

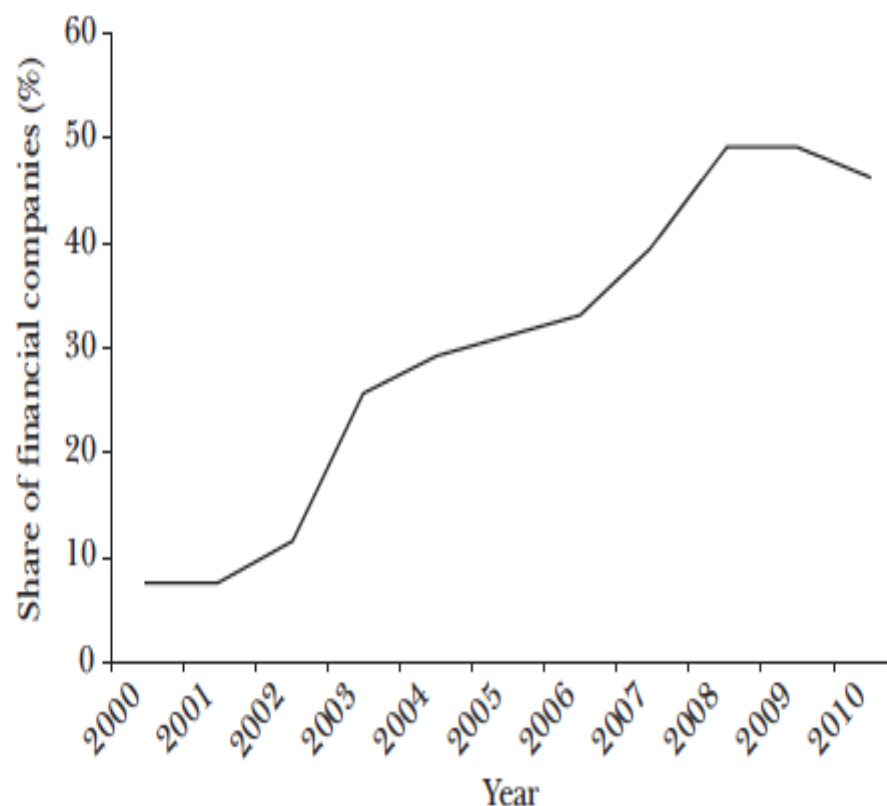
Global Distribution of Incomes  
Adjusted Net National Income Per Capita (current US\$), 2011

# The Crisis of Global Inequality



Source: World Bank WDI

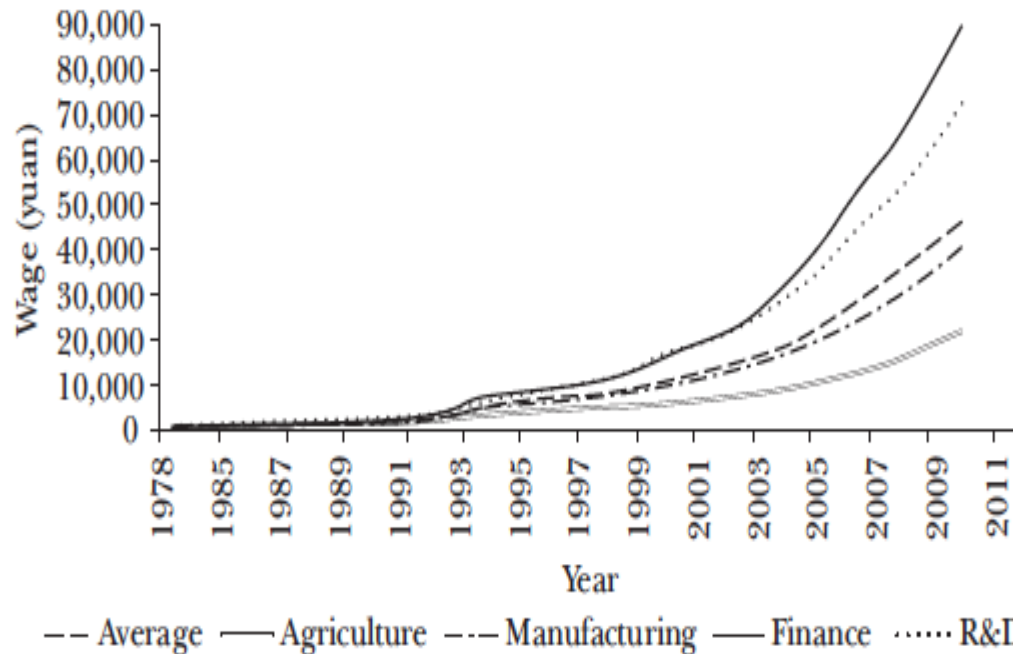
Thomas F. Remington  
Mid-Coast Forum on Foreign Relations  
October 30, 2017



**FIGURE 1. Total Net Profits of Financial Companies as a Proportion of Total Net Profits of All Companies Listed on the Chinese A-share Market**

Data source: WIND and authors' own calculations.

Note: Classification criterion for the financial industry is the one specified by the China Securities Regulatory Commission.



**FIGURE 4. Average Wage Levels of Selected Representative Industries**

Data source: NBS (1993-2012).

Note: All data are about urban areas.

Source: Yu Luo and Frank Zhu, "Financialization of the Economy and Income Inequality" *Political Studies* 2:2 (2014), pp. 46-66.

