Determinants of Income Composition Inequality

Bilyana Petrova and Marco Ranaldi

The last four decades have brought about a steep rise in economic inequality and a fundamental shift in the balance of power between capital and labor in advanced industrial democracies.[1] The Organisation for Economic Cooperation and Development (OECD) announced in 2022 that income inequality had reached its highest level for the past half century.[2] The richest 10 percent of the population earned nine times more than the poorest 10 percent, the middle class had shrunk, social mobility had decreased, and income gains primarily accrued to the wealthy. Furthermore, although labor compensation and corporate profits both rose in absolute terms, the latter grew much faster than the former.[3] Consequently, the share of national income going to labor declined from 64 to 59 percent of global GDP.[4] At the same time, while the deepening of financial markets, the development of the real estate sector, and the introduction of new financial instruments broadened access to capital,[5] capital income remains highly concentrated.[6]

These trends have produced a new economic reality where income sources that used to belong to specific groups are no longer confined to these groups. While in the past the very rich derived their income exclusively from property and stocks, today they fund a significant part of their consumption through salaried work.[7] Indeed, Berman and Milanovic estimate that the share of people with high labor and capital income in the United States doubled between 1980 and 2020, jumping from 15 to 30 percent.[8] Similarly, an increasing fraction of the middle class also draws on capital income.[9] 55 percent of Americans participate in the stock market, and, although declining interest rates have suppressed portfolios in the last twenty years, approximately 15 to 20 percent of Europeans can be described as "petit rentiers."[10] The composition of income across the income distribution in modern postindustrial democracies is therefore different from what it used to be during the early stages of capitalist development.

What explains this change? Our article investigates the political determinants of income composition inequality (ICI). ICI captures the variation of income sources across the income distribution.[11] Different income groups—the wealthy, the middle classes, and the

poor—derive income from different sources. They also depend on these sources to a different degree. Capital income, for example, makes up a much larger share of the portfolio of the rich. Wages and salaries, in contrast, are much more important to the poor, whose access to capital remains limited. By revealing the extent to which capital and labor income are held by different classes, ICI reflects the constantly evolving nature of capitalist organization.[12]

Drawing on Power Resource Theory,[13] we highlight the role of political parties and argue that compositional inequality is lower under the Left. Left-wing parties have traditionally shared a commitment to lower economic inequality. The policies that they pursue while in office are generally compatible with democratized access to capital assets, lower rents, and lower concentration of capital income, all of which bring ICI down. Furthermore, recent transformations in Europe have constrained the Left's capacity to forcefully redistribute labor income to the poor.[14] Indeed, the last few decades have witnessed a weakened ability to expand existing social policies, which has prevented an increase in the concentration of labor income among the lower classes. As a result, modern left-wing parties' profiles are consistent with policy action that decreases the gap between rich capitalists and poor workers. Consequently, governments dominated by left-wing parties should be associated with lower income composition inequality.

We test this expectation with a cross-sectional time series analysis of thirty European countries between 2003 and 2017. Using high-quality individual-level data from the European Union Statistics of Income and Living Conditions (EU-SILC) database,[15] we begin by tracing how ICI has changed over the last two decades. We proceed to show that left-of-center parties are linked to lower compositional inequality. Interestingly, this effect is not driven by changes in labor income; instead, it is mainly due to an increase in the proportion of capital owners among the three poorest quintiles when left-wing parties are in power. This suggests that the modern Left has been more successful at democratizing access to capital than at redistributing labor income over the last twenty years. Our findings are robust to different model specifications and estimation strategies.

While existing scholarship on economic inequality has focused on the drivers of wage dispersion and top income shares, less is known about the forces shaping the distribution of income composition per se. To our knowledge, this is one of the first studies that simultaneously explores the functional and the personal income distributions. As such, it conceives of inequality multidimensionally, centering on the composition of portfolios across the income spectrum. Understanding the behavior and drivers of this composition is important as it might shed light on class conflict, attitudes toward inequality, preferences for redistribution, changing patterns in voting behavior, and, ultimately, party system reconfiguration. It can also help identify specific policy instruments that address the inequitable economic growth of the past four decades.

Literature

A nascent literature in economics investigates a so-far missing dimension in distributional analyses: income composition inequality. ICI links the functional and the personal

income distributions.[16] While the former captures how total output is split between capital and labor, the latter reflects how total income is distributed across the population. Bringing the two together, income composition inequality measures the concentration of a given income source across the total income distribution. In other words, it reveals the extent to which income composition varies among the rich, the middle classes, and the poor. Maximum ICI occurs when individuals at the top and at the bottom of the income distribution derive their income from completely different sources. Inversely, ICI is minimal when all individuals, regardless of their position in the income distribution, have the same share of capital and labor income.

To better illustrate the concept, imagine an economy comprised of two individuals. *Person A* earns 1,000 USD per month. *Person B* makes 10,000 USD. A and B can receive capital (K) and labor (L) income. Perfect income composition equality would suggest that A and B derive an equal proportion of their income from K and L. Thus, A makes 200 USD, or 20 percent, from K and 800 USD, or 80 percent, from L, while B makes 2,000 USD from K and 8,000 USD from L.[17] In contrast, perfect inequality would mean that A earns 100 percent of her income, or 1,000 USD, from wages, working as a janitor in New York, while B makes 100 percent of her income, or 10,000 USD, from capital, holding government bonds, owning company shares, and renting her second apartment, without earning any salary.[18] In this case, A and B hold completely different types of income.

From a political economy perspective, income composition inequality signals the type of capitalism that characterizes different countries. A high level of ICI implies that the wealthy predominantly rely on capital income, while the poor mainly depend on labor income.[19] Such divergence has the potential to translate into class conflict as social classes care about different policy areas and have markedly different policy preferences. A low level of ICI, on the other hand, suggests a transition to a "multiple-sources-of-income" capitalism in which individuals from the top and the bottom of the income distribution depend on the same income sources. The resulting overlap in their portfolios might induce important realignments in their policy positions and political behavior.[20] Concentration measures of capital and labor income do not reveal this overlap. Compositional inequality does.

So far, existing scholarship has largely focused on identifying temporal and spatial trends in ICI. Looking at Italy, Iacono and Ranaldi show that income composition inequality fell between 1989 and 2016.[21] This decrease was mainly driven by a shift in accumulation patterns, whereby labor income accrued at the top while capital income, predominantly in the form of imputed rents from real estate, moved toward the middle and the lower classes. Shifting to Nordic countries, Iacono and Palagi document a rise in income composition inequality following the implementation of dual income taxation reforms (DITRs) in the early 1990s.[22] The resulting lower marginal tax rates on capital income led to higher concentration at the top. Recent work has thus shown that ICI depends on entitlement rules, or the norms "stating who has the right to receive a given type of income,"[23] but has so far neglected to systematically explore the effect of politics.

While research on income composition is yet to meaningfully incorporate politics, scholarship on other dimensions of economic inequality has established the importance

of political and social factors. Bengtsson and Waldenström find that the introduction of universal suffrage, the abolition of colonialist structures, and the adoption of redistributive policies were associated with a decrease in the capital income share.[24] In contrast, the erosion of trade unionism in the post-war period reversed this trend.[25] This is consistent with work on labor compensation, which attributes the marked fall in the labor income share since the 1980s to the pronounced decline in workers' bargaining power.[26] Weakened by globalization and deregulation,[27] trade unions allegedly lost their ability to effectively protect workers' interests.

This decline has been concomitant to a rise in the market power of corporations.[28] Recent studies have documented the emergence of "superstar firms," leading to higher markups and corporate profitability.[29] Indeed, Autor et al. report intensifying sales concentration across advanced democracies,[30] which has further enhanced the political weight of business[31] and magnified its voice at the negotiation table.[32] Monopolistic market structures are thus associated with lower employment levels and reduced rent-sharing, which, collectively, diminish labor compensation.

