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Sharing the national cake in post reform New Zealand: income inequality trends in terms of income sources

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Abstract

Using Household Economic Survey (HES) data in unit record form, this paper examines the trends of household income inequality in New Zealand over the period 1984–96, a period that saw New Zealand implement a wide range of economic and social policy reform. The observed changes in the overall income inequality are then decomposed by income components to measure the contributions of the different sources of personal income to the overall inequality. To our knowledge, this is the first time that the methodology for disaggregating the Gini co-efficient, including its more recent extensions by Lerman and Yitzhaki [Review of Economics and Statistics 63 (1985) 151]; Podder [Review of Income and Wealth 39 (1993) 51]; and Mookherjee and Shorrocks [Economic Journal 92 (1982) 886], has been applied to micro-level New Zealand data for computing income inequality and other, related, indices and measures reported in this study. The findings, which indicate a steady upward trend in income inequality, are examined in the light of the reform policies used at the time. Their implications for policy are also addressed.

Keywords: Income; Inequality; New Zealand

1. Introduction and the objectives of the paper

This paper investigates the recent trends in New Zealand's income distribution, and examines empirically the sources from which the observed increases in

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income inequality have stemmed. The period between 1984 and 1996 – the period of this study – saw New Zealand implement a wide range of economic and social policy reforms. These reforms involved, inter alia, the deregulation and/or privatization of many previously state-controlled activities; freeing-up of the financial market, capital flows and the exchange rate; removal or reduction of trade barriers, reform of the tax system and other fiscal arrangements; fundamental alterations to the laws governing the labour market and industrial relations; granting of formal autonomy to the central bank, and reductions in many social welfare benefit payments as part of an overall policy of reduced government involvement in the economy and society. There is a growing body of literature examining the policies used by New Zealand, and their outcome. The interested reader in referred to the article by Evans et al. (1996) and the collection of studies edited by Silverstone et al. (1996) for a detailed overview. Although a definitive verdict on the reform programme to date is yet to be delivered, it is frequently hailed as a successful experiment (Henderson 1996; Evans et al., 1996) which offers many useful lessons for other countries facing a policy quandary similar to New Zealand's in the early 1980s. The underlying aim of the reform programme, it would be useful to remember, was primarily to shift the policy emphasis from stabilisation and equity, a long-established tradition in New Zealand's public policy-making, and focus economic efficiency (Bollard, cited in Kelsey, 1995, p. 53). Naturally enough, the policies used have affected the lives and livelihoods of many New Zealanders in major ways.

However, the question as to who benefited how much from the reform measures is one that has not, as yet, been adequately addressed. A major test of any economic policy measure is how it affects the size of the 'national cake', i.e. the nation's real income, and its growth rate. A second, related, test is how it affects the manner in which the 'cake' is divided up amongst different groups in society. It is this latter issue that the present paper addresses.

The study is based on unit record data from the Household Expenditure and Income Surveys (HEIS) for 1983/84, and 1991/92, and the Household Economic Survey (HES) for 1995/96, specially made available at our request by Statistics New Zealand. Several other studies have addressed the issue of inequality and income distribution in New Zealand (Bakker, 1996; Barker, 1996; Creedy, 1996 and Creedy, 1997; and Easton, 1996, for example) in recent years, but without the use of unit record data. There are also the studies that have examined inequality mainly from a labour market perspective. The study by Winkelmann and Winkelmann (1998) for example examines the labour market outcomes, in terms of employment and incomes, for immigrants in New Zealand with the help of data primarily from the 5- or 10-yearly population censuses between 1981 and 1996. This study does not look at the distribution of incomes as such, but at the income differentials within immigrant groups, and between specified categories of immigrants and native-born New Zealanders. Dixon (1996) is concerned with the distribution of individual earnings. Within its narrow focus, it concentrates ''on the