



A Moral Response to Increasing Income Inequality: Setting up a Voluntary Solidarity Fund

Professor Josef Bonnici
Governor

May 2016



BANK ĊENTRALI TA' MALTA
EUROSISTEMA
CENTRAL BANK OF MALTA



Voluntary Solidarity Fund

Inspiration from the Gospels

The Parable of the Talents (*Matthew 25:14-30*)

- **Success is a product of our work:** the parable teaches us that we will be asked by our Lord how effective we have been in our tasks
- **We do not all have the same capacities:** diversity is woven into the fabric of creation. But success is measured by the degree of effort according to the talents given to us
- **We work for a higher purpose, not for our own selfish interests:** the money given to the servants is not their own, and the earnings created are not theirs to keep. The servants are stewards of the Master's investment
- **We will be held accountable:** the parable is about how we use our work to fulfill our earthly callings. It is not simply about not wasting a talent, but about not wasting an opportunity to create something with that talent, and for this we will be held accountable



Why increasing income inequality is bad for society - it cannot be part of God's plan

Increasing income inequality is a cause for concern given that it leads to severe negative consequences to society in terms of:

- Inequality of opportunity
- Inaccessibility to education or to develop one's human capital - education has not only become less accessible, but also the consequences of the lack of education are aggravating, leading to lower real earnings for the middle to the more vulnerable parts of society. This embodies the worsening repercussions of increasing inequality of opportunity
- Marginalisation and the inability to live with dignity
- Health and social problems (*Pickett and Wilkinson*)
- Socio-economic decay – "...for the first time, America's children will almost certainly not be as well educated, healthy or wealthy as their parents." (*Gordon*)



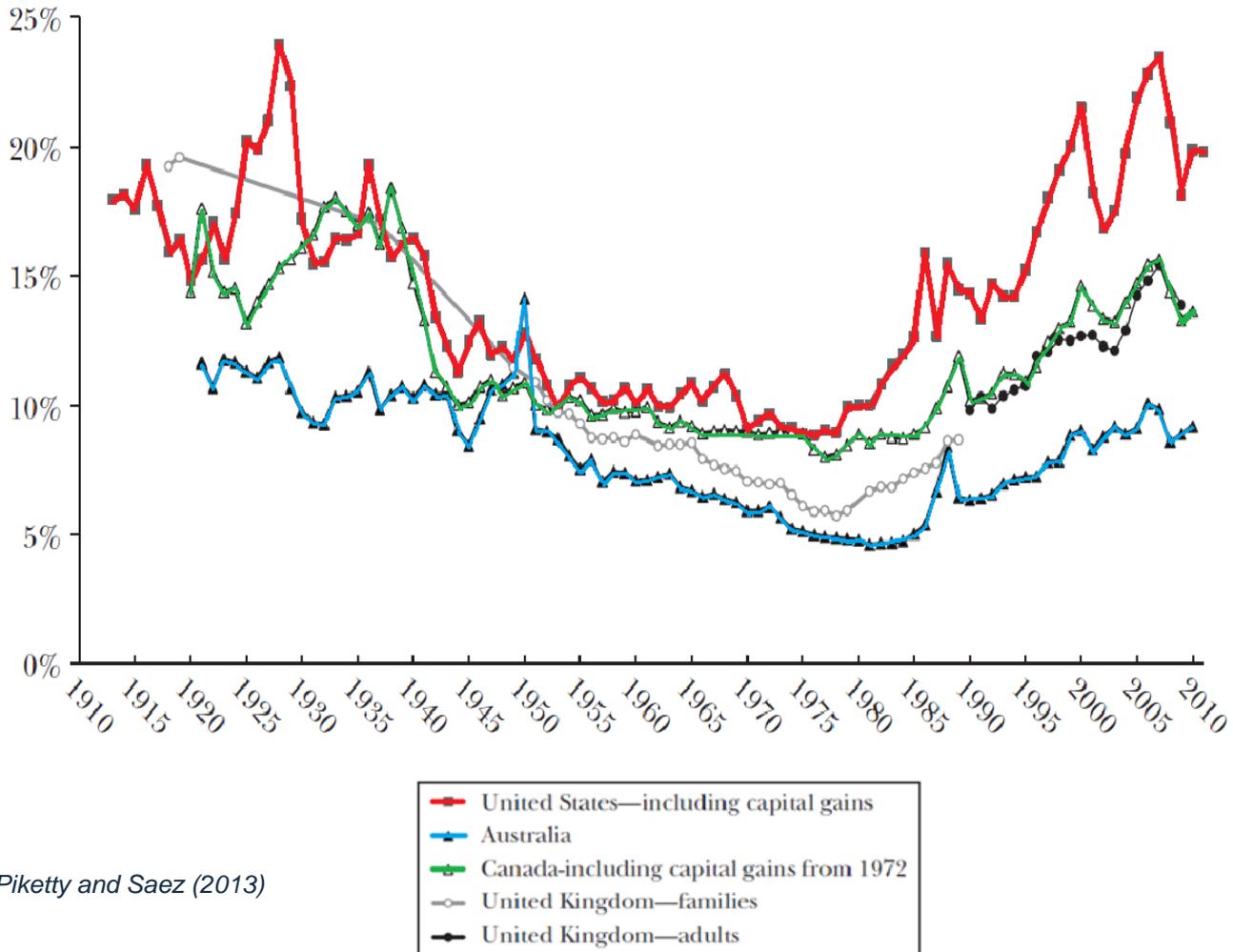
Is the economists' post war paradigm that “Growth is a rising tide that lifts all boats” still valid today?

