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Diverse Disparities

The Politics and Economics of Wage, Market, and Disposable Income Inequalities

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It is widely thought that among the countries in the Organisation for Economic Co-operation and Development (OECD), income inequality has become more widespread over the past decades. The authors show that this image is misleading. The OECD countries remain more diverse in their distributions of labor earnings and disposable income than they are in their distributions of market income. The larger and persistent cross-national variation in the distributions of work-related earnings and disposable income is attributable to the role of political actors (such as unions and political parties) as well as economic institutions. The way in which political parties are able to pursue their goals varies across forms of income. Political parties' capacities to shape the distribution of labor earnings is contingent on the degree of wage-bargaining coordination. In turn, political parties directly affect the distribution of disposable income through their choices about fiscal instruments.

Keywords: *inequality; redistribution; partisanship; economic institutions; political economy*

Since Kuznets (1955) pointed to social and political factors as the keys to understanding the changing shape of the income distribution, political economists have made significant efforts to overcome the notion that distributive outcomes are a mere reflection of market processes, both domestic and international. Indeed, ignoring politics when studying inequality comes at a high analytical price. For instance, the view, identified by Atkinson (1999) as the "transatlantic consensus," that industrialized countries are converging into higher levels of inequality because of a combination of skill-biased technological change and international economic integration (Phillips 2002) is known to overstate the uniformity in trends toward inegalitarian societies because it is surprisingly devoid of politics (Atkinson 1999; Gottschalk and Smeeding 1997, 2000; Kenworthy and Pontusson 2005; Bradley et al. 2003).

Yet, despite the increasing awareness of the importance of politics in the study of income inequality, the field is far from certain about how and when politics does matter in shaping variations over space and time in the incidence of inequality. To be sure, the study of politics as a factor shaping distributive outcomes in advanced industrial societies has come a long way since the days in which politics was subsumed around the median voter's preferences over a single policy dimension. The literatures on partisanship and public policy on one hand, and on the role of economic institutions in shaping labor market outcomes on the other, clearly suggest that the next big hurdle in disentangling the politics of inequality is to take on a multidimensional approach and model the interplay between different sets of political and institutional factors and the distribution of income. Efforts in this direction are a new frontier in the comparative political economy of redistribution and inequality (Beramendi and Anderson 2008; Iversen 2006; Iversen and Wren 1998; Rueda and Pontusson 2000; Iversen and Soskice 2006). In this article, we join these efforts to advance our understanding of the

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multidimensional character of the politics of inequality. We begin by documenting the varying patterns of inequality across different forms of income. We break the distribution of income into three components, namely, labor earnings, nonwage income, and taxes and transfers, and show how each of these dimensions presents distinctive patterns, both cross-sectionally and over time. By isolating these different dimensions, we bring out the puzzle that motivates this article: what accounts for the relatively large cross-national variation in wage and disposable income inequality and the narrower range in overall market income inequality?

In what follows, we argue that the key to this puzzle lies in the differential role that political and institutional factors play in shaping the distributions of earnings, market, and disposable income. To identify these differential effects, we work through the process by which inequalities in terms of different income concepts are linked together, thereby contributing to an area of work that has received very little attention so far (Atkinson and Brandolini 2003). Our core findings can be outlined as follows. First, while governments are able to alter labor market outcomes and to directly allocate resources to different groups in society through taxes and transfers, they generally lack the capacity to affect the distribution of nonwage market income. Second, provided that they hold office for a long period of time, incumbents of different ideological preferences are able to condition the levels of inequality directly by setting the level and types of taxes and transfers. However, the impact of partisan policy choices on the distribution of labor earnings is contingent on the behavioral responses of labor and capital and, therefore, on the presence of economic institutions regulating them. Specifically, our findings highlight the importance of institutionalized cooperation between labor and capital for the capacity of left-wing parties to moderate economic inequality. In line with Lange and Garrett's (1985) analysis of the politics of economic growth, we find that left-wing governments are able to achieve their goals of a compressed wage distribution only when capital and labor are able to coordinate their actions through highly centralized economic institutions.

The rest of this article is organized as follows. First, we examine the variation, both over time and across countries, in measures of the distribution of income in its different forms. Second, we lay out an argument about how these different income distributions are shaped by both economic and noneconomic forces. In the third step, we empirically evaluate the argument. Finally, we draw together our findings and their implications.

Is There Growing Economic Inequality Within the Countries in the OECD?

We focus on the distributions of wages, market income, and disposable income. Wages are the monetary reward received in exchange for labor provided an employer. Market income, of which wages are a component, is the broadest measure of the income an individual derives from the economic system exclusive of government transfers. Disposable income reflects the direct effects, after taxes and transfers, of government on how market income is ultimately distributed.

Let us turn to the distribution of wages. There are useful data on this variable for thirteen countries that are aggregated into five-year averages. These are displayed using the 90/10 ratio (in other words, the ratio the earnings of the top 10 percent of wage earners to that of the lowest 10 percent of wage earners; Organisation for Economic Co-operation and Development 1996).[1] These can be seen in Table 1.

The pattern in wage inequality over time was mixed across the OECD countries during the period from the late 1970s to the late 1990s (Gottschalk and Smeeding 1997, 2000). Some countries experienced increased inequality in wage dispersion, and some witnessed declines. In the United States and the United Kingdom, labor markets marked by already by high levels of wage inequality saw a surge upward through the 1980s and 1990s. Other countries (e.g., France, Finland, Denmark) experienced very little change in levels of wage inequality over the time periods for which we have data. Moreover, in other countries, such as Germany and Belgium, low levels of wage inequality shrank even further.

Wages are an important component of the income that individuals and households derive from the market. Still, they are only a part of total market-derived income.[2] Figure 1 presents three-decade averages of dependent labor income as a share of total household market-based income.[3] Wage earnings constitute about 70 percent of household income, although this varies. Correspondingly, the average of 30 percent of this income derived from sources other than dependent employment constitutes a significant part of market income. Such flows are distributed differently than wages. The implications are clear: the overall market-based distribution will be different from the wage distribution, and the forces shaping it will, at least in part, be dissimilar.

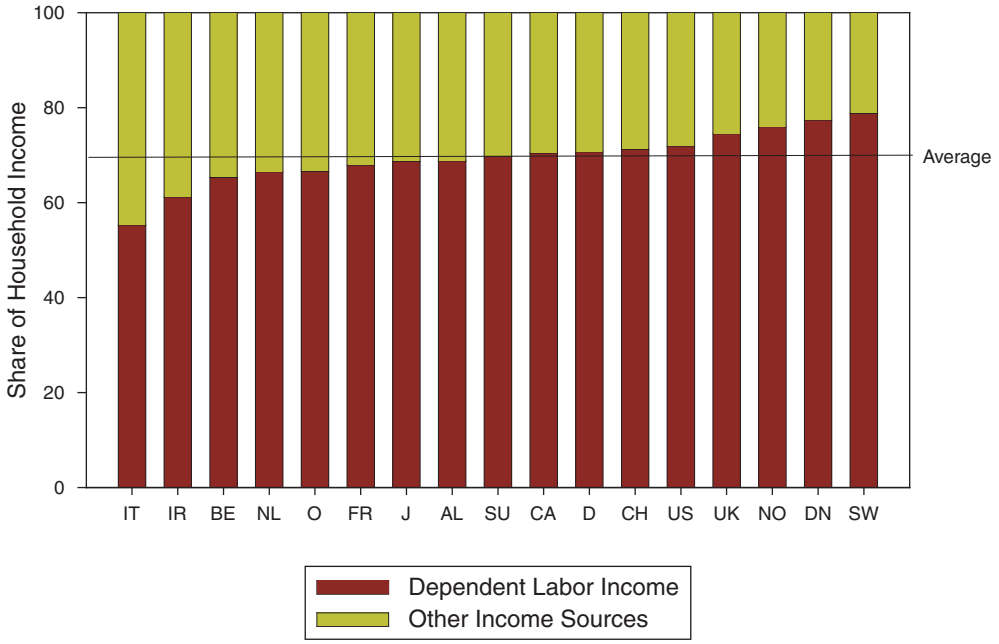
In contrast to the mixed picture on cross-national developments in wage earnings distributions, the pattern in the distribution of market income is uniform