These structural changes are complemented—and at least partly induced by—the processes of globalization and financialization. Opening the economy to trade and capital has exposed domestic labor to intensifying competition from abroad, further eroding its share in total income.[33] By giving investors an exit option, capital mobility has propelled governments to cut spending and worker protections to attract foreign direct investment.[34] Financialization, on the other hand, has greatly loosened the link between production and surplus generation, excluding workers from revenue-generating and compensation-setting processes and boosting executive remuneration at the expense of wages, especially in environments characterized by weak labor.[35] By prioritizing profit maximization, it has incentivized downsizing, promoted layoffs and subcontracting, accelerated the substitution of labor with technology, and exacerbated wage stagnation.[36]

Exposed to different pressures, national governments thus face shrinking room for maneuver. While in the postwar period left-wing parties were associated with lower market and disposable income inequality due to their commitment to redistribution and market conditioning, partisan differences play a less influential role in explaining patterns in economic inequality and welfare state reconfiguration today.[37] Indeed, recent research indicates that internal transformations and external constraints have induced traditional political parties to converge on socio-economic matters.[38] In some contexts, this has resulted in the obliteration of meaningful partisan differences on the first (economic) dimension of politics.[39] In others, it has led to the emergence of new political actors.

We seek to contribute to this debate by examining how political forces shape the evolution of income composition inequality.

Theoretical Framework

Why would politics matter for compositional inequality? Policy decisions have implications for labor compensation and capital accumulation. Consequently, the actors

behind these decisions and, by extension, the partisan composition of government, can shape ICI.

Existing scholarship has shown that different political parties have different bases. While left-wing parties—be they socialist, communist, or social democratic—have historically represented the working classes, right-wing parties have traditionally catered to the interests of upper-class constituencies.[40] Nevertheless, recent years have brought about an important reconfiguration. Social democratic parties, in particular, have undergone a re-orientation toward educated, high-skill sociocultural professionals.[41] Their voters today are thus more diverse and less vulnerable.

These different alignments imply different distributional goals and divergent views about the role of the government in economic life.[42] Left-wing formations generally espouse a more egalitarian agenda.[43] This programmatic commitment extends beyond the realm of the welfare state to market conditioning strategies such as empowering unions, updating wage legislation, adjusting employment regulations, limiting monopoly power, and broadening access to additional income streams.[44] Indeed, in the contemporary context of heightened globalization, rapid demographic change, and variegated social risks, some social democratic parties have moved away from compensatory redistribution to social investment, embracing activation, productivity, and human capital accumulation.[45] Right-wing parties, in contrast, often advocate for more limited intervention in economic life, placing emphasis on deregulation and competition.

Such policy priorities have repercussions for ICI. The direction of this effect varies depending on the specific policy instrument. Four broad types of legislation are particularly relevant: taxation, redistribution, wage regulation, and access to capital. The first two fall in the realm of the welfare state, while the remaining two pertain to labor compensation and capital ownership. With respect to taxes, lower corporate, capital gains, and top marginal tax rates facilitate the concentration of capital income. Apart from leaving a higher proportion of income in the hands of those who hold more of it, they might enhance the appeal of capital assets and enable their acquisition. Since higher earners are better positioned to take advantage of existing opportunities,[46] they are likely to undertake investment and expand their capital portfolio. Tax reforms favoring capital income can result in a more inequitable distribution of income composition. Such reforms typically occur under right-wing parties. Because left-wing parties are generally associated with progressive stances on corporate and personal taxation,[47] greater representation of left-wing parties in national legislatures should translate into lower compositional inequality.

An example would be the UK's Labor Party, which revamped tax legislation several times throughout the 2000s. While the resulting reforms did not only benefit low- and middle-income constituencies, they (at least initially) increased top tax rates and introduced incentives for small businesses. In a more radical move, French President François Hollande introduced a "super-tax" of 75 percent on earnings over 1 million euro in 2012. Similarly, the German Social Democratic Party sought a three-percentage-point increase in the top personal income tax rate (PIT) in the 2017–2018 coalition talks with the Christian Democrats.[48] These measures can slow down the accumulation of capital income among the rich by preventing the acquisition of additional capital assets and lowering

future returns. On the other side of the political spectrum, conservative Irish Finance Minister Brian Lenihan (2008–2011) announced a hike in top PIT rates in the midst of the country's severe recession in 2009 but refused to touch its competitive corporate income tax. Likewise, Hollande's center-right successor, Emmanuel Macron, lowered the corporate tax rate in France from 33.3 percent to 25 percent in 2023. Such reforms can boost the capital income share and allow dividends and capital gains to accrue to the rich.

Redistributive policies also affect ICI. Although they vary in terms of their generosity, progressivity, coverage, and eligibility criteria, most welfare states are generally oriented toward low- and middle-income households. Benefits typically target vulnerable groups facing heightened risk. Consequently, lower classes derive a higher fraction of their income from transfers and benefits. For reasons that we explain in greater detail in the empirical section but that partly revolve around the conditional attachment of some benefits to past employment and current joblessness, we include benefits and transfers in our definition of labor income. Higher social spending can therefore increase the concentration of labor income at the bottom of the distribution, resulting in higher income composition inequality. Ironically, the Left's weakened ability to expand social programs[49] might have thus helped bring ICI down.

Such behavior has not been limited to more centrist formations like the UK's Labour Party under Tony Blair (1997–2007) or the German Social Democrats under Gerhard Schröder (1998–2005), but has extended to old, deeply rooted left-leaning parties, such as the Swedish Social Democrats, who were forced to accept spending cuts due to coalitional pressures and budget constraints. Indeed, Armingeon et al. show that left-wing parties were more likely to undertake substantial welfare state retrenchment during episodes of fiscal consolidation because their historical reputation as trustworthy advocates of social programs convinced the public that cuts were necessary to ensure the sustainability of the welfare state.[50] Given the Right's ideological opposition to generous social policies, right-wing parties are still more likely to pursue social spending cuts, especially if they can be shielded from electoral backlash. Nevertheless, the Left appears less able to resist this trend and, occasionally, seems to actively participate in it. Under the former scenario, when left-wing parties accept previous cuts without increasing social spending, we expect that their (in)action would not change ICI. Under the latter, when they do engage in retrenchment, they will be associated with a fall in ICI.

Some forms of wage legislation can have a similar, though more complex, effect. Left-wing parties typically pursue minimum wage increases or salary caps for very high earners. On the one hand, these measures can increase ICI because they direct labor income toward the poor, which boosts concentration at the bottom of the total income distribution. Nevertheless, they can also decrease ICI by broadening capital income ownership or reducing its accumulation at the top. A higher minimum wage could potentially allow lower-income workers to diversify their income streams. Similarly, a cap on executive compensation can limit the prevalence of remuneration packages that include equity and stock options, ameliorating capital income concentration at the top. The effect of wage reforms—and the left-wing parties that typically embrace them—on compositional inequality is thus likely to be ambiguous.

Lastly, policies designed to broaden access to capital, such as introducing mandatory private pillars in pension systems, changing regulations on capital assets, and incentivizing homeownership, naturally limit the concentration of capital income among the rich. These policies promote a more equitable distribution of capital income. Democratizing access to capital gives the middle and the lower classes the chance to diversify their portfolios. Instead of only earning wages and collecting benefits, they also hold capital assets, such as dividends, capital gains, or property. This moves societies away from a capitalist structure characterized by two opposing social classes that exclusively control two different types of income. Since left-wing parties are more concerned about rising capital income concentration, their prevalence in national parliaments should lower income composition inequality.

The reforms that national governments pursue in a variety of policy domains thus affect ICI. Such policy action, however, is not always imperative. Policymakers do not necessarily need to implement reforms to shape macroeconomic outcomes. Under certain circumstances, independent agents' responses to a changing political landscape can induce a shift in compositional inequality without a change in policy. Possible examples would be investors abstaining from participating in additional ventures in anticipation of unfavorable economic conditions or citizens deciding against the purchase of new property due to heightened uncertainty.

A rich literature has shown that such behavioral responses are more likely under left parties. Left parties' agenda is often perceived as hostile to the interests of higher-income groups, whose assets have historically been subject to higher taxation in environments characterized by higher redistribution. If the better off expect lower returns to their investment under left-wing governments, they might limit their participation in stock markets, desist from buying property, and decide against expanding their portfolios. This might be especially likely in the period after the Great Recession, when rapidly deteriorating economic conditions and heightened economic vulnerability propelled political elites on the left to politicize economic inequality. In such circumstances, wealthier individuals might be reluctant to undertake investment. At the aggregate level, this decision might reduce the capital income share or result in a more equitable—or at least no more inequitable—distribution of capital income.