- The overwhelming evidence points to a worsening situation since the early 1980s, with income inequality increasing and threatening the well-being of society
- In the past 30 years there has been a deterioration in income growth of a significant proportion of the populations in advanced economies which coincided with slower productivity growth
- The top 10% of the population in OECD countries have an average income around 9.5 times that of the bottom 10%. In the 1980s, this ratio was 7:1 - a worsening in the gap of 33%
- In several OECD countries the Gini coefficient is higher now than in 1980 by 3 pp. In the US and UK it is 10 and 7 pp higher respectively
- Increasing income inequality has a negative effect on economic growth and its sustainability (Recent IMF studies)



Evidence of a paradigm shift: the Kuznets Curve and restrained TFP growth

A: Top 1 Percent Income Shares in English-speaking Countries (U-Shape)

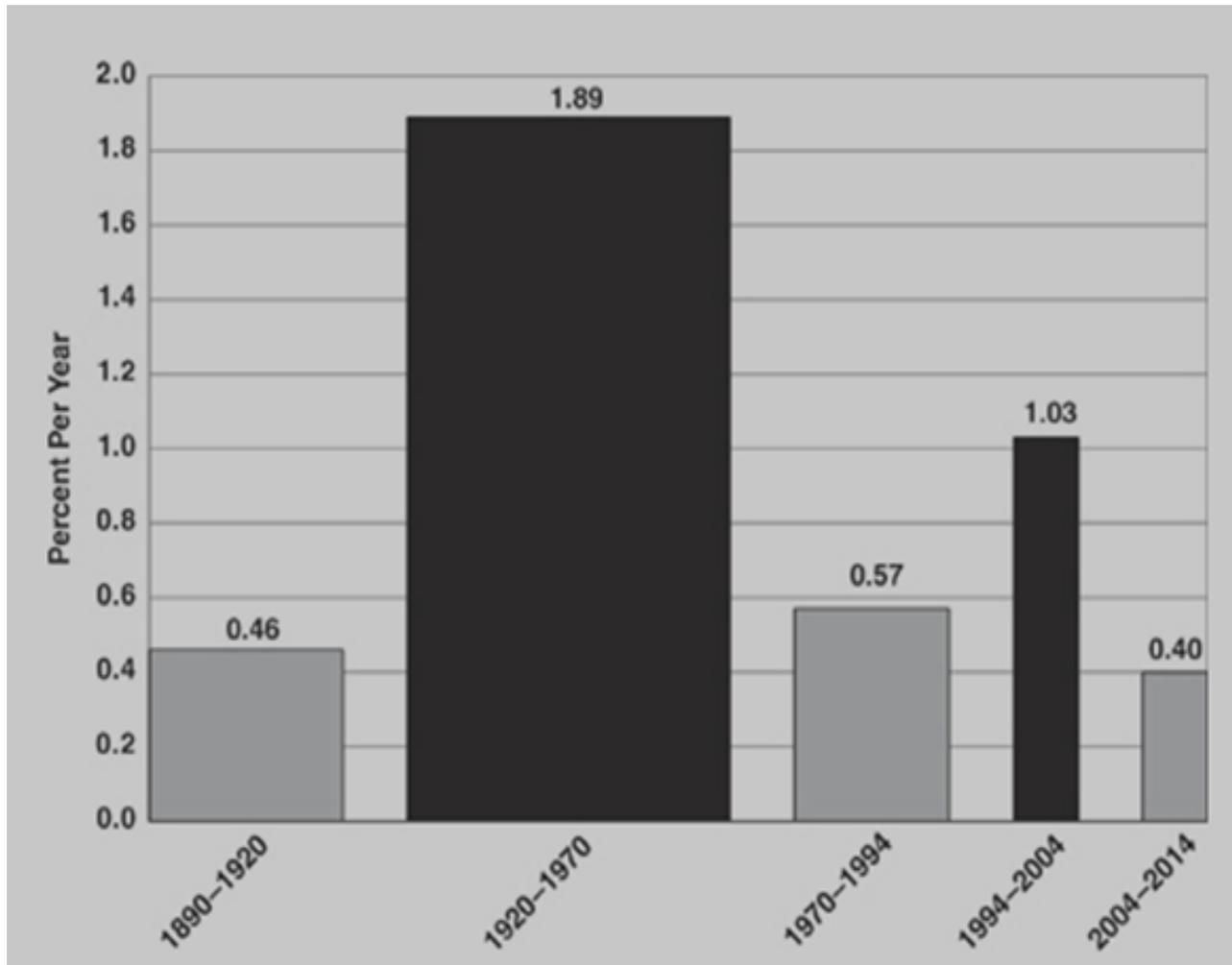


Source: Facundo, Atkinson, Piketty and Saez (2013)



