

# How wealth matters for social policy

## Introduction to the JESP special issue on social policy and wealth

Ive Marx and Brian Nolan

There has been a massive surge in academic and public interest in wealth ever since Thomas Piketty's "Capital in the 21st Century" landed on desks and coffee tables all over the world. There is a burgeoning scholarly literature on assets and wealth, in addition to an equally lively public and political debate. Much of the focus is on the top of the distribution, understandably since that is where much of wealth is held. The top 1% wealthiest Europeans own almost a quarter of total wealth, and the top 0.1% approximately 10% (Landais et al, 2020). By contrast, most Europeans possess next to nothing in comparison.

That is true even in countries with comparatively equal income distributions and extensively redistributive welfare states. In otherwise egalitarian countries like Denmark or the Netherlands, more than 60 per cent of wealth sits with the top 10 per cent and more than a quarter with the top 1 per cent. In Sweden, often taken as the archetype of the Nordic model, the bulk of wealth is effectively controlled by a surprisingly small number of individuals and families.

It has also become apparent, especially from the groundbreaking research by Gabriel Zucman, that some of the wealthy are very successful at avoiding taxation, especially the extremely wealthy. That has long been suspected but the hard evidence now in place raises a variety of important issues that have welfare state and social policy scholarship can no longer avoid. The question of how long extreme, undertaxed wealth can co-exist with persistent poverty and inequality of opportunity is obviously a fundamental one. Wealth taxation, having been in retreat for decades, is now firmly back on the agenda, not least in debating how the costs of the COVID-19 pandemic are to be met and shared.

Even if assets are concentrated among the wealthier sections of the population, they also matter for people who are less well-off. Some people who are identified as poor or financially needy purely on the basis of income or observed material living standards have meaningful assets. Those assets can be sizeable as some of the papers in this special issue demonstrate. The fact that they have such assets, or stand to inherit such assets in the future, may affect their need for welfare state protection, with wide variation across and within those support systems in whether and how this is taken into account in framing entitlements. The presence or absence of some savings is not only key to whether households can buffer shocks, it also affects the options and opportunities open to them in the short and long terms in myriad ways.

These are just some examples of how wealth matters for social policy scholarship. This special issue looks at these issues from a variety of perspectives. The articles all shed an innovative light on wealth in relation to a range of topics relevant for social policy researchers. This introduction provides an overview of the papers in this special issue, and then highlights some of the gaps and shortcomings that remain. We conclude with some reflections on what this all means for social policy.

## In this special issue

This special issue starts with a paper about how wealth, but also debt, matters for the way we measure poverty within and across countries. That is important because poverty research overwhelmingly relies on measures assessing household disposable income over a year or a month against various poverty standards. In such measures assets only play a role in so far that they generate cash income. However, households may have significant savings and assets that they can draw on to support their living standards in times of need. Conversely, they may also have debts that depress the living standard they can actually achieve with their disposable income.

Using data from the Eurosystem Household Finance and Consumption Survey (HFCS), Sarah Kuypers and Ive Marx offer a picture of poverty in 17 EU countries that takes into account assets and debt, using various approaches. It is shown that the approach taken does matter, both for the picture we get of “poverty” more broadly understood within countries as across countries. The elderly are generally less likely to be counted as poor once assets are taken into account. None the less, for much of the population the risk of being poor remains high having brought assets and debt into the picture. Importantly, this is generally the case because they have few assets rather than because of high debts. The effect of including net wealth in poverty measurement also affects country rankings. Spain, for instance, had one of the highest income poverty rates in 2018, but a relatively low percentage were found to be both income and wealth poor. This is not entirely surprising given the fact that Spain is a country with high median household wealth and a relatively low level of wealth inequality, thanks to widespread home ownership. But many of the country differences remain harder to interpret, leaving much room for further research.

The next article by Richard Rodems and Fabian Pfeffer looks more closely at the buffer function that wealth plays by focusing in some depth on the US case, and in doing so strengthens the case for taking this into account in measuring poverty. Wealth is shown to be an important buffer against income poverty in the face of negative life events provided its level is sufficiently high. However, Rodems and Pfeffer conclude that the level of wealth required to successfully self-insure against even drastic constraints of consumption is in fact remarkably high. The implication is that social security and other income maintenance provisions remain quite crucial in buffering against disruptive events causing severe income drops.

