



# The Social and Economic Impact of Rising Income Inequality

Income inequality is changing global demand for goods and services

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## KEY INSIGHTS

- Income inequality is one of the defining socioeconomic issues of our time, with far-reaching and disruptive impacts globally.
- Widening income disparity has major implications for investors: hurting growth, denying investment opportunity, and fostering populism and social divisions.
- Pressure on governments to provide wider access to affordable goods and services will ultimately drive policy change and create investment opportunities.

Income inequality is one of the defining socioeconomic issues of our time. Although levels of inequality vary considerably across the globe, the Gini coefficient, which measures income distribution and inequality, suggests that the average person has lived in a country where income disparities are widening. If this continues, it will likely lead to increased indebtedness, steeper yield curves, inflation, higher corporate taxes, and tighter trade restrictions. It will also create sectoral opportunities as consumption patterns change and the demand for cheaper goods and services grows.

There are several drivers of widening income inequality. One is that the redistributive effect of taxes and transfers has decreased as rules for claiming benefits have been tightened and tax rates on the richest 1% have fallen. Another is that many industries are becoming more concentrated,

consolidating economic power within a smaller number of firms.

Changes in labor markets, including the automation of low-skilled jobs and the rise of part-time and short-term work, have also helped to drive income inequality. In advanced economies, this has been further entrenched by the outsourcing of manufacturing to countries where wages are lower.

## Wage Disparities Fuel Populism

Income inequality has significant implications for investors. It hurts growth: The International Monetary Fund finds that making the rich richer by one percentage point lowers a country's gross domestic product (GDP) growth over the next five years by 0.08 of a percentage point, whereas making the poor and middle class richer by one percentage point can raise GDP growth by 0.38 of a percentage point. Income inequality also creates inequality of opportunity by denying people with



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lower incomes the opportunity to invest in their health and education.

Disparities in income give rise to struggles over government resources. This creates political volatility, which, in turn, can fuel the rise of populist causes and deepen social divisions. Support for closed economies has grown among blue-collar workers in developed countries who feel—with some justification—that they have not benefited from globalization, while the independence of central banks is under threat as the investment-friendly environment they have sought to create has not benefited everyone.

Political volatility typically leads to higher public spending as both right- and left-wing populists demand greater social mobility and equality. This typically results in greater indebtedness, steeper yield curves, and more accommodative monetary policies, raising inflation expectations. Inequality

has led to hostility to trade, with the result that multinational corporations are likely to face increased regulation and more stringent taxation.

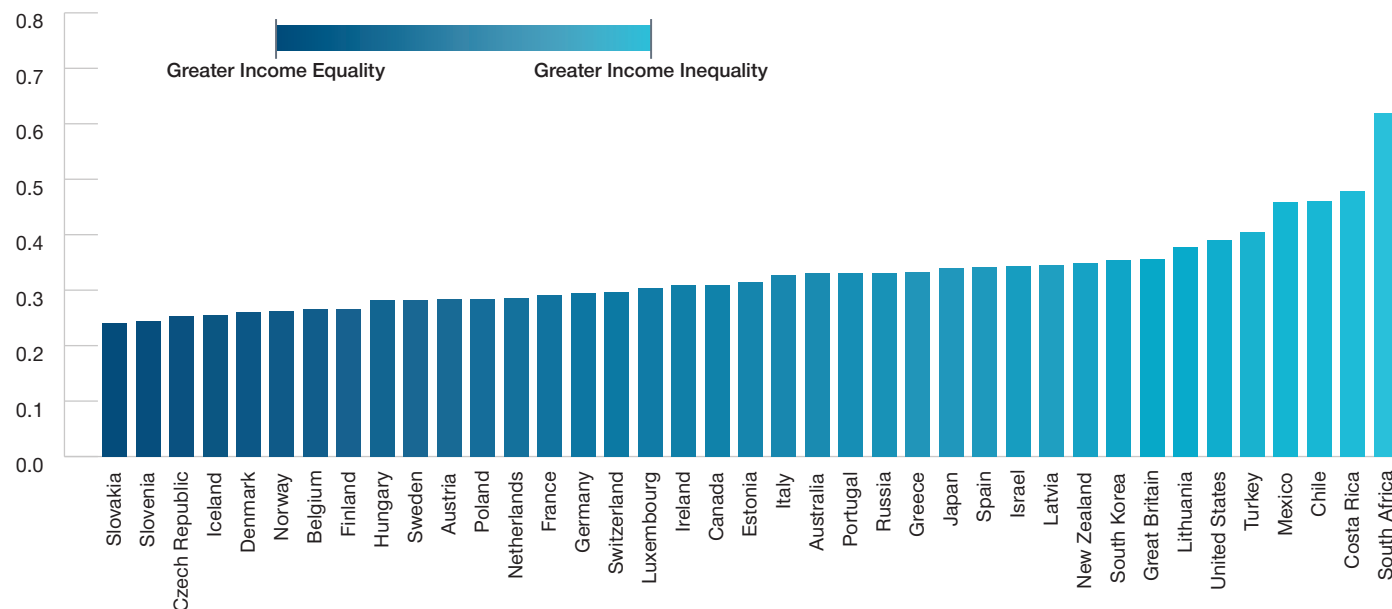
### Changing Consumption Will Create Sectoral Opportunities

Increasing income inequality is likely to negatively impact luxury goods manufacturers, but it will create opportunities in other areas. If the potential for social mobility and employment opportunities becomes more limited, for example, we believe the demand for affordable leisure will increase, leading to innovations in the tourism and leisure industries. At the same time, the high cost of accommodation in growing urban areas will provide opportunities for companies that provide solutions.

As learning will be the most likely path to higher earnings for most low-income people, we believe there will be a huge

## The Gini Coefficient

Measuring national income inequality



As of December 31, 2019.

Source: Organisation for Economic Co-operation and Development (OECD), income inequality data.

The Gini coefficient is a measure of income inequality that condenses overall income distribution for a country into a single number between 0 and 1: The higher the number, the greater the degree of income inequality. Data used are from 2019 or the latest available. South Africa has the highest net Gini score, and the U.S. has the highest for an advanced economy.

market for companies providing high-quality but affordable education, such as the Curro independent school network in South Africa. Similarly, innovative health care providers will likely find major opportunities arising.

In emerging market countries, increasing numbers of people are seeking access to financial services, creating opportunities for companies that use technology to help low-income customers better manage their finances. Tinkoff Bank in Russia and the Kenyan mobile-based money transfer company M-Pesa are early examples of this.

### **How Income Inequality Influences Our Investment Decisions**

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#### **WHAT WE'RE WATCHING NEXT**

Policy changes will occur as governments continue to respond to demands for wider access to affordable goods and services. As corporations respond to these changes, sector-based opportunities will continue to arise. We will continue to monitor income inequality around the world and incorporate it into our analysis in striving to maximize investment performance for our clients.

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