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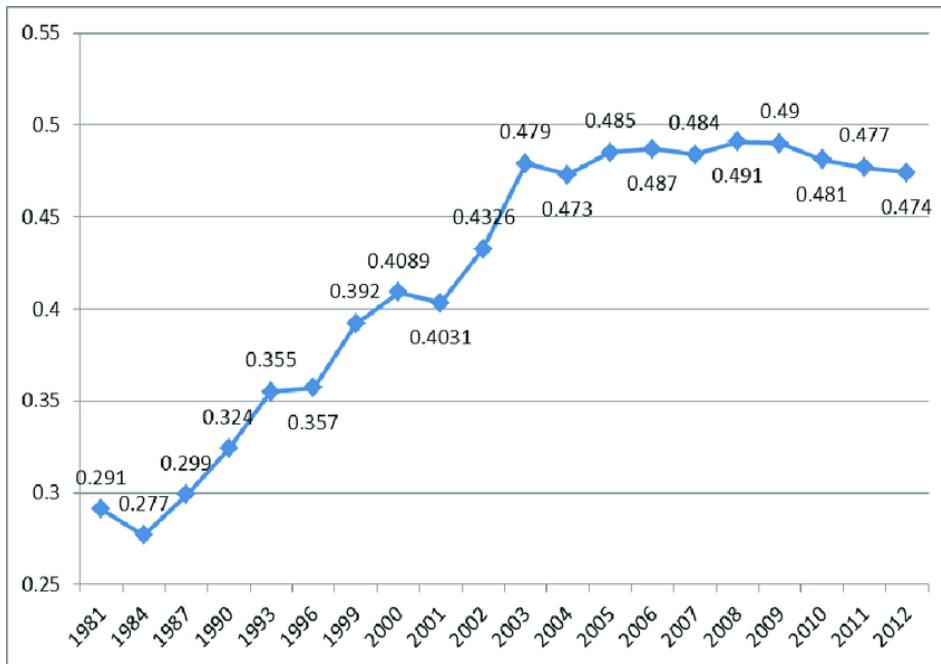
## Economic inequality The origins, myths, and solutions

By Ricky Jiang Fox News



Economic inequality is defined by the disparity of wealth and income within an economy. This means that in a perfectly equal economy, every single person would have the same amount of wealth. However, this is not the case in any countries around the world. Economic inequality can be measured by the Gini-coefficient, which calculates the economic inequality using a scale between 0 and 1. An economy with a Gini-coefficient of 0 would mean that the country is perfectly equal and everyone has the same wealth and an economy with a Gini-coefficient of 1 would mean that one person has 100% of the economy's wealth. Lesotho has a Gini coefficient of 0.63, making it the most economically unequal country in the world, whilst Slovakia has a Gini coefficient of 0.261, making it the most economically equal country in the world.

Economic inequality is not a bad thing to some degree. This is because economic inequality could be a sign of economic growth. If we look at China whose Gini coefficient has risen from a low of 0.277 in 1984 to 0.465 in 2019, we can make the statement that the gap between China's wealthy and poor has increased. However, this does not mean that the poor have gotten poorer. In China, both the rich and the poor are living in much better environments now in comparison to 1984. This is because when there is a degree of economic inequality, nations can progress economically, and wealth can be redistributed to the poor.