Evidence of a paradigm shift: the Kuznets Curve and restrained TFP growth

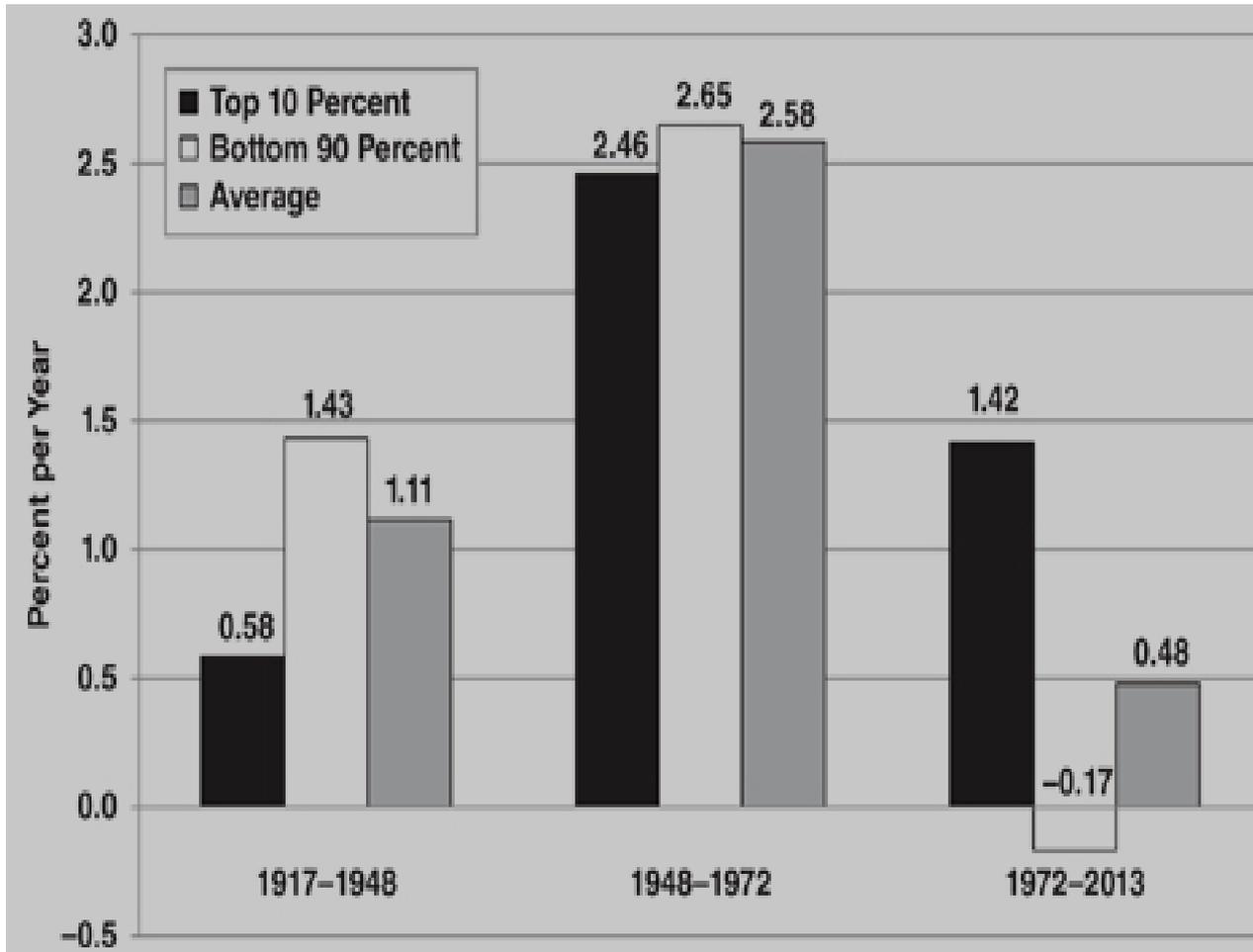
Annualised growth rates of Total Factor Productivity (TFP),
1890 – 2014





Weak growth in real incomes mirror the Kuznets curve and the restrained growth in TFP – especially the bottom 90%

Growth rate of real income in the US: Top 10 percent, bottom 90 percent and average; 1917 – 2013

