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Economic inequality has been a hot political topic as of late, particularly picking up momentum in the wake of the 2008 global financial crisis. New Zealand at one time was known for its focus on an equal society and it seemed ingrained in our culture. But like much of the western world, economic inequality dramatically increased in the 1980's. In this essay I discuss whether or not policy makers should be concerned with levels of inequality in New Zealand, policy recommendations and how these tie into the treasury's higher living standards framework.

Inequality in New Zealand

Income Inequality in New Zealand has sharply increased since the mid 1980's. The Gini coefficient is a ratio used to represent the income distribution of the residents of an economy, a value of 0 means complete equality while 1 means complete inequality. The income Gini coefficient in New Zealand took a sharp rise the mid 1980's, rising from .26 in 1988 to levels of .32 in 1996 (Perry, 2013). Since then, the coefficient has level out, although fluctuating year to year; the general trend indicates a consistent level around .32. Wealth inequality is much harder to measure than income inequality, the most recent statistics estimate a wealth Gini coefficient of 0.69 (Statistics New Zealand, 2007), showing a significant concentration of wealth. Other key measures of wealth disparity show that the top 10 percent own over 50% of the country's wealth (Statistics New Zealand, 2007), this data is from the 2003/04 Survey of Family, Income and Employment conducted by statistics New Zealand. While this information is somewhat dated, it would be judicious to assume that wealth disparity has remained at this level; or perhaps even increased. Homeownership levels have decreased between 2006 and 2013 (Statistics New Zealand, 2014), combined with house prices rising; over 50% in Auckland since 2007 (Stuff, 2015), may well increase the concentration of wealth. Interestingly a price correction in property market may serve to further increase inequality as over-leveraged investors are plunged into negative net-worth. The National Government's partial privatization of State owned assets following the 2011 election may have increased wealth inequality as well (Gupta et al, 1999).

Should policy makers be concerned?

Do these levels of economic inequality hinder or facilitate economic performance and political freedoms. Economic inequality hampers the relative education opportunities for disadvantaged citizens; this causes a dragging effect on the economy slowing GDP growth (OECD, 2014). The Ministry of Education has also found evidence to indicate that low income families struggle to provide the same education opportunities as higher income families (Ministry of Education, 2012). Income inequality has resulted in New Zealand missing out on 15.2% of potential GDP growth (OECD, 2014). This was the highest level of lost potential GDP in the OECD. Income inequality also effects long term stability of growth. The International Monetary Fund presents evidence which suggests that a ten percentile decrease in inequality can increase growth spells by 50% and is a very robust predictor of the length of grow spells (Berg & Ostry, 2011). This provides a strong economic foundation and basis to justify policy to target inequality. Inequality affects other social areas as well; countries which have greater income inequality tend to have higher levels of health and social problems (Wilkinson & Pickett, 2009). New Zealand scores particularly poor on this basis, using an index consisting of trust, life expectancy, infant mortality, mental illness, obesity, homicide and rates of imprisonment, educational scores, teenage birth rates and social mobility; New Zealand ranked 5th worst in a basket of 23 developed countries (Wilkinson & Pickett, 2009). New Zealand also ranked 5th

highest in income inequality in the same basket of countries. Policy makers should be concerned about the rising levels of economic inequality as it has consequences involving long-term economic growth and society well-being. Inequality in part can be attributed to market forces (Welch, 1999), and even with perfect equality of opportunities one would expect economic inequality to remain (Gregory Mankiw, 2013), but in New Zealand equality of opportunity does not exist (Ministry for Social Development , 2004) and on these grounds policy makers should intervene.

Policy recommendation

Thomas Piketty's book raised a particularly key point, that in the long run, the rate-of-return on capital is higher than that of the growth-rate of the economy. This then leads to an accumulation of wealth and income, by those who own the capital. Piketty argues that progressive wealth taxes and relatively high (compared to current levels) progressive income taxes can reduce inequality (Piketty, 2014). Whether this will fix the fundamental critique, that is the disparity between growth rate and the rate of return of capital would demand another essay. Save for a significant change in technology, this disparity does not seem likely to change (Pearlstein, 2014). The most recent data estimates New Zealand to have a wealth Gini coefficient of 0.69 (Statistics New Zealand, 2007). This shows a significant concentration of wealth, which in turns means a concentration of capital income. Traditionally capital meant real estate; modern economies include stocks and bonds.

Tax incentives for companies which engage in profit sharing, stock options and part ownership would serve to allow the ownership of capital and thus capital incomes to be more spread amongst the population. Positive effects of this policy is a decrease in both wealth and income inequality, lower and middle-class economic demographics are able to gain a larger share of the capital stock without the risk of sacrificing personal savings. Reducing inequality as illustrated in earlier paragraphs can improve the long-run growth potential of the economy (OECD, 2014) as well as improving social problems (Wilkinson & Pickett, 2009).

