

# **Development, Inequality and Demagogy in the 21st century**

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# Four key problems in advanced countries

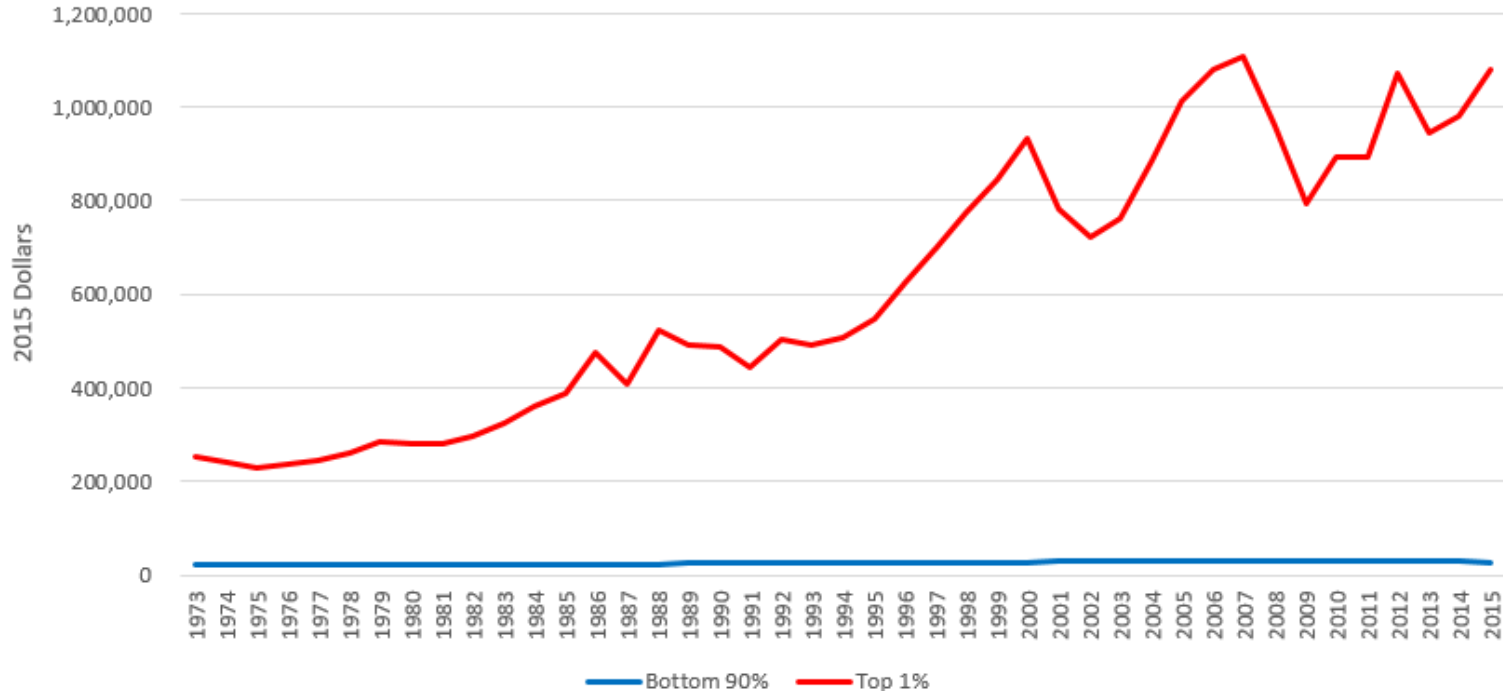
- Insecurity
- Inequality
- Lack of voice/powerlessness
- Lack of education

All of which lead to lack of hope

- Loss of hope/despair understandable

# US: bottom 90% have seen little increase in income over last third of a century

Average Income

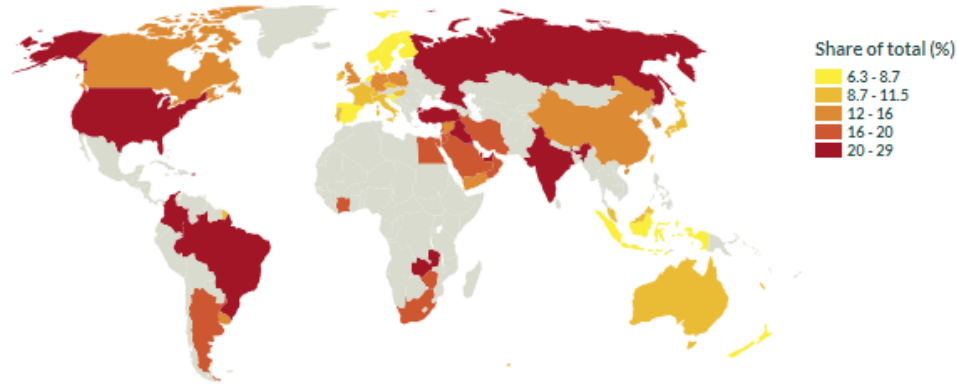


Source: World Wealth and Income Database

# Global Inequality: Top 1% National Income Share, 1975-2016

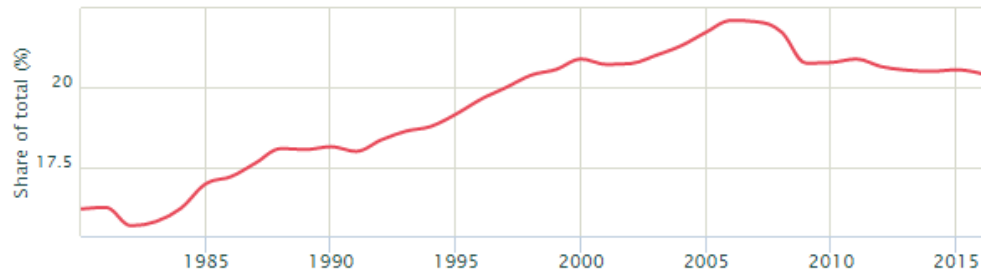
## Top 1% national income share

Region View



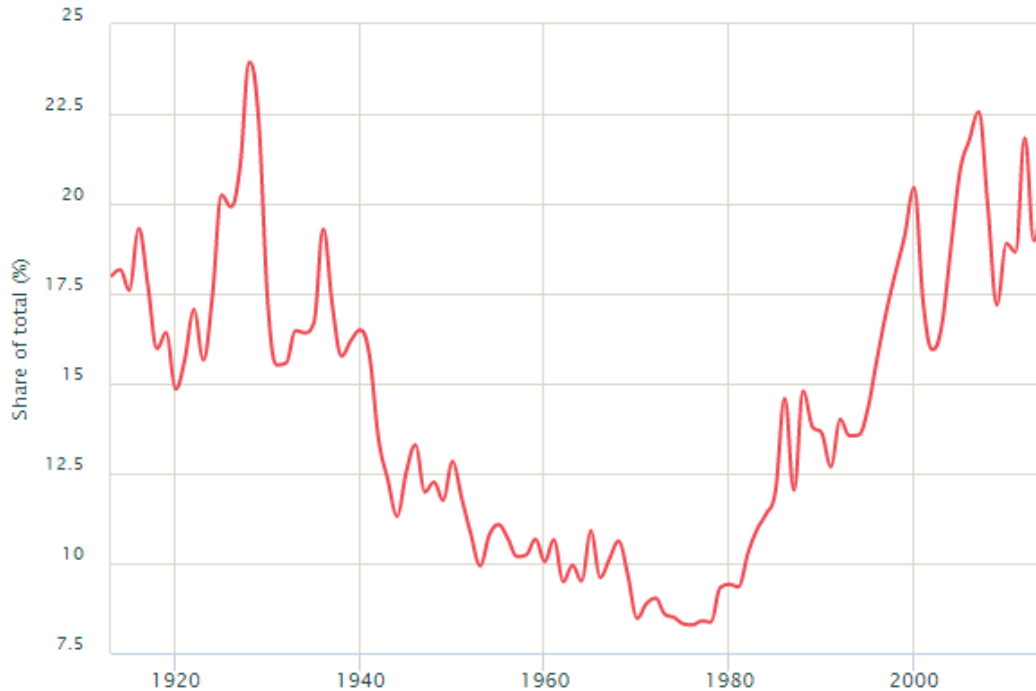
Share (%)

Share (%)



