible.

Before Ayres and Edlin's suggestion was published in the New York Times (in July 2011), the Washington Post ran a story which included the table below. A debate on inequality was taking place within the two major US broadsheet newspapers. The Washington Post suggested that if income differences between US taxpayers were to return, or were aided a little to return, to 1970s' levels, then 90 per cent of all American taxpayers would be better off and the United States would save 22 per cent of its total salary bill, or approximately £1.8 trillion dollars every year. The implicit question was: can Americans move in that direction? Rather than trying to recoup all their economic losses through increased growth, could some of the damage be mitigated by reducing the continuous redistribution of monies towards the rich?

Table 2
Income changes, US, 1970–2008

Income level	Number of people	Average income, 2008	Overall change 1970–2008	Annual income, 1970	Salary cost, 2008 ($tr)	Salary cost, 1970 ($tr)
Top 0.1%	152,000	$5.6 million	385%	$1.15m	0.9	0.2
Top 0.1–0.5%	610,000	$878,139	141%	$364,000	0.5	0.2
Top 0.5–1%	762,000	$443,102	90%	$233,000	0.3	0.2
Top 1–5%	6.0m	$211,476	59%	$133,000	1.3	0.8
Top 5–10%	7.6m	$127,184	38%	$92,000	1.0	0.7
Bottom 90%	137.2m	$31,244	-1%	$31,560	4.3	4.3
Potential saving	**22%**				**8.2**	**6.4**

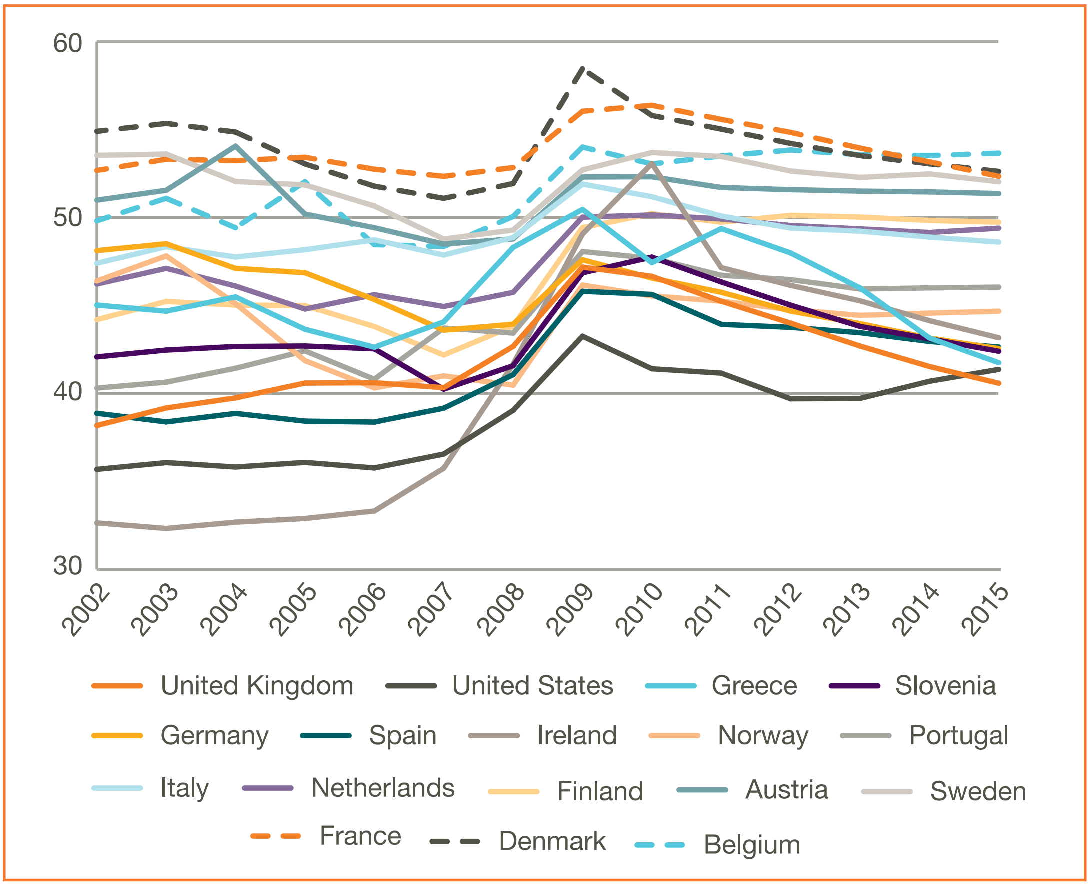
Source: *Washington Post*, July 2011: http://www.washingtonpost.com/wp-srv/special/business/income-inequality/
Note: Salary costs (1970 and 2008) derived by author; adjusted for 2008 dollars.

