

Nonsense About Inequality From The Ivory Tower

It's amazing the rubbish some academics can write.

I said in a recent article that, other things being equal, I prefer less income inequality to more but that I am more concerned about poverty and hardship – a standard position among economists and social policy analysts.

This was like a red rag to a bull to Mike O'Brien of the Social Policy and Social Work Programme of Massey University, a long-time advocate of welfarist and redistributionist policies.

He expostulated, "The evidence, however, is clear: inequality is the brake which destroys the society and the economy".

What a ludicrous proposition! Inequality has existed throughout human history. So how come so many countries are now prosperous? How come India, China and others are steadily joining them?

O'Brien did not cite the evidence. However, he may well have relied on the book *The Spirit Level* by British epidemiologists Richard Wilkinson and Kate Pickett which attributes almost every social problem to inequality.

This book has been severely criticised on the grounds that its evidence is weak, its data are selective and its analysis unsupported. As one British reviewer headlined his review, "If you want something trashy to read on the beach, here's my recommendation."

One issue is that the analysis of inequality in the book is static. It simply looks at the position of people at a point in time. It does not take account of social mobility: the movement of people up and down the income ladder over their lifetimes.

While *The Spirit Level* argues that New Zealand is a relatively unequal society, guess what country comes below New Zealand in the inequality rankings. Answer: Australia.

Inequality is the brake that has destroyed Australian society and its economy? The idea doesn't pass the laugh test. For good reason, outside social policy departments of universities, *The Spirit Level* has been largely ignored in Australia.

Worst of all on the inequality measure was wealthy Singapore!

In 2007 Australian economist Mark Harrison produced an empirical study of income redistribution for the Business Roundtable entitled *The Outcome of Income Transfers*.

He noted that some politicians, academics and welfare lobbyists appear to believe that the government can easily use income transfers to increase the share of income going to poor households significantly and eliminate poverty.

However, such proposals invariably fail to specify what taxes need to be raised to finance the income transfers and ignore the effects, such as welfare dependency, on those receiving them.

Harrison's is a rigorous quantitative analysis. He calculates the effect of transferring an additional 1 percent of aggregate household income to the bottom quintile (20 percent) of households in 2003/04. (This would be a tall order.)

He finds that would involve a \$900 million transfer; a much greater cost to taxpayers (at least double); and a likely increase in the average tax rate by over 10 percentage points.

And to what effect? Given that there were 300,000 households in the bottom quintile, the transfer would increase their annual incomes by an average of \$3,000, which would do little to reduce measured poverty rates. (The commonly suggested poverty line is 60 percent of median income, or \$28,380 in dollars of the day.)

These results highlight the need to be realistic about what the government can do to solve poverty through income redistribution and the folly of promoting equality of incomes as an objective.

They strengthen the case for growing the economy, alleviating poverty and ensuring basic needs are met. Unrestricted income transfers do not address the underlying causes of poverty (such as poor education, barriers to labour market participation and welfare dependency), and may aggravate them.

Despite professed concern about inequality, social policy advocates like Mike O'Brien typically favour things like job protection legislation, higher minimum wages, state monopoly education and lenient welfare rules. These all have the effect of leaving too many people unemployed, unskilled and in poverty.

We are living at a time of unprecedented improvements in the living standards of people in many poor countries around the world and witnessing just how powerful high growth can be in freeing people from poverty.

Yet another Massey University academic Srikanta Chatterjee disputed my argument that "growing the economic pie rather than redistributing the pieces" alleviates poverty and hardship more effectively.

Just last month the left-leaning Brookings Institution published an interesting study on global poverty.

It concluded, "For many years, a debate raged amongst development academics, advocates and policymakers on the role of growth in poverty reduction and development, with some suggesting issues such as inequality and redistribution merited greater attention. Today, the development community has thankfully largely moved beyond this debate, with a broad consensus rightfully asserting the role of growth at the centre of poverty alleviation."

Clearly this message hasn't got through the walls of some of New Zealand's ivory towers.

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