World

# Top 1% income share in the United States 1913-2015



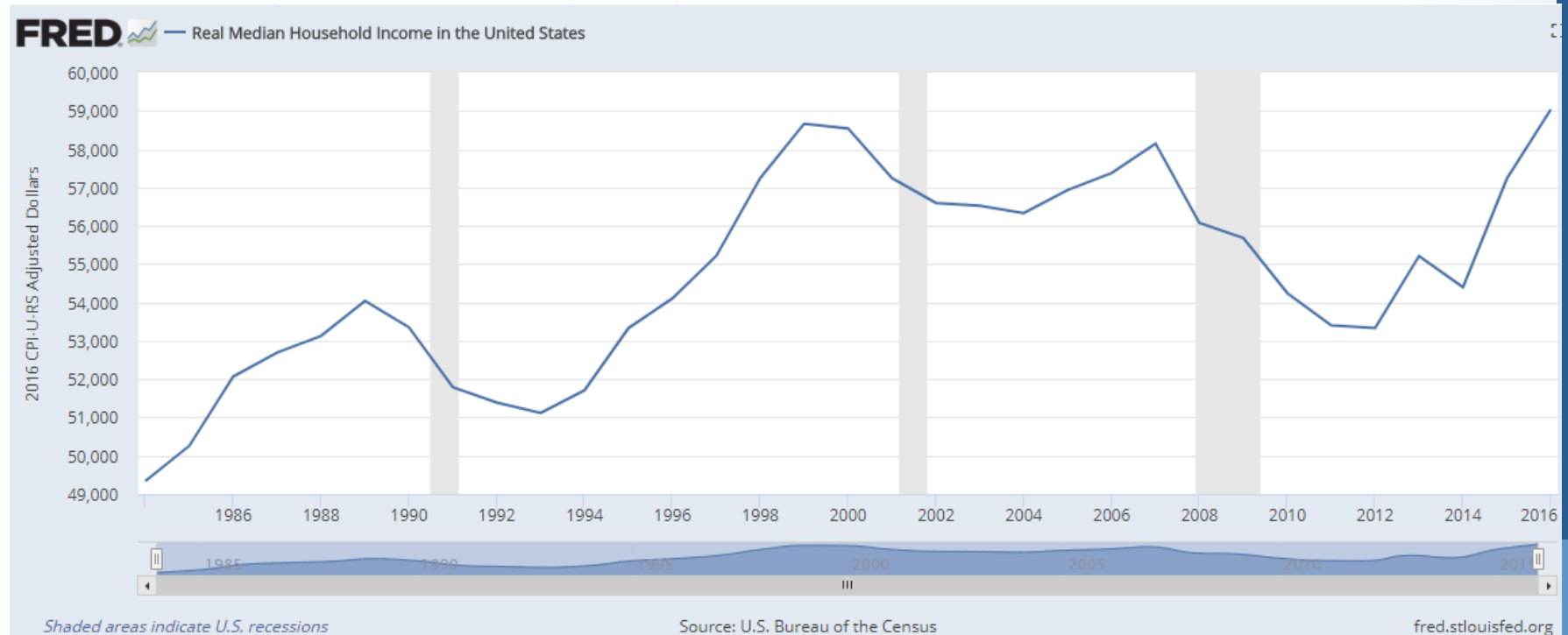
**Note:** Fiscal income is defined as the sum of all income items reported on income tax returns, before any deduction. It includes labour income, capital income and mixed income. The concept of fiscal income varies with national tax legislations, so in order to make international comparisons it is preferable to use the concept of national income. The population is comprised of individuals over age 20. The base unit is the individual (rather than the household) but resources are split equally within couples.

Source: World Wealth and Income Database.

