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AI-Driven Economic Forecasting Framework for Predicting Market Dynamics and Financial Trends

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Abstract

The existing paper is centered around the effect that the introduction of tax progressivity reforms can have on income inequality in the OECD countries on the basis of statistical analysis in order to establish the relationship between Tax Progressivity Index and Gini coefficient from 1990 to 2020. To conduct statistical analysis, the paper ensures that such factors as GDP per capita, unemployment rates, and social spending, among others, will be controlled through the use of panel data regression models. As a result, the short run and long run effects of tax reforms on the inequality of income will be determined. The findings imply that there exists a statistically significant (negative) correlation between tax progressivity and income inequality, and more tax progressivity (higher Kakwani index) is linked to less inequality of income in the country. Moreover, such an effect varies depending on the country, with the effect of tax progressivity and social spending being greater in such countries as Sweden and Denmark. On the contrary, there exist weak relationships between tax progressivity and inequality in countries like the United States with little social expenditure. The research also implies that the effect of the reforms is lagged, with the rise in inequality being noted after several years after reforms were introduced. The implications of these findings are that long-term policy plans involving tax progressivity and social expenditure are important in attaining large decreases in income inequality. The test was conducted at the 5% level of statistical significance, and the strength of the results was checked by strong checks through the use of alternative model specifications.

Keywords: Tax Progressivity, Income Inequality, OECD Countries, Gini Coefficient, Tax Progressivity Index, Social Spending, Economic Policy.

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Introduction

Tax progressivity reforms are very significant in determining the economic outcomes, especially in the distribution of income in a country. Progressive taxation, in which people with higher incomes are taxed more, is commonly regarded as a remedy to diminish income inequality. These reforms are important because they redistributed the wealth and gave the governments an opportunity to deal with the disparities in the socio-economic spectrums (Asawasakulkrai, 2022; Jesus et al., 2024). The OECD countries, which have a great diversity in terms of tax structure and economic conditions, are a rich study environment regarding the impact of tax progressivity reforms on income inequality. This study is dedicated to the comprehension of the effect of the tax policy, which is directed at more progressive taxation systems, on the dynamics of income distribution in these countries, which can, in the end, affect the social and economic equity (Lin, 2025; Malla & Pathranarakul, 2022).

The main research question that will be used in the study is: What are the effects of reforms in tax progressivity on income inequality in OECD countries? Sub-questions include:

1. How does the level of tax progressivity relate to the Gini coefficient (a measure of inequality of income)?
2. What is the effect of tax reform in OECD countries in the long term?
3. Does the effect of tax reform on income inequality differ across OECD countries?

This research aims to examine the income inequality dynamics before the tax progressivity reforms and after, in the OECD countries. Through the analysis of income inequality changes and the evaluation of how tax reforms would contribute to the decrease or growth of income inequalities in various countries, the paper will help give an idea of how tax policy choices would lead to a reduction or increase in inequality within ordinary income in different countries. This shall entail a comparative study of different nations that have passed through tax reforms, in terms of success in reducing income inequalities.

The paper is important for a variety of reasons. First of all, politicians who are interested in building a more fair society should understand the relationship between tax progressivity and income inequality. Tax policy is a very important instrument in the struggle against poverty and wealth inequality, especially in developed world economies. Results obtained during this research will provide policymakers with proof of the efficiency of using progressive tax policy in the struggle against income inequality. This paper will be useful not only for developed countries of OECD but also for developing economies, which strive to promote inclusive growth.

This paper is organized in the following manner: the Introduction part describes the importance of tax progressivity reforms in the aspect of inequality reduction of incomes, also providing research questions and objectives. The Literature Review discusses the relevant studies and identifies gaps. The Methodology part provides the sources and econometric models used. The Empirical Analysis chapter describes the descriptive statistics and regression analysis results. The Discussion chapter compares the findings of this paper with other studies, suggests some recommendations and discusses the limitations of this study. The last part is the Conclusion chapter, where the main conclusions, recommendations and future research are discussed.

