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Inequality equilibria and individual well-being

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1. Introduction

Kelley and Evan's "Societal Inequality and Individual Subjective Well-Being: Results from 68 Societies and over 200,000 Individuals, 1981–2008″ is laudable on several counts. It is thought-provoking and also impressive for its dedication to scientific rigor and thoroughness. The phenomenal number of sensitivity tests they conducted gives one confidence that no stone or even pebble has been left unturned. As the authors themselves emphasize, the study does go beyond what so far has been done in this field, firstly by testing separately for both advanced and less developed societies and, secondly, by including controls for a host of individual characteristics (especially position in the income distribution).

Considering the study's design and aims, the results are persuasive. In the advanced nations there is no connection between levels of inequality and subjective well-being; in the Third World, inequality is actually associated with more well-being. This is probably not because citizens like inequality but rather, as Kelley and Evans argue, because large populations have escaped abject poverty in the subsistence economy for paid jobs and enhanced consumption potential in the emerging urban economy. I have no quarrel with the technical side of the estimations.

My quarrels are, instead, aimed at the theoretical framework and how it was applied to empirical data. The study adopts a double theoretical anchor: a relative deprivation perspective in which status anxiety is one potential trigger of (un-) happiness – can I keep up with the Joneses? The other is the 'hope factor' according to which inequality can actually promote happiness if, that is, citizens believe they (and their children) have a genuine opportunity to make it onto the higher rungs of the social ladder.

In either version, the basic mechanisms that link inequality to well-being have to do with *expectations.* And it is on this count that I believe that Kelley and Evans have missed out on a third possible logic, one that is not so much nested in reference group comparisons as in broader societal-level expectations. Put differently, the reference is not merely a comparison group, but also citizens' judgment and expectations about what constitutes a fair, just, and attractive society. Citizens will, at least implicitly, develop a basic notion of the norms that guide social justice from not only their own personal life course experiences, but also from those of the preceding parental generation.

The alternative framework that I propose puts at center stage the presence of 'inequality equilibria', as will be elaborated further below. To summarize the key argument, within a stable equilibrium it is unlikely that the prevailing level of inequality will influence people's sense of well-being to any great extent – at whatever level of inequality. This is because it is perceived as normal, as a given to be expected. But in a context of equilibrium rupture, expectations are challenged and normative uncertainty is likely to spread.

In standard theory, an equilibrium will perpetuate itself as long as there are no exogenous shocks to the system (Durlauf, 2001). In other words, it is when a major shock occurs that we should expect decisive effects in terms of subjective well-being. Most likely, a shock that produces significantly greater inequalities should result in *less* 'happiness'; vice-versa, *more* well-being should go hand-in-hand with a big egalitarian leap forward (at least among the beneficiaries thereof).

As noted, I also have quarrels with Kelley and Evan's empirical application. They pool the data from the World-cum-European values studies over three decades. The advantage here is of course a colossal number of observations (200.000 respondents). The great drawback is the absence of any dynamics. Their study is solidly static. And this is a potential source of

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fallacy since the pooled decades witnessed abrupt and major changes in the income distribution across many countries. And in some cases the trend has been quite polarizing with the top racing ahead of the rest and the lower deciles losing ground.

The comparative statics in Kelley and Evan's study are problematic both in terms of testing their own key hypotheses (the status anxiety versus 'hope' mechanisms), and even more so if – as in my argumentation – it is radically changing circumstances that fuel altered expectations. Their study would have been far more compelling had they instead adopted a dynamic change-change design: does a major change in income distributions provoke a change in citizens' feelings of well-being?

2. Inequality equilibria

An equilibrium is essentially premised on normative expectations. It is endogenously self-reproducing across time as long as it is not met by some (major) exogenous shock that fundamentally alters its core *modus operandum*. The self-reproduction dynamics are evident when we consider the strong correlation between a society's level of income inequality and its intergenerational income mobility profile. Income mobility rates (i.e. the correlation between fathers' and sons' income) are five times higher in comparatively egalitarian nations, such as Denmark or Norway, than in high-inequality societies, such as Italy, the U.K. or the U.S. (Björklund and Jantti, 2009; Esping-Andersen, 2016). If there are significantly fewer upward mobility opportunities in any given society, the obvious outcome is more income inequality also in the succeeding cohorts and generations.

Within a stable inequality equilibrium, any given individual knows what to expect in terms of his-her life chances and those of his-her offspring. One's expectations may be modest or extravagant, but the life course scenario is quite predictable. Under conditions of equilibrium rupture, however, stability and predictability give way to uncertainty and possibly greater anxiety about what the future has in store. This should especially be the case if a new and more inegalitarian scenario is accompanied by heightened poverty risks. If so, fear of what lies ahead should show up on individuals' ratings of their level of well-being.

Henry Aaron (1978) once said that 'watching trends in income inequality is like watching the grass grow'. This depiction may have appeared valid across the postwar decades, but no more. From the 1980s onwards a large number of advanced economies experienced a sudden and basically unexpected surge in income inequality. In some, the past three decades have seen the Gini coefficient increase by double-digit figures. In the US, where inequality levels were already high to begin with, the Gini coefficient has risen by almost 20 percent since the mid-1970s, and even in the citadel of egalitarianism – Sweden – it rose by 13 percent. And yet, the trend has been far from uniform. France has experienced very little change, and Denmark even boasts a (slight) decline in inequalities.[2]

When inequality suddenly surges, this is likely to be the consequence of powerful exogenous shocks. As also Kelley and Evans note, these are typically identified as the workings of accelerated globalization and of new skill-intensive technologies. Whatever the underlying drivers, it is arguable that many countries have experienced an inequality equilibrium rupture, while others have not. And this, if my argument has any validity, should be visible in terms of changes in citizens' respective feelings of well-being.

3. Identifying equilibrium rupture

The approach that we advocate needs to address two empirical problems. Firstly, how do we distinguish between distinct inequality equilibria? And two, how do we identify the presence of an equilibrium rupture? For lack of any genuine alternatives, our approach to both is basically crude and pragmatic.

In address to the first question, the academic literature typically distinguishes between high and low inequality societies without actually applying any clear yardstick. And yet, there seems to be broad agreement as to which countries belong where. Our approach is to use the means and standard deviations for the 23 included countries' Gini coefficient at the start of our observations (i.e. in the 1980s when the first rounds of the World and European values surveys were conducted). This is arguably an excellent starting point since the inegalitarian surge typically commenced exactly in the 1980s.

Using this approach, we can roughly divide countries into three 'inequality equilibria': High, medium, and low. A country is classified as 'high' if its Gini (in the 1980s) was more than one standard deviation above the mean. The middle group includes those which fall within one standard deviation; and in parallel fashion the 'low' group includes those with a Gini below one standard deviation. Table 1 provides an overview of the three groups as observed in the 1980s.[3]

What degree of change in the income distribution would reasonably signify an equilibrium shift? This is clearly an almost impossible question to answer. It must of course imply a level of change that can be felt in a concrete way by the population that is affected. And it must be one that puts to the test citizens' expectations about how the present and future will influence their sense of security, as well as their own and their children's economic opportunities and life chances.

[2] These calculations, which will also be used further on when we estimate the effects of income change, derive from the OECD's Income Distribution Data base (IDD).

[3] We include most of the countries that were also utilized in Kelley and Evan's analyses of developed countries. We had to exclude some (like Iceland) for which there are no Gini coefficients available for the 1980s. See Table 1 for detailed statistics.