COVID-19 and Inequality

By Norma Cohen

COVID-19 Actuaries Response Group – Learn. Share. Educate. Influence.

Summary

In the face of COVID-19, governments worldwide have responded decisively and supportively. Western economies have been largely cushioned from an extreme economic slowdown through robust and expansionary fiscal policies. However, whilst the intended outcome appears to have been achieved, a less attractive secondary outcome is becoming evident: an acceleration of wealth and income inequality.

A recent Resolution Foundation report shows that asset-rich households have benefitted disproportionately compared with asset-poor households. We summarise the main conclusions reached in their report below and highlight that a reinvigoration of the social contract is likely to be needed if we are successfully to meet the twin challenges of the demographic transition combined with the need to retool the economy for a net zero world. We welcome a broad debate but suspect that substantial governmental intervention becomes more and more likely the longer robust solutions are absent. Positively, historical evidence suggests that this can also lead to a less stratified society.

Inequalities

The COVID-19 pandemic has become a crisis that goes well beyond the basic health issues that accompany widespread illness.

Indeed, it has become an economic crisis that has thrown a harsh spotlight on a trend which has become increasingly apparent for decades, but which is now demanding a public policy response: that of rising income and wealth inequality. A recent report from think-tank Resolution Foundation details the mechanisms through which the pandemic has exacerbated this trend, a trend which has been growing since the 1980's.

The effects of the pandemic have raised public awareness of inequality, amid growing demands for policies that can address it. This growing inequality occurs against a backdrop of two long-standing trends which may complicate efforts to craft fair solutions. The first of these is the rapid pace at which the changing global climate is threatening the survival of millions of human beings. The second is the changing shape of the population distribution.

The shape of the population is changing, not only within wealthy nations but among emerging economies as well. While rising longevity at older ages is building a bulge among the 'oldest old', fertility rates are now too low to maintain working age populations. Therefore, addressing the widening wealth gap while ensuring that we transition to a zero-carbon, sustainable economy at the same time as raising children and caring for our elderly become policy challenges which are increasingly difficult to separate from each other.

In line with the profession's obligation to serve the public interest, we look forward to actuaries contributing to wider understanding of these challenges and encouraging discussion about solutions.

The suffering from COVID-19 and the global loss of life have been a staggering tragedy. Nevertheless, the willingness of governments – particularly among wealthy nations – to underwrite public safety nets requiring levels of funding not seen since wartime have so far mitigated the worst economic effects of the pandemic. However, that has not been sufficient to mask the ways in which COVID-19 has sharpened existing inequalities.

The thrust of the comprehensive Resolution Foundation report is a 'Good News/Bad News' conclusion. The good news is that unlike the outcome of any UK recession in the past 70 years, total household wealth has increased, and in this case, by a staggering £900 billion. That is a 6% increase on pre-pandemic levels.

The bad news is that while in aggregate, wealth and savings have increased more than they would have otherwise and consumer debt has fallen, that improvement has not been shared equally amongst the population. Indeed, nearly a third of families in the bottom quintile of earners saw savings fall, about three times the rate of savers in the top quintile. Worse still, the effects of the pandemic had an even bigger effect on household wealth than it did on income.

If anything, the pandemic has widened what had already become a yawning gulf along the wealth distribution in Britain, widening inequality even further.

To reach its conclusions, the Resolution Foundation commissioned a special on-line survey of 8,000 individuals, conducted by YouGov, to assess how savings and spending patterns changed during the pandemic across a broad range of household incomes. To measure changes in wealth, the Resolution Foundation tracked shifts in asset values and modelled these against the Office for National Statistics granular Wealth and Assets Survey (WAS). The WAS is viewed as very accurate, but its main drawback is the time lag between collection of data and publication. The current survey used for this research is from 2018. Another drawback, according to recent research, is that it may underestimate the percentage of national wealth of the richest 1% of the population by as much as a fifth. That would raise the share held by the wealthiest to 23% of the national total from 18%.

The report looks separately at changes in incomes, spending and savings patterns and those to changes in household wealth. The reasons for changes to incomes, spending and savings are easily understood by anyone following news regularly.