All I have done to the table above is to add the last two columns by simply multiplying up the salary bills by numbers of taxpayers. This results in the $8.2 trillion total salary bill. This kind of calculation cannot be rare, but I haven't been able to find it done more generally.

In the US, it is assumed that a large newspaper readership can understand tables such as that shown above. But as yet, there is no similar debate in Britain. The Labour party, perhaps afraid of the label of 'envy-mongering' has said little about the money that could be saved through a bit of austerity among the rich, austerity which would affect only one-tenth of the population at most, and primarily only 1 per cent of all voters. In the US, $1.1 trillion of that surplus $1.8 trillion in total income is taken by the best-off 1 per cent, that is, by people who would remain incredibly wealth without some of it, or even incredibly wealthy without any of it (with $0.6 trillion to share between them).

Should people be told of the savings that could be made if inequalities were reduced, even while 90 per cent become slightly better off? Would they simply retort 'how do you achieve it?' or would they find it useful to know? In the US, knowing just how much of all additional wealth was appropriated by those at the top could have aided the election of a Democrat president in 2008 and might yet be crucial to the likelihood of his reelection in 2012. Without these facts and figures, Barack Obama's proposed policies to increase public spending in the US to levels greater than in the UK by 2015, possibly for the first-time ever, would be difficult to sell to the public. The effect of these proposals is shown in the chart below.

Figure 2
Public expenditure, selected countries, 2010 (% of GDP)



Source: Author's work from IMF data

In contrast to the US, there is widespread misunderstanding in the UK of just how low public expenditure was under the New Labour government. Or that the IMF forecast for 2015 puts the UK's forecast public spending lowest among the 16 EU nations and the US (as figure 2 shows). Over the period 2002–2007, only Spain, Ireland and the US spent a lower proportion of their national income on public goods than the UK. The countries which were spending more (and taxing more) tend to have weathered the storm a little better by comparison with some low public spenders, like the UK.

How much money could be saved by austerity among the UK's rich? What if 90 per cent of taxpayers were somehow to become better-off but income differentials were also to return to 1970s levels? Table 3 (over) shows that the country would save 27 per cent of its total salary bill, or approximately £194 billion every year. These numbers are calculated using an earlier table drawn up by Mike Brewer and his colleagues at the IFS.

Table 3
Income changes, UK, 1970–2005

Income level		Number of people	Average income, 2005	Overall change 1970–2005	Income share, 2005	Annual income, 1970	Income share, 1970	Salary cost, 2005 (£bn)	Salary cost, 1970 (£bn)
Top 0.1%		47,000	£780,043	694%	5.0%	£98,193	1.2%	37	5
Top 0.1–1%		420,000	£155,832	181%	9.0%	£55,535	5.9%	66	23
Top 1–10%		4.2m	£49,960	143%	28.8%	£20,525	21.8%	211	87
Bottom 90%		24.8m	£16,837	48%	57.2%	£11,400	71.2%	418	422
Potential saving	**27%**							**731**	**537**

Source: Based on figures given in Brewer M et al (2008) *Racing Away? Income inequality and the evolution of high incomes*, London: Institute for Fiscal Studies
Note: Salary costs (1970 and 2005) derived by author; adjusted to be equivalent, in 1970, to 2005 pounds. (The 1970 salary cost assumes a 1 per cent increase in income for the bottom 90 per cent.)