Such behavioral effects are not necessarily limited to the top of the income distribution. Depending on resource availability, low- and middle-class individuals might also alter their behavior in response to legislators that they view as more sympathetic to their interests. Left governments' rhetoric, which targets the middle and the working classes and emphasizes fairness, might inspire greater confidence in the less well-off. They might therefore be more willing to consider investing in assets and structures that they might otherwise view as unsafe. Such participation in capital markets can lead to lower income composition inequality by broadening access to capital income.

Lastly, the relationship between the Left and ICI might be dynamic in nature. The effect of the partisan composition of government might crystallize in the same year, or it might take some time to materialize. For example, if economic agents react immediately to the presence of a left-wing party in the governing coalition by liquidating capital

assets or withholding investment, ICI can change fairly quickly once a leftist party is elected to office. On the other hand, if the partisan make-up of the government affects compositional inequality through specific policy measures, ICI can register a decrease at a later stage, after reforms have taken effect. We explore these dynamics in greater detail in the appendix, where we introduce first, second, and third lags of our main IV of interest (Table A3).[51]

As a result, changes in the partisan composition of government can produce systematic variation in ICI. Specifically, a higher seat share for left-wing parties in the governing coalition should be associated with lower income composition inequality. The analysis below tests this expectation.

Empirical Strategy

Data and Measures   Our dependent variable is Ranaldi's *income-factor concentration index* (IFC).[52] The IFC index is a non-rank-based measure of the association between total income and a given income source. It is constructed through concentration curves for capital and labor income. If Π, W, and Y denote the capital, labor, and total income in an economy while Π_i, W_i, and Y_i denote the capital, labor, and total income of individual i $\forall i$, then

$$y_i = \frac{Y_i}{Y} = \alpha_i \pi + \beta_i w,$$

where $\alpha_i = \dfrac{\Pi_i}{\Pi}$ and $\beta_i = \dfrac{W_i}{W}$ are the *relative* shares of capital and labor income of individual i, such that $\sum_{i=1}^{n} \alpha_i = \sum_{i=1}^{n} \beta_i = 1$, whilst $\pi = \dfrac{\Pi}{Y}$ and $w = \dfrac{W}{Y}$ are the aggregate capital and the labor income shares. If individuals are indexed by their income ranking, $p = \dfrac{i}{n}$ is the proportion of the population with income less than or equal to y_p, and $\mathcal{L}(\mathrm{y}, p) = \sum_{j=1}^{i} y_j$, with $i = 1,\ldots,n$, is the Lorenz curve for income corresponding to the distribution y, the concentration curve for capital income $\mathcal{L}(\pi, p)$ corresponding to the distribution π can be defined as:

$$\mathcal{L}\left(\pi, p\right) = \pi \sum_{j=1}^{i} \alpha_j \quad \forall i = 1,\ldots,n.$$

Similarly, the concentration curve for labor $\mathcal{L}(\mathrm{w}, p)$ corresponding to the distribution **w** becomes:

$$\mathcal{L}\left(\mathrm{w}, p\right) = w \sum_{j=1}^{i} \beta_j \quad \forall i = 1,\ldots,n.$$

The area under these curves can be seen as a measure of income-factor concentration: the larger it is, the more concentrated at the bottom the income source is; conversely, the smaller the area, the more concentrated at the top labor or capital income is.

To measure ICI, we also need to define the zero- and maximum-concentration curves, which represent the benchmarks of minimum and maximum income composition inequality. The zero-concentration curve for capital income, $\mathcal{L}^e(\pi, p)$, is the Lorenz curve for total income multiplied by the capital share π. Defined as

$$\mathcal{L}^e(\pi, p) = \pi \sum_{j=1}^{i} y_j \quad \forall i = 1,\ldots,n$$

it describes a distribution of income sources where the composition of capital and labor income is the same for all individuals. The maximum-concentration curve for capital income, $\mathcal{L}^{max}(\pi, p)$, on the other hand, can adopt two shapes, depending on whether the concentration curve for capital income lies below or above the zero-concentration curve. In the former case, it becomes

$$\mathcal{L}^{max}(\pi, p) = \mathcal{L}^m(\pi, p) = \begin{cases} 0 & \text{for } p \leq p'' \\ \mathcal{L}(y, p) - z_- & \text{for } p > p'', \end{cases}$$

whilst in the latter case, it is

$$\mathcal{L}^{max}(\pi, p) = \mathcal{L}^M(\pi, p) = \begin{cases} \mathcal{L}(y, p) & \text{for } p \leq p' \\ z & \text{for } p > p', \end{cases}$$

with p' s.t. $\mathcal{L}(y, p') = \pi$, p'' s.t. $\mathcal{L}(y, p'') = 1 - \pi$. In (5), the maximum-concentration curve equals zero up to a given income percentile p'', and then takes the shape of the Lorenz curve. In (6), the maximum-concentration curve takes the shape of the Lorenz curve up to a given income percentile p', and then remains constant. The choice of percentiles p' and p'' depends on the capital share and the shape of the Lorenz curve.[53]

If the area between the zero-concentration curve and the concentration curve for capital income is $\mathcal{A}$ and the area between the zero-concentration curve and the appropriate maximum-concentration curve is $\mathcal{B}$, then the income-concentration index, $\mathcal{I}_f$, is:

$$\mathcal{I}_f = \frac{\mathcal{A}}{\mathcal{B}}.$$

The IFC index thus measures the association between total income and a given income source. A value of 1 indicates that capital income is concentrated at the top of the total income distribution, while labor income is concentrated at the bottom. A value of 0 suggests that all individuals have the same share of capital and labor income. Lastly, an IFC of -1 corresponds to a more difficult-to-imagine scenario in which the poor only get capital income while the wealthy only earn labor income. Contrary to

measures of inter-class inequality, which often account for the wealth or income share of specific social groups or focus on a single income source,[54] the IFC thus adopts a more holistic view. It considers all income groups (as opposed to the very poor, the very rich, or the middle class) and both income types. It does not make assumptions about the ownership structure of capital or wage assets, captures access to and reliance on both income sources, and traces the distribution of income composition across the entire income distribution.

We compute the IFC index using the European Union Statistics on Income and Living Conditions (EU-SILC) database. EU-SILC provides detailed information on different income categories for representative national samples of between 7,000 and 19,000 individuals. It covers thirty countries between 2003 and 2017 (Table A1b).[55] Originally collected by national statistical agencies through extensive surveys at both the individual and the household levels, EU-SILC data are harmonized and released by Eurostat, which ensures consistency across time and space. All income categories thus refer to the same concept for all country-years in our analysis. EU-SILC is among the highest-quality databases used for research on income inequality.

We define capital as interests, dividends, and profits from capital investments in unincorporated businesses (hy090g), income from property or land rentals (hy040g), and pensions received from individual private plans (py080g). Labor income covers gross employee cash or near cash income (py010g), company car (py021g), regular inter-household cash transfers received (hy080g), cash benefits or losses from self-employment (py050g), and government transfers.[56] We include transfers in labor income for three reasons. First, they allow us to meaningfully analyze the impact of state-sponsored redistribution on ICI. As Parolin and Gornick have recently shown, transfers powerfully shape inclusive growth in developed economies and provide a more complete picture of wellbeing.[57] Second, opting for a welfare concept that covers all sources of income helps us to identify the groups that truly benefit from capital income. Third, receipt of government benefits is often conditional on past employment, creating a strong link between individuals' work histories and access to the welfare state. Given that income definitions adopted by existing research vary considerably,[58] we consider this choice acceptable. In robustness checks (section O in the Appendix), we show that our results remain largely the same when we remove government transfers from our analysis. In line with previous studies,[59] we focus on income before taxes, as the net income categories reported by EU-SILC are not always available or precise.