Table 1
Wage Inequality across the OECD Countries (90/10 ratios)

Wave[a]	AL	BE	CA	DN	FN	FR	D	IT	NL	NO	SW	UK	US
1	2.83		4.02	2.15	2.47	3.23			2.52	2.07	2.03	3.03	3.80
2	2.84	2.42	4.45	2.19	2.48	3.14	2.91	2.26	2.48	2.11	2.05	3.20	4.14
3	2.85	2.33	4.33	2.17	2.46	3.25	2.73	2.34	2.60	1.98	2.09	3.39	4.35
4	2.88	2.25	4.28		2.33	3.11	2.79	2.37	2.72		2.19	3.42	4.56
5	2.95				2.42	3.05					2.22	3.42	4.58

Source: OECD (1996).
Note: AL = Australia; BE = Belgium; CA = Canada; DN = Denmark; FN = Finland; FR = France; D = Germany; IT = Italy; NL = Netherlands; NO = Norway; OECD = Organisation for Economic Co-operation and Development; SW = Sweden; UK = United Kingdom; US = United States.
a. Time periods follow the Luxembourg Income Study wave-dating convention: 1 = 1978 to 1982, 2 = 1983 to 1987, 3 = 1988 to 1992, 4 = 1993 to 1997, and 5 = 1998 to 2002.

Figure 1
Sources of Household-Sector Market Income across Countries in the Organisation for Economic Co-operation and Development, 1965 to 1995



Source: Authors' calculations using formulas developed by Mendoza, Razin, and Tesar (1994).

across the eleven OECD countries for which data are available. Table 2 presents Gini indices of market household income per equivalent adult. This measure is obtained by weighting overall household income on the basis of household size defined by the LIS equivalence scale, which takes into account the distributive importance of differences in terms of family structure. With the LIS equivalence scale, one gives a weight of 0.5 to the first adult member of the household and a weight of 0.25 to each of the remaining members. Regardless of the wage-leveling forces in national economies and the redistributive character of national taxation and spending regimes, market income inequality has been high across these countries and has surged to even higher levels over the past two decades. One way to think of the Gini indices presented in Table 2 is that each represents the share of total market income generated within the economy that would have to be redistributed to achieve equality across all households in terms of the amount each

Table 2
Market Income Inequality across the OECD Countries (Gini indices[a])

Wave[b]	AL	CA	DN	FN	FR	D	NL	NO	SW	UK	US
1	.37	.36			.34	.31		.35	.39	.37	.39
2	.40	.37	.39	.33	.37	.40	.36	.33	.43	.42	.42
3	.41	.39	.42	.34	.39	.41	.38	.37	.46	.44	.42
4	.41	.39	.43	.38	.47	.40	.39	.41	.45	.45	.45
5		.41		.37		.44		.42	.44	.46	.46

Source: Luxembourg Income Study (LIS) data.
Note: AL = Australia; CA = Canada; DN = Denmark; FN = Finland; FR = France; D = Germany; NL = Netherlands; NO = Norway; OECD = Organisation for Economic Co-operation and Development; SW = Sweden; UK = United Kingdom; US = United States.
a. Income adjusted for household size using the LIS equivalence scale.
b. Time periods follow the LIS wave-dating convention: 1 = 1978 to 1982, 2 = 1983 to 1987, 3 = 1988 to 1992, 4 = 1993 to 1997, and 5 = 1998 to 2002.

Table 3
Disposable Income Inequality across the OECD Countries (Gini indices[a])

Wave[b]	AL	BE	CA	DN	FN	FR	D	IT	NL	NO	SW	UK	US
1	.28		.28			.29	.24			.22	.20	.27	.30
2	.29	.23	.28	.25	.21	.30	.26	.31	.26	.23	.22	.30	.34
3	.30	.23	.28	.24	.21	.29	.25	.29	.27	.23	.23	.34	.34
4	.31	.25	.29	.26	.23	.29	.26	.34	.26	.24	.22	.35	.36
5			.31		.25		.26	.35		.26	.26	.35	.38

Source: Luxembourg Income Study (LIS) data.
Note: AL = Australia; BE = Belgium; CA = Canada; DN = Denmark; FN = Finland; FR = France; D = Germany; IT = Italy; NL = Netherlands; NO = Norway; OECD = Organisation for Economic Co-operation and Development; SW = Sweden; UK = United Kingdom; US = United States.
a. Income adjusted for household size using the LIS equivalence scale.
b. Time periods follow the LIS wave-dating convention: 1 = 1978 to 1982, 2 = 1983 to 1987, 3 = 1988 to 1992, 4 = 1993 to 1997, and 5 = 1998 to 2002.

receives.[4] One sees, for example, that in the United States, nearly half of all income would need to be redistributed to achieve equality in market outcomes. Even in an egalitarian society such as Sweden, the level of inequality in market outcomes is extremely high and at times has exceeded that seen in the United States and the United Kingdom.[5]

In addition, we have data on the distribution of disposable income for thirteen OECD countries. These are displayed in Table 3. Again, the LIS equivalence scale is used, and Gini indices of household income per equivalent adult are used to describe these distributions. Across the OECD countries, the Gini measures on disposable income are far lower than those for market income. Direct government intervention produces a much more equitable distribution of income. The scope of this intervention varies and with that the breadth of the reduction in inequality. In the last period reported (1998 to 2000), the effective level of redistribution varied dramatically between states such as Sweden (18 percent of total income) and the United States (8 percent of total income). In terms of changes in the overall levels of inequality in disposable income, one observes that in most of the countries for which we have data, the pattern over the past two decades has been one that involved a modest increase in the overall level of inequality or basically no change (as in the cases of France and the Netherlands). Three countries stand out in terms of increases in the degree of inequality. These are Sweden, the United Kingdom, and the United States.

The direct workings of fiscal systems revealed by combining the figures in Tables 2 and 3 are large, even if they differ dramatically across nations. In states with modest welfare regimes, the net amount of total income being redistributed amounted anywhere from 8 to 12 percent of total income. By contrast, nearly a quarter of total household market income was redistributed through the use of fiscal instruments in Sweden. Redistribution amounted to huge sums in a

Table 4
Coefficients of Variation across Measures of Inequality

Wave[a]	Wages	Market	Disposable
1	.24	.07	.15
2	.25	.09	.15
3	.26	.08	.15
4	.25	.07	.16
5	.24	.07	.17

a. Time periods follow the Luxembourg Income Study wave-dating convention: 1 = 1978 to 1982, 2 = 1983 to 1987, 3 = 1988 to 1992, 4 = 1993 to 1997, and 5 = 1998 to 2002.

relative sense, with on average around 20 percent in the United States and nearly 50 percent in Sweden.[6] And while in a number of countries, including the United States and Sweden, the redistributive effects of fiscal systems declined over time, they rose sharply in other countries, such as France and Germany.

In sum, there are significant differences in the incidence of inequality across OECD countries, but the range of these differences varies across different income concepts. These differences have not changed dramatically over time. Table 4 displays the coefficients of variation in the level of inequality for the three forms of income during the first through the last periods covered by this article. These figures convey two main points. First, the OECD countries have been much more diverse in their distributions of labor earnings and disposable income than they were in their distributions of market income. Second, these patterns remained unaltered through the end of the century. If anything, cross-national differences in terms of disposable income inequality have increased slightly over the past twenty-five years. In the next section, we lay out an argument to identify the factors at work behind these developments.

Parties, Institutions, and Inequality

A variety of factors shape the distributions of income within society. Not all of these are economic. Politics also plays a role. The role varies across different forms of income. Inherent to the well-documented existence of a structural dependency of the state on capital is the notion that the capacity of governments to shape the distribution of income is an inverse function of the number of exit options available to different income factors: capital and labor (Przeworski and Wallerstein 1988; Wallerstein and Przeworski 1995).[7] In line with this argument, we anticipate that government's impact on prefiscal income should be reflected primarily in the distribution of wages. Government is constrained in its actions in other markets, for example, finance. These volatile markets, whose members enjoy more exit options than wage earners, are sensitive to government intervention, and this sensitivity deters governments from attempting to directly influence the shape of the distribution of overall market income. Thus, we expect government's role in shaping the distribution of market income to be very indirect once its influence on the distribution of earnings is accounted for. In addition, there is no gainsaying that governments play a central and immediate role in shaping the distribution of (final) disposable income.