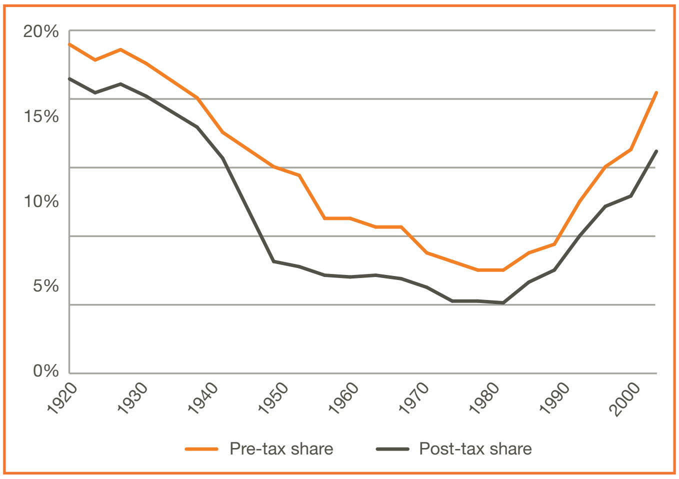
Almost £200 billion a year would be saved in a return to 1970 inequality levels, even with 90 per cent of people being made 1 per cent better off in real terms than they currently are. Even a 2 per cent move in that direction would save £4 billion a year. The last time such a saving occurred it took over 50 years to play through, from roughly 1920 to 1970, at a rate of around 2 per cent a year. So this is not a pipedream: it is what occurred the last time the UK became so unequal. It happened through a variety of mechanisms, but above all else through restraint at the top, for fear of what a lack of restraint would result in.

In a country where the income and wealth gaps have become greater than at any point in living memory, and which are greater than in almost all other similar wealthy countries, you should expect very high and rising levels of crime, social disorder, dysfunction, rising polarisation, fear and anxiety. Econometric analysis of a century of international data has shown that riots occur when public spending is cut (Ponticelli and Voth 2011). General disdain for the rich rises similarly (Priestly 1944).

During and after the second world war, the tax take was increased, accelerating the rise in equality in the UK but, as the dark line in figure 3 (over) shows, most of that increased equality occurred before tax. The most rapid curtailment in top salaries and other incomes occurred under the Conservative government of 1951–55. What was seen as decent had changed.

The trends shown in figure 3 are not economic trends but political ones. In 1918, when inequalities were last as high as they are now, the fears of the British elite were strongly coloured by the 1917 revolution in Russia. For a few years in the early 1920s the downwards trend faltered, but then its course was reset by the likes of Keynes in the 1930s, Priestly in the 1940s and even the Tories of the 1950s: 'Keynes's friend Oswald Falk once told him that, for all the veneer of theory, all he had really done was codify "the moral feeling of an age…"' (Mason 2010: 226).

Figure 3
Income share of the top 1 per cent before and after tax, UK



Source: Dorling 2011: 292

Today, a renewed rise in decency would produce losers as well as winners. Consumption of the goods listed in the Barclays Wealth report would fall: luxury cars (especially beyond the first or second luxury car per household), meals in Michelin restaurants (especially on weekdays), and the most expensive of educations (especially boarding). This would have very concentrated geographical impacts. For example, there are 11 private secondary schools in the Royal Borough of Kensington and Chelsea – seven more than the number of state secondary schools to be found there (Durston 2011).