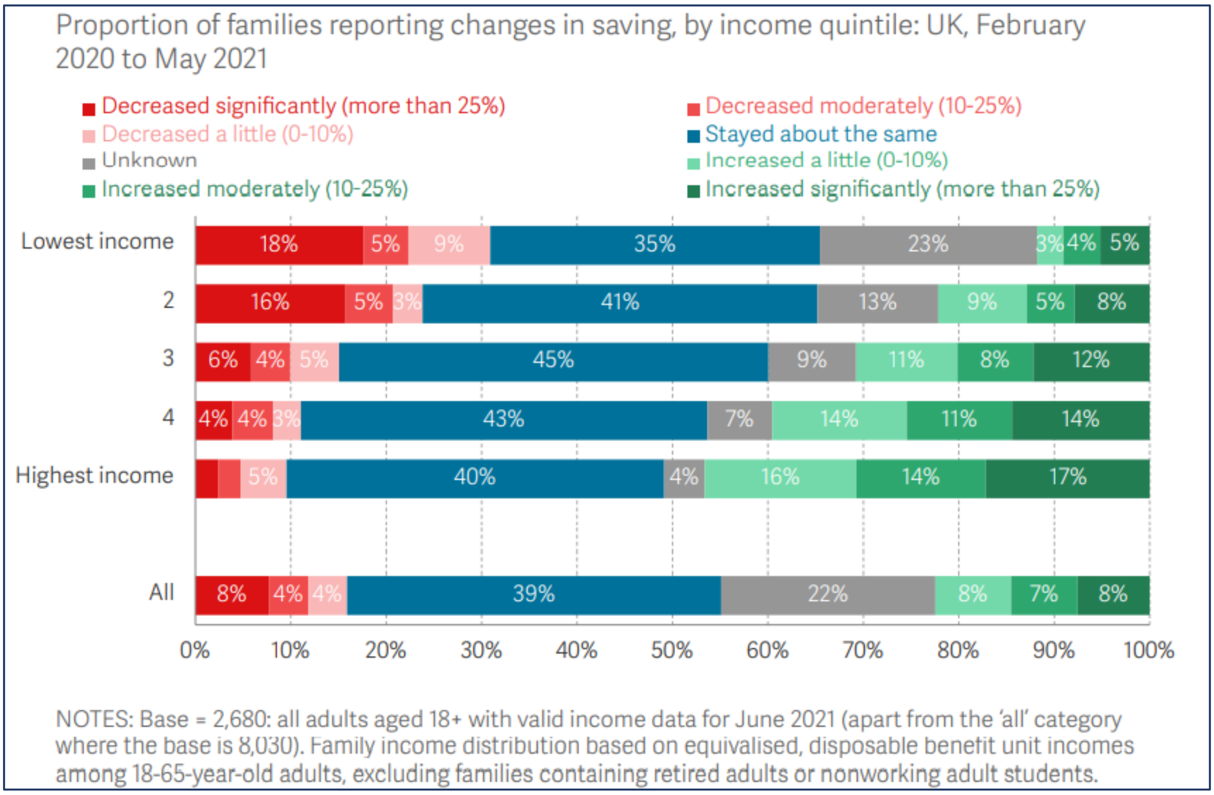
Overall, savings have increased by £200 billion compared with pre-pandemic levels while consumer debt has fallen by £10 billion. Reduced social interactions – a drastic drop in those visiting restaurants and bars, movie theatres, sporting events or just gathering with friends and family – have cut spending tremendously. These behaviour changes are both the result of government rules and general personal caution. With fewer chances to spend money, savings piled up. That is unlike previous recessions when job losses led to lower incomes and forced spending cuts. Indeed, the study found that higher income households cut spending by much more than households in the lowest quintiles. That is because poorer households spend a higher percentage of income on goods and services which they cannot do without such as food and shelter. Wealthier households have higher discretionary spending.

The rising savings and falling debt are in stark contrast to the trend seen after the 2008-09 financial crash where, in real terms, household savings and cash stagnated for six years.

Also, household income has fallen far less in the pandemic than it might have otherwise, thanks to generous government support schemes such as the Coronavirus Job Retention Scheme and furlough schemes which kept many on payrolls. Unemployment rose to 5.1% from 4.0%, a far more modest rise than that to 8.5% seen in the 2008-09 financial crisis.

However, the rise in savings and decline in consumer debt have been far from uniform across income quintiles. This explains both (some of) the rising income inequality and growing discomfort with it.

