# Rising Wealth and Income Inequality: What do we know?

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## Summary

*The background of this article is the failure of neoliberal development economics and policy to uplift fair and equitable market societies. Rather, neoliberal aversion to distribution theories and policies is considered responsible for driving such societies to unacceptable levels of wealth and income concentration and fracturing social cohesion everywhere. Thus, it is time to shift neoliberalism as the dominant development paradigm to correct failures and wrong directions. What is the rationale for this claim? Top world economists are creating a new development world view putting the question of inequality in the centre of their academic research and political motivation to change the order of things. This article tries to unveil the essentials of the new development thoughts on inequality and its consequences.*

## The Extent of Inequality: A Divided World

A comprehensive survey of the state of art in contemporary development economics and policy reveals that the question of rising income inequality is nowadays at the heart of academic, political, governments' and even tycoons' debate all over the world. What is about?

Some basic statistical facts regarding national income share among earners across time and selected regions and countries can help us explain the origin of concerns: while in 1980, the wealthiest 10% of individuals owned, on average, 29.0% of national income, in 2015, the top 10% received 46.0% of national income.[1] Obviously, the size and speed of this average outcome varies among regions and countries, but the crude reality is that wealth and income inequality have been growing since the 1980s in all the cases under observation.[2] The major worry that arises from this abysmal outcome is that the trends in rising wealth and income inequality in the near future seem to be unstoppable with severe consequences, particularly, for the least advantaged individuals and households and even worse, for global economic growth, political stability and social cohesion everywhere as we are witnessing today.

As most readers of this article may be linked to development finance agencies, investment and banking institutions, where, as is known, many people are making too much money increasing day-to-day the crater of the income disparities among earners, I would like to draw the attention of my readers to the crucial importance of rethinking contemporary development finance patterns and, even much better, shifting overall economic and finance paradigms to drastically change the noxious inequality trends that may erode not only the foundations of global and domestic financial systems but market society as such. The Great Recession and subsequent economic and financial crisis of 2008/9 provide a lot of convincing arguments to become extremely cautious with such perverse tendencies to avoid repeating the bad lesson again.

The aim of this article is two-fold: on the one hand, to give a brief introduction on the concept of inequality from development economics and policy insights; and on the other hand, to illustrate the demand for more distributive equality as emanated from the claim of the greatest economic thinkers of our time. This is an inaugural essay of a series of articles on the same topic that I want to write for this magazine.

## Decay of Neoliberalism

My appeal for shifting the development paradigm is not an ideologically motivated claim. Rather, it derives from many objective and reliable reasons. First, neoliberalism or monetarism as the dominant political and economic mainstream since the '80s is slowly becoming a decadent intellectual movement that seems conceptually disinterested and unable to tackle wealth and income inequality as one of the greatest development challenges of market societies in the twenty-first century. Second, in the interface between previous and the current century, new powerful brands of economics have emerged to counteract the force and speed of economic inequality, mostly attributed to neoliberal thoughts and policies. Third, reducing inequality embraces not only economic but other social and environmental development challenges, which have been ignored by orthodox neoliberal economics and its adherents across time.

As we are going to discuss further, there is a plethora of top contemporary development economists, who struggle to shift the neoliberal paradigm and replace it with a new development model more vigorous and comprehensive in terms of its theoretical and policy settings, and above all, much fairer and more equitable according to the needs and priorities of market societies in the current millennium. The entry point of the masters' arguments, is just the question of the extreme wealth and economic inequality as one of the most critical factors responsible for the secular deterioration of social welfare and cohesion, economic growth and political stability in several advanced, emerging and least developed countries.[3]

## Meaning of Inequality

Inequality is here meant from two convergent perspectives: as «inequality in distribution of development opportunities» which says that not all rights are available for everybody at birth to meet basic living standards; and as «inequality in wealth and income distribution» which refers to the lack of ownership of capital assets, cash flow and well paid jobs, that affect the great majority of people, all over the world. Thus, wealth and economic inequality are understood as a multi-dimensional concept that embraces ethics, legal and social claims and not only economic rationalities.[4]

