BIGMUN 2018
International Labour Organisation (ILO)

Research Report

Topic 1: The issues of projected wage inequalities of 2050

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Introduction:

Wage inequality is a difference in wages, commonly based on the different values assigned to different skills and occupations. In capitalist systems, it is unavoidable. Some would argue that it incentivises hard work, leading people to seek success and gain skills. In moderation, it is a key element in market economies. However, if inequality grows too large, it has many unfavourable consequences. The 10th goal for sustainable development, as put forth by the UN, is to "reduce inequality within and among countries."[1] This report will provide information about why, what, and where wage inequality is, establishing a common base for creating projections, and goals to achieve them, for 2050. Focus will be on the type of income inequality which occurs between the highest and the lowest paid workers within countries, or phrased differently, national income distribution among individuals and households. Delegates are expected to research how rising wage inequality may affect their interest groups, and how they best can be protected.

Definition of Key Terms:

Gini Coefficient: "The Gini coefficient is a statistical measure of distribution. It is used as a gauge of economic inequality, measuring income distribution or wealth distribution among a population. The coefficient ranges from 0 (or 0%) to 1 (or 100%), with 0 representing perfect equality and 1 representing perfect inequality."[2] It is calculated by expressing the national income of a country through the Lorenz curve (see below) and calculating the area of actual income distribution divided by ideal income distribution, or line of equality.

$Gini\ coefficient = \frac{A}{A+B}$. The larger the area of A is, the greater the inequality is.

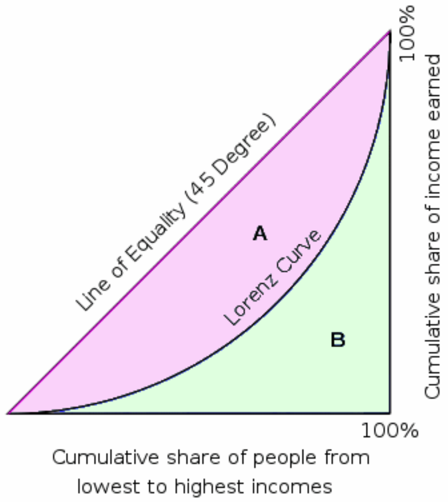

Figure 1: the Lorenz Curve
(accessed 17/01/18, https://www.intmath.com/blog/mathematics/the-gini-coefficient-of-wealth-distribution-4187)

[1] (UN, 2017)
[2] https://www.investopedia.com/terms/g/gini-index.asp

GDP: GDP, or gross domestic product, is the standard method of measuring the productivity of a given country. It is usually calculated annually, and is the monetary sum of all services and goods produced within a country. There are two main ways of calculating GDP, each striving to capture the productivity as accurately as possible. There is the income approach and the expenditures approach. The former measures GDP through the wages, rents, interests and profits from production of services and goods. Most people also include sales and property taxes in the income approach. The expenditures approach begins measures GDP with money spent on goods and services. One can address GDP per annum, or GDP per capita – which is GDP divided by the nation's population.

Welfare state: "The welfare state refers to a type of governing in which the national government plays a key role in the protection and promotion of the economic and social well-being of its citizens."[3]

Fiscal policy: Using taxation and government spending to regulate and influence a nation's economy.

Free market: An economic system where the government has no control or direct influence over a nation's economy, and market forces are trusted to keep the economy stable.

Collective bargaining: "Collective bargaining is the process of negotiating the terms of employment between an employer and a group of workers."[4]

Central banks: "A central bank or monetary authority is a monopolized and often nationalized institution given privileged control over the production and distribution of money and credit."[5]

Background Information:

The word inequality often has negative connotations, but many argue that wage inequality is not necessarily bad. It is a major component in capitalist economies, and it provides incentives to work and innovate. If an economy is functioning well, wage inequality is at a minimum, however still provides incentive. In such an economy, national GDP should have a steady growth rate. Along with this, wages should also increase, as they are a subset of GDP. This leads to increased consumer spending, increased hiring, increased government investment in public services and better education. All in all, a healthy and thriving economy. This is sometimes referred to as the virtuous cycle[6] (see The Virtuous Cycle).

