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## *Economic Recovery to Reduce Income Inequality*

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In the Economic Survey of Japan 2006 released in July, the Organization for Economic Co-operation and Development squarely discussed the growing income inequality in Japan, and this has been attracting a great deal of attention. Although the issue of inequality was already a hot topic of discussion in Japan, it had never before been pointed out by an international agency.

Is income inequality, in fact, growing sharply? Analyses by cool-headed economists have confirmed that the major factor in the growing income inequality in Japan is the increase in the elderly population. This report will verify this finding through various data and demonstrate that the inequality could decline with economic recovery.

### *Slight Increase in Wage Inequality*

In considering income inequality, let us first examine inequality among individuals by analyzing wages and then examine income inequality among households. At the individual level, it is said that economic stagnation and unemployment have heightened the risk of income declines. At the same time, it has been pointed out that income inequality has increased due to the increase in non-regular workers.

With respect to income inequality among individuals, in Japan the problem in the past was inequality due to age, gender, the scale of employer, academic background and employment status (i.e., regular or non-regular employment). Inequality due to age has been largely resolved thanks to the revision of the seniority-based wage system. Gender inequality is also diminishing thanks to the Equal Opportunities Law. On the other hand, inequality due to the scale of employer and academic background is on an upward trend. As for inequality between regular employees and non-regular employees, which has been the focus of attention in recent years, the annual income of part-time workers, who are typical non-regular employees, has for the past 10 years, remained unchanged at 32 to 33 percent of that of regular female employees. By contrast, the annual income of temporary helps, whose number has been increasing sharply, has risen from 70-79 percent of that of regular female employees to 80-89 percent of that of regular female workers, thus reducing the inequality.

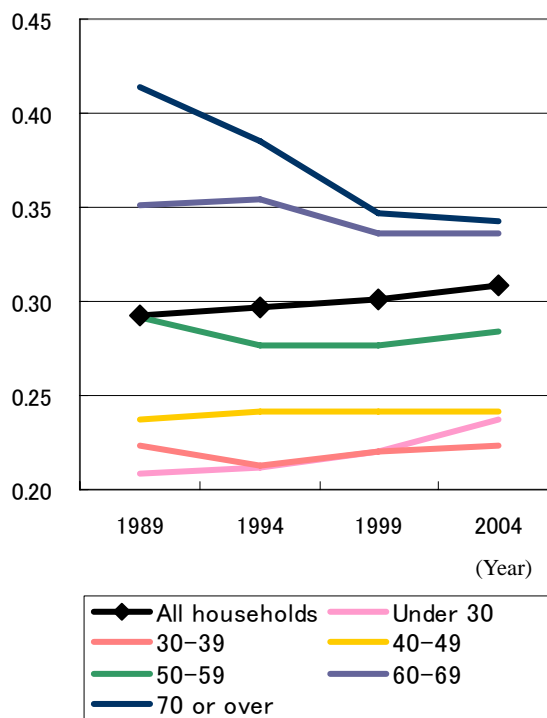
Another focus of the discussion on inequality is inequality among workers in the same age group. It is widely recognized that in the case of young workers, inequality within the age group is small, however, as workers get older, the inequality grows. With respect to regular male employees, when the wage at the ninth decile is divided by that at the first decile, it is found that since 1990, inequality has increased in the 60 to 65 year-old age group (which may be attributed to the growing scope of jobs available to people after their retirement). For people below 60 years of age, inequality declined in the mid-1990s, but has increased again to the level that prevailed in the early 1990s. Given the fact that after the economic bubble burst in the early 1990s, many businesses re-examined their seniority-based wages and switched to performance-based ones, a considerable increase in income inequality has been expected. One may even conclude that actual wage inequality has not increased as much as expected.

### *The Reduction of Income Inequality among Households*

The examination of wage inequality alone would leave out retirees. To observe overall inequality, which also includes the elderly, it is necessary to examine household statistics. Household income includes not only the income of the head but also other members of the household. Therefore, in discussing inequality, it is important to look at household income rather than wages.

