

# **EQUIVALENCE SCALES DECLINING WITH EXPENDITURE: EVIDENCE AND IMPLICATIONS FOR INCOME DISTRIBUTION\***

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July, 2011

## **ABSTRACT**

We estimate expenditure dependent equivalence scales and equivalent expenditure functions for Italian households: couples with and without children. Following Donaldson and Pendakur (2006) we incorporate generalized absolute equivalence-scale exactness (GAESE) restrictions for scale identification into a translated quadratic almost ideal (TQAI) demand system. We obtain equivalence scales declining with expenditure. This implies that scale economies in current consumption are lower for families with poor expenditure capacities. If the number of children increases, this pattern tends to become strong. The strength and the direction of scales' dependence on expenditure varies with the presence and the number of children, and with the working condition of the household members.

We also show that families living in the South and Islands suffer a substantial additional cost to achieve, *ceteris paribus*, the same level of well-being of those living in the North.

Finally, we find that ignoring the declining with expenditure pattern results in a relevant underestimation of measured inequality in Italy.

**JEL codes:** D11; D12

**Key Words:** Equivalent Expenditure Functions; Equivalence Scales; Demand Analysis

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