The Impact of Social Security Wealth on the Distribution of Wealth in the European Union

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Household wealth is commonly defined as the total value of assets minus the total value of liabilities. Social security wealth is usually not included in the value of households' assets. The first reason for the omission of social security wealth is usually the lack of data, the second is its limited liquidity (OECD, 2013). Because for the majority of households public pension entitlements are the most valuable asset (Atkinson, 1983) researchers try to estimate their value and assess the impact of social security wealth on the wealth distribution.

Wolff & Marley (1989) investigate the evolution of wealth inequality in the US in the period 1922-1983 using various wealth concepts. They find that social security wealth significantly decreases wealth inequality. Social security wealth equalizes wealth distributions also in other countries (Dunn & Hoffman, 1983; Bönke et al., 2019; Shamsuddin, 2001; Mazaferro & Toso, 2009; Roine & Waldenström, 2009; Maunu, 2010, Kuhn, 2020, Longmuir, 2021, Wroński, 2021, Jabłonowski, 2021). Although the equalizing impact of social security wealth on wealth distribution is commonly accepted, the literature has two important limitations. Firstly it covers almost only developed economies, where social security systems are usually progressive. Secondly, the availability of cross-country studies is very low (e.g. Frick & Hadey, 2009; Bönke et al, 2020, Cowell et al., 2017). Results of single-country studies are very difficult to compare because researchers use different data sources and adopt various methods to estimate the value of social security wealth. In this paper, we fill this gap by delivering comparable measures of social security wealth and its equalizing power in 19 EU economies.

In this paper, we investigate the impact of social security wealth on wealth inequality in 19 EU member states. To achieve this aim we use a novel dataset – the third wave of the Eurosystem Household Finance and Consumption Survey, which provides internationally comparable data on household wealth. Our estimates of social security wealth are based on Eurostat's (2019) demographic forecast EUROPOP 2019.

We find that social security wealth significantly decreases wealth inequality in the European Union. However, a lot of variation in the strength of the equalizing power of the public pension system exists. The impact of social security wealth on (augmented) wealth inequality is strongest in Germany, Austria, Netherlands, and Estonia, while it is lowest in Greece and Slovenia, and Luxembourg.

Equalizing power of social security wealth is positively correlated with social security wealth – private wealth ratio (which may be seen as a measure of the size of the public pension system) and the share of single households in the population. Higher homeownership and a stronger correlation between the position of the household in the distribution of private wealth and its position in the distribution of augmented wealth weakens the equalizing power of the public pension system.

We also investigate if the cross-country variation in social security wealth explains cross-country wealth gaps. Here, the evidence is mixed. On the one hand, cross-country wealth gaps assessed at chosen percentiles of the augmented wealth distribution, are smaller than in the case of private wealth distribution. On the other hand, however, the decomposition shows that augmented wealth inequality is to a larger extent generated by between-country inequality than private wealth inequality. Social security wealth/augmented wealth inequality in European Union is smaller than private wealth inequality.

In our view, the evidence presented in this paper provides important support for the inclusion of social security wealth in the household wealth measures, or at least an auxiliary analysis of social security wealth in the research of household wealth. The public pension system has an impact not only on income distribution but also on wealth distribution. Therefore, researchers investigating its distributive consequences should cover not only the distribution of income but also the distribution of wealth.