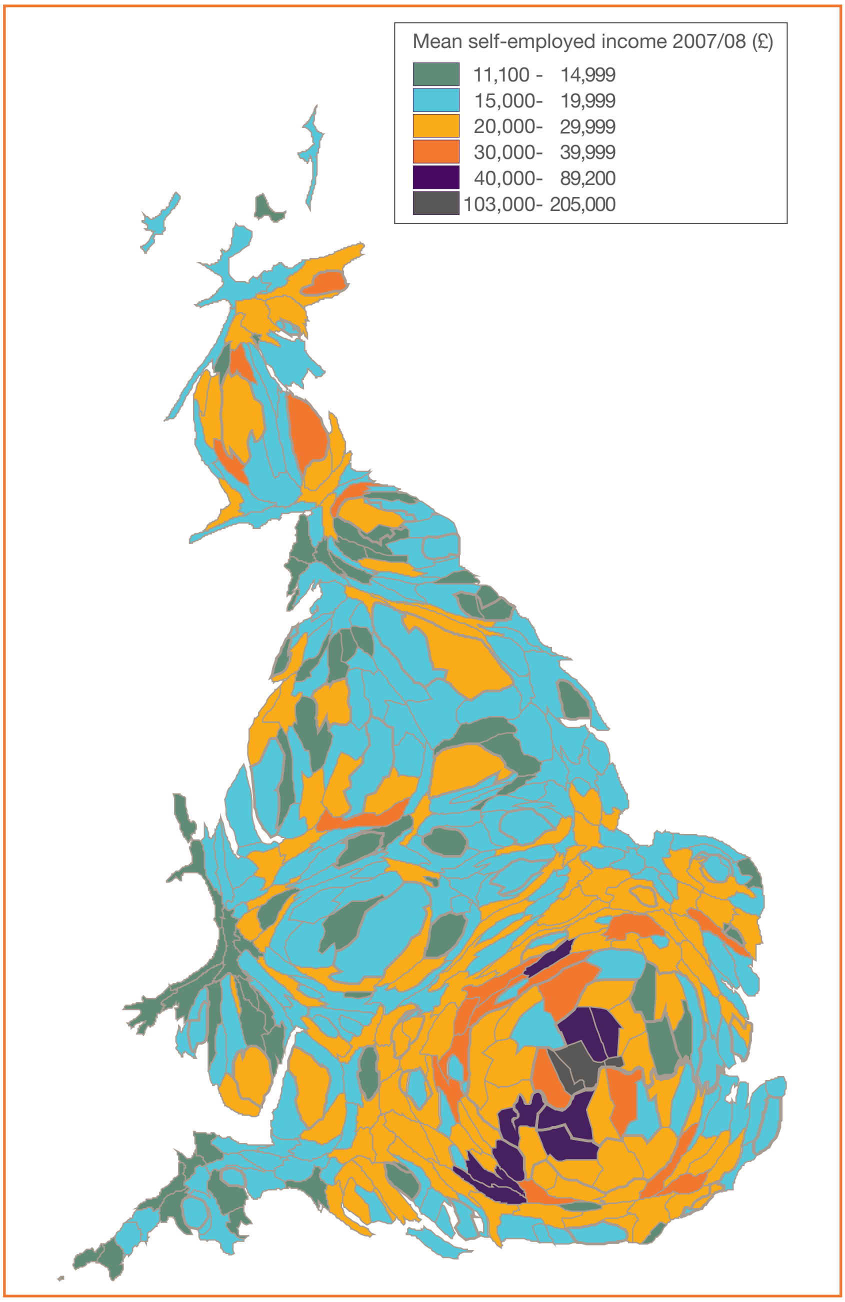
Table 4
Average self-employed income as declared to HM Revenue & Customs, 2007/08