# Stagnation: U.S. median household income

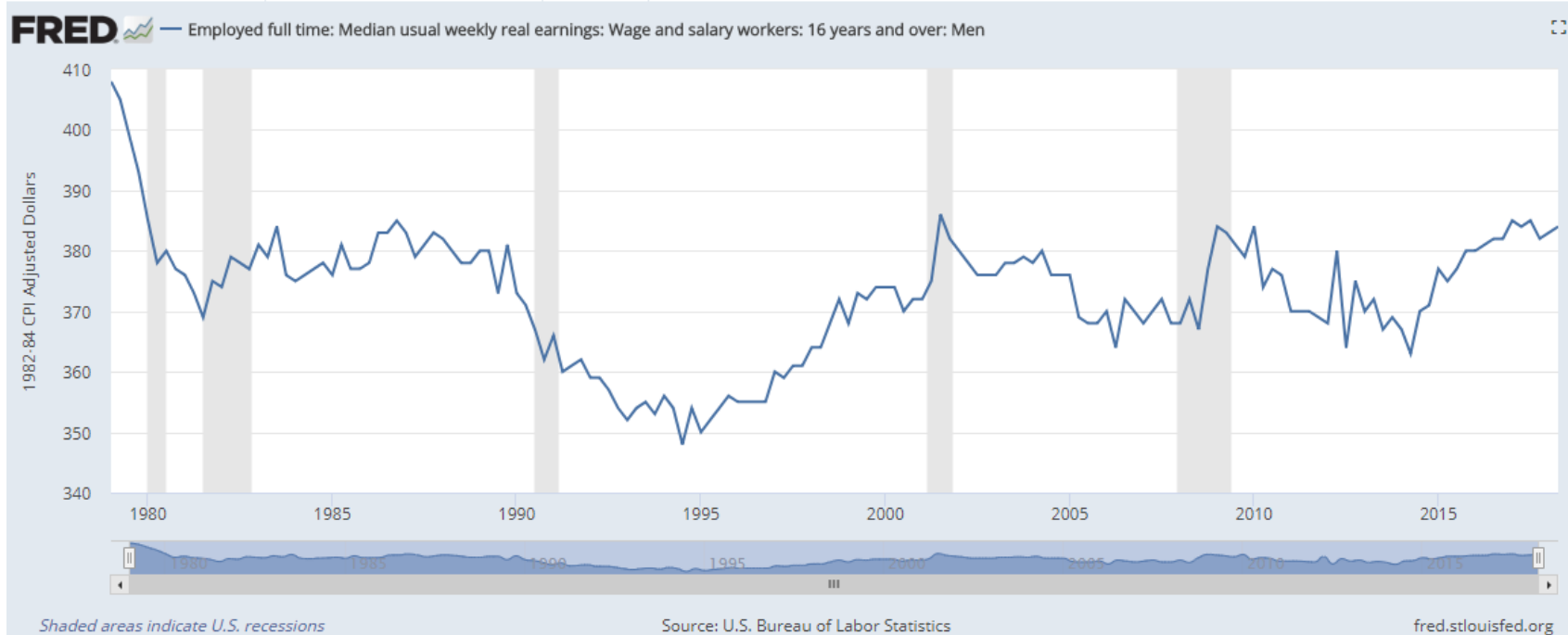
**1998:**  
**\$57,248**

**2016:**  
**\$59,039**

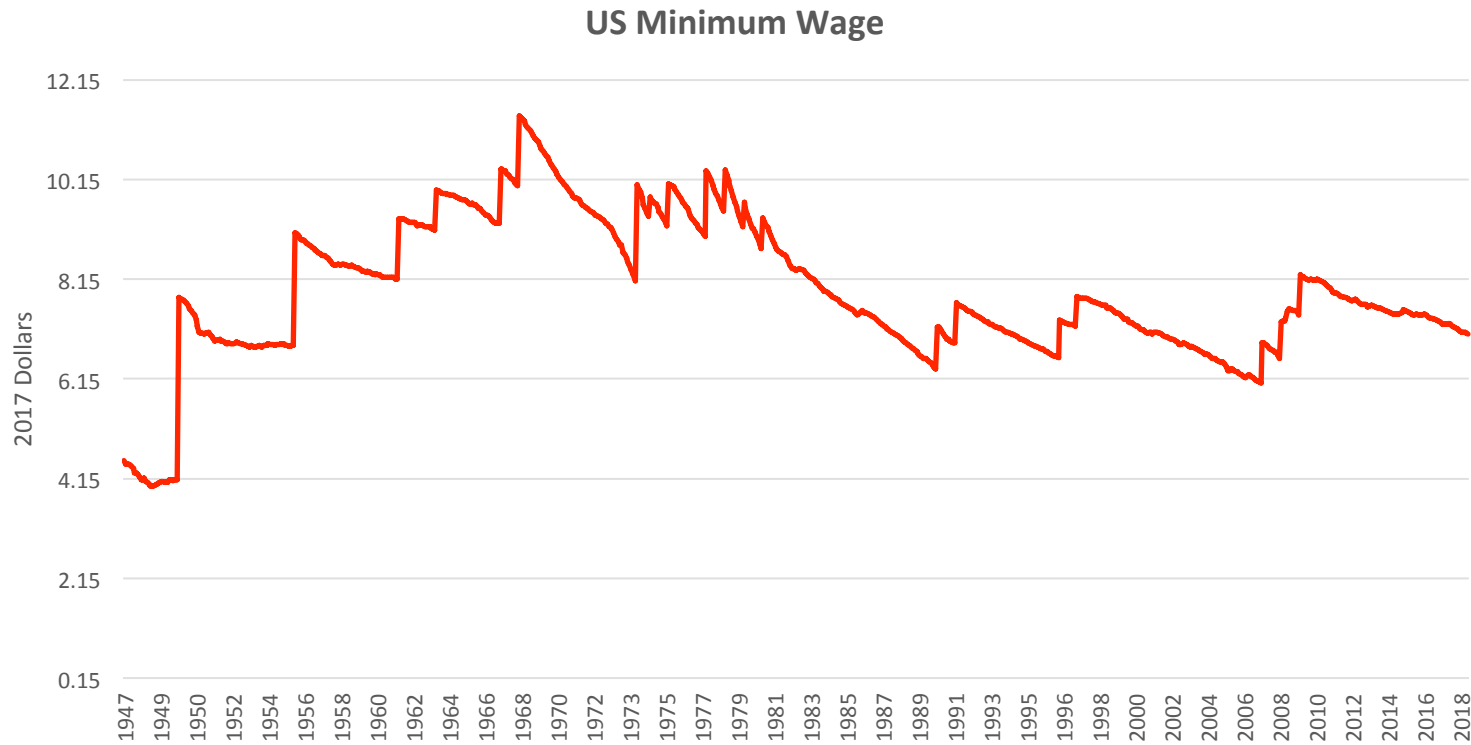


Source: FRED Economic Data.

# US: Median income of a full time male worker



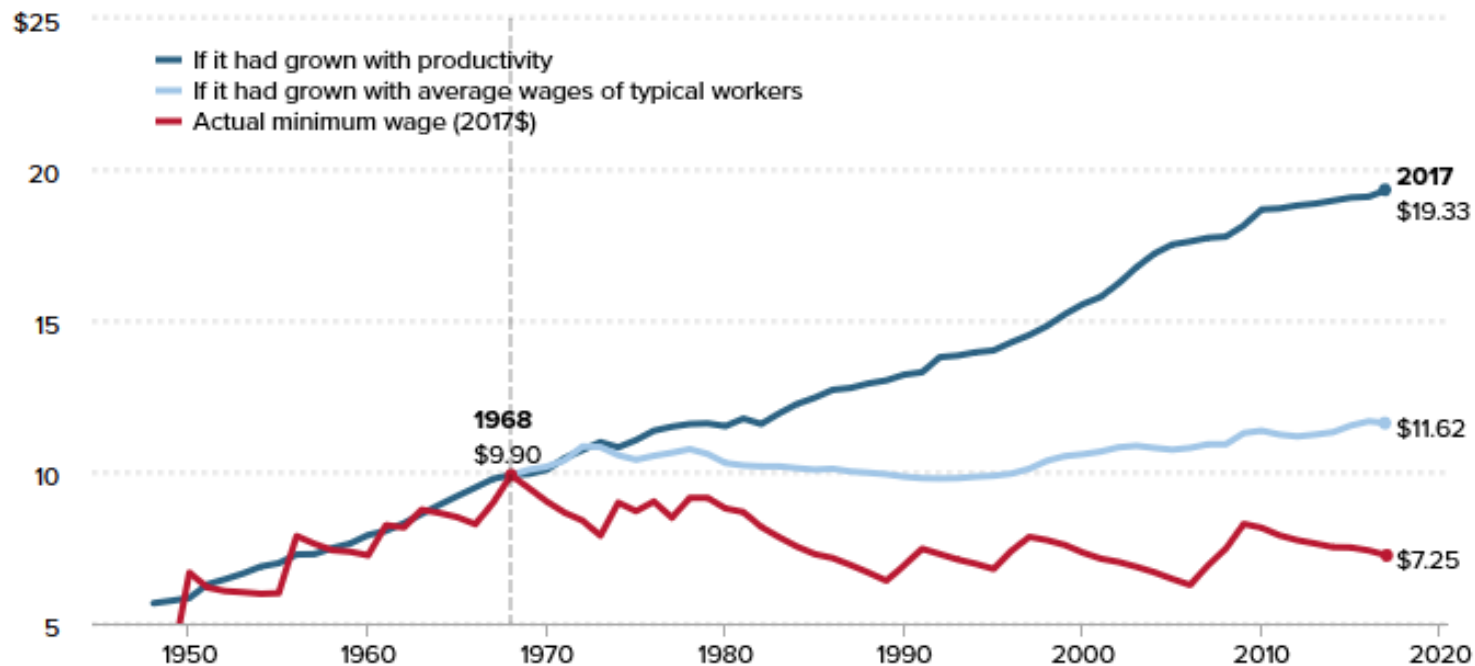
# US: Real wages at the bottom are at the level that they were roughly sixty years ago



Source: Federal Reserve.



## The value of the federal minimum wage in 2017 if it had kept up with a growing economy



# US: Disconnect Between Productivity and a Typical Worker's Compensation, 1948-2016

The gap between productivity and a typical worker's compensation has increased dramatically since 1973

Productivity growth and hourly compensation growth, 1948–2016

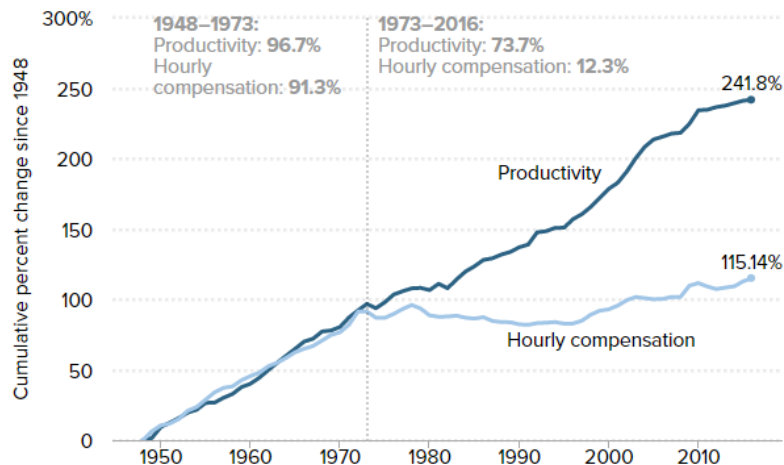


Chart Data

**Notes:** Data are for compensation (wages and benefits) of production/nonsupervisory workers in the private sector and net productivity of the total economy. "Net productivity" is the growth of output of goods and services less depreciation per hour worked.

**Source:** EPI analysis of unpublished Total Economy Productivity data from Bureau of Labor Statistics (BLS) Labor Productivity and Costs program, wage data from the BLS Current Employment Statistics, BLS Employment Cost Trends, BLS Consumer Price Index, and Bureau of Economic Analysis National Income and Product Accounts

Updated from Figure A in *Raising America's Pay: Why It's Our Central Economic Policy Challenge* (Bivens et al. 2014)

## Productivity–Pay Tracker

Change 1973–2016:

