

Abstract of the Working Paper:**Income Inequality and Organisational Trust**

Perception and Reality

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The undesirable outcomes linked to high levels of income inequality are numerous. Among several, these are poor educational performance (Kawachi et al. 1997), violence (Patterson 1991), low levels of well-being (Alesina et al. 2004) and health (Wilkinson 1992), as well as slow economic growth (Barro 2000) or low provision rates of social goods (Wilkinson and Pickett 2011). It is argued that those negative effects of inequality are channelled by low levels in trust (Wilkinson and Pickett 2011). In addition, it has been shown that social trust is indeed negatively affected by income inequality (Leigh 2006; Putnam 2007; Uslaner and Brown 2005; Gustavsson and Jordahl 2006). The essential argument why inequality reduces social trust is that in societies with high inequality, differences between individuals are too large for them to feel connected and to trust each other.

Problem However, most of the existing literature refers to social or generalised trust when trying to explain how income inequality harms society. One could assume that trust in organisations, for example, in the government or in the EU, diminishes as well in an environment of high inequality, since appropriate political representation is questioned. It is the distribution of resource which helps to explain levels of organisational trust. In a society where high income is related to high political influence, an increase in income inequality is associated to a skewed representation of the people in political bodies. The increase of inequality in political representation could result in frustration of the less influential part of the society which would then lead to a lack of trust in political institutions. Lynch (2000,

p.1202) points out that the effect of income inequality on trust can be traced back to the disparity of resources which leads to a "...systematic underinvestment across a wide range of human, physical, health, and social infrastructure...". Unwanted consequences have been also documented, for example, in health care supply (Firth-Cozens 2004), in the work of NGOs (Kramer 1999), and in banking (Seal 1998).

So far, studies on the linkage between income inequality and trust mainly suffer from three limitations. Firstly, most of the research, which concludes with a negative relation between income inequality and generalized trust, has examined the effect on a national level (Leigh 2006; Rothstein and Uslaner 2005; Jordahl 2007; Gustavsson and Jordahl 2006). The potential loss of information due to aggregation has been raised. Subsequently, other scholars have shown that individual factors like optimism in life (Uslaner 2002), personal economic success (Dohmen, Verbakel and Kraaykamp 2010), poor personal living conditions (Ross et al. 2001) or ethnic fragmentation (Alesina and La Ferrara 2002) have a notable influence on generalised trust. But even when researchers tried to contribute to this shortcoming by applying individual control characteristics on one side, the measure of income inequality, on the other side, remained aggregated.

The second problem of most of the previous studies is that even though the empirical results indicate a negative association between generalized trust and inequality, the mechanism behind the phenomenon is often not entirely clear. One line of reasoning is that the more stratified societies are, the more closed they become and people are less likely to interact with others from different economic strata.

This so called *stratification effect* can be traced back to the actual allocation of resources (Elgar and Aitken 2010; Wilkinson and Pickett 2009). Another argument is that individuals in unequal economies - particularly at the lower end of the income distribution - do not perceive the others to share the same living realities or fate (Uslaner and Brown 2005). Because of this *perception effect*, they refuse to trust others with whom they share so little. The envy of the less fortunate (Wilkinson and Pickett 2009), a lack of optimism (Rohstein and Uslaner 2005; Delhey and Newton 2001) or egalitarian values (Gustavsson and Jordahl 2006) have proven to be mechanisms through which income perception interacts with trust. Following along this line of argumentation, it would be the perception of economic disparities and not the actual economic measure influencing levels of trust. Standard objective measures of income inequality, like the Gini coefficient, would then at least partly fail to capture both the *stratification effect* and the *perception effect* in only one variable.

Sample For testing the hypothesis of a negative relationship between income inequality and organisational trust two datasets are used. The data about national Gini levels come from the EU-SILC 2009 dataset, in which all EU27 countries are included. Here, the Gini coefficient is measured on a scale from 0 (perfectly equal distribution of income) to 100 (perfectly unequal distribution). The 2009 edition of Eurobarometer (EB) on Poverty and Social Exclusion delivers the individual characteristics, categories of organisational trust, and a subjective measurement of perceived income inequality. After keeping only individuals with all necessary information, 26.635 observations in 27 countries remain.

The original question about perceived inequality in the EB reads: "Nowadays in (OUR COUNTRY) income differences between people are far too large?". Answers to this question are coded in a four-step fashion,

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with the outcomes "Totally disagree" (1), "Tend to disagree" (2), "Tend to agree" (3), and "Totally agree" (4).