This multi-dimensional approach transcends conventional wisdom of neoliberal economists that usually make, for example, both inequality and poverty two synonymous concepts. This is a limited vision and interpretation since the question of economic inequality refers not only to the welfare condition of a portion of people who live below a particular income and consumption threshold, but to a specific circumstance of social, political and economic exclusion and discrimination that may affect a much broader society's spectrum, regardless of whether a portion of the population is classified as poor. Inequality and poverty are not two indifferent concepts, but the former subsumes the latter. So, fighting poverty not necessarily means reducing inequality. For example, we can find people who live far above the poverty line but are constrained in their liberties and civil rights because of race, ethnicity, religion, nationality, political beliefs and so on, or people excluded from access to property, work and general welfare opportunities because of social status, gender, age and geographical location.[5]

The statistical measure of income inequality does not exclude the use of conventional poverty metrics through household surveys to figure out personal income calculation and distributional analysis, but instead of this, emphasises the application of quantitative approaches and methods derived from the «theory of functional income distribution», which is regarded as the contribution of the production factors (i.e. land, capital and labour) to the national income via rents, benefits and salaries, and the analysis of the respective income share across time. In a certain sense, it is about a rejuvenated coming back to the essentials of the classical political economy as conceived by Smith, Ricardo, and Marx, whose philosophical roots cope with wealth creation and income distribution among production factors and social classes.

## Inequality: Insomnia of Economic Thinkers

World-class contemporary economists and thinkers such as Thomas Piketty, Joseph Stiglitz, Anthony Atkinson, and Angus Deaton, who are leaders of modern welfare economics have in one way or another welcomed the theory of functional income distribution as the epitome to explain and describe the causes and effects of wealth concentration and income inequality in market societies in the long run[6]. Let's provide a summary of that.

Thomas Piketty, French economist, in his monumental work «Capital in the Twenty-First Century» (2014), inaugurates a new way of approaching the historic, economic and statistical analysis of the dual relationships between the variables capital and labour or, as he says, the inequality relationships between wealth (capital assets) and income (cash flow). The main thesis of his work is concise but complex at the same time: in the long run, the capital return rate (r), historically seen, rises more rapidly than the national income growth (g), which means that $r > g$. A literal reading of this mathematical expression says that the capital owners (i.e. landlords, renters, shareholders, heirs, innovators, super executives, megastars, and others) earn and accumulate a relative higher and rising portion of the national income than the rest of the society represented by the labour force (i.e. salaried class, employees, independent workers and middle class) and also by governments. The persistence of this tendency, stressed by Piketty as extremely dangerous for the global political and economic stability, should motivate governments to correct inequalities, at least seeking to make $r \approx g$ through progressive taxation, rising human capital, investing in innovation and knowledge economy, which all are defined as crucial convergence forces for improving wealth and income equality.

Joseph Stiglitz, American laureate Nobel Prize for Economics (2001), is one of the most influential leaders in the world controversy about economic inequality. In his books «The Price of Inequality» (2012) and «The Great Divide» (2015), Stiglitz makes a pathetic radiology of the extraordinary inequality growth in the United States (which is one of the greatest among OECD countries) and its consequences. In concrete terms, the author reveals that while in the early 80's, the top 1% of income earners received 12% of the total national income, in 2013 the 1% of wealthiest Americans roughly held 25% of national income. The corresponding figures in terms of wealth (capital assets) controlled by the top 1% were 33% and 40%. The increase in inequality in the United States, says Stiglitz, is the outcome of combining three interconnected problems: one, the markets are not working as is supposed, they have to do; two, the political system is unable to correct the market failures; and three, the economic system is neither fair nor stable. Stiglitz argues that inequality is a choice of the more powerful and wealthiest, based on unfair policies and wrong priorities; thus, there is no reason to accept them. To conclude, Stiglitz composed this epigraph: "The financial sector is emblematic of what has gone wrong in our economy - a major contributor to the growth of inequality - the major source of instability in our economy, and an important cause of the economy's poor performance over the last three decades".