We drop negative capital and labor income values and restrict our sample to the working-age population (18–65).[60] Consistent with existing research on ICI, we adopt the individual as the unit of analysis. This allows us to factor in important demographic characteristics, like the distribution of labor income among household members. We allocate household-level income, such as rent, to the individual level by equally splitting it across all members of the same household. To account for inter-household dynamics, which might affect labor decisions and access to capital, we work with the equalized "total household gross income" variable (hy010).

Figure 1 below shows the evolution of income composition inequality between 2005 and 2018 in the thirty economies in our sample. We notice considerable variation across time and space. The IFC index is generally positive, fluctuating between -0.25 and 0.8. It assumes particularly high values—around 0.6 and 0.8—in Czechia, Denmark, Estonia, Finland, Hungary, Lithuania, and Latvia. This implies that capital income tends to be more concentrated at the top of the income distribution, while labor income is generally prevalent at the bottom. In contrast, income composition inequality remains relatively low in Austria, Belgium, Germany, Croatia, Ireland, Italy, Slovakia, and the United Kingdom, suggesting a more equitable distribution of income sources. Temporally, the IFC index registers a noticeable increase after the Great Recession, confirming Balestra and Tonkin's finding that the economic crisis induced substantial wealth destruction among the lower and the middle classes.[61] Nevertheless, this trend is not universal, as income composition inequality declines in Malta and Slovakia in the 2010s.

Since the IFC index reflects dynamics in both capital and labor income, it might be difficult to trace which of the two is responsible for changes in overall income composition inequality. A falling IFC might be due to a more equitable distribution of either capital or labor income (or both). To gain greater analytical leverage, we use two additional dependent variables. MU_P and MU_W are the areas under the concentration curves for capital and labor income, respectively. To facilitate interpretation, we subtract them from 1. Higher values thus suggest that capital or labor income flows toward those at the top of the total income distribution. Analyzed together, the IFC index, MU_P, and

Figure 1   Income Composition Inequality in Europe (2003–2017)
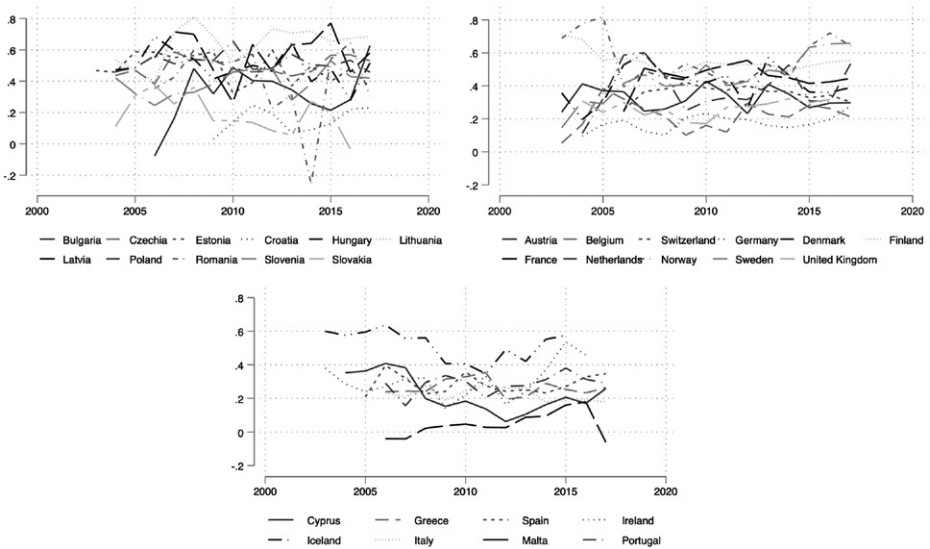
Own elaboration using EU-SILC data.

MU_W not only allow us to assess the distributional consequences of different variables, but also enable us to identify the precise channels through which income composition inequality changes.

Figure A2 in the Appendix reveals how MU_P and MU_W evolve over time. The larger area under the concentration curve for labor income indicates that a higher proportion of labor income goes to the middle and the lower classes. Capital income, on the other hand, is relatively more concentrated among the affluent. The short vertical distance between the two plots in Belgium, Croatia, Malta, Portugal, Slovakia, Spain, and the United Kingdom implies that capital income is more evenly distributed there, or that labor income inequality is high. While MU_P and MU_W both exhibit a degree of stability between 2005 and 2018, fluctuations are common. Strikingly, many of the economies in our analysis witness deepening capital income concentration among the rich in the aftermath of the Great Recession. In contrast, labor income appears to have changed less after 2010.

Our main independent variable captures patterns in the partisan composition of government. *Left parties* is the seat share of social democratic and other left parties in government as a percent of the total parliamentary seat share of all governing parties.[62] It reflects the relative power position of the Left within the ruling coalition. All entries follow Schmidt's party classification and draw on the widely used *European Journal of Political Research* and parliaments' and governments' databases.[63] A detailed list of all left-wing parties in our analysis is included in Section D in the Appendix.

Two additional variables consider other political dynamics. *Veto points*—an additive index of presidentialism, bicameralism, federalism, proportionalism, referenda, and judicial review—shed light on the ease with which policymakers can implement legislation that shapes the income distribution. Research has shown that multiple veto points promote policy drift by obstructing reform and forcing consensus-seeking.[64] *Electoral democracy* accounts for the presence of electoral competition, universal suffrage, a free civil society, clean elections, freedom of expression, and an independent media.[65] Because we are focusing on European countries in the twenty-first century, variation on this indicator is more limited, and we do not expect it to matter as much for income composition inequality.

Consistent with existing scholarship on income inequality, we control for a range of economic, social, and demographic factors. *GDP per capita growth* and *GDP per capita* capture the effect of economic growth and development. The *unemployment rate* accounts for the general health of the labor market. *Trade*, *foreign direct investment inflows*, and *capital account openness* reflect the impact of globalization. Finally, a dummy for the period after 2008 marks the *Great Recession*.

In robustness checks, we add *stock market capitalization*, which investigates if the development of the stock market democratizes access to capital, *industrial employment*, which explores the implications of deindustrialization, *female labor force participation*, which captures the incorporation of women into labor markets, and *tertiary educational attainment*, which considers the effect of higher education and the transition to the knowledge-based economy.[66] We also include the *capital income share* and *the labor*

income GINI coefficient. If capital income increases but remains highly concentrated, it is associated with rising income composition inequality. A less equitably distributed labor income can have a similar impact.[67] Lastly, *total social expenditures*, *the top tax rate*, *the corporate tax rate*, and an index of *financial deregulation* capture specific policy instruments governments have at their disposal to shape income inequality. These variables might introduce post-treatment bias, as they are likely endogenous to partisan dynamics. We look into them purely to evaluate the sensitivity of our results and the specific mechanisms that link politics to economic outcomes. Our findings in those models should therefore be interpreted with caution; we abstain from drawing definitive conclusions about their effect on ICI.

Method Cross-sectional time-series analysis poses several estimation challenges that make the standard application of Ordinary Least Square (OLS) regression inappropriate.[68] Pooled data produce temporally autoregressive and cross-sectionally correlated error terms, which result in biased and inconsistent parameter estimates.[69] To address this problem, we use two estimation techniques. First, Prais Winsten regressions (PWRs) allow us to focus on the factors that drive variation across both space and time. They account for temporal and spatial trends by combining panel-corrected standard errors with ar(1) corrections.[70] Second, fixed effects models (FEMs) zoom in on temporal variation within panels. The country dummies that they introduce control for all time-invariant differences across cases while allowing unobserved country characteristics to freely correlate with time-varying covariates.[71] We also add year dummies and an interaction term between our geographic and temporal identifiers to account for common shocks and additional time-variant country-specific dynamics. Estimating both sets of models—PWRs and FEMs—enables us to uncover the drivers of income composition inequality both over time and across European industrial democracies.

We expect these changes to be gradual, with causal impacts crystallizing over time. We therefore measure our dependent variable as a level.[72] To check the robustness of our findings, we run random effects models (Table A14), error correction models (Table A13), dynamic system-GMM models (Table A12), and detrended models (table A15). Our substantive findings remain largely unchanged.