But why do low income households have such little wealth? Salvatore Morelli, Brian Nolan, Juan Palomino and Philippe Van Kerm address one potential contributory factor, investigating the role of wealth transfers received from the previous generation in the form of inheritances and gifts *inter vivos*. Comparing households in seven rich countries, they show that households currently on low incomes are relatively disadvantaged in terms of intergenerational transfers received in the past, both in terms of the likelihood of having received any and the amounts received by those who do benefit from such transfers. The role that this disadvantage plays in the linkage between current low income and low wealth is assessed and shown to be significant. They also consider the potential impact of a widely advocated strategy to address the wealth deficits of lower-income households: a universal capital endowment on reaching adulthood. Using Italy and the US as case-studies, they find that this could lead to a marked decline in the proportion of adults with no wealth and significantly increase the wealth share of those who currently have little or none.

The subsequent article by Janet Gornick and Eva Sierminska looks in depth at the dynamics of wealth accumulation, notably the role of work careers. That naturally brings the gender dimension into the analysis since very sizeable inequalities between men and women persist when it comes to employment outcomes. Women’s employment rates remain much lower than men’s in most rich

countries, women work fewer hours, have shorter and more frequently interrupted careers and still face promotion barriers. And of course significant gender pay gaps persist in many countries. By constructing country-specific portraits of wealth outcomes and “retirement preparedness,” Gornick and Sierminska demonstrate the effect of work experience on wealth in three countries: Germany, Spain and the United States. The effect is stronger for single women than for men, leaving them in a more precarious position at retirement, with much lower expected annual wealth levels. Men have the potential to cover larger shares of their income at retirement, and thus are more able than their female counterparts, to maintain standards of living achieved earlier in life. The authors stress the importance of improving women’s labour market outcomes, not only as an end itself but also to ultimately bolster women’s capacity for wealth accumulation.

The next paper by Philipp Lersch, Markus Grabka, Kilian Rüß and Carsten Schröder, in part extending on that theme, adds the wealth dimension to what has long been a core research theme in social policy: lone parenthood. The fact lone parents face a multitude of disadvantages and challenges, not in the least combining work and care, has been well-demonstrated (Nieuwenhuis, R. & Maldonado, L. (2018). This paper shows that this disadvantage also extends to wealth. That matters because wealth is a resource that can provide children with crucial advantages early in their lives. Inequality among single-parent families is also higher than for other family types. The wealth of nonresident parents sometimes reduces the wealth disadvantage of children in single-parent families but their disadvantage remains substantial. Taken together, these findings strengthen once again the case for more adequate support of lone parents.

Taking a different angle, the paper by Nora Müller, Klaus Pforr and Oshrat Hochman looks at wealth, and more specifically debt, as determinant of life satisfaction, also taking into account state-level policies. Their main hypothesis is that while debt is not problematic per se, it can become a burden when people experience negative life events, like unemployment, a severe disease, divorce, or their partner’s death. The article probes the hypothesis that debt reinforces the impact of negative life events on general life satisfaction but that this is less so in countries where welfare policies buffer this. The empirical results suggest that this does not appear to be the case. Welfare generosity does not reduce the negative impact of debt on well-being, though debt-discharge measures do. That said, the results are ambivalent with countries patterns and differences that defy any straightforward interpretation.

Housing wealth is the single most important wealth component for ordinary households in much of Europe. There is widespread concern that young adults are finding it much harder than their parents to get on the housing ‘ladder’. Caroline Dewilde and Lindsey Flynn ask how has housing wealth inequality changed for young adult-households in the post-financial crisis period, and what is driving such change? They look at post-financial crisis developments in eleven European countries and in the United States. They find that accumulation of housing assets for a growing proportion of young adults has become slow at best and impossible at worst. Moreover, returns on housing investments for homeowners became more unequal and increasingly concentrated at the top of the income distribution. The analysis is for a short time period after the crisis but if confirmed over a longer span it would have clear social policy repercussions because historically housing wealth as the penultimate ‘middle-class asset’ has tended to be more equally distributed than financial wealth. Policy support for home acquisition, through tax incentives and other means, was and remains an important implicit form of social policy in many countries, effectively acting as a supplementary pension provision. Dewilde and Flynn argue for policies to focus on strengthening the rental sector in addition to tax, financial and banking reform.