## What other explanations are there?

- Economic theories
  - Globalization of production, investment, and trade
  - “Skill-biased technological change” and the “race between education and technology”
  - “Help explain “hollowing up” effect, polarization of wages
- Political forces
  - Declining bargaining power of organized labor
  - Mobilization of conservatives—use power of government to capture rents
- Social changes
  - Rising immigration
  - Changing family structure (eg more divorce, “assortative mating”)
  - More socio-economically homogeneous neighborhoods (affecting social networks, mobility)
- Cultural trends
  - “Hollywood effect” – compensation for perceived stars is many times greater than that of their slightly less famous or able peers. (“winner-take-all”)
  - Helps explain enormous increase in incomes at top end of distribution

Classic rent-seeking:

**Proposal 6: Call for public votes on new Detroit-Windsor bridge defeated**

By [David Eggert | deggert1@mlive.com](#)

on November 06, 2012 at 10:53 PM,  
updated November 07, 2012 at 11:02 AM

LANSGING, MI – Voters on Tuesday rejected Proposal 6, which called for public votes before construction can begin on a new bridge from Michigan to Canada. The defeat came despite a \$33 million campaign to support it. The Moroun family, owners of the aging Ambassador Bridge that spans the Detroit river to Windsor, provided the unprecedented campaign funding to stop the second bridge in its tracks. With 92 percent of precincts reporting, Proposal 6 had 1.67 million votes for and 2.49 million votes against - or 40 percent



## How does rising inequality harm society?

- Reduces willingness to provide public goods
  - Smaller middle class with common stake in society
  - Lowers social cohesion; Keith Payne: treat high inequality as a public health crisis
  - Intensifies redistributive conflict (including in displaced forms, eg nativism)
  - Shortens time horizons – growth spells shorter
  - Reduces happiness (even when level of development and other factors accounted for—cf *World Happiness Report, 2016*)
- Undermines political equality, increases political influence of those with concentrated wealth & income
- Reduces social mobility:
  - Facilitates reproduction of advantage across generations
  - Increases homogeneity of neighborhoods
- But increases number of “global elite,” ie wealthy people who live and work in multiple countries (43% of high net worth people have lived in > 1 country according to a Barclay’s survey of

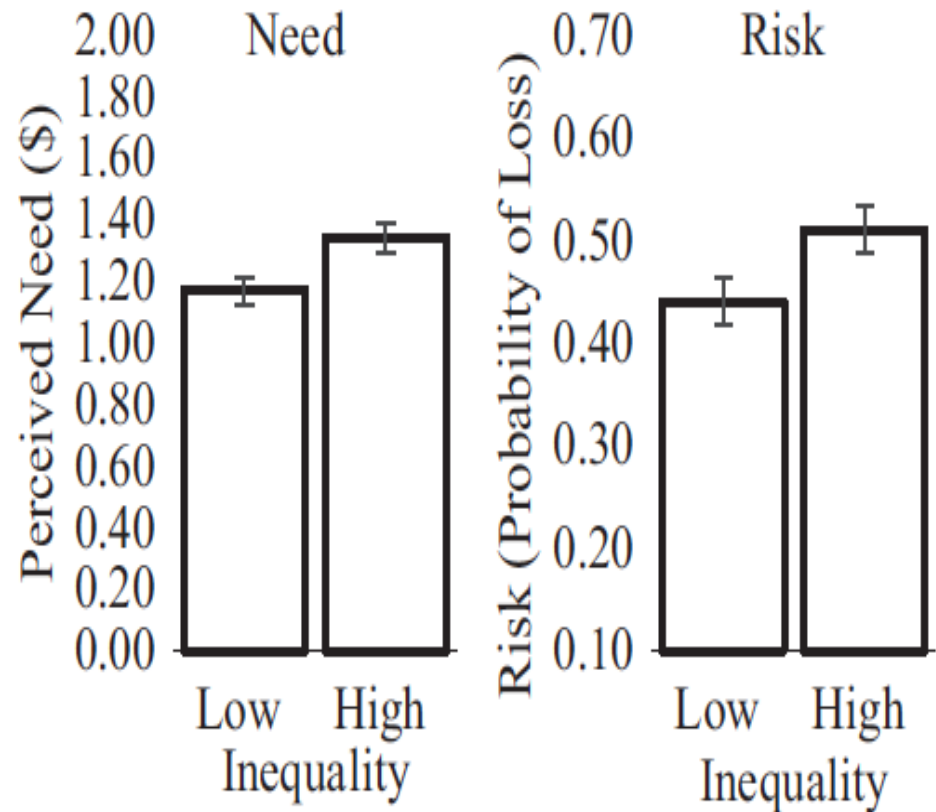
# Economic inequality increases risk taking

B. Keith Payne<sup>a,1</sup>, Jazmin L. Brown-Iannuzzi<sup>b</sup>, and Jason W. Hannay<sup>a</sup>

*Proceedings of the National Academy of Sciences* 114: 18 (May 2, 2017), pp. 4643-4648

## Significance

Income inequality is rising around the world. Increased income inequality has been linked with higher rates of crime, greater debt, and poorer health, but the mechanisms linking inequality to poor outcomes among individuals are poorly understood. This research tested a behavioral account linking inequality to individual decision making. The account suggests that more unequal outcomes lead people to perceive that they need more resources to be satisfied. Higher perceived needs, in turn, motivate greater risk taking to meet those needs. Results of three experiments and an analysis of large-scale internet search data supported the proposed account. Results suggest that inequality may promote a range of poor outcomes, in part, by increasing risky behavior.