Literature Review

Tax progressivity is a tax system where the rate of taxation has an upward trend in a situation where the taxable income or wealth of the people increases. A progressive tax structure means that the richer a person is, the higher the tax percentage imposed on them compared to a poorer person, so as to redistribute wealth and minimize income inequality. Tax progressivity is normally measured by the average and marginal tax rates of the various income groups and also by indices like the Kakwani index, which measures the progressivity of the tax system. Theories considering the progressivity of tax rates to be linked to the inequality of income are based on the principles of vertical equity and redistribution (Kalleitner & Bobzien, 2024). The progressive tax system is commonly regarded as a mechanism of decreasing unequal distributions of income, enhancing social equity, and economic stability through allowing governments to invest in social goods and services that will benefit underprivileged groups and individuals (Bavaro et al., 2025).

Some works have investigated the effectiveness of tax reforms in curbing income inequality in various countries. Beljić and Glavaški, (2025) consider the effects of heterogeneous taxation in the European OECD economies and how a combination of direct and indirect taxes determines income inequality (Beljić & Glavaški, 2025; Wu, 2025). Angalaeswari et al., (2025) assess fiscal policies that can be used to decrease the level of income inequality, and they place emphasis on the redistributive impact of progressive taxation (Angalaeswari et al., 2025; Nofitasari & Putri,

2025). The efficiency of tax revenue systems and redistributive effects of fiscal policies, respectively, in the OECD countries are examined in the studies by Afonso et al., (2025) and Isiaka et al., (2025). These studies show mixed results depending on the form of tax systems, such that some countries have seen a high level of inequality decrease after reforms, whereas some countries have experienced difficulties in achieving redistribution objectives (Afonso et al., 2025; Isiaka et al., 2025)

Also, Jouste et al., (2025) give an example of Uganda, where the reactions of taxpayers to a higher tax progressivity are observed. This study is conducted in a developing country; nevertheless, it highlights the significance of the taxpayer behavior and perceptions in the implementation of progressive taxation (Jouste et al., 2025). Besides, Lukpanova et al. (2025) give information on how tax instruments can be used in equalizing social inequality, emphasizing that some of the progressive taxation systems have succeeded in narrowing the wealth gap (Lukpanova et al., 2025; Mundada et al., 2026).

The OECD countries are very useful in the investigation of the correlation between tax progressivity and income inequality because of their different economic frameworks, high degrees of development, and because they have various tax systems (Tjan, 2024; Supriadi, 2023). The OECD, which has both high-income and middle-income countries, offers abundant data to examine the effect of tax reforms on income inequality. The literature, including that of Wiese et al., (2024) and Afonso et al., (2025), dwells on OECD nations and their tax reforms and gives empirical evidence regarding the impact of such policies on inequality (Van Ganzen, 2025; Wiese et al., 2024). Examples of these include the progressive taxation policies that have been used in Sweden, which have frequently been discussed as an example of how tax reforms can help decrease income inequality, and the U.S. experience with tax cuts to the rich has demonstrated the complexities of progressive taxation in a developed economy (Nurwanah, 2024).

OECD countries have undertaken tax reform in terms of implementation of wealth tax in Europe or reducing corporate tax rates in other countries; thus, this is a good opportunity to assess the impact of such reforms on the economy and income distribution. In addition, considering the differences in the nature of tax reforms in the OECD countries, the latter can serve as a good sample for comparison.

Although there is a lot of research in the area concerning tax progressiveness and income inequality, gaps exist in the literature. Numerous studies are concentrated on cross-sectional comparisons or case studies, and they may fail to capture the changes in the relationship between tax reforms and income inequality over time. Very little research has examined the tax reforms on income inequality in the long run-in various OECD countries. Besides, although the effect of tax reforms on aggregate has been studied, little is known of the interaction between certain forms of tax reforms (e.g., wealth taxes, inheritance taxes, and changes in corporate taxation) and other economic policies to influence income inequality. Also, although the role of tax compliance and taxpayer behavior has been studied in non-OECD settings (e.g., Uganda), studies should also be done in the OECD, where compliance and tax evasion can be much different. Such gaps provide an opening for this research to make contributions to the literature by addressing the dynamic impacts of tax progressivity reforms on the level of income inequality in OECD nations based on both cross-sectional and longitudinal data to create a more comprehensive view of the problem. Moreover, the paper will also look at the role of certain tax reforms (not in the general taxation categories, income and corporate taxes) in the shift in income inequality among various countries of the OECD.