[3] https://www.investopedia.com/terms/w/welfare-state.asp
[4] https://www.investopedia.com/terms/c/collective-bargaining.asp
[5] https://www.investopedia.com/terms/c/centralbank.asp
[6] (Reich, 2017)

The problems arise when inequality becomes too great. If too much of the national income is going to a small percentage of wealthy people, there is not enough for the rest. The effects of too much inequality are strong because it mostly affects the middle class – which is the main consumer group. Wages stagnate, even as GDP grows. The virtuous cycle is replaced with the vicious cycle. The main problem is that consumers spend less – this means that factories produce less since fewer products are sold, businesses must cut back on employers, and unemployment rises. In this situation, the government will most likely cease to invest as much money into the public – meaning worse education, less healthcare, and fewer public institutions. Unemployment rises further, personal and public debt rises, spending falls even more, and so on, in a vicious cycle (see The Vicious Cycle). [7] Inevitably, GDP growth rate falls. If accepting this economic model, the debate arises when trying to pinpoint when income inequality is at an acceptable level, and how to keep it there.

It is interesting to note that in the US, inequality was at its highest right before the crash of Wall Street in 1929, and before the one in 2008 (see figure 2). Both events threw the global economy into chaos. This indicates that excessive inequality leads to debt bubbles and market crashes. From a more social viewpoint, excessive income inequality reduces overall life quality and creates tension between rich and poor, as well as non-economic forms of inequality brought on by worse education, such as the suppression of minority groups.

Much theorizing has been done by economists to explain and predict economic inequality, but perhaps the most accepted theory is the one postulated by Simon Kuznets. It states that as a capitalist economy develops, inequality rises. Then, when average income reaches a specific level, inequality begins to fall. This is attributed to the forces of democracy and the expected development of a welfare state.[8] However, it is not clear whether this hypothesis is correct – but some countries, such as Finland or other Scandinavian countries, seem to be developing in the predicted manner.

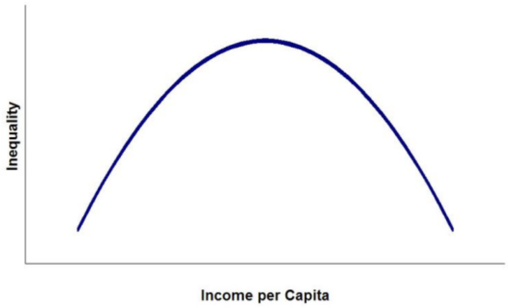

Figure 2: Kuznets hypothetical curve.
In reality, the curve is not smooth.
(accessed 2018-01-05: https://www.thoughtco.com/kuznets-curve-in-economics-1146122)

[7] (Reich, 2017)
[8] (Moffat, 2017)

However, many countries seem to disprove this hypothesis. In fact, the global average of national inequality (with population size considered) has increased by 11% between the 1990 and 2010.[9] Kuznet would claim that this is because the necessary development has not yet taken place. Not all would agree. Kuznets hypothesis is dependent on the view that democracy is the optimal form of government, and that a welfare system is the best system a nation can function by. This is disputable. Many people, and political parties (such as the American republicans), believe that the high taxation that follows a welfare state is unfavourable. According to them, the government should try to regulate as little as possible.

This sparks the debate of whether extensive fiscal policy, minimum wage, and taxation are beneficial or hurtful to business and the economy. Whether they reduce inequality or not. Is a completely free market the best way to organise an economy? How much regulation is needed, if any? Sweden's GDP, a country with a Gini coefficient of 24.9, was in 2016 comprised of 51% taxes and other revenues (GDP calculated by household and government consumption, investment in fixed capital and inventories, and export and imports of goods and services)[10]. In comparison, USAs GDP, with a Gini coefficient of 45, was comprised of 22% taxes and other revenues.[11] Furthermore, according to the OECD, Swedish inequality rose as taxes, especially those targeting the wealthy, were lessened. This could imply that taxation and a welfare state do reduce inequality. The movie Inequality For All, based on a book by the renowned economist Richard Reich, also shows a correlation between taxation and equality (see figure 2).