Basic theoretical explanation: "social comparison"  
--Payne: inequality makes everybody "feel poor"

Perceived need and risk preference as a function of inequality in study 1. Columns reflect means, and error bars reflect SEs.

“Skill-biased technological change” refers to increasing education-related wage differentials.

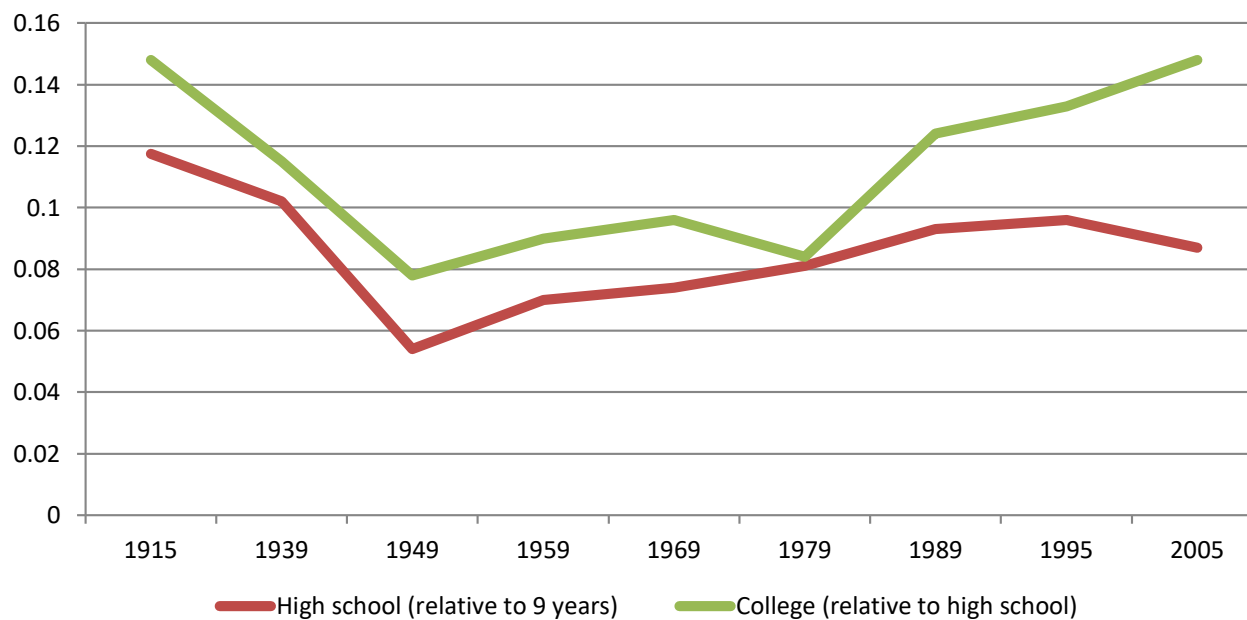
But the theory cannot explain the growing concentration of top-end incomes.

## Rate of Return to a Year of School

### Young Men, 1915 - 2005

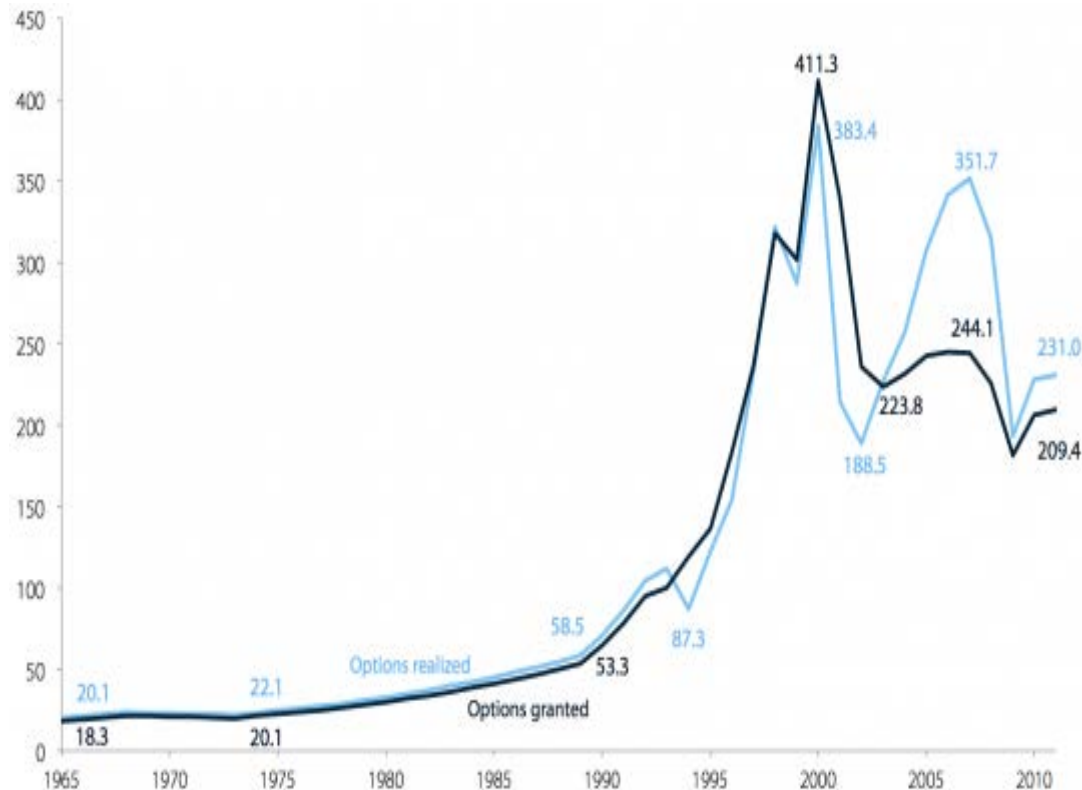
(composition-adjusted log weekly wage differentials for full-time male wage and salary workers)