The EB asks two different questions regarding the trust of Europeans in local and national authorities. The first one concerns the general trust in the national government and the national parliament. It reads: "Please tell me how much you personally trust each of the following institutions using a scale from 1 to 10 where [1] means 'you do not trust the institution at all' and [10] means 'you trust it completely'!". Answers therefore result in a 10 scale outcome. The second question elaborates on the people's trust in the fight against poverty of the following institutions; The European Union, the (national) government, regional or local authorities, NGOs and charities, religious institutions, private companies, and the citizens themselves. The question is phrased: "For each of the following, please tell me if you tend to trust it or not with regard to their action in combating poverty." The EB codes the answers to this question as "Tend not to trust it" (0) and "Tend to trust it" (1).

Conclusions First, some descriptive findings about inequality and trust are worth noticing. In the EU 27 income imbalances are perceived as relatively high. With an average numeric response of 3.5 (on a 1-4 scale), all citizens on average at least believe that income imbalances have become (far) too high in the last years. On the other hand, trust in national governments is surprisingly low. With a numeric average of 4.0 (1-10), most citizens in Europe declare, that they rather do not tend to trust their government. Second, income inequality and perceived inequality do not measure the same thing. The two measures only show a relatively weak simple correlation. Therefore, they have to be examined separately and the effort should be made to evaluate their joint potential towards institutional trust.

In our final paper, we examine the effects of (perceived) inequality on institutional trust in a mixed-effects logit model. The analysis shows that marginal effects of income inequality on trust in the government are particularly pronounced for individuals

with high levels of trust in general.

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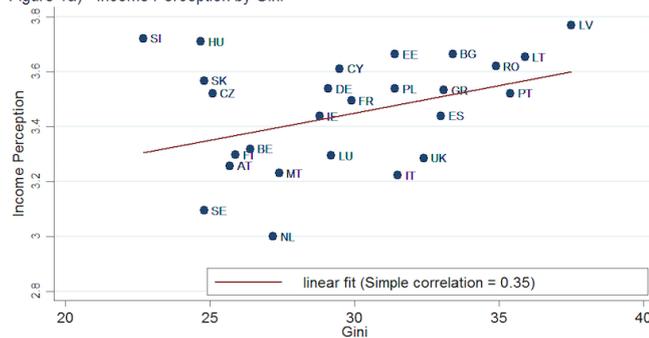
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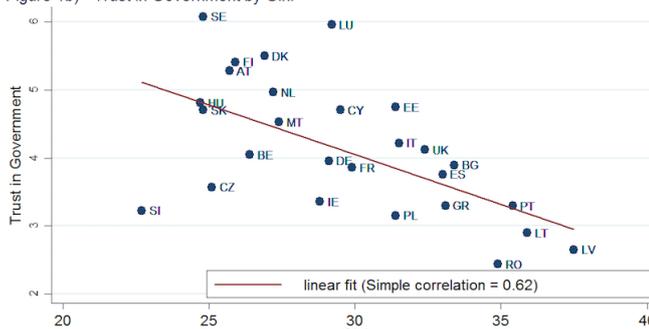
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Figure 1a) - Income Perception by Gini



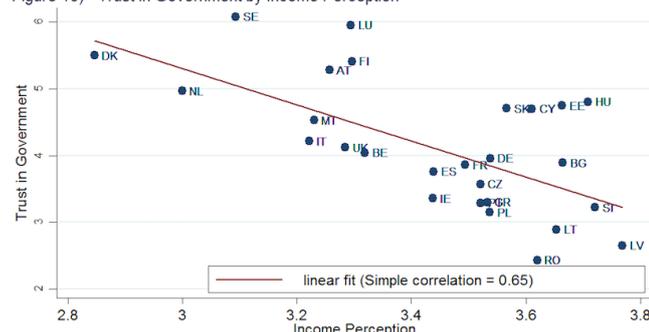
Source: Eurobarometer (355) 2009, EU-SILC 2009 and own calculations

Figure 1b) - Trust in Government by Gini



Source: Eurobarometer (355) 2009, EU-SILC 2009 and own calculations

Figure 1c) - Trust in Government by Income Perception



Source: Eurobarometer (355) 2009, EU-SILC 2009 and own calculations