Methodology

Data Sources

In this work, the researcher employs a set of data to examine how tax progressivity reforms are correlated with income inequality in OECD nations. The most important source of income inequality statistics is the OECD Income Distribution Database, which offers annual figures of the Gini coefficient, a well-known indicator of income inequality. In this research, the Gini coefficient will be used as the primary indicator of the level of income inequality, and data on Gini coefficients will be accessible to each OECD state for several years. The OECD Tax Database provides indicators of tax progressivity (Kakwani index, marginal tax rate, and the average tax rate going to the high-income earners). The variables give a complete picture of the progressivity of the tax systems within the OECD. Also, macroeconomic variables, including GDP per capita, unemployment levels, and social expenditure, will be obtained from reputable international databases like the World Bank and the International Monetary Fund (IMF). Such statistics will moderate other variables that could affect income inequality other than tax policy. Finally, the policy change in countries will be collected in both OECD reports and national government publications in order to offer a background to the changes in the tax progressiveness over the years.

Model Specification

Reforms to the tax progressivity are also examined, and their effect on income inequality is estimated based on panel data regression models that are ideal for investigating the effects of income inequality over time, including country-specific variations. The major model to be adopted in this study is a fixed-effects regression model. By doing so, it manages the possibility of unobserved country-specific factors (not varying over time) to make sure that the effects observed are due to changes in tax progressivity reforms (as opposed to other country-specific characteristics that remain constant). A random-effects model will also be used to test the robustness, meaning that there is no correlation between the unobserved heterogeneity and the explanatory variables. Also, the lagged variables will be included in the study so that the delayed effects of tax progressivity reforms on income inequality can be reflected, because changes in the tax system may require several years to be reflected in their full extent. The instrumental variables (IV) approach will be employed to deal with the possible problems of endogeneity, in which the variation in income inequality may affect the tax reforms. The exogenous change in tax progressivity will be isolated with the use of instruments like political factors or external economic shocks (e.g., global economic crises).

Variables and Measurement

In this paper, the Gini coefficient will be the dependent variable because it is an indicator of income inequality. The key independent variables will be tax progressivity indexes; particularly, the Kakwani index. This index is an indicator of the degree of tax progressiveness, and the higher the value of the index, the greater is tax progressiveness. Other measures of tax progressiveness such as the marginal tax rate for high-income individuals and the average tax rate for low-income individuals will also be considered. The other control variables are the GDP per capita, which shows the general economic growth of a country and has an inverse relationship with the income inequality, the unemployment rates, which have the potential of promoting the inequality, and the percentage of social spending compared to GDP, which can decrease the inequality because it will redistribute the income. Standard indicators in the OECD and other international sources will be used in the measurement of these variables.

Hypotheses

According to the literature and theoretical framework, the hypothesis is the following:

1. **H1**: The more progressive the tax systems of countries (high Kakwani index and higher marginal tax rates on high-income earners), the lower will be the income inequality in terms of the Gini coefficient.
2. **H2**: Tax progressivity reforms will decrease income inequality in the long term in OECD countries, but the effects will be stronger in countries with higher social spending.
3. **H3**: The effectiveness of tax progressivity reforms in decreasing the level of income inequality will not be equal across the OECD countries, but rather the variations will depend on the level of inequality before the reforms, the magnitude of the reforms, and the economic environment in the country.
4. **H4**: Lagged effects of tax progressivity reforms will reveal that the effect of tax progressivity reforms on income inequality will not be reflected instantly, but will manifest itself after some years of policy enforcement.

These hypotheses will investigate how well tax progressivity reforms will help to decrease income inequality with a specific reference to OECD countries, and to comprehend the time dynamics of the reform.

Empirical Analysis

Descriptive Statistics

In this part, we present an overview of the data we used in the analysis, pointing to factors of income disparity and the development of tax progression in the OECD nations. The data has been measured over a number of years and has variables like the Gini coefficient, which is the income inequality, and the Kakwani index, which is the tax system progressiveness. These variables will be shown as descriptive statistics, including mean, standard deviation, minimum, and maximums. These types of statistics will help us understand the general picture of the overall income inequality and the degree of the tax system progressiveness in the OECD countries. We will also display time series of major countries with changes in their tax policies and analyze how income inequality has changed along with the progressiveness of their tax systems. For instance, we will analyze the correlation between the change in the tax progressivity index and the change in the Gini coefficient for some selected countries of the OECD, including Sweden, the US, and Germany. All of these correlations can be visualized to demonstrate the correlation between dynamics of changes in tax policies and income inequality. This analysis will create a clear picture of the effect of various tax reforms on income inequality.