Source: Claudia Goldin and Lawrence Katz, *The Race between Education and Technology*, p. 84)





## The “Hollywood Effect:” CEO-to-worker compensation ratio, with options granted and options realized, 1965–2011



Lawrence Mishel and Natalie Sabadish, “CEO Pay and the Top 1%,”  
Economic Policy Institute, May 2, 2012

<http://www.epi.org/publication/ib331-ceo-pay-top-1-percent/>

Powerful interests use government to capture rents (eg by weakening regulation, share to their advantage) – ie reinforce rather than offset market-generated inequalities.

Much of the income generated is converted into wealth, often non-productive, and offshored or in luxury goods and services.

8% or more of the world's household wealth is hidden in offshore tax shelters.

Or it is invested in expensive real estate, or ...



This 370-foot yacht ("Le Grand Bleu") was anchored in Penobscot Bay and Casco Bay this past summer. It is owned by Russian oligarch Evgenii Shvidler.

*Forbes profile:*

## **Evgeny (Eugene) Shvidler**

**REAL TIME NET WORTH — as of 9/25/17**

**\$1.37 B**

Evgeny Shvidler, who became an American citizen in 1994, is the best friend of Russian billionaire Roman Abramovich. He lives in the affluent Belgravia neighborhood of London and owns a house in Snowmass, Colorado. Among his business interests are a stake in Russian steelmaker Evraz, Moscow real estate, and cash from the 2005 sale of his Sibneft stake to Gazprom. Together with Abramovich, in April 2013 he bought shares of Norilsk Nickel. Shvidler is non-executive chairman of the board of Highland Gold Mining, where he has an 12.56% stake. In January 2013 he was appointed to the board of AFC Energy, a British company that develops alkaline fuel cell technology where he owns a 4.47% stake. His vineyard at his Château Thenac in France produces seven grape varieties and his wines are beginning to garner positive reviews from critics. It also produces kosher wine. His property also has two plum orchards. His 370-foot yacht, Le Grand Bleu, was a gift from Abramovich. He was the primary funder for the rebuilding of a Jewish school in England that is now called Beit Shvidler Primary School and he funds another school, Center Beit Shvidler, in Moscow. In 2016 Cleveland Clinic's Glickman Urological and Kidney Institute received \$2 million from Eugene and Zara Shvidler to

This painting, The Savior of the World, by Leonardo da Vinci, is owned by Dmitrii Rybolovlev. He was the owner of the Uralkali potassium company, and now owns the Monaco soccer club. He will sell the painting at auction, at Christie's, in November.

The estimated price is \$100 million.

(*Vedomosti*, October 11, 2010)



Inequality fuels political polarization.

As the gap in income and wealth between rich and poor grows, the rich exercise political power to block redistribution or the provision of public goods and services.

In the US, they do so through organization, media and think tank campaigns, and political contributions.

In non-democratic countries, they do so through personal connections with rulers and through corruption.



[Wall Street Journal \(Online\); New York, N.Y. \[New York, N.Y\]24 Jan 2014: n/a.](#)

Regarding your editorial "Censors on Campus" (Jan. 18): Writing from the epicenter of progressive thought, San Francisco, I would call attention to the parallels of fascist Nazi Germany to its war on its "one percent," namely its Jews, to the progressive war on the American one percent, namely the "rich."

From the Occupy movement to the demonization of the rich embedded in virtually every word of our local newspaper, the San Francisco Chronicle, I perceive a rising tide of hatred of the successful one percent. There is outraged public reaction to the Google buses carrying technology workers from the city to the peninsula high-tech companies which employ them. We have outrage over the rising real-estate prices which these "techno geeks" can pay. We have, for example, libelous and cruel attacks in the Chronicle on our number-one celebrity, the author Danielle Steel, alleging that she is a "snob" despite the millions she has spent on our city's homeless and mentally ill over the past decades. This is a very dangerous drift in our American thinking. Kristallnacht was unthinkable in 1930; is its descendant "progressive" radicalism unthinkable now?



"There are 47 percent of the people who will vote for the president no matter what. All right, there are 47 percent who are with him, who are dependent upon government, who believe that they are victims, who believe the government has a responsibility to care for them, who believe that they are entitled to health care, to food, to housing, to you-name-it. That's an entitlement. And the government should give it to them. And they will vote for this president no matter what. And I mean the president starts out with 48, 49 percent ... he starts off with a huge number. These are people who pay no income tax. Forty-seven percent of Americans pay no income tax. So our message of low taxes doesn't connect. So he'll be out there talking about tax cuts for the rich. I mean, that's what they sell every four years. And so my job is is not to worry about those people. I'll never convince them that they should take personal responsibility and care for their lives."