Productivity

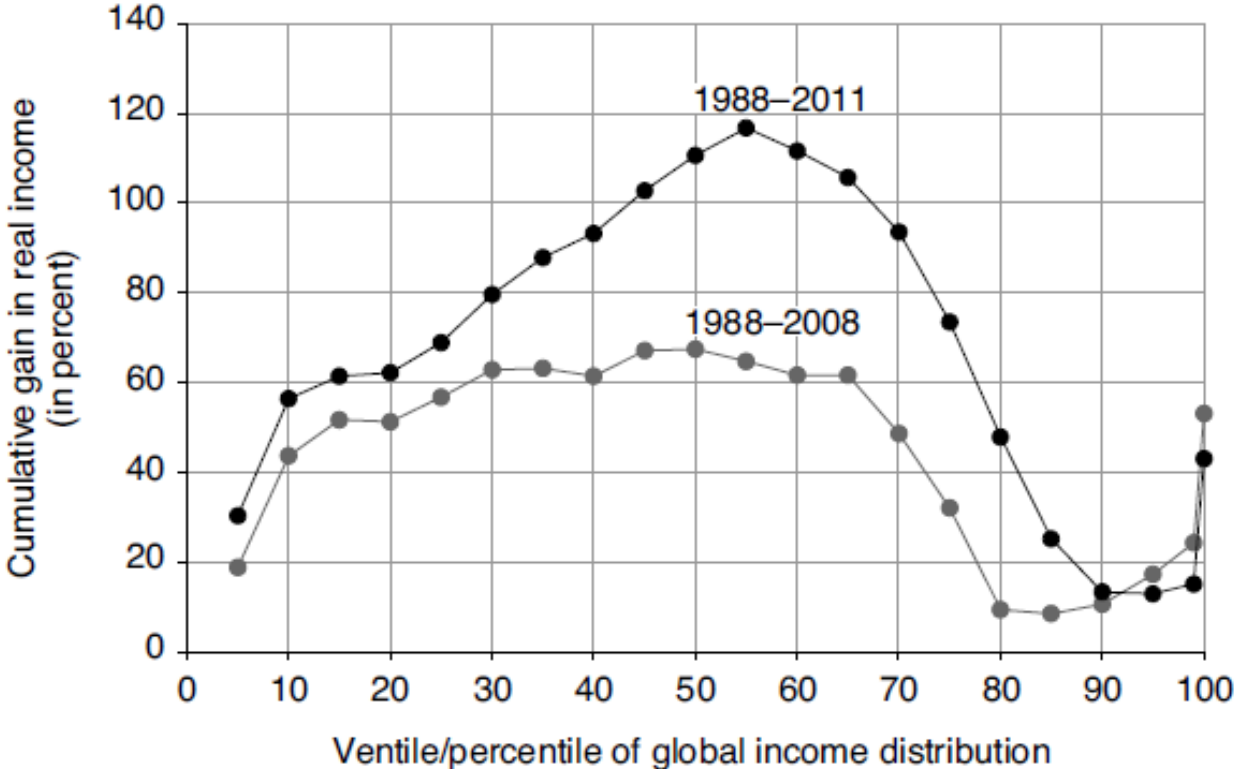
+73.7%

Hourly pay

+12.5%

Productivity has grown 5.9x more than pay

# Global Income Growth by Percentile



Source: Branko Milanovic.

# Many other dimensions of inequality

- Wealth
- Health
- Opportunity

**The Walton Family and The Koch Brothers have a net worth of \$212 billion in 2016  
That's the net worth of 115 million Americans or 35% of the country.**

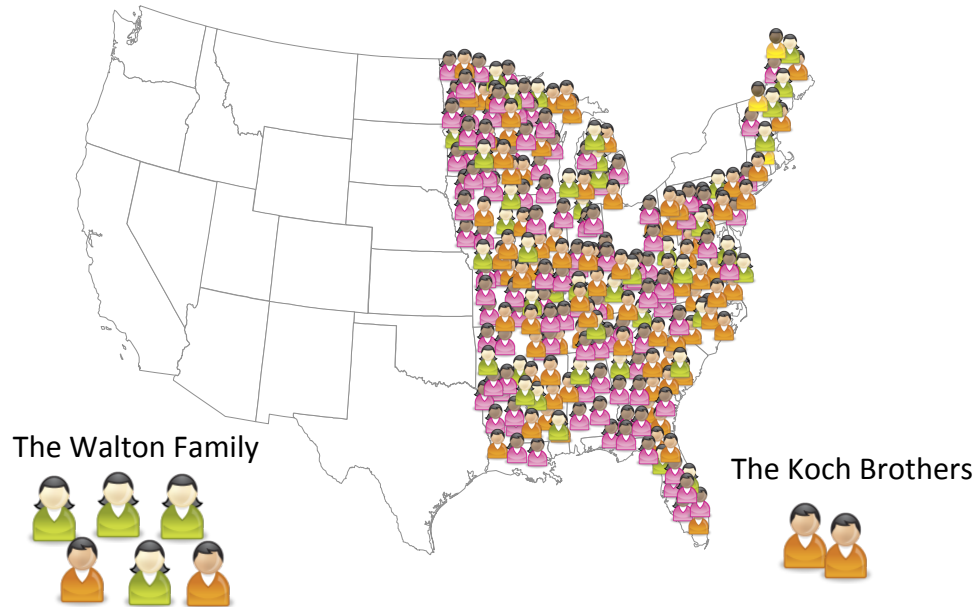
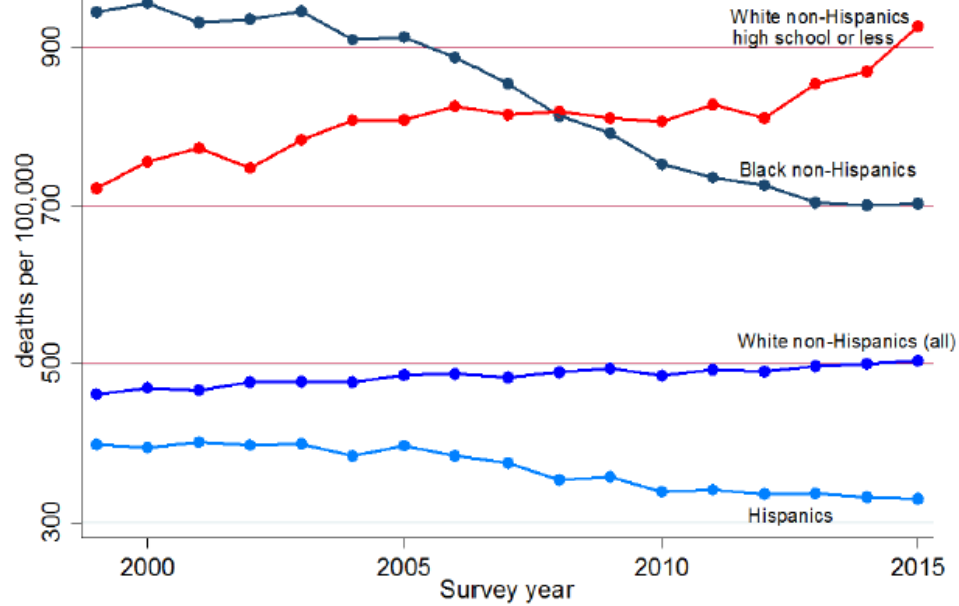
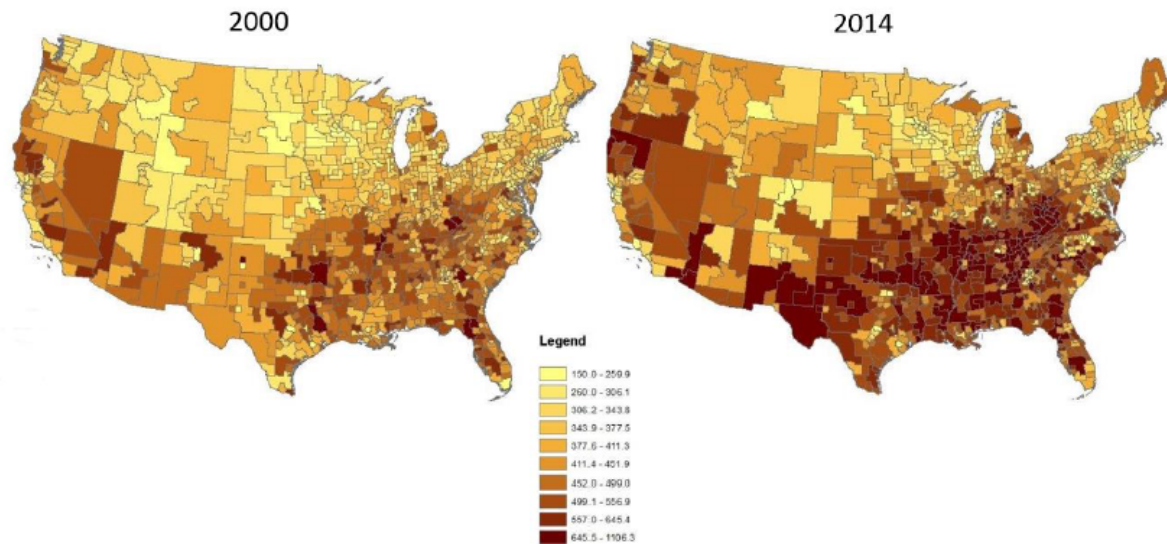


