

# ECONOMICS

## Inequality and the Distribution of income and wealth in Australia

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A major challenge of government policy is to ensure that the benefits of economic prosperity are shared fairly between different groups in society. Since the 1980s Australia has implemented policies of structural change which has made the equal distribution of income and wealth a more difficult task as adjustments costs should not be burdened by one part of society and that those already financially well off do not receive all the successes. There are many associated costs and benefits associated with inequality and Government policies introduced have had mixed success in preventing the creation of a more divided society.

Sources of income and wealth in Australia are derived mainly from the factors of production. These include wages from the sale of labour, rent from land, earning from capital such as dividends and capital gains and profit from entrepreneurial skills. Social welfare is also provided as a source of income. The level of income and wealth inequality in the economy can be measured using a Lorenz curve. This is a graphical representation of income distribution. The cumulative percentage of total income received is plotted on the vertical axis against the cumulative percentage of income recipients on the horizontal axis. The line of equality is drawn diagonally through the origin and the further the Lorenz curve is from this line the greater the degree of inequality in society. From this graph the Gini coefficient can be calculated as a single statistic that summarises the distribution of income across the population. It is the ratio of the area between the Lorenz curve and line of equality and the total area under the line of equality. The higher the Gini Coefficient the higher the level of inequality.

Australia has a relatively high level of income and wealth inequality, which has tended to increase in recent decades for several reasons. The housing boom of the late 1990's early 2000's increased the wealth of property owners which has been slowly growing in more recent years. The movement towards enterprise bargaining has tended to generate more wealth for higher skilled and income earners. The microeconomic reform agenda has appeared to disadvantage workers in certain industries whilst deregulation and privatisation has led to retrenchment for many lower skilled workers. The stock market boomed in the past decade which significantly benefited those with share investments. Although the GFC dented the value of the stock market, the recovery is allowing these investments to grow strongly.

Australia's 19 years of consecutive economic growth led to significant salary increases mainly in financial services and technology. Unemployment increased during the GFC which widened inequality as lower workers were more likely to be retrenched and struggled to find employment. However the slow down may have also reduced inequality as share market, salary and business profit reductions significantly reduced the wealth of higher income Australians. As the economy recovers employment opportunities should arise to boost equality but wealthier Australians are likely to benefit more as investments, profits and salary prices rise.

Compared to other nations Australia has an equally or higher level of inequality. This is typical as income distribution is asymmetric, meaning that a small number of households have a relatively high level of income and wealth whilst a relatively large number of households have a lower level, with wealth tending to be more unevenly distributed than income. Factors that affect inequality are mainly demographic. Young workers tend to be the lowest paid due to experience and skill level. Workers aged 25-54yrs are the highest paid as a result of their qualifications. Income then declines with age due to a reliance on retirement incomes. Females earn approximately 65% of what males earn due to labour market discrimination, time out of the workforce for family commitments and higher numbers of women in casual employment. Couples with no dependent children are the highest paid in society if both work full time, whilst single parent families and sole aged persons are the lowest paid.

Managers and professionals are the highest paid members of society whilst labourers and service workers earn the lowest income, due to the level of skills required, labour availability and union strength, such as the Australian Medical Association. Due to a lack of recognised skills or language capabilities NESB migrants have substantially lower levels of income, whilst English speaking migrants have higher levels as most are skilled business migrants. Indigenous Australians continue to suffer very low income levels due to discrimination and remote settlements.

Such inequality leads to both economic and social costs. Economically, inequality can increase the highest income earners likelihood of having a high MPS and a lower MPC which reduces economic growth and consumption. These wealthier individuals tend to increase the amount spent on conspicuous consumption which is not resource efficient. Inequality also increases the costs of welfare support and reduces the overall satisfaction in society. These social costs include social class division, creation of poverty, the vicious cycle of poverty, increased crime and reduced life expectancy and health. Diseases may increase as lower income earners are unable to afford to eat well, receive a good education or pay for medical expenses.

Despite the disadvantages there are also benefits of inequality. The labour force is encouraged to work longer, more effectively and increase education and skills in order to reach higher positions. Inequality also makes labour more mobile as wages vary depending on geographical locations. Risk taking by entrepreneurs is encouraged whilst a greater potential for higher savings and capital formation is created due to the wealthier members high MPS. Socially there are few benefits, although the most talented and capable generally rise to highest power positions in society, ensuring the most suitable individuals are at the top. However as considerable inequality of opportunity exists in society such as inheritance and education level, an individual's access to progression in society can be distorted.

Macroeconomic policies can influence the level of inequality. Through monetary policy interest rate changes can benefit or disadvantage individuals, redistributing income and wealth. Interest rate rises as is currently occurring will benefit individuals with high interest bearing deposits such as retirees whilst mortgage holders are worse off. In addition, unemployment increases tend to affect the less skilled and less wealthy members of society. If interest rates fall the opposite effects would occur. Fiscal policy can reduce inequality through the progressive taxation system and spending on transfer payments, education and health. However inequality can be increased if tax cuts and benefits are provided to the well off and spending is cut that would benefit the more disadvantaged sections of society.

In the 2010-11 budget lower income earners will benefit from a 50% reduction in the first \$1000 of tax charged on ordinary savings accounts, whilst \$500 will be given to offset contributions tax allowing these earners to benefit as higher income earners do. The simple tax return of \$500 will also increase after tax salary for 6.4m of these earners. The 47% rise in both personal income tax and company tax is expected to redistribute funds as the economy booms. Through these measures inequality is expected to increase both socially and economically.

Microeconomic policy is often criticized for its adverse impact on particular groups. In the longer term it is argued that such reforms will lead to significant increases in Australia's efficiency GDP and international competitiveness which will boost real incomes and employment levels. In the short term however many of these policies can increase the level of inequality. Reduced protection, privatisation, corporatisation and financial deregulation have led to job losses as firms strive to boost efficiency and competitiveness. This may also put downward pressure on wages especially for those less skilled. Enterprise bargaining can also raise inequality by disadvantaging those with less bargaining power. Taxation changes such as the introduction of GST have been criticised for unfairly disadvantaging those less wealthy, as it is regarded as a regressive tax and so lower income earners spend a higher proportion of their wages in GST as a result of their MPC.

Government policies recognise both the economic and social costs associated with inequality and attempt to create a more equitable society. The progressive taxation system is designed to raise higher levels of tax from higher income earners whilst transfer payments are designed to assist lower socio-economic groups. The Compulsory % superannuation, set to increase to 12% will provide a greater number of Australian's with adequate retirement savings. Medicare and the public hospital system has been established to provide health care to all regardless of their ability to pay. Similarly, the public education system provides education to all, whilst Austudy and Abstudy provide financial assistance to disadvantaged students to enable them to complete the HSC and attend higher education. The 'Fair Work Act' introduced by the Government included policies such as minimum working conditions, the right to collectively bargain and assistance to the lower paid are designed to help those workers in weaker bargaining positions. As announced in the 2010-11 budget funds will be redistributed from the wealthiest 3% of parents who claim for the childcare rebate when it is decreased from \$7778 to \$7500.

Inequality and the distribution of income and wealth in Australia remains a key priority for the Government due to the associated costs and benefits to the economy and society. Through various policies and economic actions the Government has attempted to achieve a more equitable nation and continues to strive towards achieving these goals on an international, national and local level to achieve optimum outcomes.