Rank	Income (£)	Local Authority District	Rank	Income (£)	Local Authority District	Rank	Income (£)	Local Authority District
Highest			**Middle**			**Lowest**		
1	205,000	Kensington & Chel.	201	18,200	Stafford	388	13,200	Sandwell
2	125,000	City of London	202	18,200	Fife	389	13,200	W. Dunbartonshire
3	103,000	Westminster	203	18,000	Brent	390	13,200	Orkney Islands
4	89,200	Camden	204	18,000	Broadland	391	13,100	Newport
5	54,100	Wandsworth	205	18,000	Strat.-upon-Avon	392	13,100	Blyth Valley
6	53,200	Elmbridge	206	18,000	Falkirk	393	13,000	Allerdale
7	49,400	St Albans	207	17,900	North Somerset	394	12,900	Newham
8	49,100	Rich. upon Thames	208	17,900	Wear Valley	395	12,800	Ceredigion
9	48,400	Waverley	209	17,900	Gedling	396	12,800	Torfaen
10	45,700	Islington	210	17,900	East Ayrshire	397	12,800	Caradon
11	43,200	Merton	211	17,800	Wirral	398	12,800	Chester-le-Street
12	40,100	Guildford	212	17,800	Calderdale	399	12,700	Redditch
13	39,800	Hertsmere	213	17,700	Tameside	400	12,600	Kingston upon Hull
14	37,800	Chiltern	214	17,700	East Lindsey	401	12,300	Blackpool
15	37,700	H'smith & Fulham	215	17,700	Lincoln	402	12,200	Teesdale
16	37,000	Edinburgh	216	17,600	Doncaster	403	12,100	Blaenau Gwent
17	36,900	Windsor & M'head	217	17,600	York	404	11,900	Eden
18	36,800	East Renfrewshire	218	17,600	Oadby & Wigston	405	11,800	Hartlepool
19	36,300	Sevenoaks	219	17,600	Alnwick	406	11,300	Barrow-in-Furness
20	35,800	Barnet	220	17,500	Herefordshire	407	11,100	Copeland

Source: Dorling and Thomas 2011
Note: Table shows declared income: actual income may in some cases by higher, and is unlikely to be lower.

Figure 4 shows those areas which are likely to be most and least affected based on where salaries of the self-employed were highest and lowest in recent years.

Figure 4
Mean self-employed income, 2007/08 (£)



Decency becomes popular when indecency is seen to have briefly triumphed. The deputy prime minister promoted employee ownership in the same week in January 2012 that the ITEM Club (the Independent Treasury Economic Model) warned that the double dip recession had begun. At the same time, opposition members of parliament started talking about inequalities as being the biggest issue they faced, not just nationally but also locally. MP Hilary Benn, whose Leeds Central constituency has child poverty levels of 40 per cent, said: 'The single biggest issue we face in the city is about how we overcome the gap between those with wealth and opportunity and those without' (Casey 2012).

How many people know that 90 per cent of taxpayers in Britain could be better-off and the country could save almost £200 billion a year in pay and people would have differentials between their income levels which were no greater than those enjoyed in 1970? Ministers might talk of how many people they have taken out of paying income tax altogether – but they will not mention how they have increased taxation overall, especially through increasing VAT and reducing tax credits. When their economic arguments fail, they rely on hate to maintain their credibility. Hate 'benefit-scroungers', hate 'immigrants', hate the last government said to have 'overspent' your money. Overall they are saying 'be mean'. The following is an extract from an unpublished letter to the Guardian by one S Kraemer:

> **'It is easier to be mean in a society that has lost its heart. [A previous correspondent] fails to mention the poisonous effects on social bonds of inequality, higher now in Britain than it has been since before the second world war. Why does it matter? If you picture the degree of inequality as a slope on which we all live, it rapidly becomes clear how impossible it is for people at the bottom to move upwards, but also how anxious those further up are about slipping down. Nobody feels secure enough to be generous to others at any distance from themselves.'**