Results Table 1 reports the results from our analysis of the determinants of income composition inequality. Models 1 through 3 are Prais Winsten regressions while Models 4 through 6 are fixed effects models. Models 1 and 4 explore the relationship between the IFC index and the partisan composition of government in a bivariate framework. Models 2 and 5 present the main specification.[73] Models 3 and 6 probe the robustness of our results by adding stock market capitalization, industrial employment, tertiary educational attainment, female labor force participation, the labor income GINI coefficient, and the capital income share.[74] All coefficients have been standardized to reflect one-standard-deviation changes.

Table 1 Determinants of Income Composition Inequality (Prais Winsten and Double Fixed Effects Models)

	PW 1 b/se	PW 2 b/se	PW 3 b/se	FEM 4 b/se	FEM 5 b/se	FEM 6 b/se
Left seats	-0.138***	-0.151***	-0.098*	-0.087***	-0.124***	-0.086**
	(0.05)	(0.05)	(0.05)	(0.03)	(0.04)	(0.04)
Veto points		-0.255***	-0.146**		0.496	-0.599
		(0.07)	(0.06)		(0.95)	(1.34)
Democracy		0.167	0.074		0.173	0.244*
		(0.13)	(0.14)		(0.16)	(0.14)
Union density		-0.077	-0.173***		0.713*	0.854**
		(0.07)	(0.07)		(0.39)	(0.37)
GDP per capita		-0.126	-0.313*		1.337***	0.671
		(0.15)	(0.18)		(0.46)	(0.44)
GDP growth		0.102**	0.096***		-0.028	-0.029
		(0.04)	(0.03)		(0.06)	(0.06)
Unemployment		-0.307***	-0.320***		0.01	-0.17
		(0.08)	(0.08)		(0.09)	(0.11)
Trade		-0.314***	-0.01		-0.407	0.22
		(0.07)	(0.07)		(0.36)	(0.34)
FDI inflows		-0.109***	-0.061**		-0.108**	-0.072*
		(0.03)	(0.03)		(0.05)	(0.04)
Capital account		-0.12	-0.065		-0.063	0.067
openness		(0.08)	(0.07)		(0.11)	(0.12)
Crisis		0.059	0.021		0.018	0.165
		(0.04)	(0.03)		(0.13)	(0.17)
Industrial			0.073			-0.45
employment			(0.11)			(0.30)
Educational			0.033			-0.497
attainment			(0.10)			(0.31)
Female labor force			0.433***			-0.423*
participation			(0.07)			(0.22)
Stock market			-0.066			-0.074
capitalization			(0.07)			(0.13)
GINI			0.019			0.031
			(0.08)			(0.12)
Capital income			0.454***			0.589***
			(0.06)			(0.07)
Constant	-0.006	-0.026	-0.015	-0.009	-0.086*	-0.028
	(0.04)	(0.03)	(0.03)	(0.02)	(0.05)	(0.06)
R-squared	0.017	0.18	0.388	0.052	0.172	0.399
N	415	274	265	415	274	265
Country FE	-	-	-	+	+	+
Year FE	-	-	-	+	+	+

*** $p < 0.01$, ** $p < 0.05$, *$p < 0.1$.

Consistent with the PRT, our main IV is negatively signed and statistically significant in all models. A higher seat share of *left parties* in the governing coalition is associated with lower income composition inequality. This effect is not negligible—a standard-deviation increase in left power translates into a two-point, or a 0.138/0.087 standard-deviation, decrease in the IFC index in Model 3. We can thus infer that leftist governments, whether intentionally or not, contribute to the transition to a multiple-sources-of-income society. This is despite the considerable constraints that national governments faced in the aftermath of the Great Recession and the European sovereign debt crisis.

Veto points also returns a statistically significant coefficient in the Prais Winsten regressions. Greater checks on the executive translate into lower income composition inequality. This suggests that reforms moving societies toward lower polarization between capital- and labor-income holders are easier in political systems with many invested players. Such systems might facilitate the representation of multiple interests, leading to policy action in different policy areas that ultimately obstructs concentration. Alternatively, the presence of different veto players can preclude legislation that contributes to ICI by only benefiting a very narrow part of the electorate.

Moving on to the economic variables, *GDP per capita* is linked to higher compositional inequality over time. Consistent with traditional models of economic growth and income inequality,[75] economic development might lead to a greater concentration of capital income. In contrast, higher *unemployment* is associated with lower ICI across space, as a greater number of jobless workers leads to more poor people with no labor income. Similarly, higher *FDI inflows* are connected to falling ICI. Existing scholarship has shown that capital movement and internal imbalances within the European Union have contributed to housing and constructions bubbles in the Southern periphery.[76] Regardless of its ultimate destination, foreign capital might have created economic conditions that raised dependence on rental and property income across the income distribution, as more people gained access to real estate. This could have resulted in a more equitable distribution of capital income.

The results so far suggest that governments could shape income composition inequality. The negative coefficient returned by left parties raises the question of how policymakers affect the degree of polarization between capital and labor income holders. To answer this question, we account for *total social expenditures*, *the corporate tax rate on distributed profits*, *the top marginal tax rate*, and *financial deregulation*. These variables reveal whether fiscal and financial policies matter for ICI. We acknowledge that they are likely endogenous to partisan dynamics, so we present models dropping the left parties' seat share variable in the Appendix.

Like before, the first four models in Table 2 are Prais Winsten regressions while the last four are fixed effects models.[77] Higher *top tax rates* and *distributed profits tax rates* are correlated with lower ICI across countries. Taxing dividends and top incomes could prevent accumulation at the top of the income distribution. The negative coefficient returned by *corporate taxes* in Model 7 suggests that taxing corporations might disincentivize capital ownership. In contrast, higher *social expenditure* is linked to rising ICI

Table 2 Government Policy and Income Composition Inequality (Prais Winsten and Double Fixed Effects Models, Full Specification)

	PW b/se	PW b/se	PW b/se	PW b/se	FEM b/se	FEM b/se	FEM b/se	FEM b/se
Left seats	-0.149*** (0.05)	-0.133** (0.05)	-0.132*** (0.05)	-0.145*** (0.05)	-0.143*** (0.04)	-0.132*** (0.05)	-0.118*** (0.04)	-0.113** (0.05)
Social expenditures	-0.079 (0.09)				0.531** (0.21)			
Top tax rate		-0.254** (0.12)				0.034 (0.13)		
Distributed profits tax rate			-0.298*** (0.10)				-0.289** (0.14)	
Financial reform				-0.028 (0.10)				-0.126 (0.12)
R-squared	0.185	0.202	0.209	0.162	0.194	0.148	0.167	0.150
N	274	239	239	230	274	239	239	230

*** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$.

over time, as benefits and transfers, which generally prioritize lower and middle-class citizens, induce a higher concentration of labor income at the bottom. *Marginal top tax rates* and *financial deregulation* return insignificant coefficients in the fixed effects models. It is important to note, however, that these two variables do not exhibit much variation over time and are not available for the post-communist economies in our sample. Our results do not change when we drop left-wing parties' seat share. Interestingly, our main IV retains its statistical significance, which indicates that partisan dynamics shape ICI through mechanisms not entirely pertaining to fiscal and financial sector policy.

How exactly do politics affect ICI? To further examine the precise way in which ICI changes, we explore the behavior of the areas under the concentration curves for capital and labor income. Looking into their determinants allows us to check whether left parties' seat share is associated with a more equitable distribution of capital or labor income across the total income distribution.[78]

Table 3 re-runs our models replacing ICI with MU_P and MU_W. The first two models focus on capital income while the second two look into labor income. We report standardized coefficients from Prais Winsten regressions and two-way fixed effects models. Capital income flows to the bottom of the income distribution under leftist governments. (A positive coefficient implies that a variable is linked to a more inequitable distribution of income.) This could happen because of policies that promote access to rental income among the non-rich, encourage participation in the stock market, or boost enrollment in private pension plans. In contrast, the partisan composition of government does not appear to matter for the distribution of labor income. This is in line with recent work that indicates that partisan differences have become less powerful at explaining welfare state developments.[79] While secular right governments provide favorable conditions for the concentration of income at the very top, left cabinets have struggled to constrain wage dispersion.