The final paper, by Ben Ansell and Asli Cansunar, continues on this theme of housing affordability. It looks at the impact of the quite substantial growth in house prices in Europe since the 1990s, assessing what this means for the demand for redistributive and housing policies. They find that house prices have a significant impact on social policy preferences and voting behavior. Growing unaffordability creates support for less government intervention in labor market inequality or housing and, consequently more support for the political right. That is perhaps at first sight paradoxical but Ansell and Cansunar argue that this result is driven by homeowners seeking to protect their gains of appreciation from being taxed away or undermined by growing housing supply. Growing housing unaffordability is thus likely to lead to greater success for right-wing parties and less interest in redistribution, thereby effectively reinforcing the overall trend of rising property prices. The beneficiaries of unaffordability will prefer to keep policies and parties in place that keep prices high and rising. That will be a discouraging conclusion for those who would like to see more rather than less redistribution, and social policy scholarship will need to actively engage with it.

### **Knowledge gaps and research priorities**

The papers present innovative research in a research field that is still in its infancy. As a consequence, the theoretical frameworks underpinning much of the research are in need of significant development. Although some papers in this special issue refer to the theory of 'permanent income' and related notions, none present a fully developed theoretical framework. That is perhaps not uncommon in the social policy literature but needs to be highlighted none the less.

It is also noteworthy that several of the papers present comparative results that are hard to decipher. The international comparisons presented in the various papers are revealing but often also hard to interpret. Clearly, there is still a long way to go in understanding the sometimes surprisingly large and sometimes counterintuitive observed differences between countries. Several attempts at interpretation can be found in this special issue but these are not always entirely satisfactory, pointing to an important research agenda.

A significant part of this agenda entails the critical investigation of the data, its validity and representativity. The Household Finance and Consumption Survey begun in 2010 under the auspices of the ECB represents a massive step forward in terms of comparative data on assets and debt for Eurozone countries, but it remains an imperfect data base. One well-known problem is that the very wealthy remain underrepresented despite efforts to oversample the top. There also remain important limitations for the rest of the population. One missing or at least imperfectly measured component is social security wealth, notably in the shape of second pillar and other collective arrangements. These distort international comparisons since such arrangements are more important in some countries as compared to others. According to ECB estimates, Dutch households, for example, have accumulated pension and life insurance fund assets worth more than 200 per cent of GDP. More than 90 per cent of Dutch employees participate in a pension scheme of their employer or their occupational group. By contrast, in Italy pension and life insurance funds represent less than 50 per cent of GDP and participation rates are much lower. But in the HFCS Italy appears as having far higher median net household wealth. That is presumably in major part because that wealth is directly held by households, often in the form of real estate.

Data issues also bedevil the study of debt. Debt is arguably the major variable most often missing in poverty research. One of the most frequent questions put to poverty researchers is whether they account for debt and especially for over-indebtedness, and they usually do not. And yet in public perception and indeed in the experience of many social workers debt is one of the most serious

problems facing low-income and poor people (Kramer-Nevo et al., 2017). According to Eurostat, almost one in ten people living in the EU are behind on their rent or mortgage, utility bills or hire purchase. Among certain segments of the population, such as single parents, that ratio may be as high as one in five. The debt burden, as a percentage of income, appears to be highest among the poor. But good data remains scarce. It is not particularly well covered in the EU-SILC and one may question whether the HFCS is sufficiently representative when it comes to the most deprived or vulnerable parts of society. This is an important issue because problematic debt often begins with an event that causes a person or household to fall into income poverty at the same time. That can be a divorce, an accident or job loss. For people living on a modest income, an existing debt can spiral out of control (see for example French & McKillop, 2017 and Lux and Mikeszova, 2013).

Poverty in combination with debt problems can cause intense stress, feelings of shame and isolation. There is growing literature showing that this will hamper people's ability to get out of their highly problematic situation. Psychologists studying people's behaviour under such circumstances argue that this becomes especially problematic when it results in 'tunneling', hampering the cognitive power needed to solve problems, reason, or retain information. It may also limit executive control and reduce people's ability to plan ahead. Their focus becomes immediate: putting food on the table, paying rent and other bills (Mullainathan & Sharif, 2013). There is an important role for social policy research in gaining a better understanding of how people in financially dire circumstances cope and how they actually respond to policies to help them, for example training or work activation policies.

A final feature to note about the papers in this special issue is that they mostly focus on describing and explaining wealth-related outcomes rather than analyzing (social) policy interventions. Exceptions include the paper by Morelli et al in which a capital endowment for young adults is simulated, and Dewilde and Flynn also make some concrete policy suggestions. However, research in this field clearly needs to both deepen our understanding of the role played by wealth and also prioritize the elaboration and evaluation of policy interventions across a broad span that may potentially address the wealth deficits and debt problems of low-income households.

