Predistribution opens up a new set of policy tools but also a key constraint

***Paul Gregg** discusses the case for a focus on predistribution: policies that target income inequality in a preventative sense rather than interventions in terms of higher taxes and benefits. He highlights the benefits of predistribution; for instance, that the political space for action is substantially greater than for tax and benefit redistribution, as well as highlighting a key constraint: indirect interventions often lack the power to overturn the deeper processes already at work.*

Predistribution is a manufactured word which featured heavily in a recent speech by Ed Miliband to a Policy Network organised conference around tackling Britains current economic woes and longer term challenges. It was coined by Jacob Hacker a professor of political sciences at Yale and is a play on redistribution but seeks to emphasise the role of government and wider decision making in reducing inequality at source.

Economists make a distinction when discussing income inequality between inequality in the primary (or private) distribution of work, wages and occupational pensions, and inequality observed after the secondary redistribution effects of taxes and benefits. Predistribution is thus concerned with the potential for influencing the primary distribution of incomes so as to reduce the need for heavy intervention in terms of higher taxes and benefits. It is thus analogous to prevention strategies in say public health that seek to reduce smoking and improve diets so as to reduce the need for costly health interventions later.

It is perhaps not fully appreciated that the large rise in inequality in the UK in the 1980s and early 90s was not primarily driven by reductions in higher tax rates or restricting benefits to grow in line with prices rather than earnings which had been the previous norm. Rather it was driven by a growing polarisation of work into dual earner and no earner families, with some 20% of working age families having no earner by 1995 up from around 8 per cent in the mid-1970s. This was combined with rapid divergence in wages between high and low waged earners, such that real wages for typical workers (those in the middle of the wage distribution or median) rose by 23% between 1979 and 1995, but for those near the bottom (10th percentile), the rise was just 12% and near the top (90th percentile) wages grew by an impressive 40%. For the very highest paid, the 1% of the population with the highest earnings, the growth was considerably faster still. In contrast, the growing access to second stage occupational pensions over and above the state pension saw pension incomes grow rapidly and one of the poorest groups in society caught up somewhat with other families.

What surprised many economists over Labour's period in office was that the return to near full-employment did not see a significant reversal of the wage inequality built up in the 1980s and 90s. In addition, the boost in the numbers of graduates and reduction in the numbers leaving school with few qualifications only halted the growth in the wage gap between better and less educated rather than reversing the previous trend. So in Labour's term of office overall inequality edged up despite major redistributional efforts under tax credits and the Pension Credit. This was primarily after 2002 when wages stagnated for ordinary workers and the share of national income going to workers, rather than in profits and self-employed incomes, started to fall quite sharply combined with continuing rapid increases in earnings among top earners.

Also in this period efforts to reduce child poverty were hampered by the fact that low earning males had wage growth not only below the higher paid but also lower paid women. This meant that having a second earner became increasingly important and single earner couples, where the sole earner is usually the father, saw increased poverty rates despite tax credits. This was combined with a continued growth in lone parenthhood and so redistributional efforts were partly baulked by continuing adverse trends in the primary distribution of work and wages.

Of course, as with many buzz words or phrases the underlying concept is not new. Governments of all colours have pursued policies to achieve such ends before. The National Minimum Wage to reduce wage inequality, welfare to work policies to reduce the number of working age families with no earner, and support for widespread occupational pension schemes all seek to increase incomes for key groups so as to reduce the need for secondary top ups by government.

The current political narrative plays along the lines that the high current deficits and large overall debt level means that the room for progressives to act through spending is likely to be severely constrained. Hence reducing inequality in primary distribution both reduces the need to act through redistribution but also frees up resources to address other goals. The politics also suggests a sense that the Blair-Brown era of being relaxed about the rich getting richer but to use the proceeds of growth to address poverty through redistribution has passed.

Predistribution, however, opens up a new set of policy tools but also a key constraint. The policy tools over and above tax and benefits are legal regulation, such as minimum wages, and public campaigns or consumer actions around fairness such as the living wage or fair trade campaigns. There is also the use of broader public spending to achieve social goals such as the use of conditions attached to public procurement or focusing schools on reducing the extent low educational achievement.

Finally, there is the use of competition policy to reduce prices of goods and services that affect the poor more such as rents, energy and food or framing effects such as opt out rather than opt in pensions such as NEST to raise self-protection against low incomes in old age.

The key constraint is that they are indirect effects, and indirect interventions often lack the power to overturn the deeper processes already at work. Will a Living Wage campaign backed by public sector procurement achieve the scale to overturn the steady rise in wage inequality in the UK? Will shareholder activism combined with rules around binding votes for remuneration packages of top executives halt the rise in pay unrelated to firm performance?

Furthermore, as with all preventative strategies you will need to be changing the outcomes of a much larger group than just those who would have need for treatment after the event and this can often mean the costs are higher than for waiting for events to unfold. For example, most of the lowest paid are not poor, as they live in families with other earners. Raising pay levels for all the low paid thus involves far more resources being shifted than the amounts involved in tax credits targeted to address poverty.

The case for a focus on Predistribution thus rests on three factors. First, there is a capacity to shift far larger amounts of economic resources than can be moved by redistribution in the tax and benefit system and hence this makes up for poorer targeting. Second shifting these resources comes with at least little or no economic loss from reduced economic efficiency. Third the political space for action here is substantially greater than for tax and benefit redistribution.

In terms of specific policies, there are a number of obvious policy areas but whether they are of sufficient scale to address the forces driving rising inequality is unlikely. Reducing long-term unemployment, and especially for young people, is an obvious win as time and again it has been shown how unemployment damages future earnings and employment years after a person first returns to work. Expanding the coverage of occupational pensions through NEST type schemes backed with restrictions on management fees chargeable by fund managers to make them better value to low wage savers offer hope of reducing inequality in old age. Limiting the higher prices charged by energy firms for payment systems other than direct debits, such as Charge Keys. Living wage campaigns backed by more extensive use of public procurement conditions in contacts etc. All of these offer attractive attempts to shift inequality in work and wages. But they appear limited in scale and ambition.

More challenging would be boosting employment, but in particular getting these extra jobs focused on groups that the last recovery barely reached such as people in the most deprived areas, the least educated, the disabled and the over 50s. The potential wins here are large but the key to getting employment up for older and disabled workers must be in firms offering flexibility that suits workers. As with mothers, right to return after illness and right to request part-time working are likely to be central to boosting employment but run counter to the current drive for further labour market deregulation.

Likewise with training, the current high job turnover in low wage sectors discourages both firms and workers from training, pushing towards long-term and investment focused employment contracts is likely to be central to Predistribution strategy but runs against the current employment regulation model in the UK. Focusing school resources on reducing Britain's long tail of underachievement risks alienating middle class parents, but tackling low attainment must be central to a Predistribution strategy. Thus a Predistribution strategy could represent a profound challenge to the neo-liberal economic model that has operated in the UK and US over the last 30 years or a limited rationale to avoid tough choices about redistribution in tough times.

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