

Understanding inequality and what to do about it

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Three issues that need to be addressed, ...

- 1 **Description**
just what has happened to inequality in Canada, and in other countries?
just what has happened to the share of incomes going to the top 1%?
- 2 **Explanation**
why has this happened?
 - what explains rising incomes at the top?
 - what explains stagnant and declining incomes at the bottom?
- 3 **Prescription**
what policies should be put forward to address these developments?

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in search of intelligent conversation, ...

In the recent Ontario provincial budget the minority Liberal government adopted an NDP proposal to raise the marginal tax rate on those earning more than \$500,000 by about 2 to 3 percentage points.

Should we increase taxes on the rich? (Click here to find out!)

... in order to accomplish something constructive.

Perhaps a bit more politely than others in the mainstream media, but nonetheless pretty emphatically, the Ottawa Citizen columnist Joanne Chianello told Occupiers last November that it's time to leave, and she offers some advice:

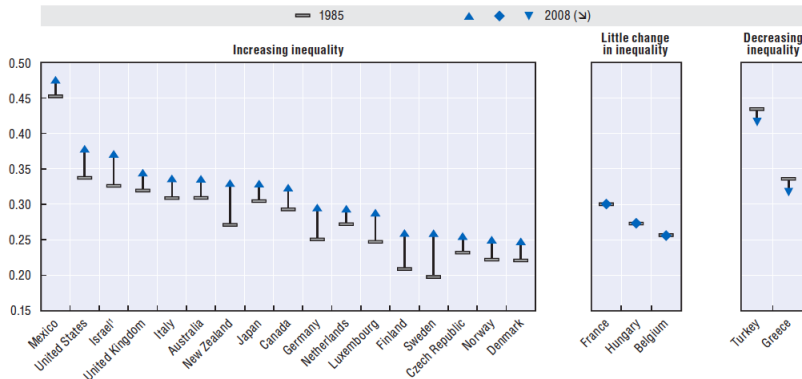
"I don't know what the answer is to the growing income gap. Unfortunately, neither do the people at Occupy Ottawa or Occupy Toronto or Occupy Vancouver. They could have contacted a lefty economist (yes, they exist) to help frame specific policy issues or demands, but they didn't. Perhaps that's the protest's "stage two" we keep hearing about." (Ottawa Citizen, November 21, 2012)

Contact a lefty economist!

Inequality has been rising in most countries, ...

Figure 1. **Income inequality increased in most, but not all OECD countries**

Gini coefficients of income inequality, mid-1980s and late 2000s

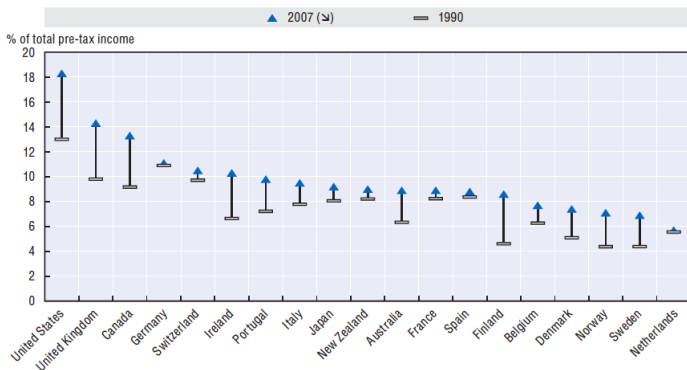


Source: OECD (2011) *Divided We Stand: Why Inequality Keeps Rising*, page 24.

... in part because top incomes have increased

Figure 12. **The share of top incomes increased, especially in English-speaking countries**

Shares of top 1% incomes in total pre-tax incomes, 1990-2007 (or closest year)



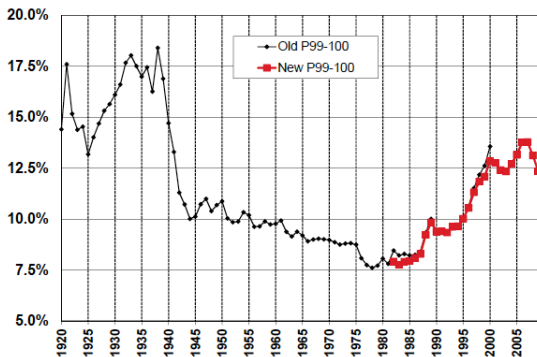
Source: OECD (2011) *Divided We Stand: Why Inequality Keeps Rising*, page 39.

The average income in the top 1% is \$453,000

- to be in the top 1% in Canada (in 2006) required \$230,000
- those with at least this much income had on average \$453,000, and about 52% of them worked more than 50 hours per week on average
- the average income of the population (15 years and older) was \$36,800, with 19% working more than 50 hours per week

Changes in top shares have been ongoing for 30 years reversing a trend during the post-war period

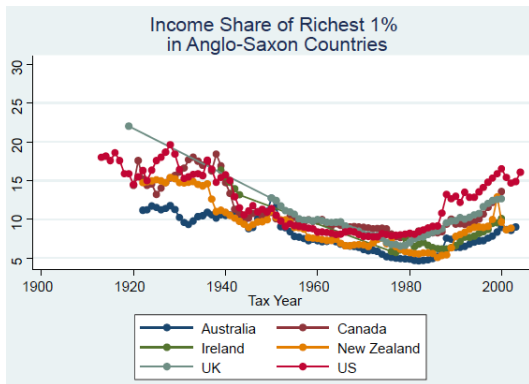
Fig. 1 Top 1% (P99-100) income shares, 1920 - 2009