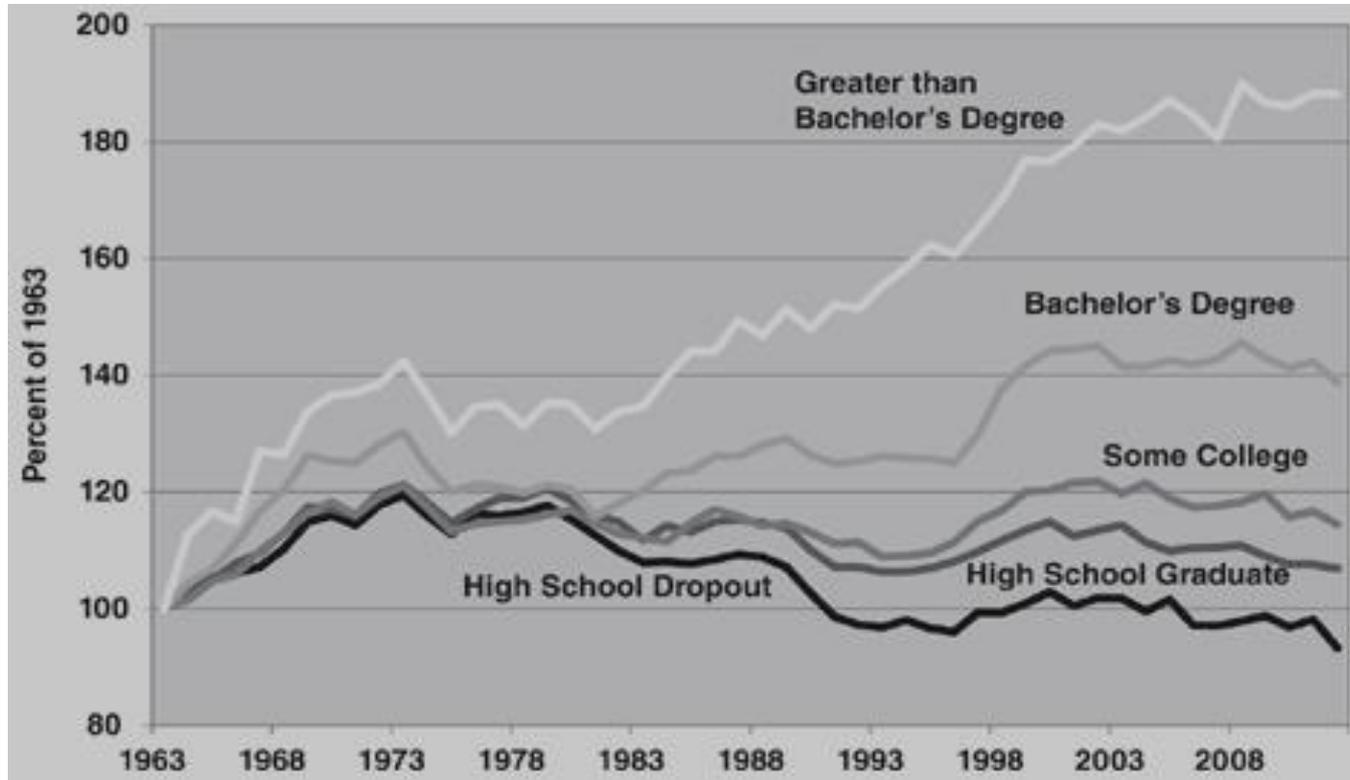


Source: Gordon (2016)



Human capital is the foremost channel of inequality: education attainment has become less accessible and the consequences of not attaining education are aggravating

US Real Weekly Earnings by Educational Attainment, 1963 = 100, 1963– 2012



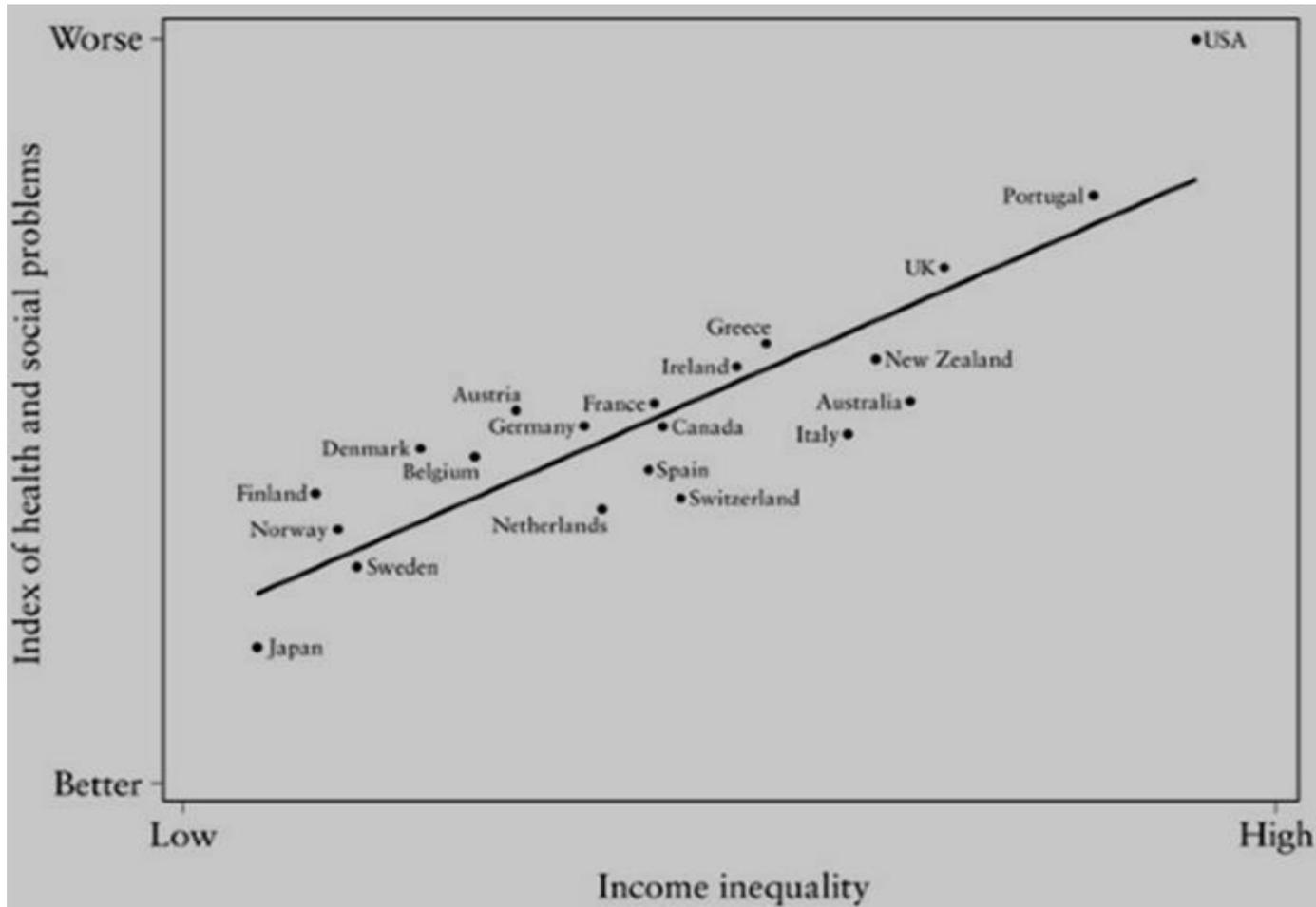
Source: Gordon (2016)