How exactly do left-wing parties shape the capital income distribution? To further explore this relationship, we calculate the proportion of respondents with positive capital income. We also look at the three components of capital income—dividends, rental income, and private pensions—separately. Tables A6 and A7 in the Appendix reveal that left-wing parties are associated with a higher proportion of individuals, especially among the bottom three quintiles, holding capital income, rental income, and capital gains. This suggests that the lower and the middle classes acquire more capital income when left parties are in power.

Conclusion

This article explores the determinants of income composition inequality in thirty European countries between 2003 and 2017. ICI sheds light on the nature of capitalist organization: low levels mean that individuals earn income from multiple sources, while high levels imply that different social classes rely on different types of income. We show that many post-industrial democracies have seen compositional inequality increase in recent

Table 3 Determinants of MU_P and MU_W (Prais Winsten and Double Fixed Effects Models, Full Specification)

	PW MU_P b/se	FEM MU_P b/se	PW MU_W b/se	FEM MU_W b/se
Left seats	-0.141**	-0.121***	0.007	0.027
	-0.05	-0.04	-0.03	-0.02
Veto points	-0.280***	0.341	-0.059	-0.273
	-0.07	-0.95	-0.06	-0.48
GDP per capita	-0.319**	0.996**	-0.817***	-0.797***
	-0.16	-0.46	-0.11	-0.23
GDP growth	0.103**	-0.019	0.011	0.01
	-0.04	-0.06	-0.02	-0.03
Unemployment	-0.260***	0.026	-0.047	-0.009
	-0.08	-0.09	-0.05	-0.05
Trade	-0.342***	-0.247	-0.043	0.122
	-0.08	-0.36	-0.1	-0.18
FDI inflows	-0.094***	-0.107**	0.023	0.008
	-0.03	-0.05	-0.02	-0.02
Capital account openness	-0.089	-0.059	0.057	-0.039
	-0.08	-0.11	-0.06	-0.05
Union density	-0.092	0.684*	-0.152**	0.205
	-0.08	-0.39	-0.07	-0.2
Democracy	0.199	0.164	0.170**	0.035
	-0.13	-0.16	-0.07	-0.08
Crisis	0.049	0.01	-0.011	0.032
	-0.04	-0.13	-0.03	-0.06
Constant	-0.039	-0.069	-0.018	0.016
	-0.04	-0.05	-0.04	-0.03
R-squared	0.177	0.144	0.248	0.239
N	274	274	274	274

years. This suggests that modern political and economic development continues to pit capital and labor against each other. Nevertheless, European countries have moved away from the early capitalist model of complete separation between capital and labor income holders. Indeed, the distance between rich capitalists and poor laborers has shrunk in the modern age.

Our results reveal that stronger left parties accelerate the transition to a multiple-sources-of-income economy. This occurs through two channels. First, left governments promote a more equitable distribution of capital income by broadening access to capital, especially among the poorest three quintiles. Absent policy action, normal economic dynamics exacerbate concentration trends. When left-wing parties are in office, however, capital income becomes less concentrated among the wealthy, either due to behavioral responses whereby the rich abstain from undertaking profitable investments if they perceive the government to be hostile to their interests, or because of specific

policy interventions that increase the participation of the poor in capital and real estate markets. Second, left-wing governments no longer seem as committed to boosting labor incomes at the bottom of the income distribution.

How substantial is this effect, though? How much room to maneuver do governments have at a time of deepening globalization and intensifying financialization? Recent work on advanced capitalist economies suggests that partisan differences have become less important in shaping distributional dynamics.[80] Our results imply that this is not necessarily the case. Instead, governments' choices might matter more for more complex forms of economic inequality that consider all income streams that citizens might have access to. In a context of permanent fiscal austerity, "There Is No Alternative" politics,[81] and stagnating wages, left-wing parties might have sought ways to assist their constituencies in unorthodox ways, turning to capital and real estate markets.[82] In this sense, even if social-democratic parties are less effective at reducing wage differentials, they might compensate poorer groups through action on the capital income front.

This raises questions about the types of economic redistribution and inequality alleviation that we might expect to see in the future. As Holland and Schneider have argued with respect to welfare states in Latin America, structural conditions, international shocks, and existing policy legacies make certain redistributive reforms "easy" and others "hard."[83] A focus on ICI, which accounts for both capital and labor income, sheds light on how governments might navigate these dynamics. While exacerbating fiscal constraints and heightening international integration might make generous social policies unfeasible, the development of financial and real estate markets might provide policymakers with additional channels to shape the income distribution. Future research should explore how the socio-economic cleavages and political coalitions that are currently emerging mold the policy choices that incumbents from different political stripes pursue.

Ultimately, our work shows that, although modern economies have moved away from the social realities and structures of the classical capitalism of the eighteenth and nineteenth centuries, present-day dynamics are not so different. They raise questions about the particular policy instruments that contemporary political actors can use to mitigate tensions and resolve the growing distance between the rich and the poor. More broadly, they shed light on the types of conflicts that might dominate the political arena in the coming years.

NOTES

1. Lucio Baccaro and Chris Howell, "A Common Neoliberal Trajectory: The Transformation of Industrial Relations in Advanced Capitalism," *Politics & Society*, 39 (2011), 521–63; Thomas Piketty, "Capital in the Twenty-First Century: A Multidimensional Approach to the History of Capital and Social Classes," The *British Journal of Sociology* 65, no. 4 (2014), 736–47; "Focus on Inequality and Growth," OECD (2014).

2. "Broken Social Elevator?: How to Promote Social Mobility,*"* Organisation for Economic Co-Operation and Development (2018); "Under Pressure: The Squeezed Middle Class," Organisation for Economic Co-Operation and Development (2019).

3. Rena Sung, Erica Owen, and Quan Li, "How Do Capital and Labor Split Economic Gains in an Age Of Globalization?," *Review of International Political Economy*, 28 (2021), 232–57.

4. Loukas Karabarbounis and Brent Neiman, "The Global Decline of the Labor Share," *The Quarterly Journal of Economics*, 129 (2014), 61–103. Karabarbounis and Neiman's work focuses on fifty-nine advanced and emerging economies. See Engelbert Stockhammer, *Wage-Led Growth: An Equitable Strategy for Economic Recovery* (London: Springer, 2013) and Tali Kristal, "Good Times, Bad Times: Postwar Labor's Share of National Income in Capitalist Democracies," *American Sociological Review*, 75 (2010), 729–63 for a discussion of the dynamics of the labor share in OECD countries.

5. Neil Fligstein and Taekjin Shin, "Shareholder Value and the Transformation of the US Economy, 1984–2000," *Sociological Forum*, 22 (2007), 399–424; Piketty.

6. Adam Goldstein and Ziyao Tian, "Financialization and Income Generation in the 21st Century: Rise of the Petit Rentier Class?," No. 801. LIS Working Paper Series (2020); Gabriela Inchauste and Jonathan Karver, "Understanding Changes in Equality in the EU," Background to "Growing United: Upgrading Europe's Convergence Machine," World Bank Report on the European Union (2018).

7. Branko Milanovic, *Capitalism, Alone: The Future of the System that Rules the World* (Cambridge: Harvard University Press, 2019).

8. Yonatan Berman and Branko Milanovic, "Homoploutia: Top Labor and Capital Incomes in the United States, 1950–2020," No. 806, *LIS Working Paper Series* (2020); Olivier Godechot, "Financialization and the Increase in Inequality," in Philip Mader, Daniel Mertens, and Natascha Van der Zwan, eds., The *Routledge International Handbook of Financialization* (Abington: Routledge, 2020), 413–24. Routledge, 2020.

9. Roberto Iacono and Marco Ranaldi, "The Evolution of Income Composition Inequality in Italy, 1989–2016," *Review of Income and Wealth*, 69 (2021), 124–49.

10. Goldstein and Tian.

11. Marco Ranaldi, "Income Composition Inequality," *Review of Income and Wealth*, 68 (2022), 139–60.

12. Milanovic, 2019; Marco Ranaldi and Branko Milanović, "Capitalist Systems and Income Inequality," *Journal of Comparative Economics*, 50 (2022), 20–32.