### **What this means for social policy**

This special issue makes the case that wealth matter for social policy. But a skeptical reader might well point out that the impact of accounting for assets in poverty measurement is not dramatic. The finding that low-income and other vulnerable households (such as lone parents) are also disadvantaged when it comes to wealth does not come as a surprise. It is also clear that asset buffers need to be very significant indeed if they are to serve as a real substitute for social security and social assistance provisions.

Moreover, insofar as low-income households have assets, these usually are not immediately or fully fungible, or only at a significant (emotional) cost, for example a family home. That said, means-tested minimum income schemes in Europe do include asset tests of all sorts. Yet how assets should properly affect eligibility for benefits and how aspects like emotional value, liquidity, divisibility etc. are to matter in this respect clearly requires deeper consideration.

This could also be seen as calling into question the policy recommendation in several of the papers in this special issue that wealth creation among low-income families is a viable anti-poverty strategy. Most European countries already encourage the ownership of real estate through tax reliefs but these are typically out of reach for those on the lowest incomes. New types of asset policies might prove an interesting addition to income-based social provisions. Individual Development Accounts

(IDA's) as exist in the United States are perhaps worth exploration. Under that scheme, for every dollar participants save they receive a matching subsidy. Evidence on the beneficial effects is mixed at best (Mills et al, 2008). They rarely result in the accumulation of financial buffers of any real significance, although they help in bridging delays in welfare payments. Fears that the prime purpose of such schemes is to offer political cover for cuts in welfare state benefits and provisions may well be legitimate.

The same may apply to capital endowment proposals. Tony Atkinson (2015) proposed a universal inheritance payable on reaching adulthood. Branko Milanovic (2019) also sees such endowments as key to "deconcentrating capital ownership". Thomas Piketty (2019) has proposed a substantial capital endowment of approximately 60% of average adult wealth (about €120,000 in France) at the age of 25. Morelli et al. in this issue find that a universal capital endowment would bring a marked decline in the number of people with no wealth. It would also increase the wealth share of those who have little more. But again, the question is whether and to what extent such endowments could constitute a real buffer against negative life events. Even the ambitious proposal by Piketty represents a very limited increase in permanent income.

Which brings us back to where we started. Wealth is mostly about the rich, and there is mounting hard evidence that some of the wealthy, especially the very wealthy, do not contribute their fair share towards helping the far less fortunate. This special issue has not considered the issue of wealth taxation in relation to poverty alleviation and other social policy goals. But clearly this is central to the policy challenges relating to wealth. If taxing the wealthy (more) is deemed desirable and if it is possible then a key issue is which functions could then sensibly be financed through wealth taxes. It would seem logical to fund the endowments we just discussed through taxation of flows of inheritances and gifts.

The OECD advocates substantial taxes on gifts and inheritances. It points out that inheritance taxes, particularly those targeting large wealth transfers, could enhance equality of opportunity. Today, only 0.5% of total tax revenues are sourced from inheritance, estate and gift taxes on average across the countries that levy them, which are not all rich countries. The OECD also notes that gifts and inheritance taxes have lower efficiency costs than other taxes on the wealthy and are easier to assess and collect than other forms of wealth taxation.

Yet it is also important to keep in mind that many forms of wealth taxation do not yield the steady income streams that welfare state services and benefits usually call for. Moreover, revenues from wealth taxes usually go down as budget demands increase during economic downturns and recessions. Capital gains taxes are a case in point. More stable revenues come from wealth transfer taxes but these are not very effective in immediately capturing top wealth holdings.

It remains a crucial question how important wealth taxes can become in financing the welfare state. Social expenditures already take up a quarter or more of GDP in many rich countries. With population ageing that share is expected to go up even further. Wealth taxes can play a role here but they would not offer a miracle solution. Landais, Saez and Zucman (2020) for example propose a substantial net wealth tax on the top 1% richest individuals. By their estimates, a progressive EU wealth tax at a rate of 1% above the top 1% threshold and an additional 1% above the top 0.1% threshold, and an additional 1% above €1 billion, would raise 1.05% of EU GDP in revenues each year. That is a sizeable amount but wealth taxation is clearly no panacea for the very substantial social policy financing needs of today and tomorrow.

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