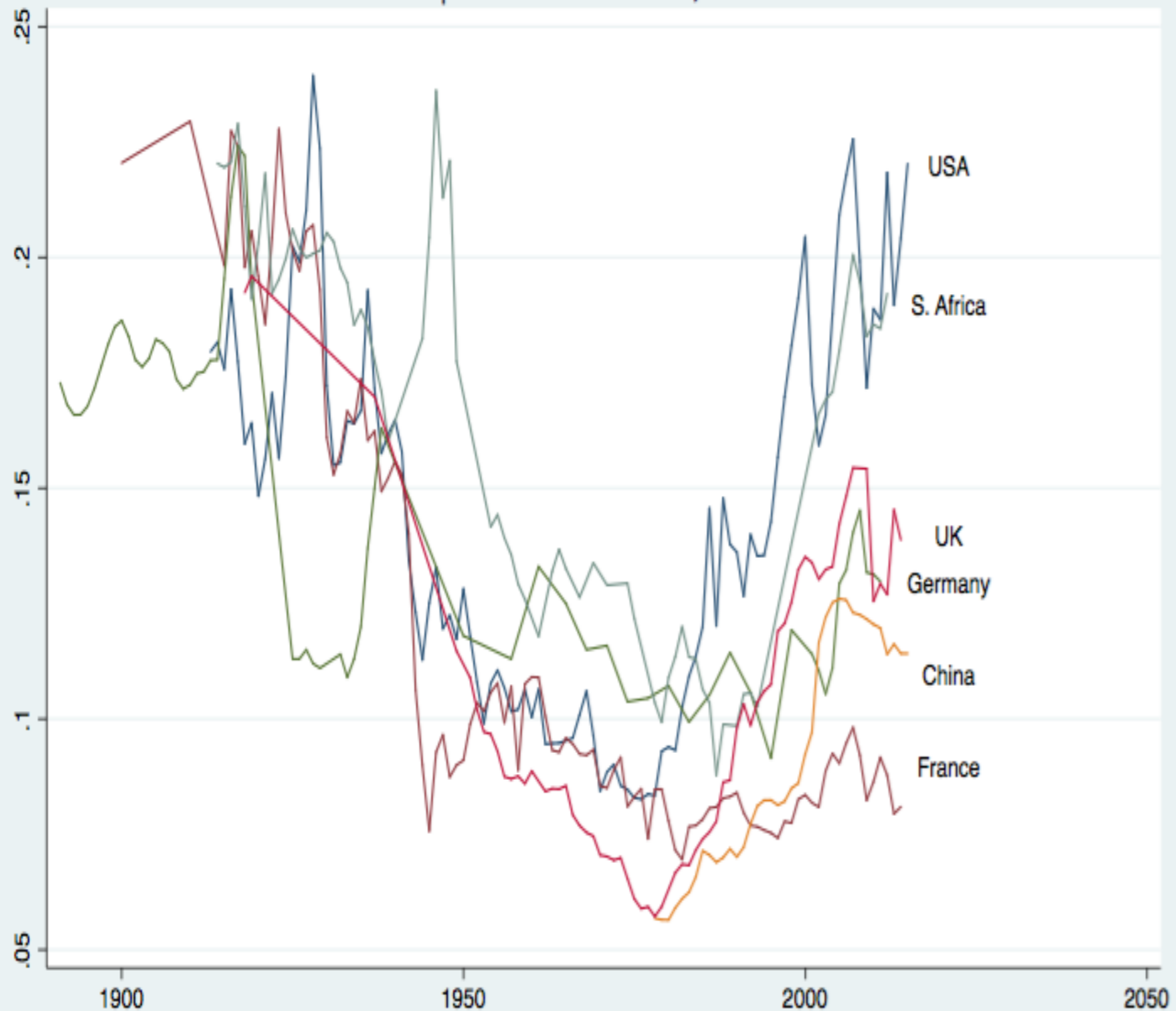
--Mitt Romney, speaking at a private reception for donors in May 2012.



Three premises:

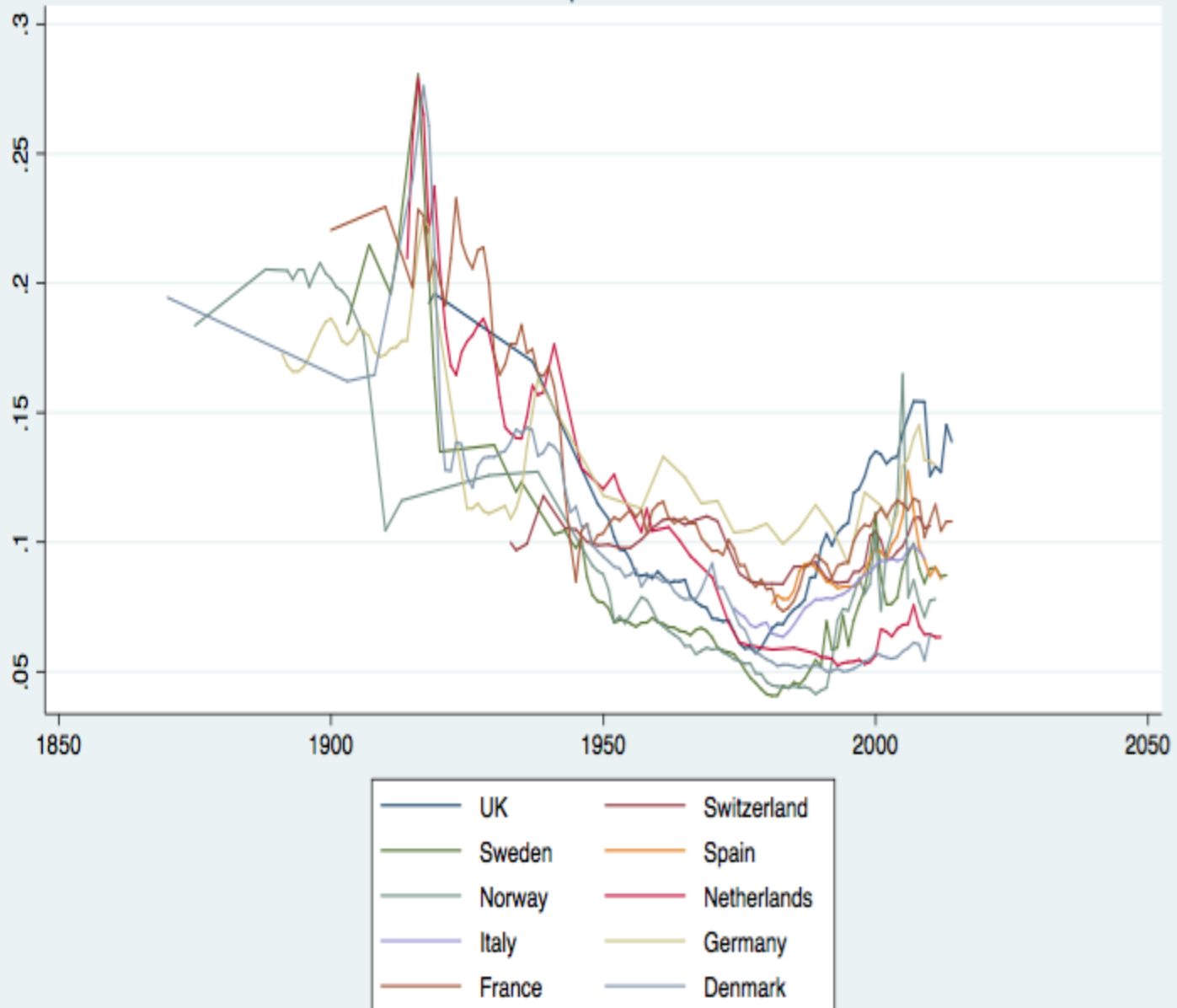
1. Inequality is not the same as poverty—they can move in opposite directions.
2. Inequality is a function of trends at the bottom, the middle, and the top of the distribution.
3. Inequality matters in and of itself and has reached a crisis stage, both within and across societies.