To what extent, then, has income inequality among households increased? Chart 1 shows that the Gini coefficient for all households has increased, giving the impression that inequality in Japanese society is increasing. However, when inequality in the same age group is analyzed, as in the case of wages, it is found that while the Gini coefficient for those under 30 has increased, that for other age groups has remained unchanged or declined. In the elderly households, in particular, inequality has diminished sharply and incomes have been leveling, thanks to the maturing of the pension system. The rising inequality for all households, despite the fact that inequality has not increased in any age group except that of under 30, may be attributed to the increase in elderly households. Otake (2005) analyzed this point in depth and

**Chart1: The Gini Coefficient of Annual Income by the Age of the Head of the Household**



Data: Ministry of Internal Affairs and Communications, *National Survey of Family Income and Expenditure* (Two-or-more-person households).

verified that the greater part of the rise in income inequality (after adjusting for household size) between 1984 and 1999 can be explained by the increase in elderly households.

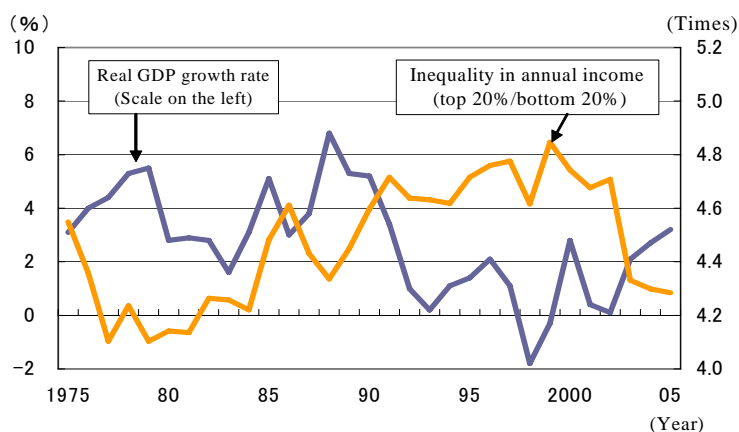
Conducted from many angles, these analyses of inequality in the wages of individuals and household income have produced the following results. 1) Traditional wage inequality due to age, gender, etc. has declined; 2) wage inequality between regular and non-regular employees has remained more or less unchanged; 3) income inequality in the same age group, which has been the focus of attention, has increased for the young but has remained unchanged or diminished for the middle-aged and the elderly; and 4) the increase in inequality in household income can largely be attributed to the increase in elderly households. These examinations of inequality based on gender, age, mode of work, etc. reveal the segment of the Japanese economy, in which inequality is emerging. In order to deal more fully with the problem of inequality, it will be necessary to conduct these cool-headed examinations on a broader scope.

For example, the OECD's Economic Survey of Japan 2006, which this writer mentioned at the beginning of this report, pointed out that not only inequality but also the poverty ratio has increased in Japan. However, in its Annual Report on the Japanese Economy and Public Finance, which it released in July, the Cabinet Office of Japan presented a counterargument to this OECD view based on an in-depth analysis. If careful analyses pertaining to inequality are made from numerous angles in response to problems raised, as in this example, discussion of this issue will become more constructive and grow in depth.

### *Negative Correlation between Economic Condition and Inequality*

Before concluding, the following is a preview of the direction of inequality relative to the economic condition. Chart 2 shows that there is negative correlation between the rate of increase of real gross domestic product and the inequality in annual household income. This relationship is statistically significant even after taking into consideration the factor of the aging population. Because the mechanism of generation of this relationship is not known, the following is no more than a conjecture, but it could be argued that when the economy expands, there is a quick recovery in jobs for the low-income stratum.

**Chart 2: Economic Condition and Income Inequality**



Data: Ministry of Internal Affairs and Communications  
*Family Income and Expenditure Survey*  
 (Two-or-more-person households).

In any event, it appears that since the 1970s, inequality in Japan has worsened when business conditions were poor and improved when the economy was buoyant. If this relationship were to hold true in the future, it is highly likely that income inequality in Japan will diminish as the economy expands steadily. A survey by Works Institute of Recruit, a private organization, shows that in fiscal 2005, which ended in March 2006, 1.23 million new regular employee jobs were offered to people who were already in the labor force, while in fiscal 2006, this figure is expected to increase by 30 percent. Thus, the employment situation appears to be improving steadily not only for those who are coming out of schools but also for young people who are willing to take on a new challenge. people who were already in the labor force, while in fiscal 2006, this figure is expected to increase by 30 percent. Thus, the employment situation appears to be improving steadily not only for those who are coming out of schools but also for young people who are willing to take on a new challenge.

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