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Decomposing income inequality into factor income components:

A comparison of different methods

Abstract:

This paper decomposes income inequality into factor components using three different methods for selected G20 countries. The paper analyses the role of employment status, type of contract and wage differentials in accounting for differences in income and its inequality. The results show that labour income is the most dominant factor contributing to inequality in all the countries under analysis using the different methods. Within the labour income, the disparities between working and non-working heads are found to be the most dominant factor. Transfers and benefits seem to be the most important factor contributing to reducing inequality using the accounting approach, while the factor decomposition method shows taxes and social contributions to be the important factors contributing to reducing inequality. The analysis also reveals that social assistance, transfers and benefits alone cannot address the issue of rising inequalities in countries where unemployment continues to be high, which requires intervention in the labour markets.