13. Walter Korpi, *The Democratic Class Struggle* (London: Routledge, 2018); John D. Stephens, *The Transition from Capitalism to Socialism* (London: Palgrave Macmillan, 1979); Evelyne Huber and John D. Stephens, *Development and Crisis of the Welfare State: Parties and Policies in Global Markets* (Chicago: University of Chicago Press, 2001).

14. Silja Häusermann, Georg Picot, and Dominik Geering, "Rethinking Party Politics and the Welfare State–Recent Advances in the Literature," *British Journal of Political Science*, 43 (2013), 221–40.

15. "European Union Statistics on Income and Living Conditions (EU-SILC)," Eurostat Statistical Database (2017).

16. Anthony Atkinson and François Bourguignon, "Introduction: Income Distribution and Economics," in Anthony Atkinson and François Bourguignon, eds., *Handbook of Income Distribution* (Oxford: Elsevier 2000), 1–58; Anthony Atkinson and Christoph Lakner, "Capital and Labor: The Factor Income Composition of Top Incomes in the United States, 1962–2006," *Review of Economics and Statistics*, 103 (2021), 892–904; Anthony Atkinson, "Factor Shares: The Principal Problem of Political Economy?," *Oxford Review of Economic Policy*, 25 (2009), 3–16; Ranaldi.

17. We assume the population's capital and labor income shares equal 20 percent and 80 percent, respectively.

18. Capital income can often be seen as a return to wealth and assets.

19. Milanovic, 2019; Branko Milanovic, "Increasing Capital Income Share and Its Effect on Personal Income Inequality," No. 663, LIS Working Paper Series (2016).

20. As Ansell (2014 and 2019) and Ansell and Adler have shown, for example, homeownership and rising housing prices, which affect rental income, shape voting choices and attitudes toward the welfare state. Ben Ansell, "The Political Economy of Ownership: Housing Markets and the Welfare State," *American Political Science Review*, 108 (2014), 383–402; Ben Ansell, "The Politics of Housing," *Annual Review of Political Science*, 22 (2019), 165–85; David Adler and Ben Ansell, "Housing and Populism," *West European Politics*, 43 (2020), 344–65.

21. Iacono and Ranaldi.

22. Roberto Iacono and Elisa Palagi, "Still the Lands of Equality? Heterogeneity of Income Composition in the Nordics, 1975–2016," *The B.E. Journal of Economic Analysis & Policy*, 22 (2022), 221–68.

23. Andrea Brandolini, "Nonlinear Dynamics, Entitlement Rules and the Cyclical Behaviour of the Personal Income Distribution," No. dp0084. Centre for Economic Performance, LSE (1992).

24. Erik Bengtsson and Daniel Waldenström, "Capital Shares and Income Inequality: Evidence from the Long Run," *The Journal of Economic History*, 78 (2018), 712–43.

25. Sung et al.

26. Engelbert Stockhammer, "Why Have Wage Shares Fallen? An Analysis of the Determinants of Functional Income Distribution," in Engelbert Stockhammer, ed, *Wage-Led Growth: An Equitable Strategy for Economic Recovery* (London: Springer, 2013), 40–70. Kristal; Petra Dunhaupt, "Determinants of Functional Income Distribution: Theory and Empirical Evidence," Global Labor University Working Paper no. 18. Geneva: International Labour Office (2013).

27. Olivier Blanchard and Francesco Giavazzi, "Macroeconomic Effects of Regulation and Deregulation in Goods and Labor Markets," *The Quarterly Journal of Economics*, 118 (2003), 879–907.

28. Simcha Barkai, "Declining Labor and Capital Shares," *The Journal of Finance*, 75 (2020), 2421–63.

29. Jan De Loecker and Jan Eeckhout, "Global Market Power," National Bureau of Economic Research No. w24768 (2018).

30. David Autor, David Dorn, Lawrence Katz, Christina Patterson, and John Van Reenen, "The Fall of the Labor Share and the Rise of Superstar Firms," *The Quarterly Journal of Economics*, 135 (2020), 645–709.

31. Thomas Philippon, *The Great Reversal: How America Gave Up on Free Markets* (Cambridge: Harvard University Press, 2019).

32. Jacob Hacker and Paul Pierson, *Winner-Take-All Politics: How Washington Made the Rich Richer—And Turned Its Back on the Middle Class* (New York: Simon and Schuster, 2010).

33. Bengtsson and Waldenström; Anastasia Guscina, "Effects of Globalization on Labor's Share in National Income" (2007), available at SSRN 956758; Rudy Fichtenbaum, "Do Unions Affect Labor's Share of Income: Evidence Using Panel Data," *American Journal of Economics and Sociology*, 70 (2011), 784–810.

34. Hilary Appel and Mitchell Orenstein, "Why Did Neoliberalism Triumph and Endure in the Post-Communist World?," *Comparative Politics*, 48 (April 2016), 313–31; Layna Mosley, *Global Capital and National Governments* (Cambridge: Cambridge University Press, 2003); Daniela Campello, "The Politics of Financial Booms and Crises: Evidence from Latin America," *Comparative Political Studies*, 47 (2014), 260–86; Charles Lindblom, *Politics and Markets* (New York: Basic Books, 1977); Kristal; Arjun Jayadev, "Capital Account Openness and the Labour Share of Income," *Cambridge Journal of Economics*, 31 (2007), 423–43; Stockhammer.

35. Ken-Hou Lin and Donald Tomaskovic-Devey, "Financialization and US Income Inequality, 1970–2008," *American Journal of Sociology*, 118 (2013), 1284–329; Evelyne Huber, Bilyana Petrova, and John D. Stephens, "Financialization, Labor Market Institutions and Inequality," *Review of International Political Economy*, 29 (2022), 425–52.

36. Fligstein and Shin; Lin and Tomaskovic-Devey; Godechot; Petra Dünhaupt, "An Empirical Assessment of the Contribution of Financialization and Corporate Governance to the Rise in Income Inequality," IPE Working Papers 41/2014 (Berlin School of Economics and Law Institute for International Political Economy (IPE)).

37. Geoffrey Garrett, "Global Markets and National Politics: Collision Course or Virtuous Circle?," *International Organization*, 52 (1998), 787–824; Huber and Stephens.

38. Eric Keller and Nathan J. Kelly, "Partisan Politics, Financial Deregulation, and the New Gilded Age," *Political Research Quarterly*, 68 (2015), 428–42; Swen Hutter and Hanspeter Kriesi, "Politicizing Europe in Times of Crisis," in Jonathan Zeitlin and Francesco Nicoli, eds., *The European Union Beyond the Polycrisis*? (New York: Routledge, 2020), 34–55; Pablo Beramendi, Silja Häusermann, Herbert Kitschelt, and Hanspeter Kriesi, eds., *The Politics of Advanced Capitalism* (Cambridge: Cambridge University Press, 2015); Alexander Horn, "The Asymmetric Long-Term Electoral Consequences of Unpopular Reforms: Why Retrenchment Really Is a Losing Game for Left Parties," *Journal of European Public Policy*, 28 (2021), 1494–517; Johannes Karreth, Jonathan T. Polk, and Christopher S. Allen, "Catchall or Catch and Release? The Electoral Consequences of Social Democratic Parties' March to the Middle in Western Europe," *Comparative Political Studies*, 46 (2013), 791–822; Karl Loxbo, Jonas Hinnfors, Magnus Hagevi, Sofie Blombäck, and Marie Demker. "The Decline of Western European Social Democracy: Exploring the Transformed Link between Welfare State Generosity and the Electoral Strength of Social Democratic Parties, 1975–2014," *Party Politics*, 27 (2021), 430–41.

39. Appel and Orenstein; Sheri Berman and Maria Snegovaya, "Populism and the Decline of Social Democracy," *Journal of Democracy*, 30 (2019), 5–19.

