Flash Economics

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The differences between the US and euro zone economies: it's all about income distribution

From the first quarter of 1999 to the second quarter of 2025, real wages rose by:

- 42% of the increase in labour productivity in the United States;
- 88% of the increase in labour productivity in the euro zone.

This major difference in income distribution helps explain:

- The much higher profitability and return on equity in the United States than in the euro zone;
- The ability of US companies to spend more on R&D and technological investment than European companies;
- The gap between household savings rates in the US and the euro zone;
- Greater income inequality and poverty in the United States than in the euro zone.

Patrick Artus
Senior Economic Advisor
patrick.artus-ext@ossiam.com
@PatrickArtus
Patrick Artus

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A big difference in income distribution between the US and the euro zone

Charts 1A and 1B show that income distribution is much more favourable to companies (unfavourable to employees) in the US than in the euro zone.

Chart 1A
United States : Real compensation per hour and productivity per hour (business sector, 1999.Q1 = 100)

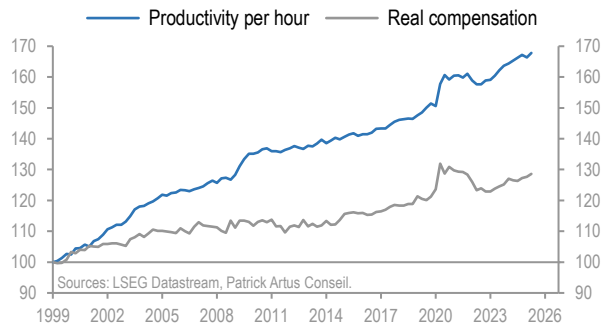
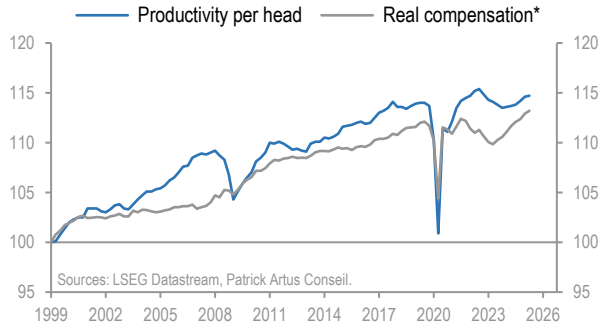


Chart 1B
Euro zone: Real compensation and productivity per head (1999.Q1 = 100)



* Deflated by GDP deflator

Since 1999:

- 42% of the rise in labour productivity has been transformed into a rise in real wages in the United States;
- 88% of the rise in labour productivity has led to a rise in real wages in the euro zone.

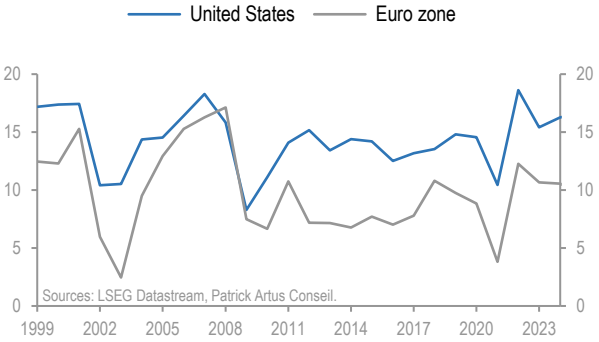
This sizeable difference in wage-setting behaviour (in the income distribution) explains most of the differences between the United States and the euro zone.

Four major differences between the United States and the euro zone that can be explained by the difference in income distributions

1. Higher corporate profitability in the United States

Return on equity (Chart 2) is significantly higher in the United States than in the euro zone, which is a normal consequence of the fact that wages in the United States grow only as a small fraction of productivity gains.

Chart 2
RoE



2. Companies' ability to finance R&D expenditure or investment in new technologies is stronger in the United States

The fact that American companies are more profitable than European companies allows them **to spend more on R&D** than European companies (**Chart 3**) **and to invest more in new technologies** (**Chart 4**).

Chart 3
Total R&D spending (as % of nominal GDP)

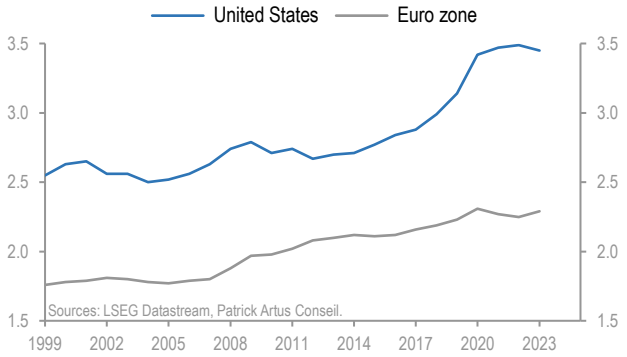
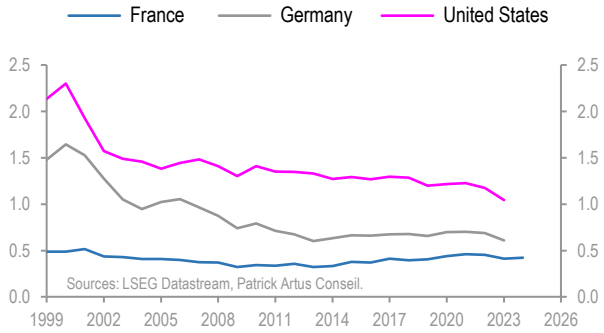


Chart 4
ICT investment (in value terms, as % of nominal GDP)



3. Much lower household savings rate in the US than in the euro zone

The low rate of increase in US households' wage income relative to productivity gains (**Charts 1A/B and 5A/B**), due to the fact that they receive only a small share of these gains, means that they have to support their consumption by saving little, hence the **much lower household savings rate in the US than in the euro zone** (**Chart 6**).