“The cost of a university education has risen since 1972 at more than triple the overall rate of inflation” (Gordon)



“Inequality seems to make countries socially dysfunctional across a wide range of outcomes”

The relationship between the occurrence of health and social problems and income inequality among rich countries



Source: Pickett and Wilkinson (2010)



Confronted with this evidence, what is our moral obligation as Christians?

In the context of this scientific evidence that large groups in society are falling behind at an increasing pace, fundamental questions arise:

- Is it possible to instill a moral obligation for the more fortunate to contribute in preventing further socio-economic decay of those falling behind?
- How to raise this awareness that we are all responsible for each other? How to contribute to the capacity of others to earn a dignified living? How to transform people into better fishermen?
- How to provide opportunities to the better off to contribute to the marginalized, both financially and in a more direct way?



The Voluntary Solidarity Fund aims to answer these questions inspired by the 'Parable of the Talents'

- Our 'talents' need to be used effectively and efficiently to accomplish God's will. A servant should not 'bury' the talents gifted to him
- We make a lot of effort to be productive in developing and investing our own talents. But can we improve the capacity of others to be more productive? Our vocation is to act as catalysts to help others generate their own talents
- It is not enough to be charitable but we should seek ways to enhance the effectiveness in generating a positive outcome for others. Talents should be multiplied and not hidden.



Voluntary Solidarity Fund: *Fundamental Principles*

- ‘Voluntary’ – voluntary willingness to help others is a fundamental aspect of Christian faith. Any charitable effort should be motivated by the moral standards of the individual’s conscience. The act of solidarity has been described in *Rei Socialis* (1987)...“we are all really responsible for all”
- Target – VSF targets the foremost channel of increasing income inequality, including access to education, access to the labour market and supporting the elderly; the VSF can widen its scope by contributing capital to promote entrepreneurship
- Enhanced role within society. The VSF aims to provide parish networks with an extra tool to help the marginalised



Voluntary Solidarity Fund proposed structure: *Funding Sources*

Funding Sources

- a) Bring together individuals, including high net worth persons, embracing the concept of solidarity as promoted by the VSF, to contribute and help in the setting up of a Solidarity Fund.
- b) Proposed guideline contributions: 1% of income (for those earning €100k) or 2% (or higher for those earning €200k or more); a contribution possibly at lower rates for those with lower income is also encouraged.
- c) Participation of private companies; contributing, say 1% or 2% of the company's profits.



Voluntary Solidarity Fund proposed structure: *Mobilizing the Funds (i)*

Use of Funds

The VSF could be set up as a revolving fund providing interest-free loans that would then be repaid gradually once the beneficiary starts earning income from employment

Main areas of marginalisation:

- i. Where individuals may lack the necessary human capital that could see them improve their capacity to contribute to society: support in the form of scholarships and training courses.*
- ii. The identification of meritorious cases could be supported by the networks at the parish level.*



Voluntary Solidarity Fund proposed structure: *Mobilizing the Funds (ii)*

iii. *Where individuals may lack the financial resources to launch a small enterprise:* as a medium term consideration, the fund could be used to promote entrepreneurship.

There is scope for potential partnerships with financial institutions to provide assessment, management and mentoring expertise that would support and fund self-initiative.