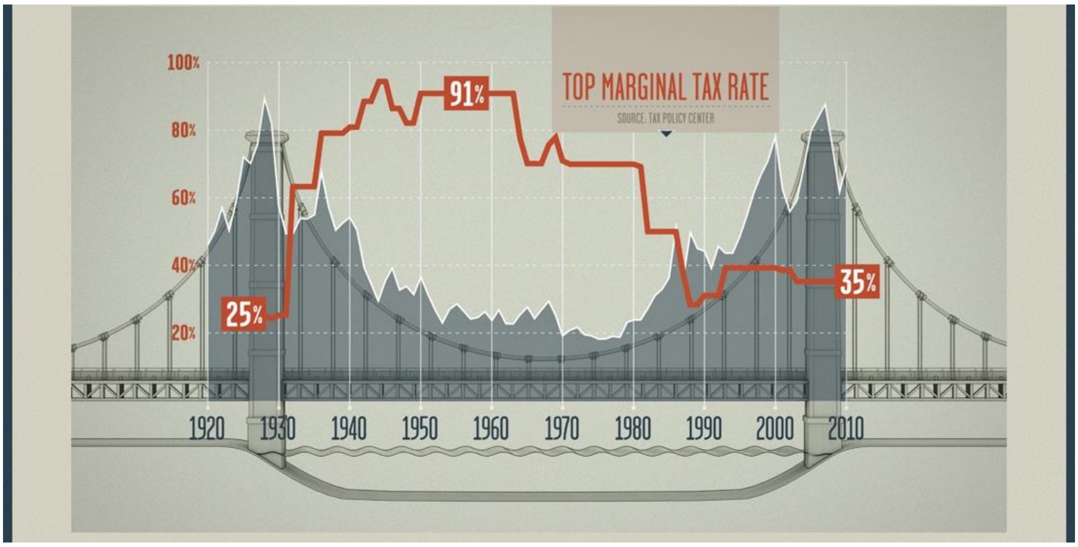

Figure 3: Inequality and tax rates
The grey graph shows inequality, measured in what percentage the highest paid 1% makes out of all national income. At the two peaks, that 1% took home more than 23% of income. At its lowest, it was about 9%. The red line is the top marginal tax rate, and the percentages on the y-axis are reflective of this.
(accessed 2018-01-05: http://inequalityforall.com/resources/#/30)

[9] (UN, 2017)
[10] (CIA, u.d.)
[11] (CIA, u.d.)

However, throughout history, much of popular Western economic theory has asserted that fewer and lower taxes are better – classical economic theory postulates that the government should not interfere with the market at all, allowing for supply, demand, production, and employment to follow its "natural" course. Neoclassical theory agrees. John Maynard Keynes, the father of Keynesian economic theory and perhaps the most famous economist ever, asserted that economies work in a boom and bust pattern. This means that inflation, prices, and employment rise and then abruptly fall, only to begin over again. The way to deal with this, according to Keynes, is to control money supply – a method that is exemplified by central banks – and government spending. He contradicts classical theory by supporting government intervention through government spending, intervention policies, and active stabilisation. Taxes should be low, but regulation should be present and ever-changing to fit the state of the economy.[12] (see Classical, neoclassical and Keynesian economics).

There is no final answer to which economic model is best suited for reducing inequality – it is very much a matter of ideologies. Some people believe that heavy taxation and extensive fiscal policy reduces GDP growth and hinders sustainable business, while others say that a welfare state allows for equal opportunities, benefiting the economy. In any case, it would greatly benefit all Members to discuss whether there should be guidelines for taxation and social and public services, such as free healthcare, free education, and so on. The ILO wage reports cited in this report state that indirect economic policies, such as an increase in public services or job availability, greatly influence wage inequality.