In government's repertoire of policy instruments are tools that allow it to shape distribution in labor market and disposable income. These instruments include regulations, taxes, and transfers. Regulations such as minimum wage laws affect the distribution of earnings. (Rueda 2004). Taxes and transfers are sometimes powerful determinants of the distribution of disposable income. These instruments of government policy also affect prefiscal income through the anticipatory behavioral responses on the parts of labor and capital (Beramendi 2001). Labor responses come in the form of labor supply decisions. Capital responds by adjusting investment decisions and labor demand. In the following, we analyze the role of political factors in shaping the distributions of earnings and disposable income.

The role of politics can be understood in terms of institutions and the ideological preferences of governments (Hibbs 1977). Parties are seen as agents of different economic interests. Parties on the Left are viewed as representing the interests of labor. Parties on the Right are held to be agents of more affluent classes. Left-wing governments are expected to tax, spend, and regulate more to achieve an equitable society (see Hibbs and Dennis 1988; Bartels 2003; Hicks and Swank 1984; Bradley et al. 2003; Iversen and Soskice 2006). Analogously, parties on the Right are expected to implement public policies that preserve inequitable outcomes deriving from the workings of the market. A second tradition in political science has highlighted the importance of labor market institutions in shaping the distribution of wage income (Wallerstein 1999; Iversen and Wren 1998). The effects of labor market institutions are both direct and indirect. The direct effects are seen in constraints imposed on the behavior of labor and capital. Indirect

effects are found in the way in which these institutions filter the impact of other determinants of inequality, most prominently government partisanship (Rueda and Pontusson 2000).

Left-wing policy aims at reducing inequality. This goal is achieved in a variety of ways. In the case of wage equality, these paths include higher minimum wages, higher levels of benefit generosity, and higher labor tax rates. Higher minimum wages raise the wage floor directly. Increases in generosity raise the wage floor indirectly by increasing the reservation wage. Both compress the earnings distribution from the bottom. Higher tax rates on labor income reduce the incentives for wage increases in the upper half of the distribution, compressing it from the top. All three policies reduce wage inequality. Left-wing parties also reduce disposable income inequality using higher levels of taxes and transfers.

Rightist governments pursue different policies. These governments can be either from a Christian democratic or from a more liberal tradition. The former support entitlements based on the insurance principle, the maintenance of status differences, and the correction of market outcomes (Esping-Andersen 1990). In implementing these principles, Christian democratic governments combine medium levels of taxes with a heavy reliance on social security contributions and public transfers. While there is no reason to anticipate that this policy reduces wage inequality, a certain degree of income redistribution can be expected. The egalitarian impact of this policy is smaller than that of a left-wing government. Right-wing liberal policy is anchored in the tenet that the market should be the dominating societal resource allocation mechanism. Taxes, transfers, and regulations are minimized. The redistributive effect of government policy is at its lowest level. Therefore, liberal policies are expected to lead to higher levels of both earnings and income inequality.

Political parties are not alone in shaping income distribution. Unions and employers' associations also matter. Union impact is to be seen in wage inequality and in redistribution. Unions have an aversion to wage inequality (Hibbs 1991). The stronger the union movement, the greater the effects of this aversion; to the extent that this greater strength rests on the inclusion of low-wage earners, the aversion is heightened (Freeman 1980). The power resources approach to the welfare state emphasizes the strength of the working class (Korpi 1983). The extent to which it is organized, for example in unions, determines its abilities to influence government policy. With this influence, the working class is able to achieve a greater redistributive effort on the part of government, thereby reducing the level of inequality in disposable income.

Accounts of redistribution and inequality based on the power of the working class treat employers as passive agents endorsing a unitary opposition to state intervention and redistribution. Yet, employers' preferences about state regulations and redistribution vary, among other things, according to the size, the sector of production, and the skill intensity of the firms (Mares 2003). Moreover, they are far from being mere spectators. Employers' control of the levels of private investment and labor demand gives their associations significant leverage over government policy. The potential reaction by employers may operate as a veto against particular forms of taxes, transfers, and regulations. This implies that both unions and employers' associations have input into the politics of inequality. As a result, an important part of the explanation of government policy and its distributive effects lies in the way in which the interplay between unions, employers, and the incumbent party is institutionalized. This brings us to the issue of coordination within the economy.

The degree of wage coordination between capital and labor is regarded as a crucial aspect of the difference between liberal market economies (LMEs) and coordinated market economies (CMEs) (Hall and Soskice 2001). Let us consider briefly the nature of such differences and their implications for the politics of inequality. In LMEs, firms coordinate their activities via competitive market arrangements. Relations between capital and labor are organized by individuals, not by associations. Capitalists value their capacity to adjust to market fluctuations, and so too does labor by investing in portable, general skills. Neither has an incentive to coordinate outside the market. Alternatively, markets are organized very differently in CMEs. Firms find incentives to coordinate with unions and the government around a fundamental "non-market-based" equilibrium between capital and labor. Such an equilibrium becomes politically effective via the wage coordination compromise between capital, labor, and the government.

By virtue of this compromise, labor restrains wage demands, contributing to lower inflation and better economic conditions and, most important, gaining a degree of income insurance for workers (Wallerstein, Golden, and Lange 1997). Government uses fiscal policy to compensate labor for its sacrifice, thereby reducing the costs of the compromise. A large public insurance system guarantees a good income level in recessions as well as longer term earnings (pensions).

Furthermore, unions obtain higher leverage in wage negotiations and greater control over the implementation of some important public policies (Swenson and Pontusson 2000).

This compromise between capital and labor is one facet of overall non-market-based coordination in CMEs that distinguish them from LMEs. The institutional arrangements of corporate governance and their interplay with the workings of labor markets are also part of the picture. Firms within CMEs rely more on bank-based financing and display higher levels of cross-shareholding. By virtue of these arrangements, investors privilege long-term performance and firms pool risks. This institutional setup creates the conditions for long-term investments both by firms and by employees (specific skills). The resulting pressure on companies and workers to maintain continuous levels of profitability is reduced. This facilitates the sustainability of the compromise within the labor market (Hall and Gingerich 2001).

This way of organizing the economy has distributive consequences. Within the labor market, the institutional position of unions is enhanced. Therefore, unions are better positioned to push for an egalitarian wage distribution, which should be reflected in lower levels of wage inequality (Wallerstein 1999). The distributive consequences of coordination go beyond the labor market. By making firms' decisions less responsive to short-term profits, corporate governance arrangements in CMEs create the conditions for employers to accept a large welfare state. This acceptance facilitates income redistribution and should be reflected in lower levels of disposable income inequality.

In addition, coordination matters because of its interaction with partisan politics. According to one view in the literature, high levels of coordination between capital and labor constrain the impact of parties on public policy and therefore mute the impact of partisanship on the distribution of income (Pontusson, Rueda, and Way 2002; Rueda and Pontusson, 2000). The intuition behind this is that collective agreements generally incorporate all workers in a company or sector regardless of union membership status and that wage developments are at least indirectly tied to one another. Given these conditions, it is difficult to entertain the notion that government can significantly influence these autonomous bargaining agreements and thus influence wage distribution (Pontusson, Rueda, and Way 2002). In short, high levels of wage-bargaining coordination have the effect of muting partisan effects on wage inequality.

Our view on how the interplay between political parties and labor market institutions affects income inequality extends and qualifies this argument, in particular in the context of coordinated economies. High levels of wage-bargaining coordination, one of most prominent features of a CME (Hall and Gingerich 2001), facilitate the implementation of left-wing policy and constrain the implementation of policies favored by the Right. In contrast, the absence of coordination between capital and labor facilitates the implementation of right-wing preferences and constraints the egalitarian effects of left-wing policy. Let us elaborate on why this position seems more plausible than that held by Pontusson, Rueda, and Way (2002).