Chart 5A
Etats-Unis : Median usual weekly real earnings
(CPI ajudsted dollars, 1999.Q1 = 100)



Chart 5B
Real compensation (1999.Q1 = 100)

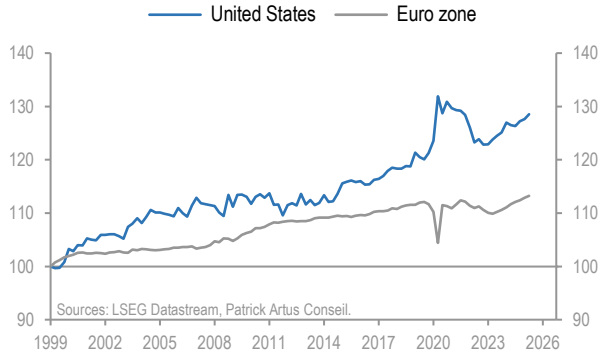
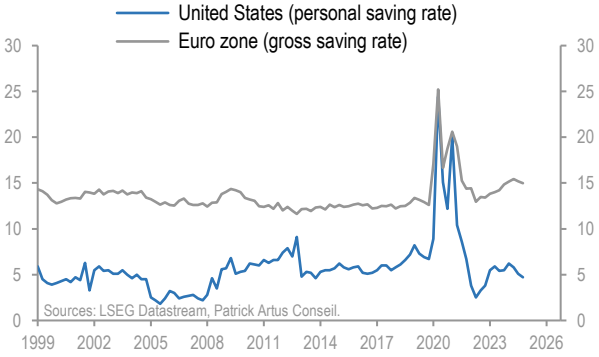


Chart 6
Household savings rate (as %)



4. Income inequality and poverty are higher in the US than in the euro zone

The low share of households in total income unsurprisingly means that **income inequality** (**Charts 7A/B**) **and poverty** (**Chart 8**) are much higher in the US than in the euro zone.

However, income inequality before redistribution has been amplified in the euro zone by the high level of unemployment, especially in the 2010s.

Chart 7A
Gini index of income inequality (before redistribution)

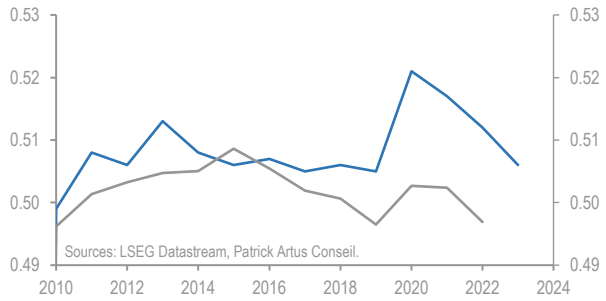


Chart 7A
Gini index of income inequality (before redistribution)

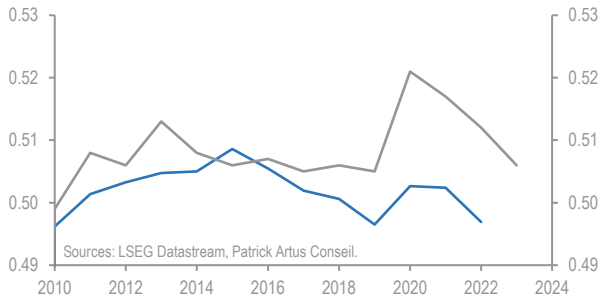
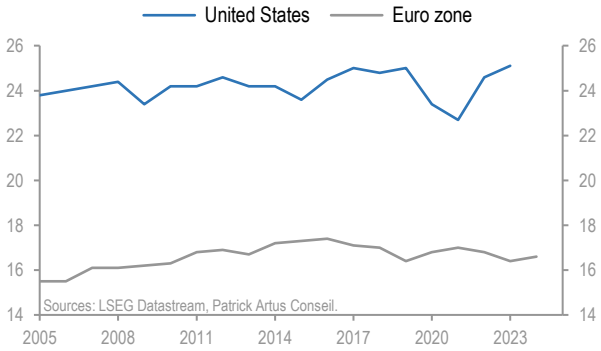


Chart 8
Poverty rate*

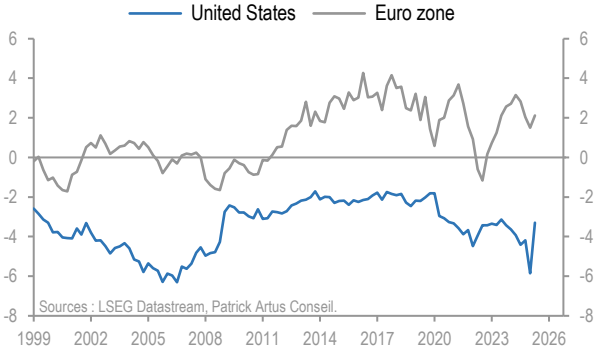


(*) Poverty rate based on disposable income, 60% of the national median disposable income

Summary: advantages and drawbacks of unequal income distribution

Income distribution benefits profits at the expense of wages more so in the United States than in the euro zone. This has favourable consequences for the US economy, in particular the strong capacity of companies to spend on research and development and to invest in new technologies. But it also has unfavourable consequences: a low household savings rate to support consumption, leading to a very large external deficit (**Chart 9**), and high inequality and poverty.

Chart 9
Current account balance (as % of nominal GDP)



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