In general, most economic forecasts assert that inequality will continue to rise over the next forty years. The OECD released a report regarding this (Gross Earning Inequalities in OECD Countries and Major Non-member Economies), which included this graph:

[12] (Investopedia, u.d.)

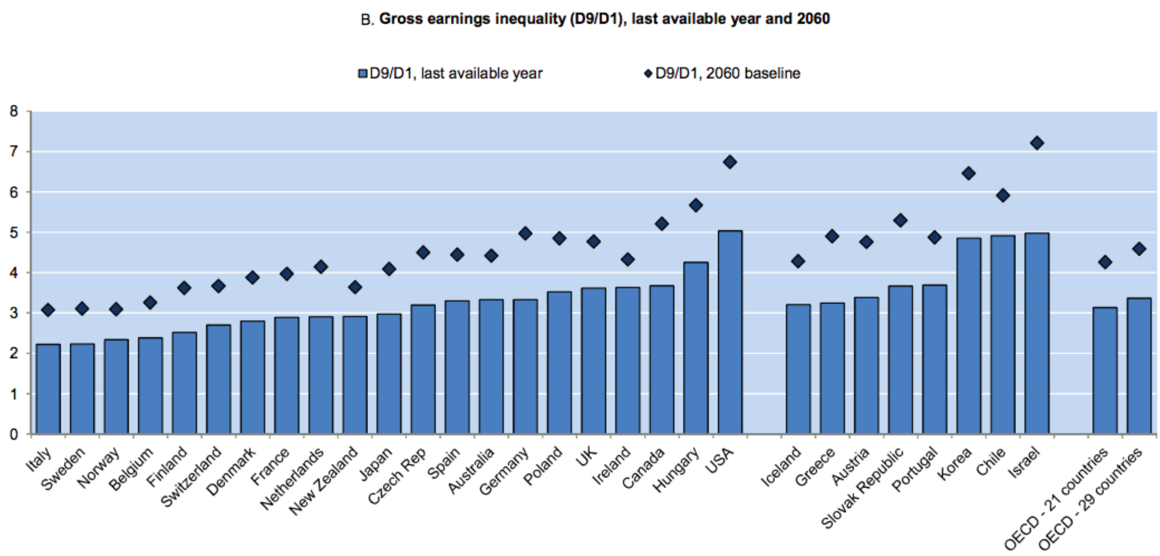

Figure 4: This graph uses gross earning deciles (The highest paid decile D1, and the second lowest, D9) to measure inequality.
Accessed 2018-01-02: http://www.oecd-ilibrary.org/docserver/download/5js3777lbxzn-en.pdf?expires=1514630679&id=id&accname=guest&checksum=716AB22EC7B848C998F2DB64D517DFBA

On average, earning differentials are expected to increase by 30% in OECD countries by 2060. Another figure illustrates that not only will inequality grow, global GDP growth rate will slow. This is relevant as wage inequality is closely tied to GDP growth.

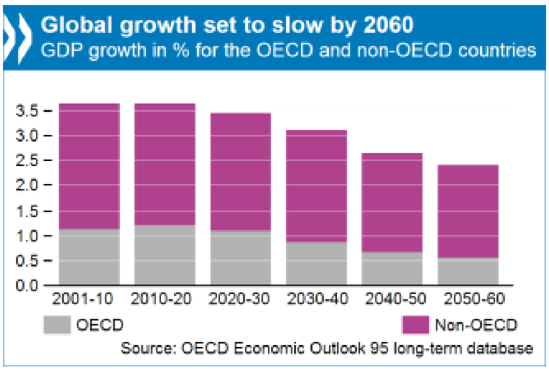

Figure 5:
Many non-OECD countries are developing economies, which is why their GDP growth rate is higher than OECD countries.
Accessed 2018-01-03: http://www.oecd-ilibrary.org/docserver/download/5js3777lbxzn-en.pdf?expires=1514630679&id=id&accname=guest&checksum=716AB22EC7B848C998F2DB64D517DFBA

It is important to remember that the question is not how to eliminate economic inequality (unless one is advocating for communism) – it is; at what level is it acceptable, and how does one achieve that level. Parties involved must be careful not to hinder economic growth and productivity in their quest to reduce earning differentials.