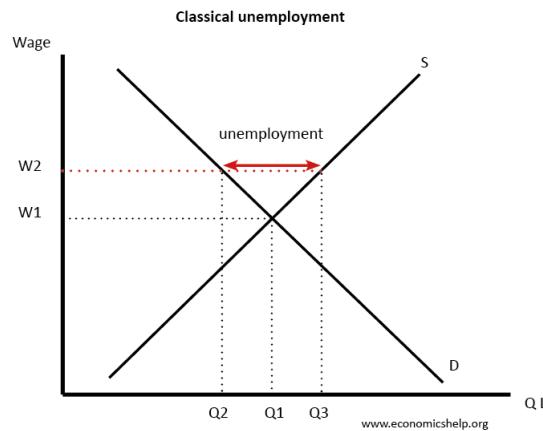
Apart from government policies, there are many other factors that contribute to economic disparities between countries and economies within a country. One of them is geographical locations. For example, Nepal which is situated in mountainous areas suffers, as they are more isolated to other countries, meaning that trade between Nepal and other countries is harder. Age differences between different demographics is another one, For example, the average age of a white American is 58, whilst the average age for an African American is 27. Therefore, it is not fair to compare the income levels of white Americans and African Americans. A more accurate representation would be to compare the income levels at a specific age group. Cultural differences between different demographics can also explain economic inequality. It is a fact that different demographics put more emphasis on things such as education, which can lead to further wealth disparities. Family structure also contributed to economic inequality. Families with both parents involved tend to see their children succeed at higher rates. In the United States, children without a father are five times more likely to live in poverty and commit crimes, nine times more likely to drop out of school, and twenty times more likely to end up in prison. These factors won't be explored in this article but should be noted as a few of the many factors that contribute to economic inequality.

### **Increase the minimum wage**

An increase in the minimum wage would theoretically increase the wage of the lower-class workers, as the lower class would gain more income thus closing the gap between the poor and the rich, right? Well, research has shown that this may not be the case.

An increase in minimum wage laws increases the incentive for business owners to cut staff and reduce their working hours, as the cost to hire them would increase. From the graph below, we

can see that an increase in the minimum wage would cause the demand for jobs to contract, thus causing unemployment.



Minimum wage laws only affect lower-skilled workers who are earning lower amounts of income. In fact, larger businesses welcome minimum wage laws, as this will reduce competition from the industry. Research done by Harvard Business School concluded that a one-dollar increase (USD) in the minimum wage leads to a 14% increase in the likelihood of a 3.5-star restaurant to exit the market, whereas there is no effect on 5-star businesses. This is because smaller businesses simply cannot afford to increase the cost of production, as they will have to bump up prices in general, which leads to less demand for their food, whereas larger businesses can afford this increase in the minimum wage.

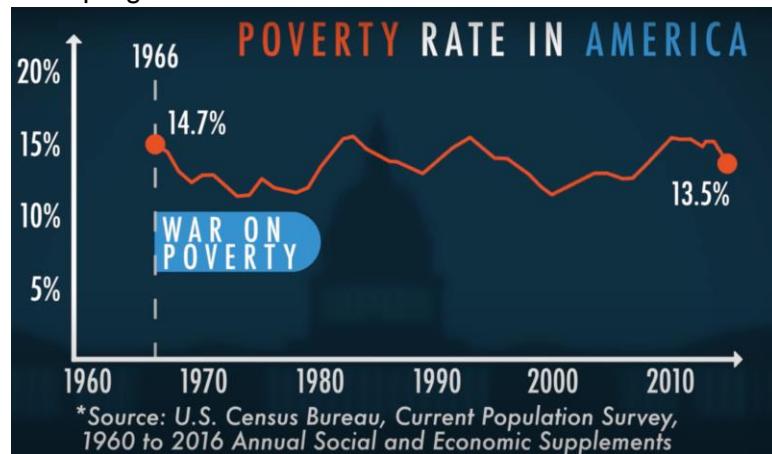
Furthermore, this would increase the cost of living. Businesses will be forced to charge higher prices for their product as a result of higher prices in production. This will affect the overall price of all goods in the economy.

I believe that countries should replicate the Scandinavian countries when it comes to wages. In countries such as Sweden, Norway, and Denmark, they have no minimum wage, but wages are compromised and discussed between unions and the industries. This allows wages not simply to be bounded by one single figure across all industries, but to be determined by the ability of a business to pay its wages to employees. To look at the successes of this model, we can take a look at Norway, which has one of the lowest Gini-coefficients in the world, coming in at 0.275. In comparison to Australia which has a minimum wage law of \$19 per hour, Australia has higher unemployment rates than Norway, and also a higher Gini-coefficient. Ultimately, unions and businesses can come to the most reasonable wage prices, which leads to businesses being able to survive, whilst workers receiving the amount of money appropriate to their skill levels.

