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Subject: submission to Senate inquiry into income inequality
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To: The Secretary, Senate inquiry into the Extent of Income Inequality in Australia

I congratulate the Senate for initiating this important inquiry, and offer the submission below.

Frank Stilwell

Inequality in Australia: trends, problems and budget impacts

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Introduction: Knowledge about Inequality and its Consequences

The broad patterns of economic inequality in Australia have been monitored and analysed in many studies. My own research over more than four decades has sought to make some contribution to this knowledge. On request, I will happily provide members of the Senate inquiry with copies of one of my books on the topic, co-authored with Kirrily Jordan, titled 'Who Gets What?: Analysing Economic Inequality in Australia', and published by Cambridge University Press, Melbourne. The more recent book 'Billionaires and Battlers' by Andrew Leigh MHR admirably explores these issues further. Suffice to say here that the inequalities are larger than is popularly perceived; they are stratified by class, gender, ethnicity and region; and they vary over time in long swings.

Numerous studies have also been undertaken by social scientists and epidemiologists, revealing the statistical and causal connections between economic inequality and a range of economic, environmental and social problems, such as mental and physical health, crime and violence. The widely-discussed book by Richard Wilkinson and Kate Pickett, 'The Spirit Level: Why More Equal Societies Almost Always Do Better', is a useful and accessible compilation of some of the international evidence. So there are good reasons to be concerned about keeping income inequalities in check: failure to do so generates considerable public economic and social costs (in physical and mental health services, in policing and in prison incarceration, for example). Surveys also show that, in general, nations that are relatively equal in their distribution of wealth have happier people: the correlation is not perfect but the evidence coming from the growing field of happiness research, points in this direction. Australian surveys, including those cited in my own book noted above, have fairly consistently shown most people think society should be more equal.

It is also notable that a book on inequality has been making major waves worldwide this year. This is Thomas Picketty's 'Capital in the Twenty-First Century'. It describes and analyses the trends in inequality across many countries and over many decades. One does not normally look to big, statistical academic tomes to find triggers for widespread public concern. But here is such a book, and it has become a publishing phenomenon. Picketty's blockbuster book evidently feeds on, and contributes to, a climate of widespread public concern about how growing economic inequality impairs social justice, social cohesion and social stability .

Patterns and Trends

Notwithstanding a popular self-image of being an egalitarian nation, Australia is not an egalitarian society: rather, it is generally middle-ranking on the international league tables for the standard measures of economic inequality. It is also becoming more unequal. The increased income inequality that has occurred here over the last three decades is similar to what has been happening in many other countries, especially those whose economic policies have been influenced by neoliberal prescriptions. These increased income inequality reverses the general trend towards reduced inequalities that had been evident in OECD nations during the period from the second world war to the 1970s. It is the result primarily of the phenomenal growth in the income and wealth of the super rich during the last three decades, rather than being due to increasing rates of absolute poverty (although relative poverty tends to rise whenever there is surging growth at the top and stagnation at the bottom).

The top 10% of households has done disproportionately well in the race for riches over that last three decades. The top 1% of households has increased its share most spectacularly: in Australia it has nearly doubled its income share. The concentration of accumulated wealth – always more unequally distributed than current income – has become even more extreme.

Effects of the 2014-5 Australian Budget

It is in this context that the controversy generated by the currently proposed Federal Budget measures can be understood, considering both the budget's posited macroeconomic rationale and its distributional effects. These two aspects are interconnected, because the former paves the way for the latter.

The budget's central assumptions are the existence of a budget emergency and the need for major cuts in government spending. But the posited fiscal crisis is nowhere near emergency or crisis levels, as many independent professional economists have pointed out. Indeed, the Australian government's debt is one of the lowest of all the OECD countries. The size of the current budget deficit relative to GDP is also quite manageable. It could be eased back over a number of years by a combination of further economic growth and revenue measures targeted at those with the greatest capacity to pay. But it would be economically irresponsible to jeopardize that growth now by expenditure cuts that cause job losses and reduce aggregate demand. That sort of posited 'fiscal consolidation' could indeed exacerbate the deficit because of the impact or reduced levels of macroeconomic activity on revenues and expenditures.

By focusing on Federal Government expenditure reductions and targeting the cuts as announced by the Treasurer, social hardship is also disproportionately imposed on the relatively poor. This widespread concern has been given particularly sharp bite by the Federal Treasury's own estimates which show that the budget, if fully implemented, would hit the poor harder than the rich. Treasury's modeling estimates that the total effect of the spending cuts and tax changes would leave the richest third of households \$517 a year worse off but make the poorest third of households \$844 worse off. Another recent report from the Australian Consumers Association reveals the intensity of cost-of-living pressures already being felt by a broad swathe of Australian households, two thirds of whom say they are having to cut back on their spending. The Treasurer's recent public statement about poor people being less affected by rising fuel prices because they don't drive as much showed him to be fundamentally out of touch with these public concerns.

Quite apart for the government's failure to effectively 'sell' its policy, however, is not surprising that the budget has provoked such widespread opposition. The predictable concerns of those most directly affected by the austerity measures that the Treasurer announced have been swelled by expressions of broad social concern about unfairness. Even people who emerge relative unscathed from the tax and spending changes seem to sense that it runs counter to social concerns with equality and social cohesion. It is perceived as violating the cherished Australian ethos of 'the fair go'.