Coordination reduces employers' resistance to a generous welfare state and dampens its economic costs by ensuring the agreement of unions to wage moderation. Moreover, agreements between capital and labor facilitate the adoption of significantly higher taxes on labor (Cusack and Beramendi 2006). In such an institutional context, left-wing parties are free to use the tools at their disposal to reduce wage inequality without incurring negative economic externalities. In this sense, left-wing incumbency and wage-bargaining coordination reinforce each other's egalitarian effects on wage distributions. As a result, wage inequality will be at its lowest levels in those countries where coordination is high and left-wing parties are in power.

In contrast, strong coordination creates a hostile environment for the implementation of right-wing policy. A number of mechanisms are at work in producing this outcome. First, the exchange of wage moderation for social protection implies a more complex distribution of capital and labor preferences concerning government policy. While unions will certainly oppose any attempt at market "flexibilization" and welfare state reduction put forward by right-wing parties, employers will not necessarily favor these attempts. Second, high levels of coordination imply that both employers and unions enjoy a degree of veto power over government policy. In highly coordinated environments, then, right-wing parties may choose to moderate their political platform in the first place. But even if they do not, right-wing parties will ensure that their actual policy is much further away from their conventional positions than it would be in the case of a social democratic government. Thus, if right-wing parties hold office in highly coordinated environments, earnings and disposable income inequality are likely to reach intermediate levels.

The picture changes in the absence of coordination. Under such conditions, right-wing parties receive the full support of employers and leave unions with far less institutional leverage. A right-wing party's capacity to let the market work as freely as possible is not constrained, and therefore, one would expect inequality to be higher.

The absence of coordination also has implications for the capacity of left-wing parties to promote their distributional goals. While these parties retain their capacity to compress the distribution of disposable income through fiscal redistribution, their leverage to affect wage inequality is much more limited. In coordinated contexts, the government uses fiscal policy as a means to influence the behavior of labor and capital within wage agreements. In the absence of coordination, the signals sent by government through its fiscal policy are less effective in shaping union behavior. Unions have no guarantee that the government and the employers will agree to the development of a large public insurance system. Hence, unions have no incentive to agree to wage moderation. Additionally, there is no enticement for them to accept the burden of higher taxes on labor needed to sustain a generous welfare state (Cusack and Beramendi 2006). Rather, unions will demand large levels of redistribution while still pressing for nominal increases to sustain real wages. Under such conditions, governments lack the capacity to trade income insurance for wage moderation and high taxes on labor. As a result, there is no reason to expect that left-wing parties are able to compress the shape of wage distribution in a significant way.

The inability of left-wing incumbents to control the market responses of capital and labor is crucial to this expectation. A discussion of the effects of minimum wages helps illustrate. Minimum wage legislation is the main tool of leftist cabinets have to compress the wage distribution in low-coordination environments. Indeed, there is evidence of a significant relationship between left-wing incumbency and the introduction of higher minimum wages (Rueda 2004). Yet, the key issue from the point of view of the link between left-wing partisanship and inequality is not simply whether leftist cabinets increase the minimum wage but, more important, whether these increases actually have the effects intended by the governments enacting them. This brings us to the impact of minimum wage regulations on the behavior of employers and employees.

Economic theory suggests that an increase in the minimum wage leads employers to reduce the demand for low-skilled workers. As a result, employment levels decline, and the bottom half of the distribution is compressed (Benjamin, Gunderson, and Riddell 1998). Were this disemployment effect to be the only one at work, left-wing parties in low-coordinated environments should undoubtedly be associated with less wage inequality. Yet, the specialized literature has also identified an efficiency effect that helps increase employment levels at the lower end of the earnings distribution (Rebitzer and Taylor 1995). The basic intuition behind this second effect is as follows: a higher minimum wage increases the cost of losing the job. In addition, more people are willing to work if the salary is better. In other words, there is a higher supply of labor in the market. These two factors force low-skilled employees to work as efficiently as possible, which in turn reduces the monitoring costs of employers. This frees up resources and allows the firm to hire more workers around the minimum wage level. Finally, a higher minimum wage could also generate a spillover effect by way of which the earnings of workers in the upper parts of the distribution should be raised by an amount at least similar to the increase in the minimum wage. Otherwise, their incentives to continue to work would be undermined. Should the efficiency and spillover effects be the dominant ones, it is conceivable that an increase in the minimum wage could generate higher employment levels for low-skilled workers without compressing at all the distribution of earnings. In fact, depending on the distributional assumptions made, higher minimum wages could even lead to higher levels of earnings inequality. The ultimate direction of the sum of these three effects cannot be anticipated theoretically. The direction and magnitude of these effects is ultimately an empirical question, but case studies on France and the United States suggest that there is certainly no reason to anticipate that, in the absence of coordination, left-wing parties will be consistently associated with more compressed wage distributions.

In closing, this section has outlined the process by which political parties and institutions shape the distribution of income. Table 5 summarizes the expected relationships between different political and institutional conditions and the levels of wage inequality. As we have argued above, the effect of government partisanship is contingent on the level of wage-bargaining coordination. For the reasons presented, we anticipate partisan effects only when the level of wage-bargaining coordination is high. Alternatively, in the absence of coordination, the egalitarian effects of left-wing policy are muted, and no partisan differences are expected. In addition, Table 6 recapitulates the

Table 5
Political Parties, Wage-Bargaining Coordination, and Wage Inequality

Political and Institutional Conditions	Policy Choices	Political Process	Expected Levels of Wage Inequality
High levels of wage-bargaining coordination/left-wing incumbency High taxes on labor	Union wage moderation; High welfare state generosity	Left-wing policy and coordination reinforce each other	Low
High levels of wage-bargaining coordination/right-wing incumbency	Union wage moderation; Medium welfare state generosity; Medium levels taxes on labor	Coordination constrains right-wing policy	Medium
Low levels of wage-bargaining coordination/left-wing incumbency	No union wage moderation; High welfare state generosity; Medium levels taxes on labor	Lack of coordination constrains left-wing policy	High
Low levels of wage-bargaining coordination/right-wing incumbency	No union wage moderation; Low welfare state generosity; Low levels taxes on labor	Low levels taxes on labor; Right-wing policy is facilitated by lack of coordination	High

Table 6
Political Parties, Economic Institutions, and Disposable Income Inequality

Political and Institutional Conditions	Policy Choices	Political Process	Expected Levels of Disposable Income Inequality
High overall coordination in the economy/left-wing incumbency	Union wage moderation; High welfare state generosity; High taxes on labor	Left-wing parties and unions promote redistribution; Coordination facilitates redistribution	Low
High overall coordination in the economy/right-wing incumbency	Union wage moderation; Medium welfare state generosity; Medium levels taxes on labor	Right-wing parties oppose redistribution; Coordination facilitated by redistribution	Medium
Low overall coordination in the economy/left-wing incumbency	No union wage moderation; High welfare state generosity; Medium levels taxes on labor	Left-wing parties and unions promote redistribution; Noncoordination limits redistribution	Medium
Low overall coordination in the economy/right-wing incumbency	No union wage moderation; Low welfare state generosity; Low levels taxes on labor	Right-wing parties oppose redistribution; Noncoordination limits redistribution	High

expected relationships between political parties and economic institutions on one hand, and disposable income inequality on the other. Here, the anticipated pattern is different. Partisan differences with respect to the welfare state and redistribution are expected at all levels of coordination of the economy. We turn now to an empirical assessment of these arguments.

