Taxing the rich is good for the economy, IMF says

Research paper debunks theory that taxing rich people slows overall growth

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A new paper by researchers at the International Monetary Fund appears to debunk a tenet of conservative economic ideology — that taxing the rich to give to the poor is bad for the economy.

The paper by IMF researchers Jonathan Ostry, Andrew Berg and Charalambos Tsangarides will be applauded by politicians and economists who regard high levels of income inequality as not only a moral stain on society but also economically unsound.

Labelled as the first study to incorporate recently compiled figures comparing pre- and post-tax data from a large number of countries, the authors say there is convincing evidence that lower net inequality is good economics, boosting growth and leading to longer-lasting periods of expansion.

In the most controversial finding, the study concludes that redistributing wealth, largely through taxation, does not significantly impact growth unless the intervention is extreme.

In fact, because redistributing wealth through taxation has the positive impact of reducing inequality, the overall affect on the economy is to boost growth, the researchers conclude.

“We find that higher inequality seems to lower growth. Redistribution, in contrast, has a tiny and statistically insignificant (slightly negative) effect,” the paper states.

“This implies that, rather than a trade-off, the average result across the sample is a win-win situation, in which redistribution has an overall pro-growth effect.”

While the paper is heavy on the economics, there is no mistaking the political implications in the findings.

In Canada, the Liberal party led by Justin Trudeau is set to make supporting the middle class a key plank in the upcoming election and the NDP has also stressed the importance of tackling income inequality.

Stephen Harper’s Conservatives have boasted that tax cuts, particularly deep reductions in corporate taxation, are at least partly responsible for why the Canadian economy outperformed other G7 countries both during and after the 2008-09 recession.

In the Commons on Tuesday, Employment Minister Jason Kenney said the many tax cuts his government has introduced since 2006, including a two-percentage-point trim of the GST, has helped most Canadians.

Speaking on a Statistics Canada report showing net median family wealth had increased by 44.5 per cent since 2005, he added:

“It is no coincidence because, with the more than 160 tax cuts by this government, Canadian families, on average, have seen their after-tax disposable income increase by 10 per cent across all income categories. We are continuing to lead the world on economic growth and opportunity for working families.”

Tax doesn’t kill jobs

The authors concede that their conclusions tend to contradict some well-accepted orthodoxy, which holds that taxation is a job killer.

But they say that many previous studies failed to make a distinction between pre-tax inequality and post-tax inequality, hence often compared apples to oranges, among other shotcomings.

The data they looked at showed almost no negative impact from redistribution policies and that economies where incomes are more equally distributed tend to grow faster and have growth cycles that last longer.

Meanwhile, they say the data is not crystal clear that even large redistributions have a direct negative impact, although “from history and first principles ... after some point redistribution will be destructive of growth.”

Still, they also stop short of saying their conclusions definitively settle the issue, acknowledging that it is a complex area of economic theory with many variables at play and a scarcity of hard data.

Instead, they urge more rigorous study and say their findings “highlight the urgency of this agenda.”

The Washington-based institution released the study Wednesday morning but, perhaps due to the controversial nature of the conclusions, calls it a “staff discussion note” that does “not necessarily” represent the IMF views or policy. It was authorized for distribution by Olivier Blanchard, the IMF’s chief economist.