Figure 1.1 All-cause mortality by race and ethnicity, ages 50-54



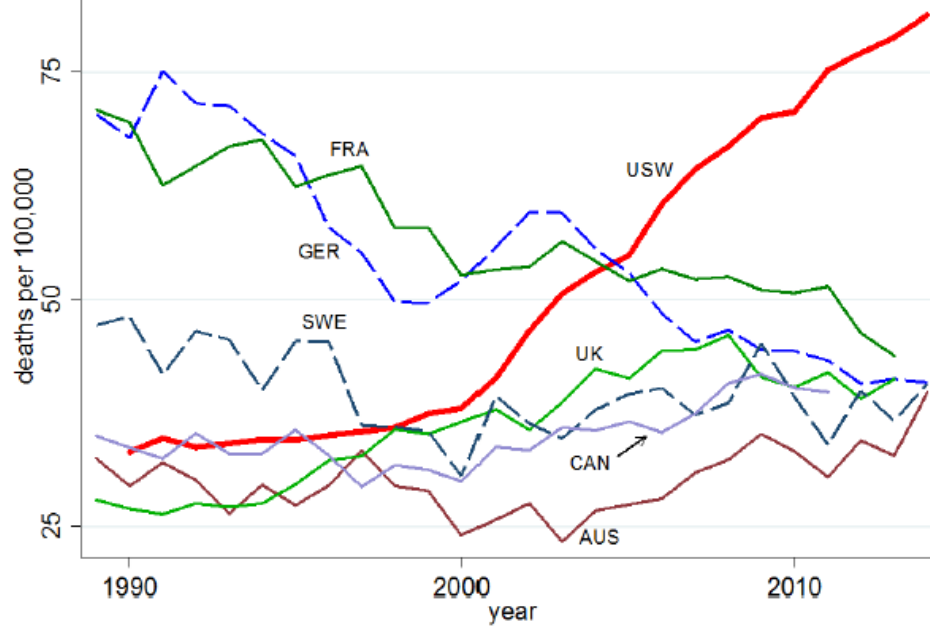
Source: "Mortality and Morbidity in the 21<sup>st</sup> Century", Anne Case and Angus Deaton, Brookings Papers on Economic Activity, March 17, 2017.

Figure 1.9 All-cause mortality, white non-Hispanics, ages 45-54



Source: "Mortality and Morbidity in the 21<sup>st</sup> Century", Anne Case and Angus Deaton, Brookings Papers on Economic Activity, March 17, 2017.

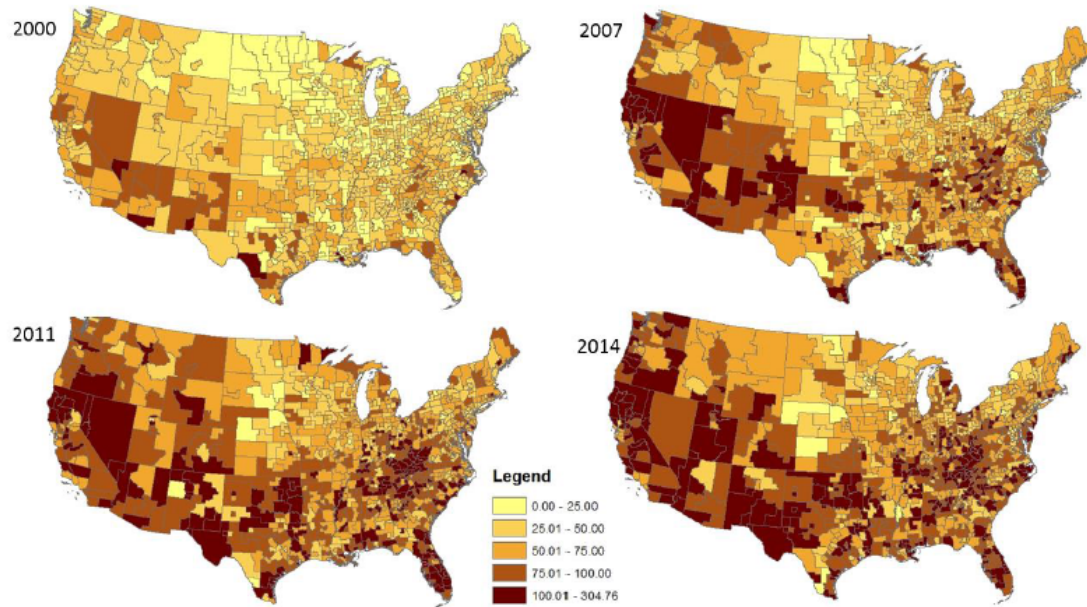
Figure 1.5 Drug, alcohol and suicide mortality, men and women ages 50-54



Source: "Mortality and Morbidity in the 21<sup>st</sup> Century", Anne Case and Angus Deaton, Brookings Papers on Economic Activity, March 17, 2017.



Figure 1.6 Drug, alcohol and suicide mortality, white non-Hispanics ages 45-54



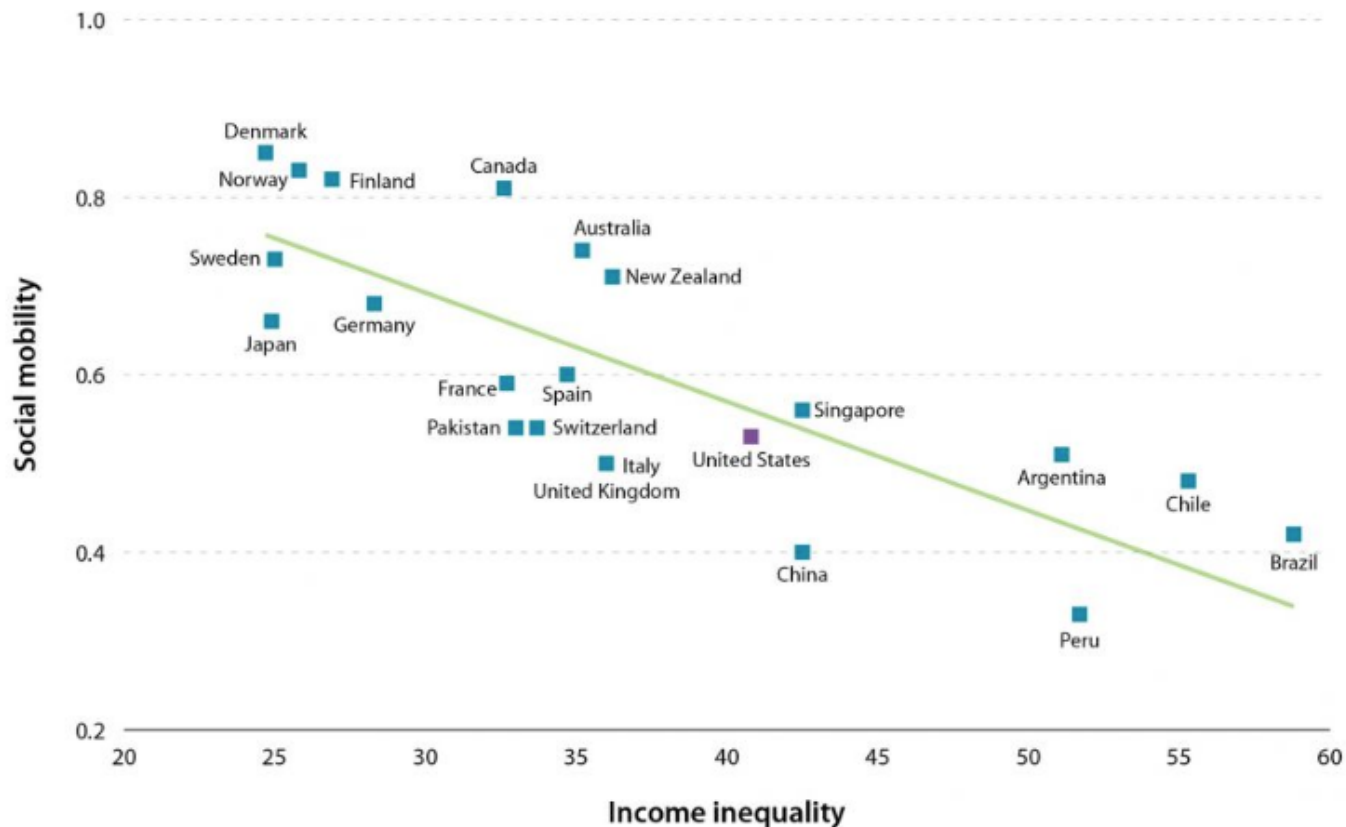
Source: "Mortality and Morbidity in the 21<sup>st</sup> Century", Anne Case and Angus Deaton, Brookings Papers on Economic Activity, March 17, 2017.

# Most invidious aspect: inequality in opportunity

- America among the countries with the least opportunity—in spite of the notion of the country being the land of opportunity (American dream)
  - Life prospects of a young American more dependent on the income and education of his parents than in other advanced countries
- Not a surprise: systematic relationship between inequality in incomes (outcomes) and inequality of opportunity

# The Relationship between Income Inequality and Social Mobility

Around the world, high income inequality is associated with low social mobility.