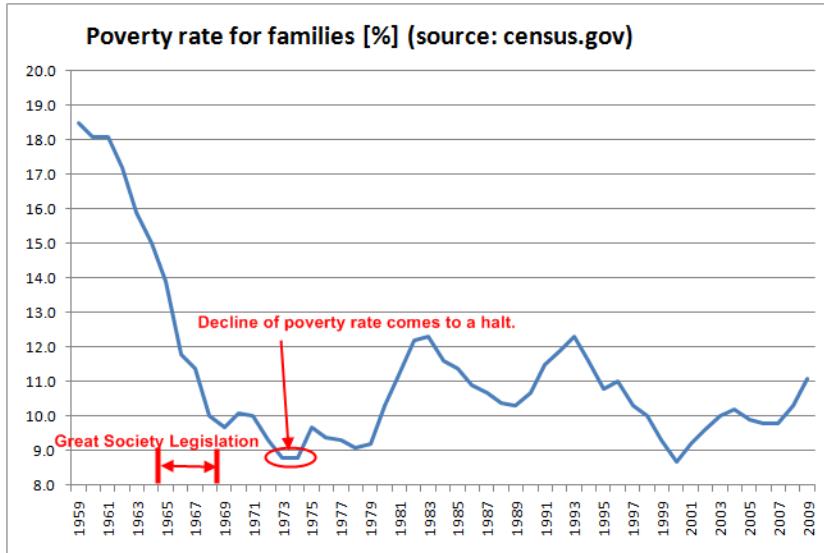
To conclude, evidence has suggested that higher minimum wages do not reduce economic inequality. Contrarily, it could actually increase economic inequality by forcing smaller businesses out of the market, cause unemployment, and also increase the cost of living.

## More Welfare:

Another way in which some people propose to reduce economic inequality is to impose higher taxes on the rich, and for more money to be put into welfare. This again has adverse effects on the economy. The 1960 War on poverty is a case study that we can use to examine the effectiveness of the welfare system. From the graph below, we can see that from the time when the War on Poverty had fully kicked off, the poverty rate in USA had fallen from 14.7% in 1966, to 13.5% in 2017. A mere 1.2% drop, which cost the US Government 20 trillion USD in poverty relief programs.



I think it is also crucial to know that prior to the War on Poverty, the US was actually on a steep decline in regards to teenage pregnancy, murder rates, single-parent families, etc. This led to a dramatic fall in the poverty rate in the US. Several years after the War on Poverty has taken place, we see that the sharp decline in poverty rates actually reverses, and the number of single-parent households, crime rates, etc to increase. In the 1960, 5% of America's children entered the world without parents married to each other. In 2015, the number reached 41%. In a society where families actually benefit from not working and becoming single parents, it comes to no surprise that there would be no incentive to improve their economic status. This highlights the fact that people become overly dependent on the welfare system.



However, if we were to abolish the welfare system, I believe that this would cause mass retaliation and protests, as this would stun many people living on welfare.

### Universal basic income

A universal basic income is essentially a floor for the citizens of an economy, in which it guarantees the citizens a certain amount of money above the poverty line. The theory is that once people live above the poverty line, they will be able to further expand on themselves and work for a better life. This, in my opinion, is a much better approach than the welfare state, as there are fewer incentives to fail. When applying for welfare, it disincentivizes people to look for jobs, because if they do, they will ultimately be kicked off of welfare, and perhaps earn less money than if they were to stay on welfare. With the UBI, it would be condition free, meaning that even if you do have a job, you would still receive this amount of money. Because the amount given to people will be just above the poverty line, people will still have the incentives to work in order to purchase their wants and not just their needs. People will still be employed to work, meaning that they will give back to society whilst receiving the benefits of the welfare system. In a society where automation is becoming more and more prevalent, I believe that UBI can help, especially those jobs with low skill requirements. The UBI has been tried a handful of times, and many politicians and economists are fond of the UBI.