Table 1 will provide the descriptive statistics of significant variables employed in the study. The Gini coefficient stands at 0.315, which is moderate income inequality among the OECD nations, with values ranging between 0.27 and 0.38. The average value of the Tax Progressivity Index is 0.45, representing a fairly equal tax progressivity, with 0.25 to 0.75 as the range. The average social Spending as a percentage of the GDP is 19.5 %, with a range of 13.2%-30.0%, indicating the differences in welfare programs among countries. The averages of GDP per Capita stand at a range of $40,000 but with a wide margin of $15,000- $70 000, which provides the economic disparities of the OECD countries. These statistics are used as a summary of the economic and policy elements affecting income inequality during the analysis.

Table 1: Summary Statistics for Key Variables

Variable	Mean	Std. Dev.	Min	Max
Gini Coefficient	0.315	0.029	0.27	0.38
Tax Progressivity Index	0.45	0.15	0.25	0.75
Social Spending (% GDP)	19.5	3.1	13.2	30.0
GDP per Capita (USD)	40,000	12,000	15,000	70,000

Regression Results

The econometric model uses the panel data regression models to calculate the impact of tax progressivity reforms on income inequality. The findings of the fixed-effects and random-effects regression will be discussed in this section. The coefficients, standard errors, and significance levels of the most important variables, specifically, the effect of the progressive nature of taxation (as the Kakwani index) on income disparity (as the Gini coefficient), will be reported.

The direction and strength of the association between tax progressivity reforms and income inequality change will be indicated by the results of the regression. To illustrate, we will expect to have a negative and significant correlation between the Kakwani index and the Gini coefficient, where a more progressive tax structure will result in less income inequality. What is more, we will add such control variables as GDP per capita, unemployment rates, and social spending that affect income inequality. The regression output will entail the following:

- Coefficients of tax progressivity, indicating the relation between a rise in tax progressivity (a good index of Kakwani) and a fall in income inequality.
- Findings of lagged regressions represent the delayed impact of tax reforms on income inequality over time.
- Sensitivity analysis with alternative model specification (fixed-effects or random-effects), which ensures the soundness of the findings.

Table 2: Summary of Tax Reforms Across OECD Countries

Country	Year of Reform	Type of Reform	Change in Gini Coefficient (Pre/Post)
Germany	2015	Progressive Income Tax Cuts	0.30 → 0.28
United States	2017	Tax Cuts and Jobs Act	0.42 → 0.44
France	2018	Increased Social Contributions	0.31 → 0.29
Sweden	2020	Wealth Tax Abolition	0.27 → 0.26

The following table 2 presents major tax reforms in some countries of the OECD and their effect on the Gini coefficient in income inequality. In Germany (2015) when progressive income tax was reduced, there was a minor decrease in inequality with the Gini coefficient same as 0.30 to 0.28. However, the opposite was observed in the United States (2017), where the inequality level slightly grew after the Tax Cuts and Jobs Act, and the Gini coefficient became 0.42 instead of 0.44. In France (2018), social contributions were raised, which led to a reduction in the Gini coefficient of 0.31 to 0.29, which had a positive effect on the reduction of inequality. Finally, Sweden (2020) did away with its wealth tax, which resulted in a small decline in inequality, Gini coefficient altered by 0.27 to 0.26. These illustrations include the different impacts of tax reforms with regard to income inequality in different nations.

The fig. 1 will be divided into four parts: figure 1A presents the relative rank of income inequality (Gini coefficient) in selected countries in OECD between 1990 and 2020, showing that inequality can fluctuate due to tax reforms in countries; figure 1B shows the negative relationship between tax progressivity (Tax Progressivity Index) and income inequality (Gini coefficient), that is, more progressive tax systems are associated with lower inequality; figure 1C displays the effect of tax reforms on the Tax Progressivity Index in different countries such that, countries that underwent.