Why Seek to Reduce Inequality?

These concerns about equality are of long standing across a broad political spectrum. They are deeply embedded in traditional small-l liberal concerns to create equality of opportunity. They have pervaded social democratic ambitions for greater equality of outcomes.

However, a long-standing constraint on achieving those social outcomes has been warnings from people schooled into neoclassical economic thinking that pursuing greater equality would impair the material incentives necessary for greater overall prosperity. Formally, this is the notion of an efficiency-equity (or sometimes growth-equity) trade-off. In less technical language, it is the fear that more equality would have a significant economic cost in terms of lower levels of overall GDP. But that conventional economists' warning has recently been killed off because of contrary evidence of economic outcomes in practice. A particularly significant nail in its coffin is a recent IMF report, based on empirical study of the international evidence and showing that there is no general trade-off. In other words, pursuing inequality does not impair a nation's productivity nor its economic growth, contrary to what many mainstream economists had previously asserted. That this conclusion comes from a conservative institution like the IMF is a particularly powerful blow to those vested interests who are opposed to the egalitarian principles and policies.

So is the pursuit of greater economic and social equality a longstanding concern whose time has come? It previously had traction following the second world war and led to progressive tax policies and the welfare state, but the last quarter

century has seen that liberal and social democratic momentum stalled by the neoliberal backlash. Australian government policies have put more emphasis on trying to foster economic growth and have made the tax system less progressive and redistributive. The resulting erosion of the tax base, particularly during the period when Peter Costello was Treasurer in the Coalition Government led by John Howard, has left us with a sorry legacy. The current Treasurer's budget worsens it by pushing for the abolition of two significant tax measures that the previous government put in place – the carbon tax and the minerals resource rent tax - as well as reducing corporate taxation at the margin.

The big challenge now is to chart a different direction with explicitly egalitarian characteristics. An alternative policy agenda that emphasizes greater equality needs to be constructed and effectively implemented by a not-too-far-in-the-future government. The dominant budgetary emphasis needs to be on generating a fairer and more substantial revenue base. Although there is no immediate fiscal emergency, as previously noted, there are good reasons for improving the Australian government's revenue base in the medium-term. Financing Australia's need for improved infrastructure and public services needs a more buoyant public revenue stream. And it needs to be targeted at those with the ability to pay, especially where their wealth derives from rent-seeking, inheritance and other forms of unearned income. It is time to abandon the strictures of neoliberalism and the inappropriate politics of unnecessary austerity, replacing them with a new agenda for a fairer and sustainable society.

Policies to Promote Greater Equality

There are plenty of policies to achieve more egalitarian outcomes if there is the political will to embrace and use them.

The options for tax reform include:

- cracking down on the abuse of family trusts and other tax rorts
- making the tax arrangements for superannuation less generous to high income earners
- dropping negative gearing that operates primarily as a way of reducing tax rather than redressing housing problems
- increasing the effective rate of capital gains taxation
- extending land and wealth taxes.

These are all potential tax reforms that could be developed in ways that would be both potent in generating revenue and equitable in their social impacts.

Ideally, these policy package would also include incomes policies designed to make the initial distribution of incomes between wages, profits, rent and interest less unequal in the first place. For example, remuneration payments to CEOs that exceed, say, 20 times the average level of wage payments to employees in those companies could be disallowed as tax-deductible business expenditures.

There are also important equity considerations in most areas of public policy.

Policies for education are a particular case in point because, properly designed, they can help to promote more equitable socio-economic outcomes over the long-period because they affect generational opportunities and outcomes. The Gonski

reforms need to be implemented in full for this reason. In the higher education sector restored public funding for universities and the abandonment of the currently proposed deregulation are imperative if we are to provide opportunities for all young people of ability rather than skew the system to the reproduction of a wealthy elite.

As a signal of the Parliament's concern with these issues, I recommend that consideration be given by the Senate to commissioning a **National Inquiry into the Distribution of Wealth in Australia in 2015**. The last officially commissioned census of the nation's wealth distribution was in 1915, believe it or not ! Doing it again exactly 100 years later would have a symbolic significance: indeed, it is a national scandal that a comprehensive national wealth analysis has been neglected for so long. More importantly, setting up a major national inquiry would signal the intent to get serious about looking at the accumulated wealth patterns that underpin the income inequalities and the other social concerns that your current Senate inquiry is examining.

Looking Ahead...

I hope your current inquiry becomes an effective turning point in the Australian Parliament and Australian public life – a turning point away from growing inequality and the policies that fuel it and towards trying to establish in reality the cherished ideal of a more egalitarian society. The nation needs a renewed drive to redress unjustifiable and socially-costly inequalities while also establishing a stronger basis for our collective, cooperative and sustainable economic future. The potential and policies are there if the political will is present. The current controversy over the perceived unfairness of the federal budget signals that the time is appropriate for a fundamental change of direction.

I would be happy to elaborate on any of the above reasoning and/or the proposed policy measures if invited by the Senate inquiry to do so.