Model Specification and Estimation

The empirical evaluation of these predictions requires one to assess the impact of political and institutional factors as well as other conditioning factors on the distribution of income. The three different forms of income need to be treated as objects of explanation. This is accomplished by specifying and estimating the system of three equations below:

$$WI_{it} = \alpha_1 + \beta_1 ME_{it} + \beta_2 TWI_{it} + \beta_3 FP_{it} + \beta_4 HC_{it} + \beta_5 UD_{it} + \beta_6 LG_{it} + \beta_7 EC_{it} + \beta_8 LG_{it} \times EC_{it} + \varepsilon_1, \quad (1)$$

$$MI_{it} = \alpha_2 + \beta_9 WI_{it} + \beta_{10} SMC_{it} + \beta_{11} OP_{it} + \varepsilon_2, \quad (2)$$

and

$$DI_{it} = \alpha_3 + \beta_{12} MI_{it} + \beta_{13} EC_{it} + \beta_{14} UD_{it} + \beta_{15} LG_{it} + \varepsilon_3. \quad (3)$$

Wage inequality (*WI*), market income inequality (*MI*), and disposable income inequality (*DI*) are the dependent variables in this system. Table 1 displays the values of the dependent variables used in the analysis. The interdependence across the equations is restricted in that the dependent variable of the first equation, *WI*, is independent of the other two equations' dependent variables, while the second, *MI*, depends on a set of exogenous variables plus the dependent variable of the first equation, *WI*, and the third dependent variable, *DI*, is a function of the second, *MI*, and another set of exogenous variables.

This system of equations has a variety of labels, including *recursive*, *triangular*, and *hierarchic*. Such a system can be consistently estimated with equation-by-equation ordinary least squares (OLS; Greene 2000). We have used a number of different estimation techniques. In one, a less conservative strategy, we used single-equation techniques. Two alternative methods were used, OLS with robust standard errors and OLS with panel-corrected standard errors (PCSEs). The results were practically identical, so we report only the estimates based on the robust standard errors.[8] In the second, more conservative tack, we used two-stage least squares to take into account the limited interdependence across the equations.

Each observation represents a five-year average. These conform to the LIS waves. Limited data on income inequality restrict the number of observations available. Compounding this, a number of cases are lost because of missing observations on the independent variables used. Using a panel design, there are forty-one cases for which all the income inequality data plus data on the independent variables are available. The countries included in this restricted sample are listed at the bottom of Table 1. For some countries, we have as many as five observations. The sample is smaller for others, sometimes having as few as two cases.

Let us outline the reasoning that stands behind the forms specified. We first address equation 1, for wage inequality. The first four terms included on the right-hand side of this equation represent a variety of factors that are meant to control for important transformations going on inside the labor market of all of the OECD economies that can be expected to have significant effects on the distribution of wages. *ME*, the number of manufacturing workers expressed as a percentage of the working-age population, captures the inegalitarian effects of deindustrialization as people lose jobs in the relatively high-paying manufacturing sector and need to take on lower paying positions in services (Esping-Andersen 1990). Both variables used come from the OECD's *Labour Force Statistics*. The sign on β_1 is expected to be negative.

The second economic variable (*TWI*) included is imports from the Third World, expressed as a percentage of gross domestic product (GDP). The trade data derive from the International Monetary Fund's *Direction of Trade Statistics*. The GDP data come from the International Monetary Fund's *Financial Statistics* CD-ROM. The inclusion of *TWI* is justified by the need to control for the effects of Third World competition on wage levels in the manufacturing sector and their implications for the overall distribution of wages (Wood 1995). Our expectation is that the effect of this variable, captured in the parameter β_2, is positive.

The third economic control is the female labor force participation rate, *FP*. This factor has been introduced to control for the inegalitarian consequence of high numbers of women being employed in the labor market. This distributional effect derives mainly from the wage discrimination practiced against women (Blau and Kahn 2000) and preferences for part-time employment given familial burdens. Data were taken from the OECD's *Labour Force Statistics*. The expectation is that the parameter (β_3) capturing the effect of this variable is positive. The last of the four economic controls is the proportion of college educated in the adult population. This variable aims to capture the distribution of human capital in society, *HC* (Barro and Lee 2000). In the context of a process of skill-biased technological change, a more unequal distribution of human capital should be reflected in a more unequal distribution of wages. The relationship is expected to be positive ($\beta_4 > 0$).

In addition to this set of economic controls, equation 1 includes a group of political and institutional terms reflecting the arguments presented in the last section. A compressing effect on the distribution of wage earnings is captured by the strength of the labor movement (the level of union density measure, UD_{it}) and its capacity to achieve a valued goal of egalitarian wage structure.[9] The expectation is that the associated parameter (β_5) would be negative.

This brings us to the cluster of variables dealing with government partisanship (*LG*) and economic coordination (*EC*). The partisan term used is on the basis of a long-term measure, left government inheritance. It represents the average of the past twenty years of a government ideology measure.[10] We expect that the effects of the ideological position of government are not all immediate. Rather, they work slowly

through time. Recall that in the absence of wage-bargaining coordination, we have identified several processes working in different directions. Thus, the net outcome cannot be anticipated theoretically, and the sign and significance of the parameter (β_6) for the partisan inheritance become empirical questions. A more straightforward effect for the economic coordination variable is expected. Thus, the parameter (β_7) on that variable is anticipated to be negative: as the degree of coordination in the economy rises, the level of wage inequality declines.[11] Finally, the parameter (β_8) on the interaction between these two terms, partisan inheritance and wage-bargaining coordination, is predicted to be negative, which is in keeping with our argument that coordination in the economy facilitates the egalitarian effect of left-wing government policy.

In the second equation, that for market income, there are three variables on the right-hand side. The first is wage inequality, *WI*. Since an appreciable amount of market income derives from dependent labor, it is clear that the level of inequality in the former is necessarily dependent on the degree of inequality in wages. The second variable expected to directly influence the level of market income inequality is that degree of stock market capitalization, *SMC*.[12] We anticipate that this variable has an inegalitarian effect in that only those with some degree of wealth and/or high incomes can afford to take advantage of the opportunity to earn even more income. Finally, to capture the inequality heightening effect on market income of a growing pension-age population, we include a demographic measure, *OP*, which has been operationalized as the percentage of the total population in retirement age, i.e., aged 65 years and older (data from various years of the OECD's *Labour Force Statistics*). Note that all three parameters in this equation (β_9, β_{10}, and β_{11}) are anticipated to be positive and significant.[13]

The final equation deals with the inequality in disposable income. It concentrates on those political and institutional factors that, for a given distribution of market income (the effects of which are captured by β_{12}), ultimately shape the allocation of income within society. By using the current level of market income inequality as a control variable, we isolate the effect of the variables of interest from all other determinants of the distribution of disposable income, including the feedback effects of previous redistributive policies (Beramendi 2001). In line with our argument, the level of inequality in disposable income is specified as a function of union density (*UD*), the overall degree of coordination within the economy (*EC*), and government partisanship (*LG*). Here, we use the same indicator of the level of coordination within the economy (*EC*) used in the wage inequality equation. Our expectations regarding the parameters in this equation are that, aside from that for the positive effect of the market income inequality variable, all of the others take on negative signs (β_{13}, β_{14}, and $\beta_{15} < 0$). Finally, note that the estimation techniques used are similar to the ones implemented in the case of market income inequality.

Before entering the discussion of the results emerging from this analysis, let us address an important issue concerning any effort at identifying empirically the effects of government policy on income inequality. The issue, often referred to as the "counterfactual" or the "incidence" problem, speaks to the conjecture that fiscal policies and regulations entail second-order effects in the form of behavioral responses by capital and labor to previous (or anticipated) policy choices. Among these second-order effects, investment and labor supply decisions occupy a central role in that they directly affect employment levels of specific social groups, thereby shaping through the back door the distributions of wages and market income (Beramendi 2001). While second-order effects have a number of theoretical and empirical implications that are beyond the scope of this article (for an example of these implications on the interplay between gender and partisanship, see Korpi 2000), we take a number of steps to diminish their impact on the empirical evaluation of our argument. First, as discussed above, controlling for female labor force participation and the share of the manufacturing labor force incorporates, albeit partially, a significant share of the second-order effects at work in the labor market. Second, in an effort to include a more direct control for these effects, we have reestimated our wage inequality models including an additional control for the previous levels of welfare state generosity. The findings reported below are not sensitive to the inclusion of this additional control (results available on request). Finally, the way the system of equations is set up controls for any possible second-order effects in the models predicting market and disposable income inequalities. By controlling for wage inequality, equation 2 incorporates, even if crudely, any potential second-order effects affecting market income inequality through the wage distribution. Likewise, by controlling for market income inequality, equation 3 controls for any potential second-order effects affecting disposable income inequality through the distribution of market income. Overall,

Table 7
Estimation Results for Wage Inequality (Equation 1)

Variable	OLS (robust *SE*)
Manufacturing employment	0.000 (0.020)
Imports from Third World	–0.072** (0.035)
Female force participation rate	0.023*** (0.008)
Distribution of human capital	0.018** (0.007)
Union density	–0.019*** (0.004)
Left government inheritance	0.710*** (0.171)
Overall economic coordination	0.306 (0.248)
Left Government Inheritance × Overall Economic Coordination	–1.69*** (0.302)
Constant	2.32*** (0.360)
R^2	.90
n	41

Note: OLS = ordinary least squares.
**$p < .05$. ***$p < .01$.

these three aspects of our approach provide a reasonable, yet necessarily imperfect, basis to deal with the counterfactual problem. We turn now to a discussion of our empirical findings.