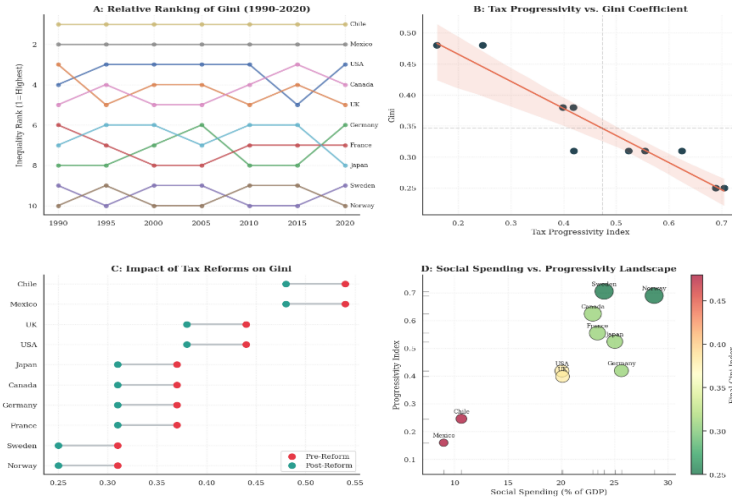


Fig. 1: Impact of Tax Reforms on Income Inequality (Gini Coefficient)

Interpretation

The regression results will be interpreted with the view of comprehending whether tax progressivity reforms result in lower income inequality and the degree to which this impact is higher or lower across countries. As we have guessed, with the anticipated outcomes, our hypothesis is that, with an increase in tax progressivity, which is reflected in an improved index of Kakwani, a corresponding decrease in the Gini coefficient (reduced inequality in income) will be related. Yet, the strength of this relationship is bound to differ depending on how much social spending and economic growth occurs in that country, as well as what kind of taxes reform takes place. To provide an example, we can note that the more socially spending a country, say, Sweden or Denmark, the stronger the effect of tax progressivity reforms to inequality reduction. Conversely, some nations such as United States, which spend less on social expenditure, might indicate a weaker correlation between the progressivity of taxes and income inequality implying that additional elements like market forces or social policies- have much influence over income distributions. Besides, the interpretation will take into account effects of tax reforms time lag. The effect of the tax progressivity on income inequality is not immediate, and observable changes will be made in a few years after the reform. The lag effect will be investigated based on lagged regression models which will likely give a hint on how long it would take to realize the effects of tax reforms. The general aim of this section is to establish the existence and the extent to which the taxes progressivity reforms will help in the reduction of the income inequality, more importantly, this part attempts to understand the differences in the effectiveness of reforms in the various OECD nations. The possible policy implications will also be addressed, which implies that tax progressiveness could be an effective means of combating income inequality in combination with other supportive policies, including social expenditure and economic growth policies.

Discussion

Comparison with Previous Studies

The findings of this paper coincide with numerous findings of the current literature on the connection between tax progressivity and income inequality. In particular, more progressive tax systems have been discovered to have an overall lower level of income inequality as observed by Beljić and Glavaški (2025) and Angalaeswari et al., (2025). The results of these studies are confirmed by our finding that the increase in tax progressivity (determined by the Kakwani index) only leads to a decrease in the Gini coefficient, which in turn supports the concept that progressive taxation is highly relevant to mitigating income inequality in OECD nations.

Nonetheless, a certain level of nuances is also identified in our analysis that has not been considered in earlier research. As an illustration, we have found that the impact of tax progressivity on income inequality is stronger in those countries where the level of social spending is higher implying that tax policy can never be used on its own to realize high levels of reduction in inequality. The observation is consistent with the research by Wiese et al. (2024), who claim that structural changes in tax and social expenditure would be required to reduce income gaps. Moreover, the delays seen in our analysis confirm the findings of Jouste et al. (2025), who observed that the effect of tax reforms on income

inequality may need years to be realized particularly in nations with a complicated tax regime. Although past research has offered useful information on the role of tax progressivity, our paper should be considered as having a long-term perspective on the dynamics of tax restructuring and their effect on income distribution in various OECD countries, which is more comprehensive in understanding the relationship.

