Income Inequality and Tax-Transfer Policy: Trends and Questions

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Isolating impact of income tax and cash transfer changes

- Uses NATSEM’s STINMOD model (Version 06A/v2)
- Comparing 1996-97 with 2006-07
- Eight ‘private income’ levels (adjusted for inflation in earlier year – that is, ‘real’)
  - $1000 in 2006-07 -> $774 in 1996-97 $
- Six ‘illustrative’ family types
- Two children aged 8 and 10 years
- Two income couples have 50:50 income split
- ‘Disposable’ income means after-income-tax, after cash transfers – income ‘in the hand’
- This methodology isolates the impact of changes in tax and transfer policy from changes in labour force status and earnings growth
Aged with some private resources are the big winners
Single income couples with children on lower to middle incomes also big winners

Note: The faint orange line is the single 66 yr old and the faint green line is the single 25 yr old (shown in pervious slide)
Two income couples without children do less well: sole parents on welfare with children aged 8+ do poorly

Note: The faint orange line is the single income couple with two children (shown in previous slide). Note that outcomes for sole parents whose youngest child is aged < 8 yrs would be similar to these. The loss shown above is due to welfare to work changes placing sole parent on NSA.
Taking Other Effects Into Account: Labour Market and Family Composition Changes
Real earnings up, job numbers up

- Earlier analysis isolated impact of tax-transfer system for typical families with ‘frozen’ real private incomes
- But in the real world:
  - Pay packets increased (21% increase in full-time AWE for adults);
  - Unemployment fell -> more people in jobs;
  - More families became two income;
  - Population ageing and other social trends changed family composition
- Following figures show change in real disposable incomes between 1996-97 and 2006-07
  - Changes are estimates, using NATSEM’s STINMOD model
  - Estimates are subject to revision as STINMOD is continuously updated as new data become available
  - All following estimates based on ‘aged’ ABS 00-01 and 02-03 income surveys:
    new ABS 03-04 data shows spectacular increase in incomes at bottom end
Change in real disposable income by family type

- **Couple, no children**: 
  - Income in 1996-97: $774
  - Increase by 2006-07: +23%

- **Couple, with children**: 
  - Income in 1996-97: $1,035
  - Increase by 2006-07: +29%

- **Sole parent**: 
  - Income in 1996-97: $538
  - Increase by 2006-07: +26%

- **Single adult**: 
  - Income in 1996-97: $411
  - Increase by 2006-07: +15%

- **ALL**: 
  - Income in 1996-97: $647
  - Increase by 2006-07: +19.5%
Have the rich got richer and the poor got poorer?
Methodology

- Calculated average real change in equivalent disposable income unit income over the 10 years
- Assigned this income to all persons in income unit and then divided them into deciles
  - 10% of Australians in each decile
  - ‘income unit’ means couple with dependent children, couple without children, sole parent, single person
  - Employed Gen Y still in parental home is a ‘single person’
- Calculated equivalent disposable income of the income unit
  - New OECD equivalence scale
  - All results are for persons, categorised by income of the income unit they live in
Middle income families and singles made the greatest gains
Conclusions from previous figure

- **Average increase in equivalent disposable income is 24.7 per cent ($113 pw of equiv disp income)**
- **Largest gains in needs-adjusted income made by the middle one-fifth of the population**
  - 29% and 32% increases
  - About $115 to $120 pw in equivalent dollars
- **Incomes at top of income spectrum increased by about ¼**
  - Even after the large 2006-07 tax cuts
- **Strong income gains across the board** (except for decile 2 - see below)
- **Impact of population ageing already evident**
  - No. aged 75 yrs+ grew by about 390,000 in 10 yrs to 06-07 (ABS)
  - No of singles in decile 2 up by 360,000, to almost 1m
  - No of persons living in ‘couple without children’ units in decile 2 grew 214,000, to about ¾ million
  - Singles now make up almost ½ of all the 2.08 m Aussies in decile 2
  - So suspect income outcomes for decile 2 are being driven by outcomes for max rate single and couple pensioners with little or no private resources (many of them aged pensioners)
Implications for the future
ABS projects doubling in number of Aussies aged 60 yrs + by 2040

Source: ABS Population Projections
Projected revenue and spending under current policy: deficit > 5% of GDP

Budget will be under tremendous pressure

- Baby boomers now aged 46 to 61 years -> many already retiring
- Insufficient savings: median superannuation of female baby boomers in 2004 was $8,000 (males $30,700)*
- NATSEM building APPSIM dynamic microsimulation model with 13 govt agencies as partners, to simulate future impact of policy changes

Work incentives and labour supply to become a major issue

% of persons aged 15-64 yrs facing effective tax rates of > 50%

- **All**: 4.8% (1996-97), 7.1% (2006-07)
- **Men**: 5.2% (1996-97), 6.9% (2006-07)
- **Women**: 4.3% (1996-97), 7.3% (2006-07)

Improving health to allow greater labour force participation now a high policy priority

These conditions include Asthma, Diabetes, Injury prevention, Mental health, Cancer and Cardiovascular health

Conclusions

- Aged with some private resources and traditional families have benefited most from structural changes in tax-transfer policy
- Substantial gains in real after-tax income in past decade (driven primarily by earnings growth)
- Income increases across the income spectrum
  - But greatest for middle one-fifth of Australians
  - Population ageing already evident in income outcomes
- Can we maintain current largesse given population ageing?

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