Voluntary Solidarity Fund proposed structure: *Governance*

Governance

VSF needs to be built around a strong governance framework supported by:

- a) Technical and managerial competence
- b) Organisational capacity
- c) Accountability and transparency
- d) Internal and external audit processes



Conclusion

- VSF introduces a new dimension to solidarity making it: efficient, effective and economic; enabling it to extend reach and scope.
- VSF's mission is to enhance the capacity of individuals to build their own human capital, to participate in society in a dignified way.
- VSF offers an opportunity to people to meet their moral obligation to help others through an expertly governed structure that enhances the impact of contributions.



Annex

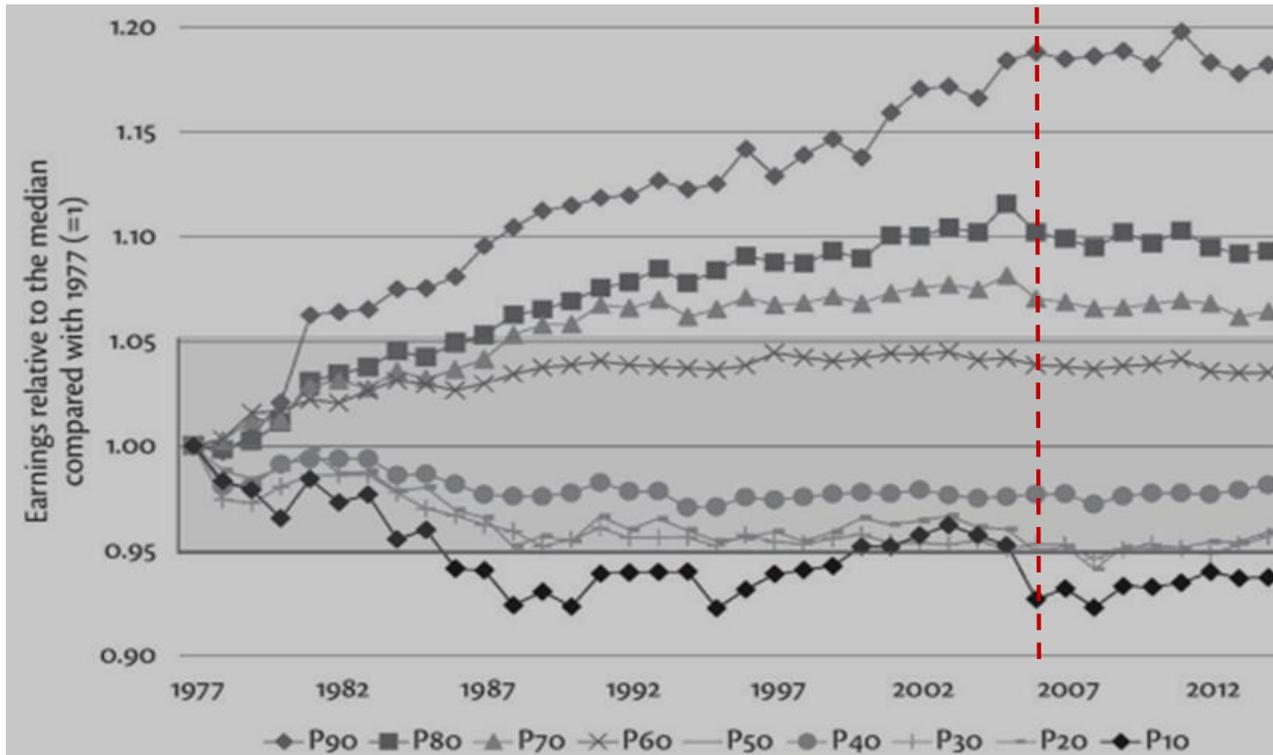


BANK ĊENTRALI TA' MALTA
EUROSISTEMA
CENTRAL BANK OF MALTA



During the last decade, earnings in the UK stagnated for all income groups except the top 10%