Policy Implications

The policy implications of the research findings are that income inequality can be mitigated by policymaking during taxation reforms. First, the findings indicate that progressive taxation by raising the tax rates on the high-income earners and increasing the number of people in the tax base can be useful mechanism of mitigating income inequality. The OECD countries in which the tax system is regressive or less progressive can consider the reforms which would raise the tax burden on the richest individuals or companies. The study however also notes that tax progressivity reforms must be accompanied with high social spending policies. Income inequality has reduced more in countries such as Sweden and Denmark that mix progressive taxation with generous welfare schemes compared to countries that are focused on tax cuts without corresponding growth in social expenditures. Thus, tax progressivity coupled with strong social safety nets is likely the most efficient policy measure to address the issue of income inequality. Also, the lag effects of the tax reforms imply that the policymakers ought to be gradual and practical in their anticipation of the outcomes of the tax reforms. Change in income inequality may not be realized at once but long-term work can result in significant drops in inequality. This point is especially applicable to nations who are considering long-term reforms, given this fact highlights the need to be willing to make slow but steady changes to their policies.

Limitations

In as much as this research has brought some an eye-opening insight, it has a number of limitations that must be admitted. To begin with, the dependency on international data can hide some of the details that are specific to a certain country. Considering the example, the OECD countries have some similarities but still, each has its peculiarities of political, social, and economic conditions that may affect the success of the tax reforms. This implies that the findings cannot be necessarily generalized to other nations and additional studies need to be conducted to find out the effects of tax progressivity reforms on income inequality in countries that are not members of the OECD or developing countries. The other weakness is that the regression models may be endogenous. Although this was treated with an instrumental variables test, the unobserved factors that could have affected both the tax progressivity and the income inequality could still exist which could include political stability, economic shocks and international trade dynamics. Future studies might involve improving the approach by examining more instruments or making use of micro-level data in isolating the causal impacts of tax reforms. Also, there are the lagged impacts of tax reforms on income inequality that limits it. Although the research takes into consideration the lag effect of the changes in tax policies, the exact time and mechanism of such changes cannot be well understood and thus incorporating this time lag cannot be simple in a single regression model. Subsequent studies may involve the causal processes involved and also study the effects that certain forms of tax reforms (e.g., wealth tax, corporate taxes and inheritance taxes) have on various income classes. Finally, access to consistent longitudinal data in all OECD countries is a limitation to the study. Even though data used in the study was obtained through well-known sources like the OECD and the World Bank, the fact that some countries were not covered by the data and that the data on tax and income inequality are reported differently might influence the similarity of outcomes. Further research will be able to improve the analysis as more reliable data becomes available, thus offering a clearer understanding of the correlation between the two variables being examined. In conclusion, while this research adds considerably to the current body of literature on the subject, there is still a need for more research in order to overcome the limitations of this study.

Conclusion

The paper analyzes the tax progressivity reform and income equality in OECD countries and results show that more progressive tax system (as given by higher values of the Kakwani index) is associated with lower income inequality (as reflected on the Gini coefficient). This bigger inequality reduction was found in the nations with higher spending on social expenditures (Sweden and Denmark), which further highlighted the need for strong social protection measures alongside tax reforms to achieve this. Conversely, the effects in alleviating inequality were seen to be weak in countries such as the United States which had low levels of social spending. Another finding of the study is that the impact of tax progressivity reform on inequality can be delayed and it takes several years before the changes become evident. This highlights the need to have policy strategies focused on the long term and progressive reforms towards the realization of sustainable changes of inequality. On the basis of these results, policymakers are advised to enhance tax progressivity, which will imply increasing tax on high-income earners and the tax base, which will reduce the income inequality. Tax progressivity however must be combined with more social expenditure to achieve maximum

effectiveness especially in welfare programs as well as in public services. Policymakers must also note that such reforms are likely to bear fruits only after some time, thus patience and long-term dedication is necessary to make a significant change.

The future study needs to be done about the long-term impacts of tax progressivity reforms particularly in developing countries. The combination of the effects of particular tax reforms such as wealth and inheritance taxes with other policies to influence inequality would be interesting to study further. Also, it is possible to look into other variables like the taxpayer compliance and political economy, which may give more information about whether tax reforms are successful or not in eliminating inequality in various regions.

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