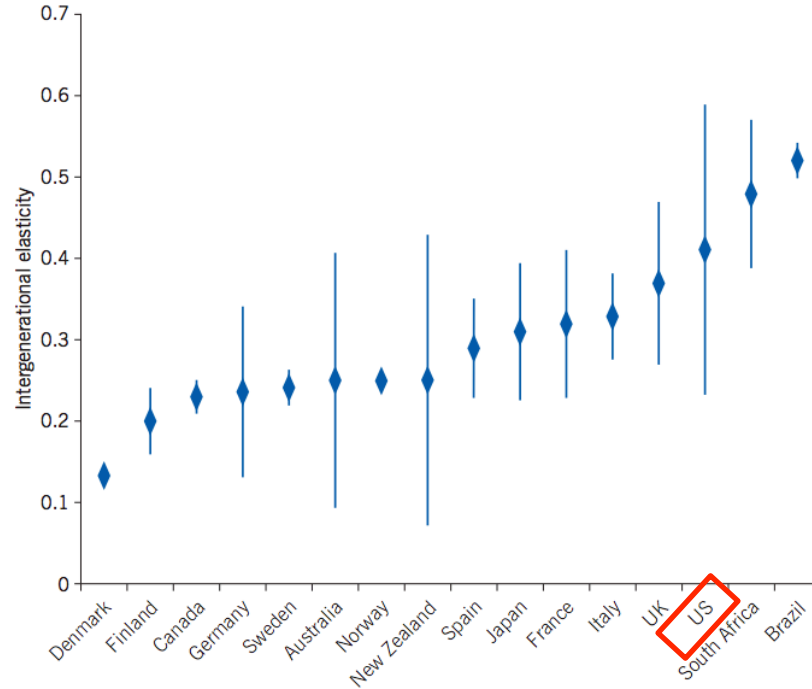


Source: Corak (2013); World Bank (2013).

Note: Reproduction of figure 2 from Corak (2013). Data points for Italy and the United Kingdom overlap. The x-axis shows Gini coefficients as reported by the World Bank. The y-axis is a measure of social mobility and is equal to 1 minus the intergenerational earnings elasticity for each country.

# Intergenerational Elasticity

Correlation between a child's income and his parents' income

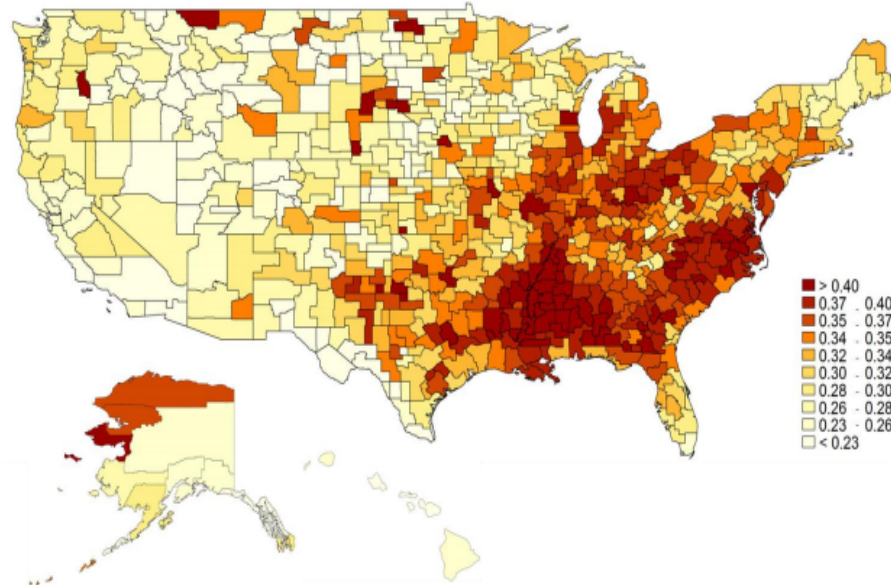


Note: The bars, which mark 95% confidence intervals, indicate the extent of statistical uncertainty associated with each estimate of intergenerational elasticity.

Source: Updated from Figure 1 in Mazumder, B. "Fortunate sons: New estimates of intergenerational mobility in the United States using Social Security earnings data." *The Review of Economics and Statistics* 87:2 (2005): 235-255 [1].

Source: "Intergenerational income persistence", Jo Blanden, IZA World of Labor, 2015: 176.

FIGURE 3  
Intergenerational Mobility (Parent-Rank and Child-Rank Income Correlation)



*Notes:* This figure maps CZ coefficients from OLS regressions of adult children's income rank on their parents' income rank, with rank defined by income centiles within each CZ. Darker areas represent lower intergenerational mobility. See Section 2.2 for details on the construction of local IGE measures.

Source: Chetty, Hendren, Kline, and Saez, 2013. "The Economic Impacts of Tax Expenditures." Harvard.

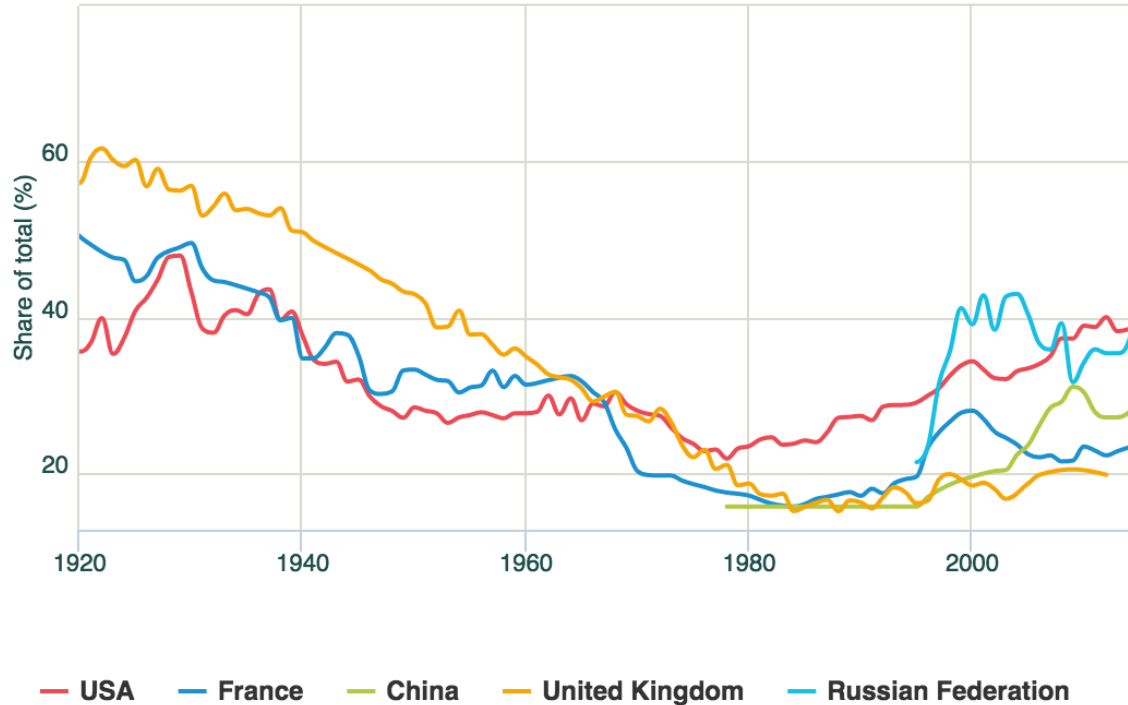
# Some global perspectives

- US has more inequality than any other advanced country
- Not all countries have been experiencing an increase in inequality—some have had a decrease
  - *Inequality has been a choice*
  - *Not just driven by technology and globalization*
  - *But by policies and institutions*
- Globally, wealth inequality is worse than income inequality

# Global Inequality in wealth

- Oxfam reports on wealth concentration at the top: how many of the richest people have as much wealth as bottom 50% (3.8 billion people!)
  - In 2010: 388
  - In 2017: just 42
- 82% of all growth in global wealth in 2016 went to the top 1%, while the bottom half saw no increase at all.
- The richest 1% continue to own more wealth than the whole rest of humanity.
- Big winners during last quarter century: global 1% and global middle class (middle class in China and India)
- Big losers during last quarter century (not sharing in gains): those at the bottom and the middle class in advanced countries

# Inequality in Wealth: Top 1% Net Personal Wealth Share, 1920-2015



018.

