Inequality in EU Crisis Countries:

How Effective Were Automatic Stabilisers?[1]

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The advent of the Great Recession and the widespread adoption of fiscal austerity policies have heightened concern about inequality and how well tax-benefit systems redistribute. We examine how the distribution of income in the EU countries which were hardest hit during the Great Recession evolved over this time. Using a recently developed framework, the overall change in income inequality is decomposed into parts attributable to the change in market income inequality, automatic stabilisation effects, and changes in discretionary policy. We implement this approach using the microsimulation software, EUROMOD, linked to EU-SILC survey data, to produce the relevant counterfactual ("no reform") scenarios. We show that automatic stabilisation played a large role in shaping income distributions in “crisis” countries over the course of the Great Recession. Results for Greece, Portugal, Italy and Ireland suggest that automatic stabilisation almost completely counteracted the increased inequality brought about by market income changes. The existing tax-benefit systems in Spain also cushioned market income inequality, albeit to a lesser extent. The effect of old-age benefits and unemployment benefits, which account for most of social protection expenditure in these countries, was found to vary. Countries which devoted more resources to unemployment supports, such as Ireland and Spain, were also those in which unemployment protection played an important role in cushioning inequality. Old–age benefits were important stabilisers in all countries but were most important in countries which devoted a larger share of their social protection expenditure to old-age supports. Across countries, automatic stabilisation played a larger role than discretionary policy in reducing inequality, highlighting the importance of a well-designed tax-benefit system in dealing with unexpected market shocks.

[1] The results presented here are based on EUROMOD version G4.0+. EUROMOD is maintained, developed and managed by the Institute for Social and Economic Research (ISER) at the University of Essex, in collaboration with national teams from the EU member states. We are indebted to the many people who have contributed to the development of EUROMOD. The process of extending and updating EUROMOD is financially supported by the European Union Programme for Employment and Social Innovation ‘Easi’ (2014-2020). The results and their interpretation are the authors’ responsibility.

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