Change in earnings in the UK since 1977



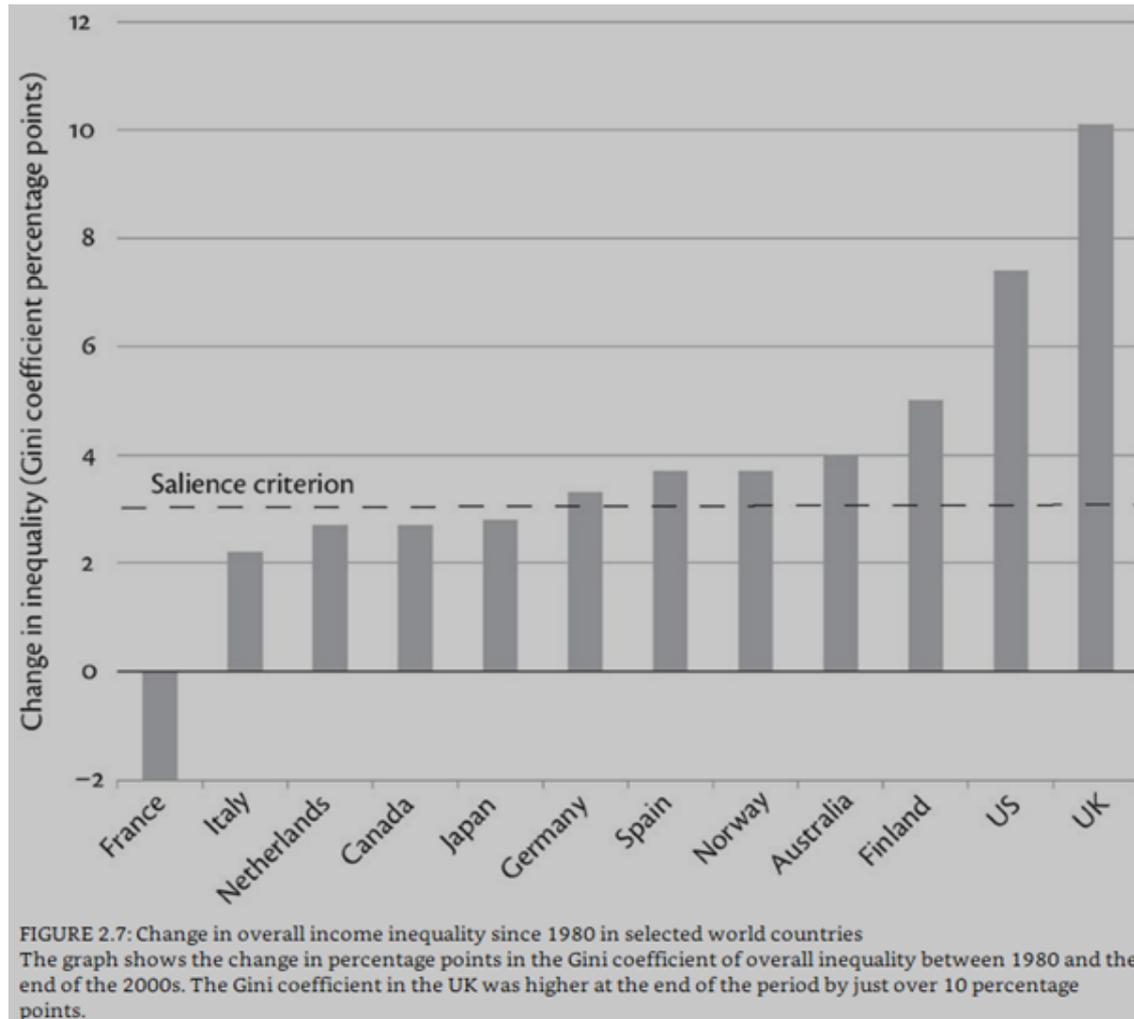
Source: Atkinson (2015)

Data points represent comparisons of different earnings groups with the median earnings indexed at 1977 = 1.0. The graph shows that the relative earnings of people in the top half of the earnings distribution (P90, P80, P70, P60) have grown between 1977 and 2014, while the relative earnings of people in the bottom half (P40, P30, P20, P10) have fallen.



Overall inequality - as measured by the Gini coefficient - has risen in many countries

Change in overall inequality since the 1980s



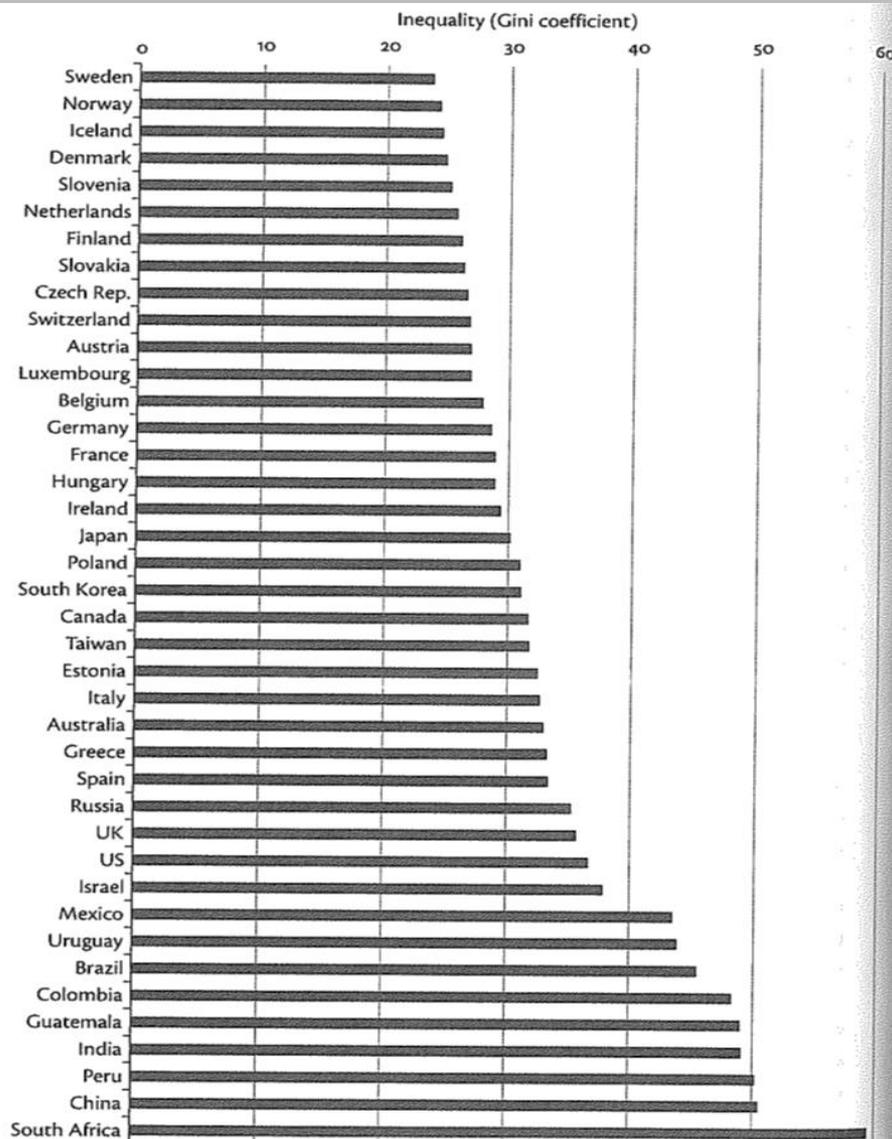
Source: Atkinson (2015)