### So how is it funded?

The UBI will be funded by large corporations in the form of VAT (Value added tax), which is tax levied on every point in which the product's value has been sold at an increased value. In Alaska where they have UBI, the money is funded by oil reserve royalties. The amount that will be given is dependent on the politician. If it was to simply be above the poverty line, then \$13,000 USD would be sufficient.

### Has it worked?

Finland stopped its two-year UBI plan in 2018. The positives that can be taken from this is that the citizens who were part of this reportedly had better financial wellbeing, fewer issues relating to physical health and mental health. Recipients of the basic income felt that their financial situation and their ability to influence it was better, and they were also more confident in their financial situation in the future. The UBI has also reduced crime rates. Despite this, many people have claimed that this was ultimately a failure. The results were that the UBI had minor effects on employment, as it did not spur the unemployed to find work, which ultimately resulted in the stoppage of the UBI in Finland.

However, many people have also said that the sample size in Finland was simply too small. This is because the UBI was only tried on 2000 recipients, and low amounts of money were actually guaranteed (560 euros per month).

Whilst the UBI in Finland did not necessarily succeed, I believe that there is still a future for UBI. With more and more jobs becoming automated, we will see a stronger influence on UBI. I believe that the theory behind the UBI is good but needs further research to be conducted.

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### School choice

A way in which economic inequality can be reduced is to give people better educational opportunities. In Norway, Sweden, and many other countries, school choice is given to everyone. School choice is a system in which citizens can choose the school that they want to go to, whether it is a form of public school, private school, charter school, etc. In the USA, low-income families are restricted to their local schools, which in many cases prove to be poor academically, which sets them up to receive an education that is not equivalent of an affluent area where schools are more effective. Parents who pay their tax money on education should have the right to send their children where they see fit. This will also make schools competitive because parents will choose the best school to send their children. In Sweden's school voucher system, it forces schools to compete. Private schools perform better than public schools, and even public schools in the vicinity of private schools perform better, simply because, in order to

stay competitive, they will need to increase the efficiency of their education system in order to persuade parents to send their children to their schools.

The implementation of charter schools in the lower-income areas can also serve to improve educational results. Charter schools are essentially the same as public schools and are funded by the public. The difference is that they operate independently from the established school system, and students are picked by a lottery. This means that they are able to manage funds more effectively and put money where it is most needed. Students go through tougher disciplinary standards, are encouraged to work harder by having longer school hours, and ultimately achieve results equal to or even better than those schools in affluent areas. Teachers in these schools are not protected by the union, meaning that if they don't do a good job teaching, they are fired. This process is not replicated in standard public schools, where teachers who are ineffective in their job, have job security backed by the union. Charter schools unlike traditional public schools in the USA where monopolies form based on the district survive because they attract the clientele necessary for survival. This gives them further incentives to perform well, so that they can attract more clientele, unlike public schools, where it is not necessary for them to advance their educational strategies.

Charter schools have been attacked by numerous groups, and many argue that charter schools achieve results similar to public schools. To an extent, this is a true statement, but not a fair comparison. In charter schools, the majority of the students are Hispanic or African American, whereas, in public schools, the students are White and Asian, and as previously mentioned, different racial groups place different emphasis on education. The fact that these charter schools filled with African Americans and Hispanics are performing to the same level of public schools, indicates that the gap between the results of these demographics have been narrowed, and highlights the successes of charter schools. It is also worth mentioning that incarceration rates and pregnancy rates are lower in charter schools than in public schools.

