



interesting to observe not only the ordering of the curves for the various countries (the ones that lie to the right are the farthest from the 45-degree line and thus indicate a country with more inequality), but also whether the lines cross and where. Until the thirty-fifth percentile, Finland is the country in which the poorest families earn the smallest fraction of total earnings. From that percentile on, the U.S. emerges as having greater income inequality than Finland or any of the other countries we study.

Economic theory (for a survey, see Mortensen and Pissarides, 1999) suggests that workers' labor decisions depend, among other things, on the social security safety net that is in place: In countries with more generous social insurance systems (such as unemployment benefits), workers will be pickier and there will be more people with zero earnings, since they receive transfers from the government. In this case, the workers are deciding not to work, or not to work for a longer period because of the availability of benefits; thus, they may be better off than the workers in countries that do not offer such generous benefits. The incentives to retire early also affect the

number of people at low levels of earnings.<sup>10</sup> These incentives differ across countries, and we provide evidence that they are particularly strong in Finland.

Looking at the earnings of households between the fortieth and eightieth percentiles, the ordering of the countries from most equal to most unequal is Germany, Sweden, Canada, Finland, and the U.S.

Figure 2 displays the Lorenz curves for gross income across the five countries.<sup>11</sup> After adding private and government transfers, the U.S. displays the most concentrated distribution by far for all percentiles. Until the eighty-fifth percentile, the ordering of gross income inequality from the most equal to the most unequal is Sweden, Finland, Germany, Canada, and the U.S. After adding transfers, the poorest people in the other countries are noticeably better off than in the U.S. This is not the case for the earnings distributions in figure 1. As we discussed for table 1, transfers go a long way in redistributing income, especially at the lower levels of

earnings. For all countries but the U.S. and Germany, they are the instrument most used to redistribute income. However, economic theory predicts that a