Findings

The estimation results for wage inequality equation (see Table 7) are based on OLS with robust standard errors. Let us first comment on the set of control variables meant to capture the social and economic transformations in OECD labor markets. The anticipated inegalitarian effect of deindustrialization (β_1) on wages is not observed. Nor is the impact of wage competition through the increase in imports from the Third World (β_2) as expected, in that the estimated coefficient appears to have the "wrong" sign. However, the anticipated distributive impact of increasing female participation in the labor force ($\beta_3 > 0$) receives support. Similarly, the expected inegalitarian impact of human capital ($\beta_4 > 0$) is confirmed by the estimation results. Thus, as the proportion of adults with completed college education increases, wage inequality grows.

The strength of the union movement displays the anticipated egalitarian effect on the wage distribution. The coefficient for union density (β_5) is both negative and statistically significant. The substantive effects are best illustrated with an example. In a country in which 42 percent of the labor force is unionized and all other variables in the model are set at their mean values, the predicted level of wage inequality would be 3.02. If in such a country the levels of unionization were to increase to 52 percent, wage inequality would decline to a ratio of 2.84. Thus, countries with strong and encompassing unions will be marked by much lower levels of wage inequality.

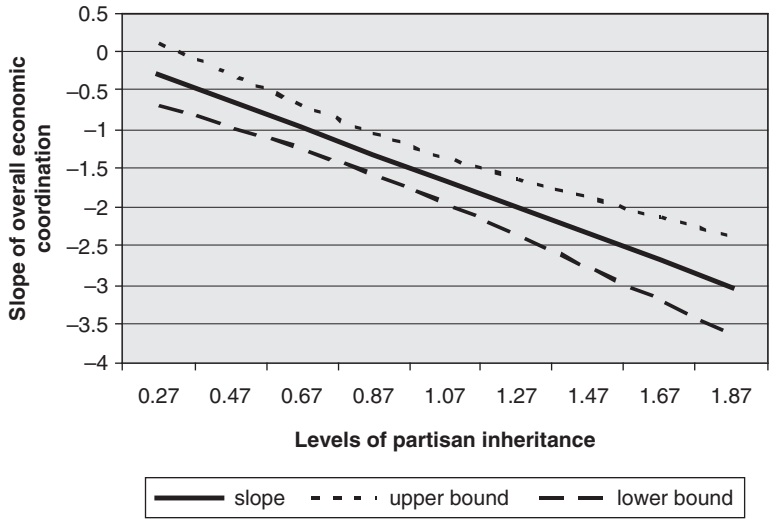
Examining the estimates on the institutional and partisan variables (β_6 to β_8) allows one to portray how the interplay between government partisanship and economic coordination shapes wage inequality. Figure 2 displays how the effect of overall economic coordination is contingent on different values of government partisanship. In turn, Figure 3 presents the slope of government partisanship on wage inequality given different levels of coordination in the economy.

There are two central features in Figure 2. The first is brought into relief by noting that the values on the vertical dimension are all negative. In essence, the effect of institutionalized economic coordination is to always reduce wage inequality. The second feature is the amplifying effect of leftist partisan inheritance. Economic coordination's egalitarian impact rises as the level of left partisan inheritance increases. This result suggests the existence, highlighted by our argument, of a mutually reinforcing effect between high levels of coordination and a long history of government dominated by the Left.

Just as partisanship moderates the impact of coordination, so too is the impact of partisan inheritance conditional on the levels of coordination in the economy (Figure 3). Where one has little or no wage coordination, a right-wing partisan inheritance modestly elevates the levels of wage inequality, while a left-wing partisan inheritance has the perverse effect of increasing that inequality to even greater levels (see Table 8). On the other hand, when one operates within a coordinated economic environment, the Left finds itself in a favorable situation; the greater the level of leftist partisan inheritance, the higher the egalitarian effect on wage distribution.

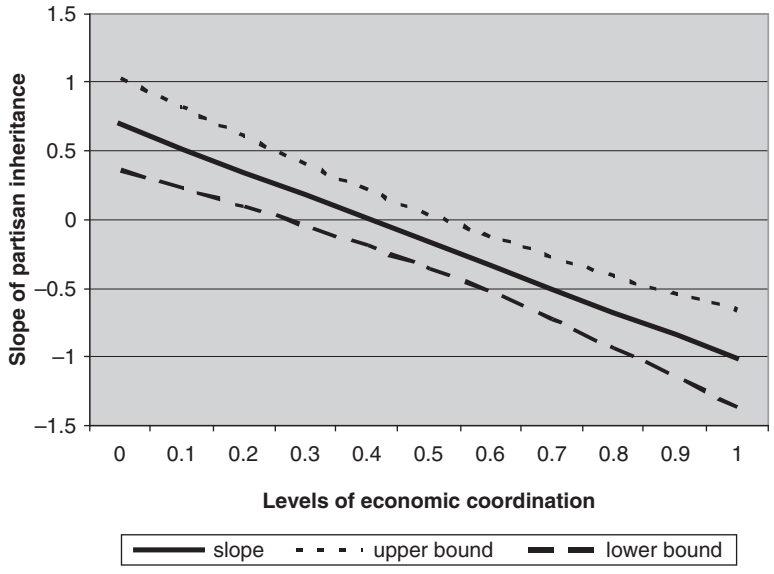
This point is conveyed by Table 8, in which the predicted levels of wage inequality under different partisan and institutional conditions are reported. In noncoordinated environments, left-wing policy is not only incapable of creating wage equality (as anticipated by our argument), it also seems to be the source of a number of responses by labor and capital that drive wage inequality in a direction opposite that intended by the government. More specifically, in the context of our previous discussion of minimum wage regulations, our results seem to suggest that on average, the efficiency and spillover effects offset the disemployment effects associated with minimum wage policy. Alternatively, an institutional environment with high levels of coordination constrains the inegalitarian

Figure 2
Effects of Economic Coordination Contingent on the Levels of Partisan Inheritance



Source: Authors' calculations using formulas developed by Mendoza, Razin, and Tesar (1994).

Figure 3
Effects of Partisan Inheritance Contingent on the Levels of Economic Coordination



Source: Authors' calculations using formulas developed by Mendoza, Razin, and Tesar (1994).

effects of right-wing policies. In sum, our conception of the relationship between partisan politics, wage-bargaining coordination, and wage inequality receives a good deal of empirical support.

Four sets of estimation results on the equation for market-based income inequality are presented in Table 9. The first two columns report estimates of the market income equation as specified above (equation 2). The goodness-of-fit measures are the same across the two techniques used, namely, OLS with robust standard errors and two-stage least squares. All the parameter estimates obtained (β_9 to β_{11}) display the expected

Table 8
Predicted Values of Wage Inequality

	High Wage-Bargaining Coordination	No Wage-Bargaining Coordination
Left-wing government	2.36	4.24
Right-wing government	3.04	3.17

Note: Predictions are based on Table 3. High coordination refers to the maximum value of Hall and Gingerich's (2001) coordination index in our data set, which is 0.95. The lack of coordination (zero) implies, among other things, fragmented wage bargaining and an absence of institutionalized corporate governance. The partisan inheritance values are the same values reported on the horizontal axis of Figure 2. A value of 0.27 represents right-wing partisan inheritance, whereas a value of 1.78 captures the far left partisan inheritance. All other variables are at their mean values.

signs and are statistically significant. Substantively, the estimated effects are of similar size with the exception of the parameter on wage inequality (β_9). This parameter has a significant and positive effect in both estimations. However, it is appreciably higher in the two-stage least squares results. The transmission of cross-national differences in wage inequality to market-based income inequality appears to be muted in comparison with other factors.[14] Clearly, other elements not related to the labor market are also at work in shaping the distribution of market income.

