Saturday, May 25 2013

Growing gap between rich and poor

T. K. JAYARAMAN

The Report on the growing divide between rich and poor by a 34-nation Organisation for Economic Cooperation and Development (OECD), based in Paris surprised many.

The surprise is not in regard to the finding: austerity measures under the supply side economics hypothesis in the wake of the world economic crisis since 2008 led to a rise in wealth gap in Europe.

The surprise is OECD, which is committed to free market ideology, has finally recognized the fact: growing poverty.

The OECD consists of Australia, Austria, Belgium, Canada, Chile, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Israel, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United Kingdom and United States (USA).

Rising income inequality

Income inequality rose more in the three years to the end of 2010 than in the previous 12 years. The richest 10 percent in OECD countries pocketed 9.5 times as much market income as the poorest 10 percent in 2010, up from 9 times in 2007, a year before the recession began. Chile, Mexico, Turkey and the USA experienced the widest gaps. Iceland, Slovenia, Norway and Denmark were the most egalitarian societies.

Welfare payments to unemployed help counter the adverse impact on disposable incomes. When governments embark on austerity measures under the banner of fiscal consolidation, transfer payments are the first casualty. The result is more people began to slide into poverty.

The OECD expressed its concerns:

"As the jobs crisis persists and fiscal consolidation takes hold, there is a growing risk that the most vulnerable in society will be hit harder as the cost of the crisis increases". Due to austerity measures “poorer households either lost more income from the recession or benefited less from recovery”.

It is also an indirect admission by OECD, the pro free-market think- tank that welfare state has the capacity to soften the blow of hard economic times.

Fiji’s welfare measures including 2013 budget’s provision of F$32.3 million for Poverty Alleviation and Social Protection deserve mention here. The welfare payments to the absolute poor (maximum of F$150 per month), who are the hardest hit, indicate government’s readiness to play a welfare role that is legitimately expected by society.

The debate

Referring to a near zero interest rate monetary policy by US central bank, Professor Robert Reich of University of California at Berkeley, a former Secretary of Labour under President Clinton, wrote in *Christian Science Monitor*:

“Easy money from the Fed can’t get the economy out of first gear when the rest of government is in reverse”.

He was referring to cuts in government expenditures and layoffs in the US.

The debate is “between Keynesians (who want more government spending and lower interest rates in order to fuel demand) and supply-side “austerics” (who want lower taxes on the wealthy and on corporations to boost incentives to hire and invest, and who see government deficits crowding out private investment)”.

Reich says the weakness of the Keynesian approach is that there is no “clear answer for how much spending is necessary in an economy, in which wages keep dropping and government debt keeps growing”.

The fact remains both sides have neglected the scourge of widening inequality. When the rich get richer, the rest of the population is deprived of purchasing power. When aggregate spending declines, the economy declines too.

Widening inequality could be reversed. Reich suggests:

- Tax cuts to companies, which link the wages to profits and productivity.
- Keep the total pay of their top 5 executives within 20 times the pay of their median worker and impose higher taxes on companies that don’t.
- Raise the minimum wage to half the average wage.
- Increase public investment in education, including early-childhood.
- Pay for this by adding additional tax brackets at the top and increasing the top marginal tax rate to what it was before 1981 – at least 70 percent.

Raise tax rate on upper income brackets to pay for growth?

That is what President Hollande of France wanted: Tax annual income of more than one million euros (US$ 1.3 million) at the rate of 75 percent.

Hollande defended the rise on a notion of "fiscal justice." Last December, the French Constitutional Court rejected it as unconstitutional.

Hollande has not given up. He is trying his plan again: this time with a carrot to business: a reduction in capital gains tax but with 75 percent rate on incomes of millionaires.