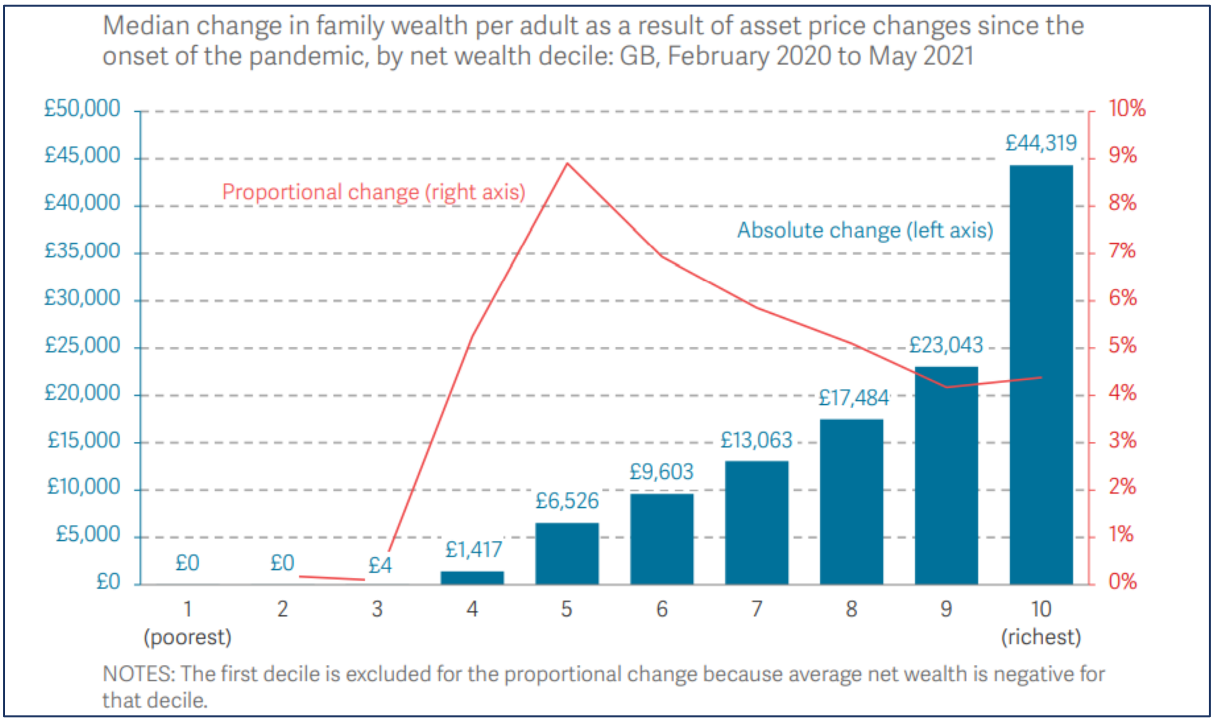
Across households, 23% increased savings while 16% reduced them. But among the lowest income quintiles, only 9% increased savings moderately or a lot. In contrast, 31% of those in the highest income quintile did so. Moreover, among households that cut savings moderately or a lot, nearly a quarter – 23% – of those in the lowest income quintile were forced to do so, while fewer than 5% of those in the top quintile did.



However, the Resolution Foundation study found that the greatest inequalities opened by the pandemic concern not income, but rather, wealth. It has been the large swings in asset values – and in the UK particularly, assets in the form of housing – that have widened the wealth gap. *"Crucially, who benefits from this depends not on what people earn, but on what they already own"* the report concludes.

Asset price performance has been striking in the COVID-induced recession, the report notes. While these fell sharply early in the pandemic, they have not only recovered but risen well above levels seen before illness struck. In fact, when the effects of rising savings, reduced indebtedness and rising asset values are added together, total wealth in the UK has risen by £134 billion.

Using the WAS to model asset prices, the report authors concluded that households in the middle of the wealth distribution saw wealth rise by 7% each, the largest proportionate increase of any group of households. The reason for the disproportionately large rise among this group is because housing constitutes its most common form of wealth. Among households in the fourth through sixth income deciles, housing constitutes between 48% and 52% of total wealth. However, households at the top end of the wealth distribution – where housing accounts for only a third of total wealth – saw wealth rise by much more. That is because they are not only benefitting from rising house prices but also from rising values of other assets such as financial securities. The richest 10% of households had average gains in net wealth of £44,000 per adult.



That this should be the outcome is not completely surprising given the findings of another economic historical researcher. Economist Thomas Piketty, looking at centuries of wealth holdings in the US and Europe, demonstrated that over long periods of time, returns on capital are significantly higher than those on labour. Those holding capital in the form of housing and financial assets – as the wealthiest households in Britain already do – will obtain the highest returns.

But the rise in asset values during a recession is highly unusual, the Resolution Foundation notes. Equities markets – with a few exceptions – typically fall sharply in such periods. Although share prices globally did fall sharply at the outset of the COVID-19 pandemic, the pace at which these have recovered is striking. Among the factors driving investor optimism has been the speed with which vaccines have been successfully rolled out. In addition, governments in wealthy nations have enacted income support and job protection programmes that have shielded a swathe of the population from the worst effects of the drop in consumption stemming from the need to socially isolate.