40. Arvid Lindh and Leslie McCall, "Class Position and Political Opinion in Rich Democracies," *Annual Review of Sociology*, 46 (2020), 419–41. In line with Armingeon et al. (2023), when we talk about left-wing parties, we refer to Social Democratic parties and political formations to the left of social democrats. This denomination thus includes Socialist, Communist, and Green parties. While Green parties have mainly focused on environmental issues, they typically share a commitment to social justice. In some countries, such as in Germany and the UK, their platforms highlight taxation and redistribution. In any case, these formations rarely take part in governing coalitions, and, when they do, they are typically junior partners. Klaus Armingeon, Sarah Engler, Lucas Leemann, and David Weisstanner, *Comparative Political Data Set 1960–2021* (University of Zurich, Leuphana University Lueneburg, and University of Lucerne, 2023).

41. Tarik Abou-Chadi and Markus Wagner, "The Electoral Appeal of Party Strategies in Postindustrial Societies: When Can the Mainstream Left Succeed?," *The Journal of Politics*, 81 (2019), 1405–19; Beramendi et al.; Jane Gingrich and Silja Häusermann, "The Decline of the Working-Class Vote, the Reconfiguration of the Welfare Support Coalition and Consequences for the Welfare State," *Journal of European Social Policy*, 25 (2015), 50–75; Herbert Kitschelt, *The Transformation of European Social Democracy* (Cambridge: Cambridge University Press, 1994); Amory Gethin, Clara Martínez-Toledano, and Thomas Piketty, "Brahmin Left Versus Merchant Right: Changing Political Cleavages in 21 Western Democracies, 1948–2020," *The Quarterly Journal of Economics*, 137 (2022), 1–48.

42. Korpi; Stephens.

43. Evelyne Huber and John D. Stephens, *Democracy and the Left: Social Policy and Inequality in Latin America* (Chicago: University of Chicago Press, 2012).

44. Nathan Kelly, *The Politics of Income Inequality in the United States* (Cambridge University Press, 2009); Jana Morgan and Nathan Kelly, "Market Inequality and Redistribution in Latin America and the Caribbean," *The Journal of Politics*, 75 (2013), 672–85; Raghuram G. Rajan, *Fault Lines* (Princeton University Press, 2011).

45. Beramendi et al.

46. Andreas Fagereng, Luigi Guiso, Davide Malacrino, and Luigi Pistaferri, "Heterogeneity and Persistence in Returns to Wealth," *Econometrica*, 88 (2020), 115–70.

47. Garrett; Scott Basinger and Mark Hallerberg, "Remodeling the Competition for Capital: How Domestic Politics Erases the Race to the Bottom," *American Political Science Review*, 98 (2004), 261–76; Carla Inclan, Dennis P. Quinn, and Robert Y. Shapiro, "Origins and Consequences of Changes in US Corporate Taxation, 1981–1998," *American Journal of Political Science* (2001), 179–201.

48. https://www.sueddeutsche.de/politik/grosse-koalition-spitzensteuersatz-und-durchstecherei-entzweien-union-undspd-1.3817888.

49. Huber and Stephens, 2021.

50. Armingeon et al., 2023.

51. Supplementary materials are available at https://bilyanapetrovacom.files.wordpress.com/2024/01/petrova-ranaldi-appendix.pdf

52. Ranaldi.

53. For further details on the choice of the two percentiles, please see the related methodological paper (Ranaldi).

54. Christian Houle, "Why Class Inequality Breeds Coups but Not Civil Wars," *Journal of Peace Research*, 53 (2016), 680–95; Fernando Alvaredo, Anthony Atkinson, Thomas Piketty, and Emmanuel Saez, "The Top 1 Percent in International and Historical Perspective," *Journal of Economic Perspectives*, 27 (2013), 3–20.

55. This temporal scope unfortunately prevents us from looking into the evolution and drivers of ICI during the 1990s and the early 2000s. We hope that the expansion of the Luxembourg Income Study (LIS) will allow such analyses in the future.

56. Unemployment (py090g), old-age (py100g), survivor's (py110g), sickness (py120g) and disability benefits (py130g), social exclusion not elsewhere classified (hy060g), and education-related (py140g) and family/children-related allowances (hy050g).

57. Zachary Parolin and Janet C. Gornick, "Pathways toward Inclusive Income Growth: A Comparative Decomposition of National Growth Profiles," *American Sociological Review*, 86 (2021), 1131–63.

58. United Nations Development Programme, 2019.

59. Ranaldi.

60. Our results remain largely the same when we focus on the entire population.

61. This reduced these sectors' capital income—or return to wealth—in subsequent years. Carlotta Balestra and Richard Tonkin, "Inequalities in Household Wealth Across OECD Countries: Evidence from the OECD Wealth Distribution Database," OECD Statistics Working Papers, No. 2018/01 (Paris: OECD, 2018).

62. Armingeon et al., 2023.

63. Manfred Schmidt, "When Parties Matter: A Review of the Possibilities and Limits of Partisan Influence on Public Policy," *European Journal of Political Research*, 30 (1996), 155–83.

64. Ellen Immergut, *Health Politics: Interests and Institutions in Western Europe* (CUP Archive, 1992); Peter Enns, Nathan Kelly, Jana Morgan, Thomas Volscho, and Christopher Witko, "Conditional Status Quo Bias and Top Income Shares: How US Political Institutions Have Benefited the Rich," *The Journal of Politics*, 76 (2014), 289–303.

65. Coppedge et al., "The Methodology of "Varieties of Democracy" (V-Dem)," *Bulletin of Sociological Methodology/Bulletin de Méthodologie Sociologique*, 143 (2019), 107–33.

66. This variable is highly correlated—at 0.70—with the proportion of the labor force in knowledge-intensive services. It can thus be seen as a proxy for the changing economic structure of advanced capitalist democracies.

67. The last two variables are highly correlated, so their inclusion in the same model is problematic. Our substantive findings do not change if we add them separately.

68. Alexander Hicks, "Introduction to Pooling," in Thomas Janoski and Alexander Hicks, *The Comparative Political Economy of the Welfare State* (Cambridge: Cambridge University Press, 1994), 169–88.

69. Evelyne Huber, Jingjing Huo, and John D. Stephens, "Power, Policy, and Top Income Shares," *Socio-Economic Review*, 17 (2019), 231–53.

70. Nathaniel Beck and Jonathan Katz, "What to Do (and Not to Do) with Time-Series Cross-Section Data," *American Political Science Review*, 89 (1995), 634–47; Nathaniel Beck and Jonathan Katz, "Modeling Dynamics in Time-Series–Cross-Section Political Economy Data," *Annual Review of Political Science*, 14 (2011), 331–52.

71. Kenneth Bollen and Jennie Brand, "A General Panel Model with Random and Fixed Effects: A Structural Equations Approach," *Social Forces*, 89 (2010), 1–34

72. Paul Pierson, "Not Just What, but When: Timing and Sequence in Political Processes," *Studies in American Political Development*, 14 (2000), 72–92.

73. Our sample size decreases considerably once we include all of our controls. This decrease is mainly driven by *union density*. The appendix shows that our results are robust when we impute this variable (Table A10).

74. We acknowledge that these additional controls are likely to be endogenous to the left party seat share.

75. Alberto Alesina and Dani Rodrik, "Distributive Politics and Economic Growth," *The Quarterly Journal of Economics*, 109 (1994), 465–90.

76. Wade Jacoby, "Surplus Germany," *German Politics*, 29 (2020), 498–521.

77. They are run against the full specification, but we only show the relevant coefficients to save space. The full output is in Table A5 of the Appendix.

78. The denominator of the IFC index does not explain much of its overall variation (Ranaldi).

79. Huber and Stephens, 2001.

80. Enns et al.; Huber and Stephens, 2001; Hacker and Pierson; Helmut Herwartz and Bernd Theilen, "Partisan Influence on Social Spending under Market Integration, Fiscal Pressure and Institutional Change," *European Journal of Political Economy*, 34 (2014), 409–24.

81. Paul Pierson, "Coping with Permanent Austerity: Welfare State Restructuring in Affluent Democracies," *Revue Française de Sociologie* (2002), 369–406.

82. Rajan.

83. Alisha Holland and Ben Ross Schneider, "Easy and Hard Redistribution: The Political Economy of Welfare States in Latin America," *Perspectives on Politics*, 15 (2017), 988–1006.