Source: Mike Veall (2012), presentation to the University of Ottawa

But not entirely in the same way in all countries

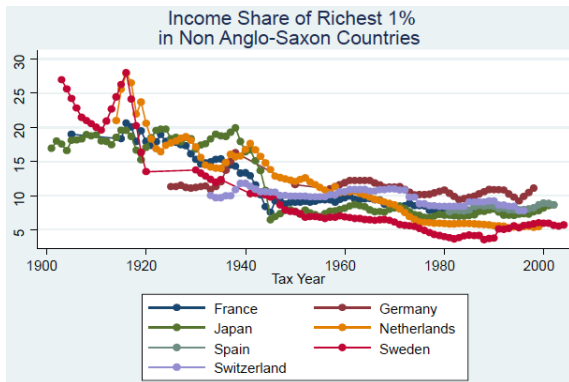
top income shares have risen in "anglophone" countries



Source: Mike Veall (2012), presentation to the University of Ottawa

But not entirely in the same way in all countries

top income shares have not risen in “non-anglophone” countries



Source: Mike Veall (2012), presentation to the University of Ottawa

Three facts to take away

- 1 Rising inequality is a global phenomenon that has occurred in all rich countries ...
- 2 but not in the same way, top shares have been rising only in some countries.
- 3 Patterns in top incomes are wrapped up with events in the United States, but we need a broader explanation for inequality as a whole.

Growing labour market inequality

Three sources of inequality:

- the top 1% ... globalization, technology, corporate governance
- the top 20% ... returns to higher education and firm specific skills
- the bottom half ... decline in the return to low skilled work

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In Canada the top 1% are a select group demographically ...

older,		highly educated,		men.	
the top 1%	the pop- ulation	the top 1%	the pop- ulation	the top 1%	the pop- ulation
only 5% younger than 35	29%	58% have a BA	12%	83%	48%
80% between 35 and 64	55%	30% more than BA	7%		

Source: Nicole Fortin et al. (2012).

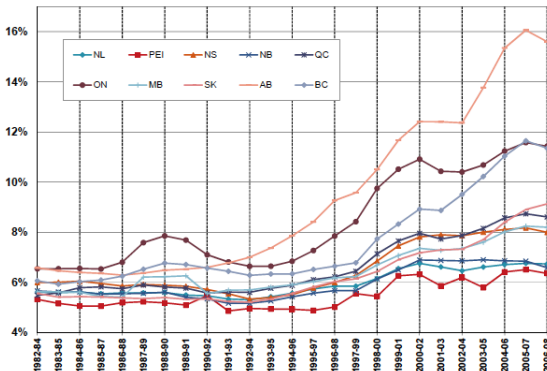
... but a diverse group occupationally

	top 1%	the population
Management	19.1%	6.1%
Senior Management	14.1%	0.9%
Health Professionals	11.6%	2.0%
Professionals, business, finance	7.1%	1.8%

Source: Nicole Fortin et al. (2012).

The resource boom has in part fuelled top incomes about one-in-twenty 1%ers work in the mining, oil, and gas sectors

Fig. 5 Top 1% After Tax Income share by province
(3 year moving average including capital gains)



Source: Mike Veall (2012), presentation to the University of Ottawa

In Canada there has been a change in corporate culture arising from proximity to the US, and also a resource boom

There are a number of leading hypotheses to explain rising top income shares:

- 1 Globalization and skill biased technical change have combined to create an economics of “superstars”
- 2 Tax changes
- 3 Changes in corporate governance, and changes in social norms

Labour markets and institutions

The struggle to maintain a middle income existence is more difficult, and there has been a decline in average incomes at the bottom—particularly among the young and less educated—because:

- 1 Globalization and skill biased technical change favour the more educated, say the top 20%
 - in 1980 a BA implied 30% more earnings than a high school diploma, twenty-five years later 40%
 - but work experience also has a higher premium since earnings gaps by age cohort increased
 - someone starting work with a high school diploma earned 10 to 20% less in the 1990s and 2000s than in the 1980s

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 - minimum wages
 - Unions (within sectors, between sectors)

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- 2 Erosion of labour market institutions influenced lower earnings
- 3 The gender wage gap has been reduced and this is a force reducing inequality

Recommendations 1: Policies to make work pay

Institute a Guaranteed Income for the working poor by subsidizing low-pay work, and adopting immigration and education policies to create high pressure economy for those with low skills.

- A job is central to material well-being, but many jobs increasingly do not pay enough to adequately support a family
- top-up wages more generally with a conditional transfer based upon work effort (The Working Income Tax Benefit)
- develop alternatives to university education that upgrade skills and move the service sector up a value chain: “an artisanal economy”
- limit low skill immigration, and promote immigration of high skill workers

Recommendations 2: Tax policies for inequality

Tax reforms that introduce more progressive taxation.

- Increase income tax rates, broaden the tax base, close loop-holes
- Heavily tax rents in the business sector (particularly in resource driven economies)
- Permit income averaging over several years for tax purposes, for example offering rebates to families suffering permanent losses in income

Some principles for public policies: understanding what to do

The comma in my title was missing intentionally. “Understanding inequality, and what to do about it” vs “Understanding inequality and what to do about it”

- 1 Some things you can change, some things you can't
- 2 Don't make things worse, watch out for unintended consequences
- 3 Evidence based, in a spirit of experimentation