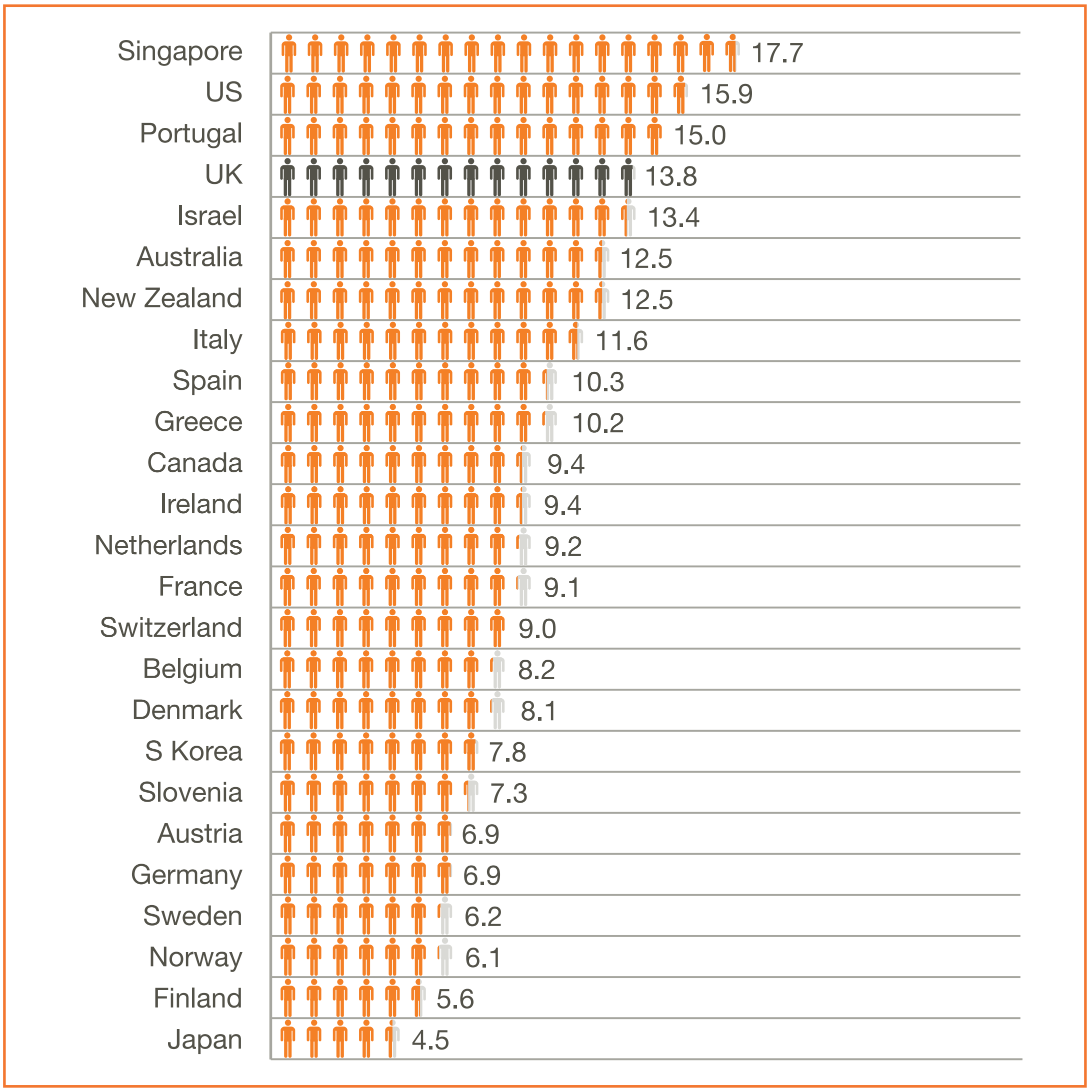
In 1918, our forebears began to become a little less mean, partly through the fear generated by distant events, by revolution and uprisings the year before, by some turmoil at home, by beginning to see a little more clearly. In 2012, how will their great-grandchildren respond? What is really in their best interests?

This paper ends with a graphic which makes clear the contemporary international inequality comparisons. When that graph is next updated, will the UK overtake Portugal on the back of further growth in inequality, or will we better our nearest rival Israel – will we have become just a little more equal?