In France, the Gini coefficient has increased from 28.9% in 2004 to 30.6% in 2011, but this still leaves it 2 pp. below its 1979 value

In several OECD countries the coefficient is higher now than in 1980 by **3 pp.**



Inequality in selected world countries, 2010

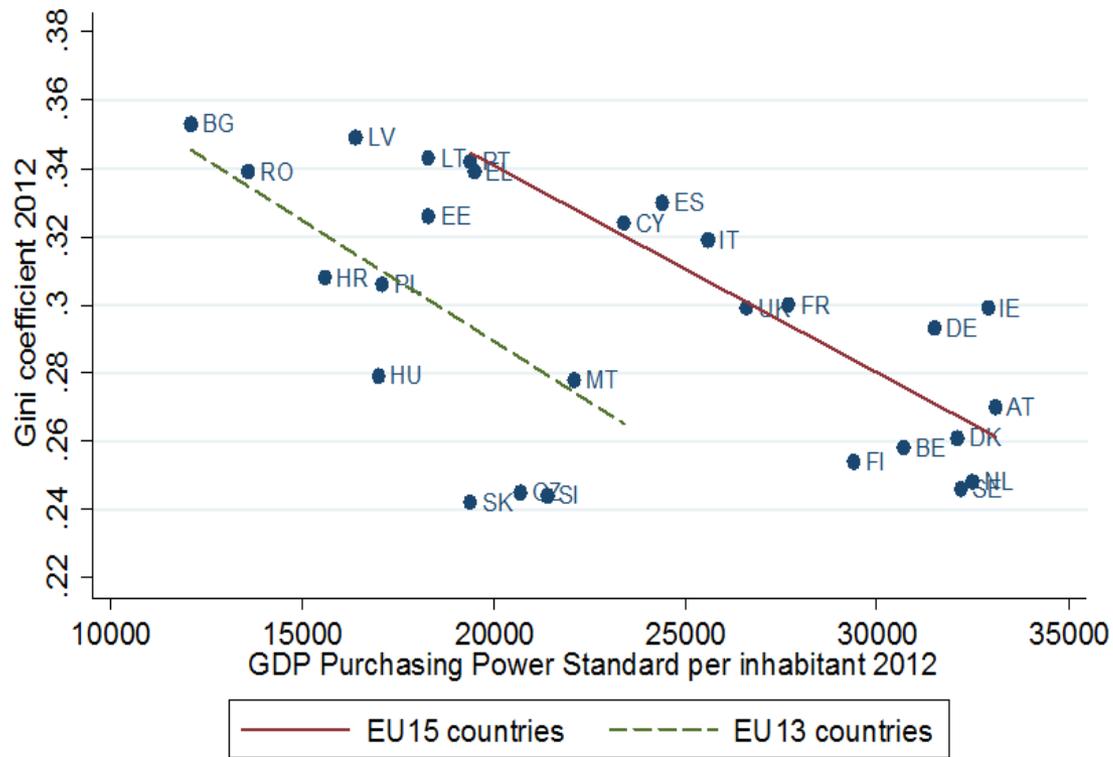


Inequality is measured by Gini coefficients based on equivalised household disposable income (income after taxes and transfers).



Rising inequality has a negative impact on growth

Correlation between GDP per capita and the Gini Coefficient



Note: Luxembourg is omitted from the graph.

Source: European Commission, Eurostat, cross-sectional EU-SILC 2012, UDB August 2015
European Commission, Social Situation Monitor

A higher Gini coefficient and therefore higher income inequality tends to be associated with a lower GDP per capita. A number of IMF studies have also found that income inequality (as measured by the Gini coefficient) has a negative effect on growth and its sustainability (Ostry, Berg, and Tsangarides 2014; Berg and Ostry 2011).



Thank you



BANK ĊENTRALI TA' MALTA
EUROSISTEMA
CENTRAL BANK OF MALTA