Moreover, from the early days of the COVID-19 outbreak in Europe and the US, it became clear that not only economic inequality was exacerbated by the need to limit the spread of disease. Indeed, the very basis of who became ill, and who died, in part reflected existing economic inequalities between communities. This, too, has heightened public awareness of inequality; those on the lower rungs of the socioeconomic ladder are generally less able to protect themselves against disease.

Initial reports of exactly who became ill and died in Britain from COVID-19 focussed on the elderly as the most vulnerable group. This has been borne out by research in nearly every country that has looked at illness and death and when older adults contract the disease, that these are more likely to need hospitalisation and more likely to die.

Moreover, it became clear that even with unprecedented government assistance for those unable to work, there were distinct groups of people for whom social isolation would be impossible. These include so-called ‘front line’ workers employed in shops, warehouses and certain factories, many of whom are relatively low waged to begin with. That ensured that those within the lower income quintiles and who could not adapt to ‘Work from Home’ practices would be more vulnerable to illness.

In addition, within months, it became obvious that Black, Asian and other Ethnic Minority groups were disproportionately vulnerable to illness: the risk of infection from COVID-19, and subsequent mortality, were generally higher for these groups than for their White counterparts. Initially there was speculation that genetic characteristics may have predisposed some ethnic groups to illness and made them more vulnerable after contracting the disease. The pattern has been found not only in the UK; similar patterns appear across the multi-ethnic US, for example.

However, a recent study suggests that it is socioeconomic factors more than anything that predispose Britons to illness, not race or ethnicity. Researchers associated with Nuffield College, Oxford and medical researchers in Catalonia, Spain, looked at over 415,000 cases from the UK's BioBank, a large UK data cohort, to assess correlations between ethnicity, socioeconomic status, and risk of morbidity. The data found that ethnic minorities were indeed overrepresented among those testing positive. But, of these, almost twice the proportion of tested (21.0%) and infected participants – 23.4% - lived in the most deprived areas of Britain as measured by the Index of Multiple Deprivation than non-tested participants. Also, those with COVID-19 had higher incidences of conditions known to be comorbidities with COVID-19 including hypertension, diabetes and ischaemic heart disease.

'Despite a number of initial reports declaring differences in genetic predisposition to COVID-19 according to ethnicity, this difference has been disproved more recently as the virus has spread globally…' the research concluded.

Similarly, researchers at Brookings Institute looked at the disproportionate decline in life expectancy among Black and Latino men in the US stemming from the spread of COVID-19. Although longevity has fallen more sharply among this group, the Brookings researchers concluded that it is the 'Social Determinants of Health' that account for rising death rates rather than genetic traits associated with ethnicity. In addition, these ethnic minorities are more likely than the White population to be employed in high-risk, in-person workplaces and lack access to health insurance which, in the US, is largely employer-provided.

The conclusion from both pieces of extensive research is hard to escape: those with lowest levels of income and wealth are not only the most likely to have suffered the greatest economic hardship from the pandemic, they were also the most likely to become ill, and to succumb to the illness itself.

These trends, increasingly well documented not only in Britain but in wealthy countries everywhere, are raising awareness of the general price that is being paid for the yawning gulf that has opened up since the 1980's between those at the top end of wealth and incomes and those at the bottom.

In thinking about addressing the widening inequality along with the challenges of climate and population change, it may be helpful to remember that the twenty-first century is not the first time the UK has undertaken this task. Indeed, economic historians such as Anthony Atkinson and Harry Campion, along with Thomas Piketty, date the decline of inequality to another life-challenging event facing Britain: the outbreak of the First World War.

To marshal the financial capital and the resources to fight the war, Britain had to gradually abandon all of the economic orthodoxies which had supported its growth to the world's wealthiest economy at the outbreak of war. These included adherence to the Gold Standard to maintain the purchasing power of Sterling, maintenance of free trade principles and adherence to a 'balanced budget'. The last of these included not only a refusal to spend more than that collected through taxation but also a gradual reduction of historic government debt built up while fighting the Napoleonic wars a century before. But the sense of inequality of sacrifice in wartime led to increasing bitterness during the interwar years between social classes that threatened the social contract that had held Britain together and aided victory.

While many assume the erosion of inequality started with creation of the welfare state in the aftermath of the Second World War, it dated, in fact, from the need to spend previously unthinkable sums to ensure survival of Britain in the First World War.

As in wartime, it may be that the outbreak of the COVID-19 pandemic should prompt a re-think of economic orthodoxies which have stood it so well in the late twentieth century and consider whether other ideas should prevail.

23 November 2021

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