Anthony Atkinson, British economist, is one of the most renowned theorists of modern welfare economics and a great contributor to the economics of inequality and poverty. Atkinson dies in 2017, a few months after publishing his book: «Inequality. What can be done? » It is about smart economic research aimed at responding to the question of how to reduce inequality, understood in its double meaning: firstly, as income inequality and secondly, as inequality of opportunities. Starting from a historical study of the inequality in Europe, built on a robust statistical evidence, Atkinson learnt that during the post Second-War World years (1945-1980), inequality declined in Europe due to the action of a series of equalizing mechanisms than can offer a guide for the future. In contrast, from the '80s onward, inequality has continuously grown. What is happening? He asks. The list of factors is large and includes economic phenomena such as globalization, technological change, growth of financial markets, changes in salary payment schemes, reduced role of unions, regressive tendencies in taxation and social transfers. Apparently, says Atkinson, these are phenomena out of our control but behind which, are government policy decisions as well as firms and corporations that influence the direction and sense of economic processes. Because of this, income distribution mostly benefits capital rents and not salary income. The redistributive policies to reduce inequality as proposed by Atkinson go beyond the conventional fiscal actions through progressive taxation to the wealthiest and social transfers to the most vulnerable. His main thesis for public action says that under the recognition that inequality is an illness inherent in the whole social and economic structure, a significative reduction of the problem has to take into consideration much broader aspects than the conventional ones involving areas such as technology, employment, social security, sharing of capital, and taxation. All these policies and political actions should lead to building much fairer and more equitable market societies.

Angus Deaton, British economist. He was awarded with the Nobel Prize for Economics in 2015 "for his analysis of consumption, poverty, and welfare". In his book «The Great Escape: Health, Wealth and the Origin of Inequality» (2013), Professor Deaton sustains the thesis, (helped by meticulous and robust statistical facts), that the history of humankind is the history of the great escape from poverty and early death as measured by variables of health, sanitation, hygiene, and nutrition. The amazing human progress registered since the industrial revolution in the eighteenth and nineteenth centuries and the technological revolution after WWII in the 1950s show that progress sooner or later offers an escape from human misery. Thus, the great challenge of governments is to increase the escape speed, so that no one is left behind. But this is only one facet of the story. While millions of people escaped from poverty and early death in the last 250 years, the truth is that today millions of people are still trapped by poverty and misery and do not enjoy the prosperity reached by others. And what is worse, despite the progress, gaps in economic inequity have increased far above tolerable levels. Real salaries are stagnant while the income of the wealthiest continuously increases leaving evidence that the two phenomena are interlinked. He states that inequality is a consequence of progress for good and sometimes for ill. Inequality influences the process of the inventions to alleviate the suffering of people in need. Globalization and technological change are per se beneficial for human progress but can be unfair if deflate the work-value of less-skilled people to the benefit of well-educated classes or if they lead to real salary stagnation as it has been happening, by way of illustration, in the United States in the last 50 years. Deaton provides a lot of remarkable conclusions in his book for policy action. The following text can synthesize very well the wealth of his thought and vision: "With the right policies, the capitalist democracy can work for all. We do not need to abolish the capitalist system or selectively nationalize the means of production. But what is needed is to put back the power of competency at the service of the working and middle classes".

## One Concluding Remark

This article is coming to an end. Many conclusions can be drawn from the meaning of income inequality as a multifaceted concept and from the worries of prominent development economists about its consequences for the future governance and stability of market societies. However, I would like to stress the relevance of only one point as a concluding comment: the time of shifting the neoliberal paradigm just arrived! The key question is: what should be the next development paradigm after neoliberalism? This is a central matter to be discussed in the next articles as early indicated above.

 

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## Footnotes

1. Reference is made to the wealth and income concentration in India, US-Canada, Russia, China, and Europe following the statistics provided by the World Inequality Report 2018.

2. So, India moved income concentration from 32% in 1980 to 56% in 2015; USA-Canada from 34.5% to 47%; Russia from 21.5% to 46%; China from 27% to 42%, and Europe from 32.5% to 37%. Ibidem.

3. Concerning the features, significance, and prospects of income inequality in the advanced economies, see the conclusions of a penetrating econometric and policy study conducted by a pool of international agencies (ILO, OECD, IMF, and WB), entitled: “Income inequality and labour share in G20 countries. Trends, Impacts, and Causes”. Turkey, September 2015.

4. See, Alfonso, H., La Fleur, M. and Alarcon, D. “Concepts of Inequality”. Development Issues No 1. ONU. Department of Economic and Social Affairs. 21 October 2015.

5. See, McKay, A. “Defining and measuring inequality”. In: Inequality Briefing No 1. Overseas Development Institute and the University of Nottingham. March 2002.

6. An iconic name is missing from the list. It is about Amartya Sen, the great Indian philosopher, and economist, who was awarded the Nobel Prize for Economics in 1998. The reason for this omission is because the next article will be mostly devoted to him.