Major Countries and Organisations Involved:

Wage inequality is relevant for all parties, every country, and every individual. On a national level, low inequality generally results in stable GDP growth and reduced unemployment rates.

Governments must decide how heavily they wish to tax their population, whether there should be increased taxes for those making a large amount of money, and, in general, work to ensure that their fiscal policy benefits economic growth and the population.

On a corporate level, businesses must balance profit with adequate and fair wages. It is natural in capitalist economies that CEOs and people in important positions should be paid more that labourers, but how much more? To ensure that economic growth and profit will not be hindered by extensive regulation, it is vital that businesses show their side of the argument, but also remain aware of the plight of the workers.

On an individual level, from the perspective of the workers, each person must act to ensure sufficient and fair pay. The unions representing these workers should cooperate with businesses and the government, but also make sure that their members are taken seriously and paid properly. It is in their interest to ensure fiscal policy that benefits workers as much as possible. The middle class must be protected to ensure a stable economy and adequate, hopefully optimal, living standards.

Relevant ILO Conventions:

Concerning collective bargaining:
C098, passed 01/07/1949 in Geneva at the 32nd ILC session on *Right to Organise and Collective Bargaining*. Available at:
http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO::P12100_INSTRUMENT_ID:312243
C154, passed 03/06/18981 in Geneva at the 67th ILC session on *Collective Bargaining*. Available at:
http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO:12100:P12100_INSTRUMENT_ID:312299:NO

Concerning wages:
C095, passed 01/07/1949 in Geneva at the 32nd ILC session on *Protection of Wages*. Available at:
http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO:12100:P12100_INSTRUMENT_ID:312240:NO
C131, passed 22/06/1970 in Geneva at the 54th ILC session on *Minimum Wage Fixing*. Available at:
http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO:12100:P12100_INSTRUMENT_ID:312276:NO

Concerning equality:
C100, passed 29/06/1951 in Geneva at the 34th ILC session on *Equal Remuneration*. Available at:

http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO:12100:P12100_INSTRUMENT_ID:312245:NO
C111, passed 25/06/1958 in Geneva at the 42nd ILC session on *Discrimination (Employment and Occupation).* Available at:
http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO:12100:P12100_INSTRUMENT_ID:312256:NO

List of all ILO conventions:
http://www.ilo.org/dyn/normlex/en/f?p=1000:12000:::NO

Previous Attempts to Solve the Issue:

Every nation has its own way of tackling wage inequality, some more successfully than others. Often, the advocated economic policies and ideologies that affect inequality are, even just within a country, very different. Political parties all have their own opinions. Businesses and unions likewise. However, businesses are generally more concerned with profit, while unions focus on workers' rights. Each delegate should investigate past attempts within their country to solve the issue. Furthermore, it would be beneficial to research what ideologies and economic policies that the body they represent advocates for.

In Brazil and Argentina, the setting of a minimum wage helped considerably to lessen wage inequality[13]. Although different, but achieving the same effect, some countries have very strong unions (such as Denmark), which allow for collective bargaining to take place easily. The ILO advocates for collective bargaining in the belief that it reduces inequality.[14] Other countries have a strong culture against unions. The reasoning is that, according to some branches of Marxist economic theory, unions will lead to social revolution and then to communism or socialism. This may be a rather extreme view.