Source: World Wealth and Income Database



# Despair has provided opportunity for demagogues

- Blame others—migrants, globalization, “elites”
- Elites promised that globalization and liberalization (and in Europe, the euro) would bring prosperity for all
- Hasn't happened
- Predictable and predicted
  - Globalization was oversold—benefits exaggerated
  - Distributive costs ignored—weakened bargaining position of workers
  - Trickle down economics didn't work—almost never has

Among key messages of J. E. Stiglitz, *Globalization and Its Discontents Revisited: Anti-Globalization in the Era of Trump*, 2017

# Demagogues have been aided and abetted by conservatives, business community, “moderate right”

Who have seen this as an opportunity to advance their conservative agenda

- Reduce taxes for the rich
- Further liberalization
- Weaken environmental standards

Pursuing an array of policies which hurt those who voted for the demagogues

- Total cynicism
- Real danger: undermining social cohesion and the basis of progress —the Enlightenment
- Happened before: read history of the rise of fascism

# The critical role of the Enlightenment

- Development of science
- Development of basis of social organization not dependent on authority
  - Rule of law
    - Many subtleties in what that means
    - Evident in transition of regimes
  - Based on reasoned discourse/deliberation
    - Couldn't engage in "controlled experiments"
    - Had to employ thought experiments
    - Advancing our understandings of social interactions
- Result was the basis of the wealth of nations
  - **Growth not based on the exploitation of others**
  - Changing the stagnation that had lasted for centuries
  - Adam Smith couldn't have fully understood this: he was writing at the onset of a new era, before the advent of the knowledge economy

**Key message of J. E. Stiglitz and Bruce Greenwald, *Creating a Learning Society: A New Approach to Growth, Development, and Social Progress*, 2015.**

# Some insights from Smith

- **Role of markets**

- Pursuit of self-interest leads, as if by an invisible hand, to the well-being of society

- Not even Adam Smith believed in invisible hand—arguing for government intervention to prevent monopolies, to foster education, to reduce poverty

- **Need for anti-trust**

- “People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices”

# Further insights

- **Concerted effort to exploit workers**

Masters are always and everywhere in a sort of tacit, but constant and uniform, combination, not to raise the wages of labour above their actual rate [...] Masters, too, sometimes enter into particular combinations to sink the wages of labour even below this rate. These are always conducted with the utmost silence and secrecy.

- **Political economy of labor legislation**

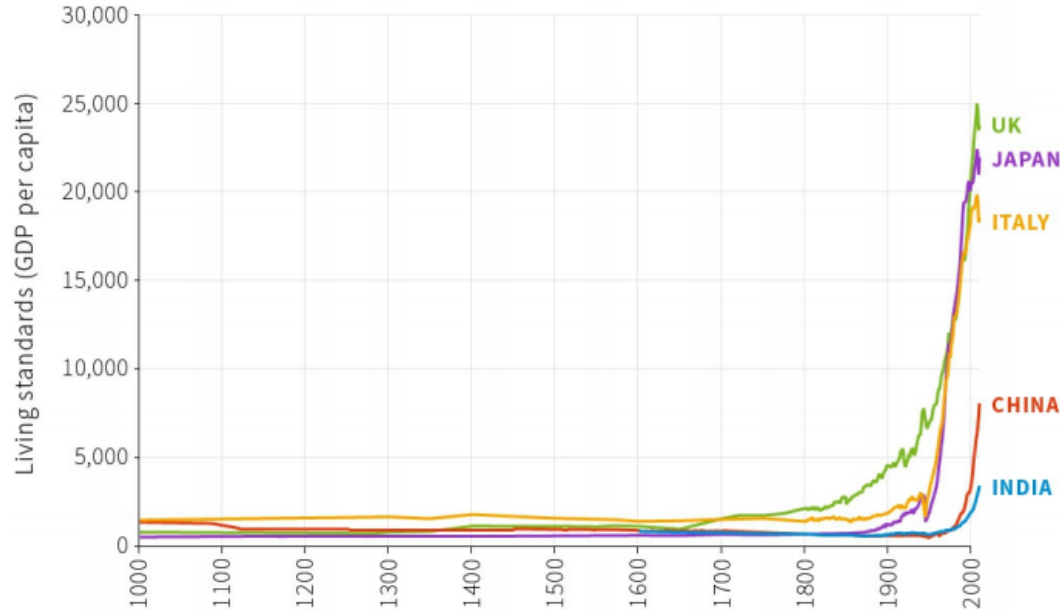
When workers combine, “the masters [...] never cease to call aloud for the assistance of the civil magistrate, and the rigorous execution of those laws which have been enacted with so much severity against the combination of servants, labourers, and journeymen.”

# Role of regulation in determining the distribution of income and social justice

- *When the regulation, therefore, is in support of the workman, it is always just and equitable; but it is sometimes otherwise when in favour of the masters*
- ***More than law is needed: trust and norms***

*If trust is too low in a society, savings will be insufficient to sustain positive output growth. Such a poverty trap is more likely when institutions – both formal and informal – which punish cheaters are weak.*

# Historical living standards



Source: INET

# Real wages of London craftsmen, 1200-2000

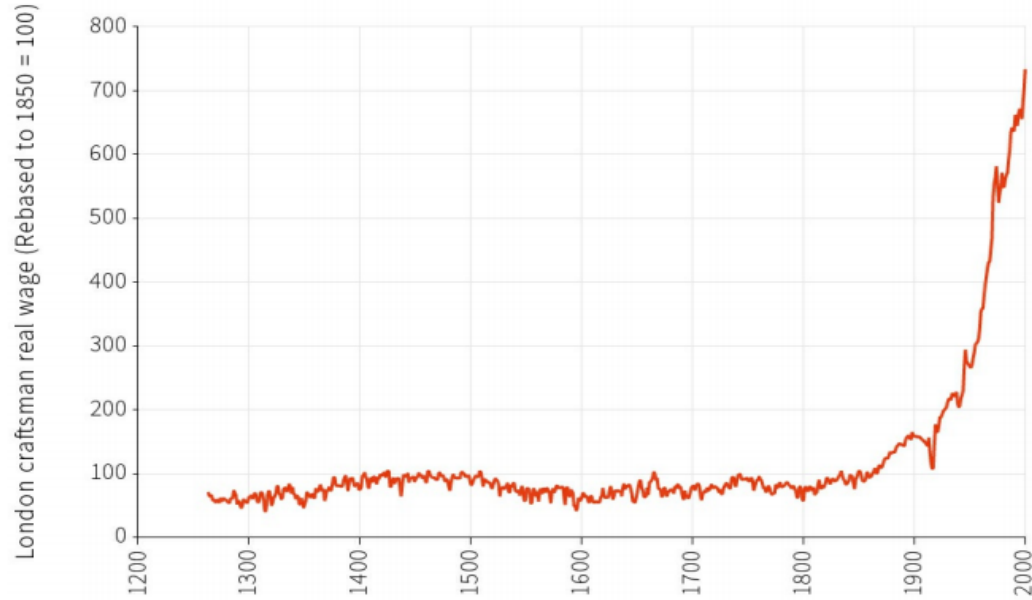
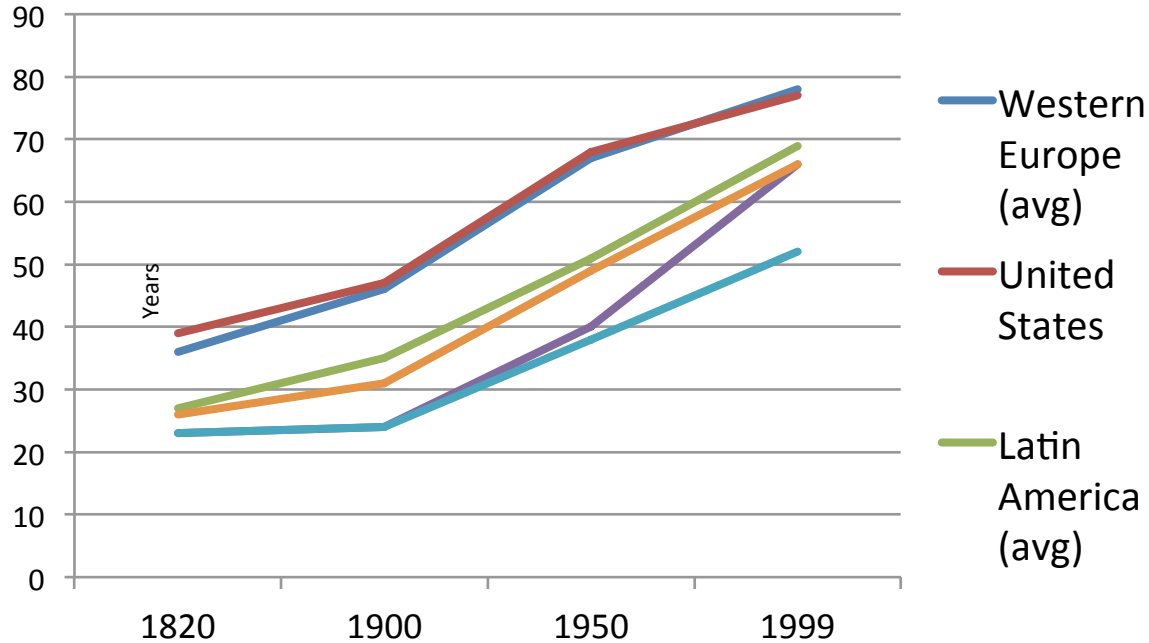


Figure 3. Real wages over seven centuries: craftsman (skilled worker) in London (1264-2001).