Recall that on the basis of the notion of a structural dependence of the state on capital, our argument contends that once the distribution of earnings is controlled for, parties are not able to directly affect the distribution of market income. Adding a control for partisan inheritance to the market income equation (equation 2), columns 3 and 4 in Table 9 provide an empirical evaluation of this claim. The results strongly support our argument. Thus, the question still remains as to what other determinants are shaping the distribution of market income.

The degree of stock market capitalization is one of these. As anticipated, the estimated parameter (β_{10}) is positive and statistically significant. This is consistent with the notion that in countries where participation in the stock market is heavily regulated by the government, the ability of wealthy families to increase their income is constrained. Alternatively, countries with unregulated stock markets provide wealthy families with profitable investment opportunities and thereby expand their share of market-based income. The scope of government's control on the workings of the stock market is a political decision. Thus, in light of our findings, the degree of stock market capitalization can be seen as a channel through which the distribution of market income becomes politicized, at least in an indirect way.

In addition, the parameter (β_{11}) capturing the effect of the share of pension-age population displays the expected sign and is significantly different from zero. This result supports the expectation that as the share of population that has completed the transition from the labor market into retirement increases, market-based inequality also increases as these people lose their principal source of market-based income, wages and salaries from employment.

Finally, Table 10 reports parameter estimates on the determinants of disposable income inequality. OLS with robust standard errors and two-stage least squares are the two techniques being used. Both of the estimated equations show the same overall goodness of fit. Once again, all the parameter estimates display the expected signs and are statistically significant. They are also very similar in the magnitude of their effects, with the exception of the parameter (β_{11}) on market-based income inequality. Its effect is larger in the two-stage least squares estimation. In both equations, however, the expectation that a positive relationship prevails between market-based and disposable income inequality is confirmed.

We turn now to the factors outlined in our argument that will alter a one-to-one duplication of market income distribution in the distribution of disposable income. These three factors included the overall levels of coordination, the degree of unionization of the labor force, and the government's partisan inheritance.[15] All three of these factors' parameters (β_{12} to β_{14}) take on the expected negative values and are statistically significant. What are the implications of these values? First, in those societies in which there is little or nonexisting coordination, employers have no incentive to accept redistribution through the welfare state. Alternatively, in those societies in which firms pool risks through cross-shareholding and coordinate with labor, employers concede higher levels of redistribution. In other words, economic coordination brings down the level of inequality in disposable income. Our findings on the role of union density conform to results previously developed by other scholars (Huber and Stephens 2001; Bradley et al. 2003). In those societies in which larger shares of workers are unionized, governments need to be more responsive to labor's demand for insurance and redistribution. Therefore, all else equal, larger unions imply more compressed distributions of disposable income. Finally, left-wing partisan inheritance

Table 9
Estimation Results for Market-Based Income Inequality (equation 2)

Variable	OLS (robust *SE*)	TSLS (*SE*)	OLS (robust *SE*)	TSLS (*SE*)
Wage earnings inequality	.015* (.008)	.021* (.012)	.014* (.008)	.024** (.012)
Stock market capitalization	.025*** (.007)	.022*** (.006)	.024** (.007)	.022*** (.006)
Pension-age population	.009*** (.002)	.011*** (.003)	.009*** (.002)	.011*** (.003)
Partisanship inheritance	—	—	–.003 (.007)	.007 (.01)
Constant	.250*** (.060)	.210*** (.080)	.25*** (.06)	.189** (.085)
R^2	.58	.57	.58	.57
n	41	41	41	41

Note: OLS = ordinary least squares; TSLS = two-stage least squares. ; SE = standard error
*$p < .10$. **$p < .05$. ***$p < .01$.

Table 10
Estimation Results for Disposable Income Inequality (Equation 3)

Variable	OLS (robust *SE*)	TSLS (*SE*)
Market income inequality	.326*** (.069)	.444*** (.093)
Coordinated market economy	–.042*** (.005)	–.039*** (.008)
Union density	–.0009*** (.0001)	–.0008*** (.0004)
Left government inheritance	–.019*** (.005)	–.017*** (.007)
Constant	.242*** (.032)	.190*** (.042)
R^2	.87	.87
n	41	41

Note: OLS = ordinary least squares; TSLS = two-stage least squares.
***$p < .01$.

reduces inequality through the long-term institutionalization of higher levels of redistribution.[16] This result is consistent with the recent findings about the cumulative impact of government partisanship on poverty reduction (Iversen and Soskice 2006).

The magnitudes of the effects of interest are analyzed in Table 11, in which the predicted values of the Gini coefficient for disposable income inequality based on the OLS model in Table 10 are presented. The values in Table 11 are the predicted levels of disposable income inequality under different combinations of partisanship, union density, and economic coordination. Market-based income inequality is set at its mean value (0.39). This exercise reveals that union density can reduce the Gini coefficient of disposable income inequality by up to seven points. This implies that in countries with strong unions the amount of redistribution necessary to achieve a perfectly egalitarian society is nearly seven points lower. In turn, overall economic coordination and partisan inheritance reduce such amount by four and three points, respectively.

An alternative way of reading the results reported in Table 11 would be the following: holding all other variables constant, a change from the minimum to the maximum observed level of union density implies a 22 percent proportional reduction in the value of the Gini coefficient. With similar kinds of changes in the levels of overall economic coordination (i.e., from 0 to 0.95) and partisan inheritance (i.e., from 1.27 to 2.78), proportional reductions in the level of disposable income inequality equal to 13 percent and 9 percent, respectively, would be brought about.

In closing, two aspects of our approach require further discussion. The first concerns the time dimension implicit in our measurement of partisanship. The second refers to the possible existence of institutional complementarities in the way countries face the transition between market and disposable income inequalities. The partisan inheritance variable used throughout the analysis begs the question of how long parties of different ideological preferences need to be in office to effectively implement their platforms. Additional analyses indicate that our findings hinge on the medium- to long-term continuation of parties in office. Our findings are not robust to the use of short-term (one year) partisan indicators (results available on request). We do not see this as a problem for our argument, because there is no reason to expect fiscal policy effects to be immediately visible on the distribution of earnings and disposable income. Indeed, we take this lack of robustness to short-term indicators as an indirect proof of our theoretical premise that partisan effects take time to crystallize and get reflected in (otherwise rather sticky) income distributions.

Table 11
Disposable Income Inequality

	Low Overall Coordination		High Overall Coordination	
	Low Union Density	High Union Density	Low Union Density	High Union Density
Left-wing partisan inheritance	0.31	0.24	0.27	0.20
Right-wing partisan inheritance	0.34	0.27	0.30	0.23

Note: Predicted values based on Table 10 (ordinary least squares). In calculating the predictions, "low" and "high" refer, respectively, to the minimum (0) and the maximum (0.95) values in the sample. A low value of union density means that only 10 percent of the labor force is unionized, whereas a high value implies that this percentage rises to 87.9 percent. Finally, a low value on the partisan term (0.27) represents right-wing partisan inheritance, whereas a value of 1.78 captures the far left.