Before there is any hope of progress the myth that reducing tax rates for the richest increases the amount of tax they pay has to be more widely dismissed. Figure 3 above shows how, from the early 1980s, income inequalities rose as the richest 1 per cent took more and more pay for themselves . As they took more pay for themselves their share of direct taxation also increased so that it is now well over 25 per cent of all income tax. That share did not rise because the top tax rates were reduced to 40 per cent in 1988 by Nigel Lawson.

Had Lawson not reduced top taxes in 1988 the rich might have been less encouraged to become so greedy. In a more equal, more normal UK the tax take would be far more evenly spread because salaries and wages would be more similar. If pay were a little more evenly spread then far more people would know they were contributing to the common good, rather than being told they were to be taken out of paying income tax altogether because they were so poor.

Figure 5
Income/consumption ratio: top 10 per cent vs bottom 10 per cent



Note: In some cases estimates of income based on levels of consumption are used in creating this UN data, although that is unusual in the case of affluent countries. This remains the most up-to-date set of estimates on decile income inequality and those I would consider most reliable as a source for the ranking of affluent nations. They are also far easier to understand as a set of statistics in comparison to Gini coefficients and other more obscure measures. See Dorling 2012, chapter 44 for more details and sources.

References

Ayres I and Edlin A (2011) 'Don't Tax the Rich. Tax Inequality Itself', *New York Times*, 18 December 2011. http://www.nytimes.com/2011/12/19/opinion/dont-tax-the-rich-tax-inequality-itself.html

Barclays (2011) *2011 UK Wealth Map: A white paper in co-operation with Ledbury Research*, London: Barclays Wealth

Brewer M, Browne J and Joyce R (2011) *What levels of poverty might there be for children and working-age adults by 2020?*, London: Institute for Fiscal Studies and Joseph Rowntree Foundation. http://www.jrf.org.uk/publications/child-and-working-age-poverty-2010-2020

Casey S (2012) 'Stark truth of the Leeds child poverty gap', *Yorkshire Evening Post*, 15 January 2012. http://www.yorkshireeveningpost.co.uk/news/latest-news/central-leeds/stark_truth_of_the_leeds_child_poverty_gap_1_4127423

Dorling D (2011) *Fair Play*, Bristol: Policy Press

Dorling D and Thomas B (2011) *Bankrupt Britain: An Atlas of Social Change*, Bristol: Policy Press

Durston J (2011) 'SW3 house prices hit the roof', SW Londoner website, 15 December 2011. http://swlondoner.co.uk/content/1512710-sw3-house-prices-hit-roof

Kraemer S (2011) unpublished letter to the *Guardian*, by correspondence with the author, 8 December 2011

Lee N and Wright J (2011) *Off the map? The geography of NEETs: A snapshot analysis for the Private Equity Foundation*, London: The Work Foundation

Mason P (2010) *Meltdown: The end of the age of Greed*, updated version, London: Verso

Pidd H (2011) 'Tax us more, say wealthy Europeans: German group latest to volunteer for higher contributions, saying country could raise €100bn in two years with a 5% wealth tax', *Guardian*, 29 August 2011. http://www.guardian.co.uk/world/2011/aug/29/tax-us-more-say-wealthy-europeans

Ponticelli J and Voth H-J (2011) *Austerity and Anarchy: Budget Cuts and Social Unrest in Europe, 1919–2009*, Centre for Economic Policy Research. http://www.voxeu.org/sites/default/files/file/DP8513.pdf

Priestly J B (1944) *An Inspector Calls*, London: Penguin

Taylor-Gooby P (2012) 'Root and Branch Restructuring to Achieve Major Cuts: The Social Policy Programme of the 2010 UK Coalition Government', *Social Policy and Administration*, 46(1): 61–82

Wren-Lewis S (2011) *The case against austerity today*, London: IPPR. http://www.ippr.org/publications/55/8033/the-case-against-austerity-today