### **Free trade vs protectionism**

Many people are in favour of protectionism in order to keep blue collar jobs in the economy. Because of free trade, domestic industries cannot compete against the low-cost levels of other economies due to cheap foreign labour. However, history has proven that tariffs can have adverse effects on an economy. In 1929 during the global financial crisis, unemployment peaked at around 9%. Over the next several months, unemployment reduced to 6.3% in 1930. The Smoot Hawley Tariff act passed in 1930 increased the import duties in order to protect American industries from foreign competition and keep jobs in the United States. However, this tariff did not do what it was set out to do, because after the tariff took place, unemployment never fell below double digits in the 1930s. This is because 25 countries retaliated against these tariffs and set tariffs of their own on American goods. We can see similar results on Trump's tariffs on China. China retaliates with Tariffs of their own, and as a result, the general price levels for goods in the USA have increased. Whilst these tariffs may have benefited certain industries in the USA, the general consensus is that the tariffs have had more harm done than good. Of the 20 major manufacturing categories in the USA, only six have grown at a faster rate

as a result of these tariffs, whilst the other industries either didn't experience faster growth rates or lost ground during the period.

### **A closer look at the Nordic model**

The Nordic Model often receives high praises, as the nations have low Gini-index figures. In the Nordic Model, we can observe an economy where economic freedom is at the same level as it is in the United States, but there are significantly higher tax rates on personal taxes. Essentially, it is a free market economy with redistributive factors such as high-income taxes, which are then allocated into things such as education, welfare, pensions, etc. After taxes, an average American has a 27% higher disposable income than a Danish person. The average Danish person pays 50% in consumption and income taxes, whilst earning 15% less than the average American. Therefore, the notion that things such as healthcare is free in the Nordic Model is nonsensical. Furthermore, Denmark did not become rich from this system. Denmark prior to the 1960's, was already a successful nation. They had similar levels of taxation rates in the United States. It was only after-tax reforms in the 1960's, did tax rates become so high.

However, I do believe that because these schools are "free", it allows people from low income households to go to whatever school they want to. In combination to its voucher systems, school choice and charter schools, it ensures that the Swedish citizens have equal opportunity.

The quality and effectiveness of free healthcare and education have to be questioned. In Sweden, approximately 650 thousand Swedes have private health care insurance despite having access to free health care. One of these reasons could include the fact that dental care, cancer treatments and medical repatriation is not given by free healthcare. Private healthcare also offers significantly shorter waiting times for surgery. Swedish law claims that patients should wait no more than 90 days to undergo surgery or see a specialist. Yet every third patient waits longer, according to government figures. Between 2010 and 2015, the number of people with private health insurance in Sweden increased by 50%. Despite education being "free", one in five parents still send their children to private schools. Furthermore, the debt to income ratio for Swedish people are extremely high. Whilst the schools are technically "free", things such as rent are not free. As a result of high taxes, the cost of living is very high. Students who have no jobs or work minimal amounts will have high amounts of debt after graduation. The debt to income ratio in Sweden is 80%, whilst it is 60% in the USA. However, this can partially be explained by the fact that Swedes have more pressure to pay for things on their own.

Another reason as to why these Nordic countries have low economic inequality is that they are largely culturally homogenous. Even immigrants who entered Sweden today previously lived in other Scandinavian countries or Western Europe. These immigrants are highly productive, and even had lower unemployment rates in comparison to native Swedes. 44% of immigrants that come from the Middle East are living on the welfare state, whilst fewer than 7% of immigrants from other countries in Scandinavia and Western Europe lived on welfare.

Ultimately, the redistributive side of the Nordic model cannot be celebrated as the sole factor that reduced economic inequality. A combination of factors including access to education and the fact that it is culturally homogenous, makes these countries economically equal.

## Conclusion

In conclusion, economic inequality stems from a multitude of reasons. In general, I believe that to truly reduce the gap, is to offer everyone equality of opportunity, and not just equality of outcome. This should happen through school choice, charter schools, or possibly the universal basic income, whilst minimum wage laws, welfare and protectionism can potentially harm the economy and its people.

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