Finally, we turn now to the issue of institutional complementarities in redistribution. Even if independent from one another, the effects of union density, economic coordination, and partisan inheritance combine very differently in the real world. In some countries, such as the Scandinavian nations, all three factors will be very high, thus reducing disposable income inequality to its lowest observed levels. In some other countries, the situation is reversed: coordination, union density, and partisan inheritance are very low, and as a result, disposable income inequality reaches its maximum levels. These patterns may lead the reader to wonder about the existence of complementarities between some of these elements, for instance, left-wing parties and overall economic coordination. This being the case, an interaction effect between these two factors should be observed. If left-wing parties facilitate the existence of wage bargaining agreements and depend on them to create an egalitarian wage distribution, should the capacity of left-wing parties to shape the distribution of disposable income not be contingent as well on the overall degree of coordination in the economy? The answer is that no such complementarity is in place, as confirmed by the reestimation, including interaction terms, of the models presented in Table 10 (results available on request). And the reason for this lies in how directly governments are able to shape the distribution of disposable income inequality as opposed to the distribution of earnings. As argued above, government's effects on wage inequality are indirect in that they are contingent on the agreement of unions to wage moderation and accept high taxes on labor. Such agreement only takes place under conditions of high wage-bargaining coordination, thereby producing the observed interaction effects. Alternatively, an increase in fiscal redistribution reduces disposable income inequality directly (i.e., without any other actors taking part in shaping the final outcome). Thus, for a given value of market income inequality, left-wing governments can make use of fiscal redistribution to reduce inequality regardless of the institutional position of any other actor. As a result, no interaction effect is to be observed.

Conclusion

We have shown that in the OECD countries, the patterns of cross-national variation across different forms of income distribution are quite diverse. There is little evidence of a dramatic convergence on greater inequality in the distributions of labor earnings as well as the postfisc distributions of disposable household income. In turn, there are signs pointing to widespread growth in inequality in overall market income. This can be seen as a manifestation of the structural dependence of the state on capital. While governments are able to shape the distributions of labor earnings and disposable income through taxes, transfers, and regulations, there are certain forms of prefisc income that are sheltered from direct government intervention.

Larger cross-national variations in earnings and disposable income distributions are attributed to the roles played by political actors and institutions that allow actors to coordinate their activities. The way in which political parties are able to pursue their distributional goals varies across forms of income. Through their legislative legacy,[17] these parties work their effect on the distribution of disposable income via fiscal choices. However, their capacity to influence wage earnings is highly contingent on the national economic institutional framework. While high levels of economic coordination facilitate the leftist goal of a more egalitarian wage distribution, the pursuit of such goals in the absence of coordination generates perverse effects.[18]

In conjunction with the distinction between labor earnings and market income, our focus on coordination and its interplay with partisan traditions helps explain why there is more cross-national variation in terms of wages and disposable income inequality than there is in terms of market income inequality.[19] Finally, insofar as the sources of divergence in distributive outcomes among advanced capitalist societies identified in this article remain in place, the realities of inequality will continue to be as distant from the "transatlantic consensus" as they are today.

Notes

1. In line with the other two measures of income inequality used in this article, relating to market and disposable income, we would have preferred to use data drawn from the Luxembourg Income Study (LIS). Comparability problems (related to the availability of information on the labor market status of household heads) on the wage data in the LIS would greatly reduce the number of observations. In addition, the OECD wage data are available only in terms of interdecile ratios and not in any other form, such as the Gini indices that we use in conjunction with the LIS-based data.

2. A household's market income includes not only earnings from dependent employment but those deriving from self-employment, as well as interest, dividends, rents, and any other income from nonstate sources.

3. Calculations follow the lead of Mendoza, Razin, and Tesar (1994).

4. In providing a summary measure of the distribution of income, the Gini indices have the disadvantage of potentially obscuring processes taking place in different parts of the distribution (Atkinson and Brandolini 2003, footnote 6). Note, however, that the arguments throughout this article are concerned with the overall degree of dispersion across forms of income.

5. John Stephens has suggested that our analysis is misleading because it includes pensioners. The concern is that pretax inequality in countries with "comprehensive" public pensions systems (i.e., the Nordic countries) would be "artificially" high because pensioners in these countries make no provisions for retirement outside the public system. Since our concern is with society-wide income inequality, it seems inappropriate to consider only "one variant of the working-age population." We do not deny that the welfare state has as some of its primary clients those in retirement age. Indeed, the failure of some welfare states to adequately support those of pensionable age is a major problem and should not be pushed aside nor relegated to the status of a nuisance. Stephens and his coauthors (Bradley et al. 2003, footnote 5, 224-25) "demonstrate that the assertion that the welfare state merely redistributes income across generations is wrong." We question neither their contribution nor the fact that the welfare state does more than engage in intergenerational redistribution. However, in showing that redistribution is not simply across generations, there is no gainsaying that the intergenerational redistributive aspect of the welfare state is important to a significant proportion of the citizenry. In addition, a good deal of cross-class redistribution occurs within pension systems. Most pension systems are not guided exclusively by insurance principles. Finally, as we point out later, the findings that we present hold regardless of the demographic base used for our income distribution measures.

6. Note that Alesina and Glazer's (2004) recent work on the differences between the United States and Europe in terms of both poverty and the efforts of the state to relieve it is somewhat misleading in its portrayal of transatlantic differences in market income distribution. It proceeds under the assumption that the gulf in the level of inequality between Americans and Europeans is very wide before taxes and redistribution (pp. 3, 56, 58), indeed far wider than it really is, and the authors thereby infer that the European welfare state systems are less redistributive than they actually are. A cursory examination of Tables 2 and 3 would show how inaccurate Alesina and Glazer's portrayal is.

7. For related empirical analyses, see also Cusack and Beramendi (2006) and Ganghof (2004).

8. We do not report the results based on PCSE estimates because of the small number of time units (cf. Wallerstein and Moene 2003). The PCSE results are available on request.

9. Union density is the percentage of the labor force who hold membership in unions.

10. This variable is a measure of the center of political gravity that characterizes the cabinet (see Cusack and Engelhardt 2002).

11. We use the coordination index developed by Hall and Gingerich (2001). Our results, however, are not sensitive to substituting Hall and Gingerich's measure for the wage coordination index developed by Kenworthy (2001).

12. *SMC* represents stock market capitalization expressed as a percentage of GDP. The data are from the World Bank's Database on Financial Structure and Economic Development (Beck, Demirgüç-Kunt, and Levine 2000).

13. Two different estimation techniques are used for this equation: OLS with robust standard errors and two-stage least squares.

14. These results hold even when we adjust our analysis to take into account the suggestions by John Stephens (see note 5). As he points out, if his criticisms hold, the impact of the wage dispersion term on market-based income inequality should be much stronger than we find. We examined this conjecture. First, we calculated the Gini indices of market-based inequality for the more restricted population group Bradley et al. (2003) used. Second, we replaced the variable measuring the share of pension-age population with the unemployment rate. We estimated the equation using OLS with robust standard errors and two-stage least squares. The estimates obtained are similar to those in Table 9. The parameter estimate using OLS on these data is .018, as opposed to .015. In turn, the parameter estimate using two-stage least squares is .041, as opposed to .021. (Complete results for the two are available on request.) We do not see the fact that these parameters are slightly larger as undermining our argument. We address this issue again when discussing the estimates for the disposable income inequality model.

15. Some have argued that any specification including both union density, wage bargaining centralization, and partisan inheritance is inappropriate because of the presence of high levels of multicollinearity (Bradley et al. 2003). In our view, even if these three factors may partially covary, the causal logic linking each of the three factors to inequality is sufficiently independent to permit their inclusion in the model. From a statistical point of view, none of the variables included in the model has a variance inflation factor higher than 1.3. Thus, there is no multicollinearity problem.

16. Our results are independent of the use of either the total population or the "working-age population" that Bradley et al. (2003) used. The parameter estimates and the associated statistics are practically the same as those found in Table 10. Again, the results are available on request.

17. Our findings complement those of Bradley et al. (2003) in highlighting that the achievement of a more egalitarian distribution of income requires a long-term presence of social democratic parties in office.

18. This finding is related to earlier contributions by Rueda and Pontusson (2002); Pontusson, Rueda, and Way (2002); and Rueda (2004) on the relationship between partisanship, the varieties of capitalism, and wage inequality. While they see partisanship and coordination as substitutes of each other, our analysis suggests that left-wing partisanship and economic coordination are better understood as complements of each other.

19. These results directly complement Iversen and Soskice's (2006) analysis of how proportional representation systems bias electoral outcomes toward the Left, thereby shaping the politics of redistribution.

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