Firms which participate in profit sharing experience a positive effect on employee empowerment, which has a positive effect on employee turnover and intent to stay (Kruse, Blasi, & Freeman, 2011). Experiments involving employee owned companies found that employee productivity increased and employees had a greater propensity to provide assistance to co-workers (Frohlich et al., 1998). There is a number high-profile employee owned businesses in New Zealand, namely Beca Group; an employee-owned engineering and consultancy firm, and Tui-balms; a cooperative from Wainui Bay. Although successful, similar firms are few and far between. One can come to the conclusion that it isn't economically viable for business to change their ownership structure, even with the increase in productivity; otherwise businesses would already implement employee ownership and profit sharing structures. Providing incentives to make alternative ownership structure economically viable could increase efficiency and therefore GDP, in addition to positive effects on inequality. With this policy the corporate tax structure can be viewed as less of general tax on businesses to raise revenue and more of a tax on behaviour that the government would like to de-incentivise, comparable to a tax on say tobacco.

Higher Living standards

Economic Growth.

This policy works incredibly well within the Treasury's higher living standards framework, as there are limited trade-offs between the different tenants that make up the framework. The Treasury defines economic growth as "the level and growth of average income of New Zealanders" (Treasury , 2013), it also refers to the distribution of income. Economic growth will be positively effected through not only a higher absolute value of national income, but also a more equal distribution. There is a positive effect on human capital, with more profit sharing and employee owned firms, the productivity of workers would increase, increasing GDP (Frohlich et al., 1998). Providing tax breaks for firms may encourage employee-owned and profit sharing firms to set up in New Zealand, further aiding in economic growth.

Sustainability for the future.

The treasury defines sustainability for the future as "development that meets the needs of the present without compromising the ability of future generations to meet their own needs" (Treasury , 2013). High levels of inequality pose threats to long term economic growth (Berg & Ostry, 2011), as growth periods can be significantly shortened. Inequality adversely affects the education opportunities for younger generations, harming long term economic growth (OECD, 2014), by reducing economic inequality, the long-term sustainability of human capital is increased through better education opportunities. Employee owned firms provide a work place which is more productive, more enjoyable and therefore less of turnover rate of employees (Kruse, Blasi, & Freeman, 2011), this helps keep talented and educated New Zealanders in New Zealand, no doubt a positive effect on the sustainability of human capital.

Social Infrastructure.

The treasury defines social infrastructure as "the features of social organisation, such as trust, norms and networks that can improve the efficiency of society by facilitating coordinated actions" (Treasury , 2013). High levels of inequality can have profound effects on social infrastructure, Wilkinson & Pickett argue in their book *The Spirit Level* that high levels of economic inequality adversely affect social structures such as social mobility, mental health and "erodes trust" (Wilkinson & Pickett, 2009). Profit sharing firms give their employees a larger sense of empowerment (Kruse, Blasi, & Freeman, 2011) and willingness to help others in the work place (Frohlich et al., 1998), this sense of community could translate into areas other than the workplace. Links between status anxiety and economic inequality have been explored, but inconclusively and at times contradictory (Paskov et al, 2013). Anecdotally it feels like there is a level of status anxiety in New Zealand and it seems plausible that this is linked to inequality.

Managing Risk.

The treasury defines risk as uncertainty in events and its effect on objectives. Economic inequality poses a number of threats to the wellbeing of New Zealand. Economically we are more susceptible to recessions with this level of inequality as opposed to a lower level (OECD, 2014), decreasing

inequality would help mitigate that risk. This would decrease the risks to social capital as education opportunities for disadvantaged would increase (Ministry of Education, 2012).

Equity.

The Treasury defines equity as "commitment to equal rights, a safety net that protects the vulnerable, and the opportunity to participate in society" (Treasury , 2013). Equity is probably the tenant which is affected the most through this policy. By definition, employee-owned and profit sharing firms offer rewards and compensation based on performance. Providing shares of profits in addition to their wage or salary, such that employees are protected from systematic risks, employees will be rewarded for their effort. Capital income is also disproportionally weighted in favour of wealthier individuals, by increasing the share of capital to poorer workers; the share of capital income is more evenly distributed (Gupta et al, 1999). Human capital is positively effect through an increase in education opportunities, when families have their incomes increased (Ministry of Education, 2012).

In conclusion, providing corporate tax incentives for companies which participate in profit sharing or offer employees part-ownership will reduce economic inequality. Inequality has far-reaching effects on societal problems and economic problems, reducing inequality will therefore help mitigate those problems. We found that like much of the western world, inequality has taken a sharp increase in New Zealand since the 1980's and because of its negative effects on the economy and society policy makers should be concerned.

One particular caveat of my analysis is that of a lack of a case study. Effects of this policy have been determined through drawing together evidence from a number of sources and bundling it together to attempt to find a conclusion. Without real-world examples of this policy it is hard to accurately predict the effects; there are huge number of endogenous risks associated with this policy. Most OECD countries operate with corporate tax rates somewhere between 20-35%, taking a significant deviation from this may have significant effects on New Zealand's foreign relations.

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