Some countries administer wealth tax on dividends, very high bonuses, or high salaries, meaning that the more money one makes, the more one pays in taxes. Of course, many of those who are taxed extra are against this policy – why should they pay more than everyone else, when they have worked so hard to receive the salary they get and achieve the position they are in?

Possible Solutions:

The ILO Global Wage Reports[15] recommend solutions to the problem, as well as stressing the importance of global policy coordination. It is highly recommended to read at least the short versions of both. The points here are subheadings taken from the reports:

[13] (Julián Messina, u.d.)
[14] (ILO, 2016/2017)
[15] (ILO, 2016/2017)(ILO, 2014/2015)

- Minimum wages and collective bargaining
- New initiatives by employers and workers to reduce inequality through collective bargaining
- Top salaries: Enterprise self-regulation or more regulation?
- Productivity growth for sustainable enterprises
- Addressing unequal wages between groups of workers, including women and men
- Fiscal policies, in the form of taxes and transfers, to address wages and inequality
- Policies that affect wages and wage distribution indirectly as important elements of a comprehensive response
- Promoting job creation

Resources

CIA World Factbook, 2016. *Inequality ranked by country.* [Online]
Available at: https://www.cia.gov/library/publications/the-world-factbook/rankorder/2172rank.html
[Accessed 3 1 2018].

CIA, n.d. *CIA World Factbook Countries.* [Online]
Available at: https://www.cia.gov/library/publications/the-world-factbook/geos/sw.html
[Accessed 5 1 2018].

ILO, 2014/2015. *ILO Global Wage Report 2014/2015 FULL.* [Online]
Available at: http://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/---publ/documents/publication/wcms_324678.pdf
[Accessed 22 12 2017].

ILO, 2014/2015. *ILO Global Wage Report 2014/2015 SHORT.* [Online]
Available at: http://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/---publ/documents/publication/wcms_324839.pdf
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Available at: http://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/---publ/documents/publication/wcms_537846.pdf
[Accessed 22 12 2017].

ILO, 2016/2017. *ILO Global Wage Report 2016/2017 SHORT.* [Online]
Available at: http://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/---publ/documents/publication/wcms_537982.pdf
[Accessed 22 12 2017].

Investopedia, n.d. *Investopedia; terms.* [Online]
Available at: https://www.investopedia.com/terms/c/classicaleconomics.asp
[Accessed 07 01 2018].

Julián Messina, J. S., n.d. *Inequality in Latin America.* [Online]
Available at:
https://openknowledge.worldbank.org/bitstream/handle/10986/28682/9781464810398.pdf?sequence=11&isAllowed=y
[Accessed 5 1 2018].

Moffat, M., 2017. *Essential economic terms: Kuznets curve.* [Online]
Available at: https://www.thoughtco.com/kuznets-curve-in-economics-1146122
[Accessed 22 12 2017].

OECD Publishing, 2015. *Structural reforms and income distribution.* [Online]
Available at: http://www.oecd-ilibrary.org/docserver/download/5js3777lbxzn-en.pdf?expires=1514630679&id=id&accname=guest&checksum=716AB22EC7B848C998F2DB64D517DFBA
[Accessed 22 12 2017].

OECD, 2017. *OECD Income Distribution Database (IDD).* [Online]
Available at: http://www.oecd.org/social/income-distribution-database.htm
[Accessed 22 12 2017].
Piketty, T., n.d. *Thomas Piketty: Publications.* [Online]
Available at: http://piketty.pse.ens.fr/en/publications-en
[Accessed 7 January 2018].

Reich, R., 2017. *Inequality for all.* [Online]
Available at: http://inequalityforall.com/
[Accessed 22 12 2017].

The World Bank, 2017. *Databank: World Development Indicators.* [Online]
Available at: http://databank.worldbank.org/data/reports.aspx?source=world-development-indicators
[Accessed 3 1 2018].

UN, 2017. *United Nations Sustainable Developement Goal 10.* [Online]
Available at: http://www.un.org/sustainabledevelopment/inequality/
[Accessed 07 01 2018].