Source: INET



# Improvements in life expectancy since 1820



Data are estimates from A. Maddison, 2001, "The World Economy: A Millennial Perspective," OECD.

# Key insights of thinking about social organization

- Importance of coordination
  - Stop lights simplest example
  - Massive coordination failures
- Necessity of regulation
  - Pervasive social externalities
    - One person's freedom is another person's unfreedom
  - Limitations of markets
- Necessity of collective action
  - Markets don't exist in a vacuum—markets have to be structured
    - Thus law must *underlay* economics—sets rules of game
    - Key battles are about the rules of the game
    - **One of key explanations for increase in inequality and poor performance of US economy and that of many other advanced countries is that the rules of the game have been rewritten** beginning in the 1980s
      - **See J. E. Stiglitz *et al* *Rewriting the Rules of the American Economy: An Agenda for Growth and Shared Prosperity*, 2015**
  - Many problems where markets won't suffice—public goods

# “Chicago” (market fundamentalist) views of economics and society

- **Based on a particular view of markets and human nature**
  - **Presumption that they are competitive**
    - Even when there is a natural monopoly, competition for the market replaces competition in the market, yielding efficient solutions (markets are contestable)
    - Schumpeterian competition: monopolies are temporary, competition to be monopolists spurs innovation
    - So little need for anti-trust law
  - **Presumption that there is little need for regulation of externalities**
    - conditions of Coase “theorem” are satisfied
  - **Preferences are fixed, and in particular are unaffected by how the economy/society is structured**
- **Each of these presuppositions is wrong**

# Broader view of law and economics

- Law is formalization of norms, but also helps shape norms
- Markets, Law and norms reflect and shape who we are as individuals and the nature of our society
- Markets are just one form of social organization, one which has certain advantages, but many limitations and disadvantages
  - **Including shaping individuals to be more selfish**
- Successful economies and good societies may consist of an ecology of institutional arrangements
  - Mix may change over time, with changing circumstances
  - Socially based microcredit schemes were more successful (and more sustainable) than for profit microcredit schemes and DeSoto's land titling agenda
  - **In many places, cooperatives have proven themselves to be a better form of economic and social organization**

# Social organization without inherited hierarchical authority

- Based on rules, undergirded by rule of law
- Based on some version of merit
- Recognizing human fallibility
  - Dangers of concentration of power
  - Importance of checks and balances/separation of power
    - But with excessive inequalities, perspectives of wealthy will prevail
    - Can't be real democracy or an effective system of checks and balances
    - Gave rise to progressive policies on competition and redistribution
- Based on notion of deliberation (reasoning *together*)-
  - Representation/representativeness
- Dangers of inequality—benefits of equality (in income, power, etc)
  - Broader benefits of empowerment—the importance of voice and participation

# Key role of truth-telling institutions

- Social organizations can't function without some way of assessing truth of competing claims (necessary for deliberations over “fairness,” resolution of disputes)
- Multiple and complementary truth-telling institutions
  - Universities, research institutes, and other education institutions
  - Media
  - Judiciary
  - “Administrative Bureaucracy”
  - Intelligence agencies
- While science emphasizes the inherent uncertainty with which we know things, there is no alternative reality, no alternative “facts”

# Making Democracy Work

- Democracy was part of Enlightenment project
  - Particular form of social organization directed at collective action
  - Principles outlined in previous slides
- Can easily be corrupted by money
  - Rules of the (economic and political) game are set by political process
  - Economic power translates into political power
  - Political power used to perpetuate and reinforce economic inequalities
  - Those with wealth know that the perpetuation of their position is at risk with democracy
  - In societies with excesses of economic inequality, it is inevitable that those with wealth attempt to undermine democracy
    - By limiting and discouraging participation, by promoting and embedding anti-democratic rules (gerrymandering)
    - By constraining what government can do

- High levels of wealth inequality and democracy may thus be incompatible
- Can be multiple equilibria: “good” equilibrium with high levels of economic and political equality—with true democracy, bad equilibrium marked by political and economic inequality
  - US may be in bad equilibrium, more closely described by “one dollar one vote” than “one person one vote”



# The rise of populism and demagoguery in US perhaps understandable

- Economic and social system had failed large parts of America
- Myths had been undermined
  - American dream: those at the bottom and middle never made it to top, real risk was falling down a ladder the rungs of which were increasingly far apart
  - Justice for all: justice for rich White Americans
    - Wrongful convictions, even for murder
    - Mass incarceration
    - No system of justice in disputes with large corporations
    - Private arbitration
    - In crisis, people were thrown out of their homes who did owe any money

- “Stories” told by educated elites—globalization, liberalization would benefit all: things didn’t turn out as expected
  - But elites were excessively confident, closed to open discussion
- Now “education” “Enlightenment values” “reasoned discourse” are blamed for the problems
  - Governance by “emotions,” gut feelings
  - Role of a strong leader
  - Some recent polls show that most Republicans think universities are bad! Large numbers are suspicious of science
- Enlightenment has to be relitigated every day
  - Attack on most fundamental values and understandings of Progress

# Demagogues represents a threat to our economic and political system

- And to the Enlightenment Project which has underlay advances in economy in the past two hundred years and to our economy
- Not even based on good market economics
  - **Rent seeking marked by exploitation of others and of political system**
    - For profit universities excel in exploitation and have resisted regulation
    - Exploitation of bankruptcy laws, weaknesses in our legal system
    - Taking advantage of political influence to get zoning changes, etc.
    - Getting paid above market prices for goods and services sold to government, paying less than market prices for assets purchased from the government
  - **Markedly different from the real bases of the wealth of nations**
    - Fail to understand difference between the creation of wealth with innovation and learning and the accumulation of wealth through exploitation
    - Worse: attacked our education and science institutions

# The real danger of demagogues

- Threatens to undermine the bases of our civilization
  - Most serious threat is to our “epistemology” and to the rule of law, the premises on which our democracy and our economy rest
    - Has sown doubt about both well established truths and our truth telling institutions
    - If one can sow doubt about whether cigarettes cause cancer and have other adverse effects, if one can sell bad products, one can sell bad ideas
    - Damage may be long lasting
    - We are just beginning to see its corrosive effects

# Economies based on exploitation rather than science, knowledge, and wealth creation

- Threatens long term growth
  - Failure to deal with climate change is an existential threat
- **Changing who we are as individuals and how our society functions**

# Alternative explanations of US problems and those of other advanced countries

- Caused by mismanagement of technological change and globalization
  - And, since 1980, rewriting rules of the economic and political game to favor those at the top and to undermine social protection of the rest
    - Didn't lead to higher growth: growth actually slowed
    - And predictably so
      - **Partially because we now realize that more equal societies have better performing economy**
- The demagogues have attempted to blame others (trading partners, immigrants) for failures, when the real blame is ourselves
  - Terms of trade agreements were largely dictated by US and reflected US corporate interests
    - They were unfair to developing countries and to workers everywhere—but not overall unfair to US
  - Trade deficit is determined by macroeconomics (disparity between domestic aggregate investments and savings)
    - Trade agreements affect who we trade with but not overall level of trade deficit
    - Massive increase in fiscal deficit will result in an increase in trade deficit *regardless of trade negotiations*
  - Trade policies will only worsen the plight of those who have been doing poorly
    - Hysteresis effects: deglobalization is costly

# Alternative Remedies

- Not inherent in capitalist system?
  - Need to rewrite the rules of the economy
  - Need to rewrite the rules of democracy—take out the influence of money
    - Rethink the balance between “expertise,” independent agencies, and parliamentary processes
    - Reinforcing systems of checks and balances—preventing abuse of power
  - Need more active polices of redistribution
  - More access to education
- Redistribution of wealth: only real check
- Need to get a better balance in our society
  - Between the market, state, and community
  - Between different forms of organization
  - Between the present and the future
  - Between humans and nature
  - Remembering that the design of our social, political, and economic institutions shapes who we are
- Market fundamentalism/neoliberalism lost the balance

# There is hope

- Especially among young people, there is a widespread understanding of some of these issues (e.g. how money in politics is corrupting our democracy; that our planet is at risk; that there is more to life than the accumulation of material goods)
- At other times in US history when inequality reach extremes, we pulled back from the brink