WID World: Top 1% Income Share, Selected Countries



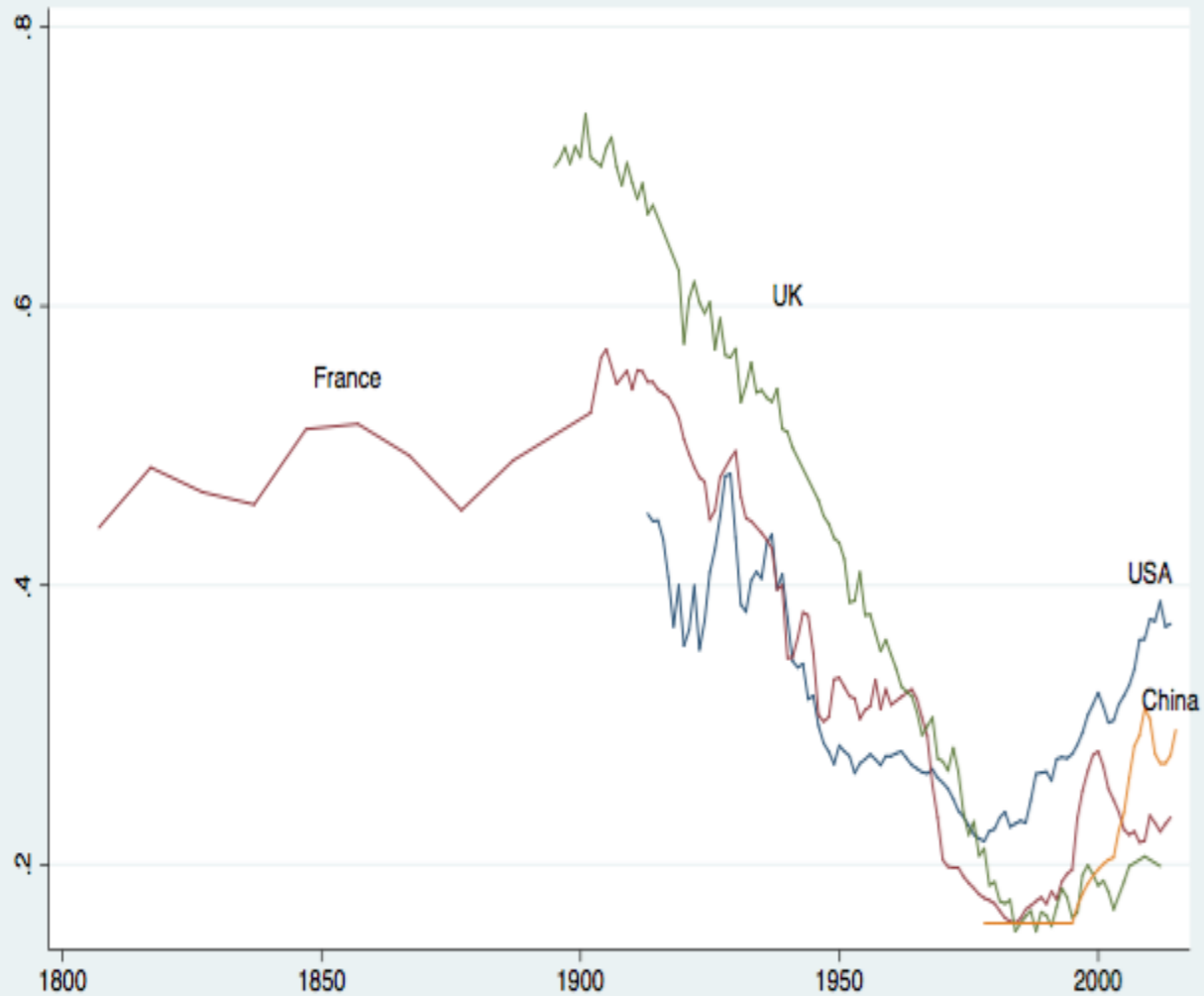
Source: WID World

## WID World: Top 1% Income Share



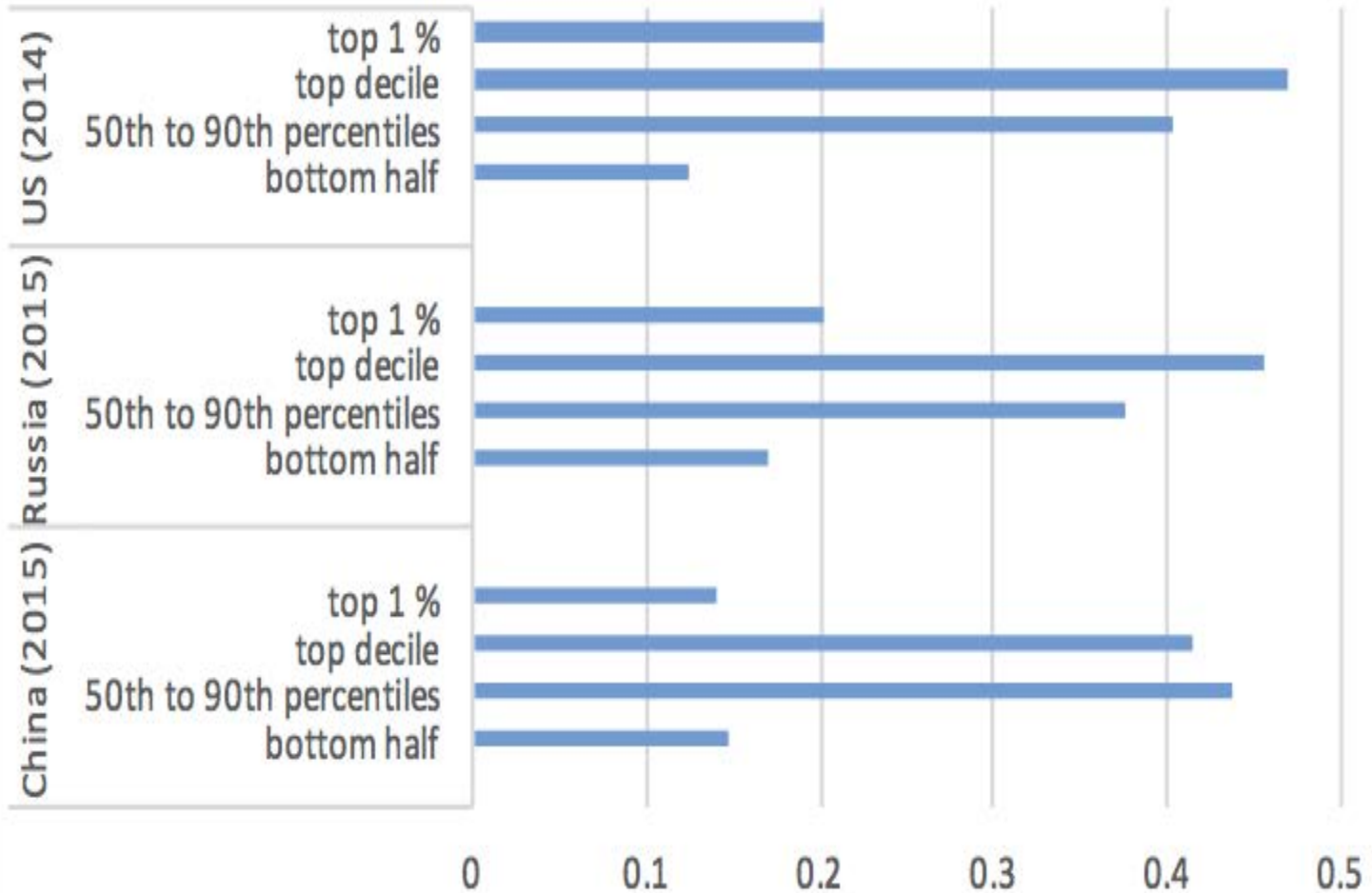
Source: WID World

Top 1% shares of net household wealth, 1807 - 2015  
selected countries

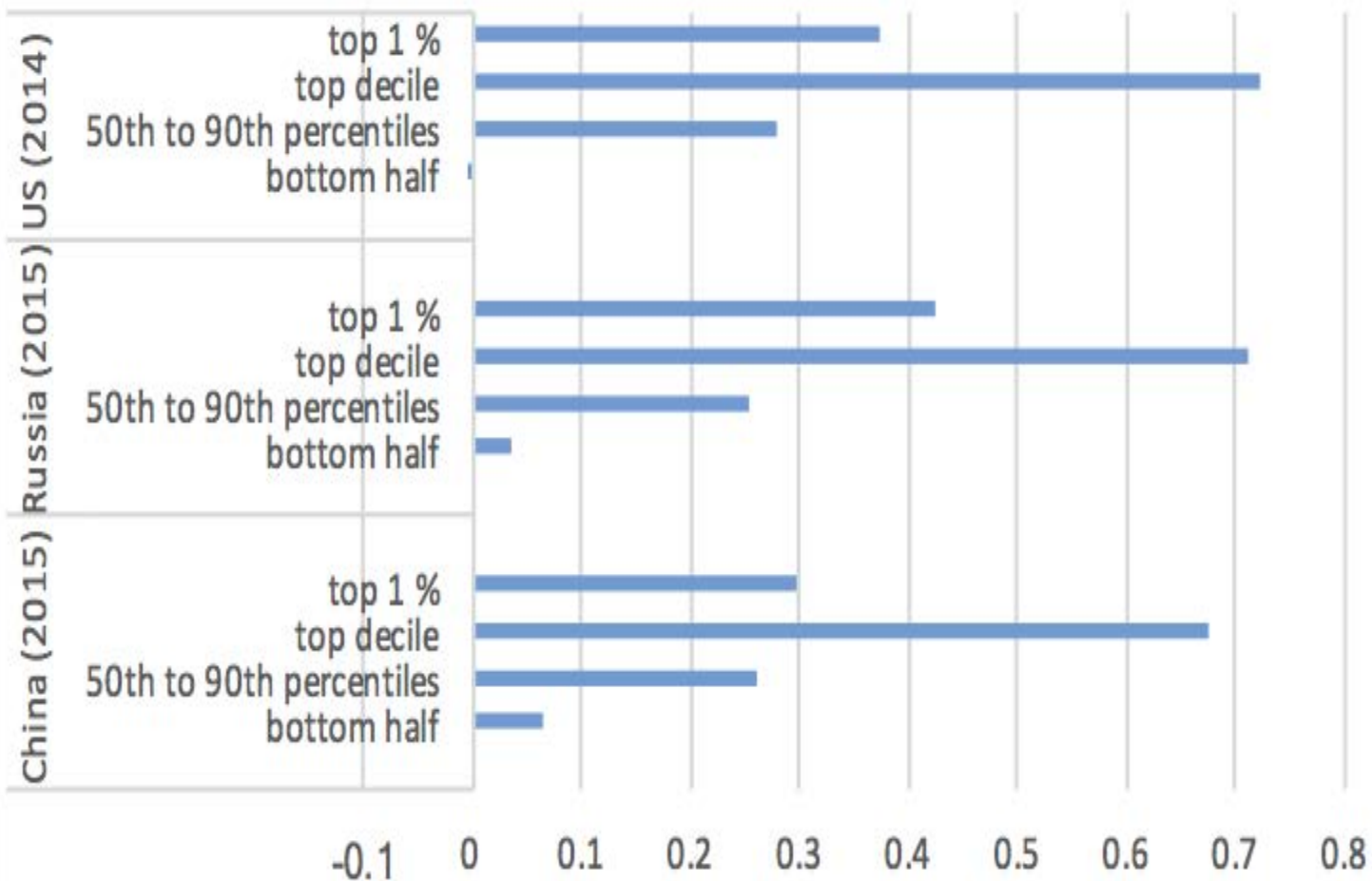


Source: WID World

## Income Distribution



## Wealth Distribution

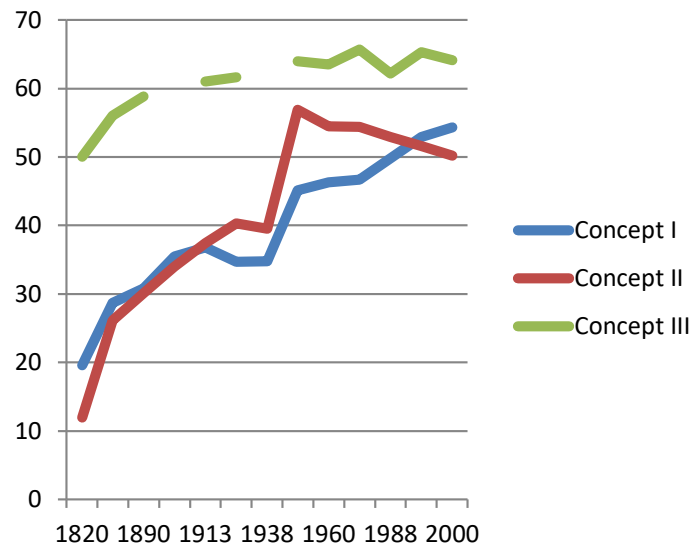


Has global inequality grown?

Within most societies, income and wealth inequality has risen.

But whether global inequality has grown depends on the measure used...

The World Bank economist Branko Milanovic has estimated global inequality using three alternative measures. Concept I means inequality of national income means. Concept II means inequality by weighted nation means. Concept III treats the world's population as if they all belonged to one society. Concept II inequality has gone down because of the income gains in China, India, and other Asian countries.



Source: Branko Milanovic, *Worlds Apart*, (Princeton University Press, 2000)  
Table 11.1: "World Inequality in Historical Perspective", p. 142.



Milanovic's figures show that historically, global inequality has moved through three phases:

1. Traditionally, most inequality was within-country; the poor in one country were not appreciably poorer than those in another, likewise the rich. The largest share of global inequality was *within* countries
2. After the industrial revolution, mean incomes in some countries grew much faster than in others; most global inequality was due to differences across countries. The poor in rich countries were richer than the rich in poor countries.
3. Today, with within-country inequality rising again in most regions of the world, we are moving back to a situation where more inequality is within countries relative to the amount caused by cross-country differences

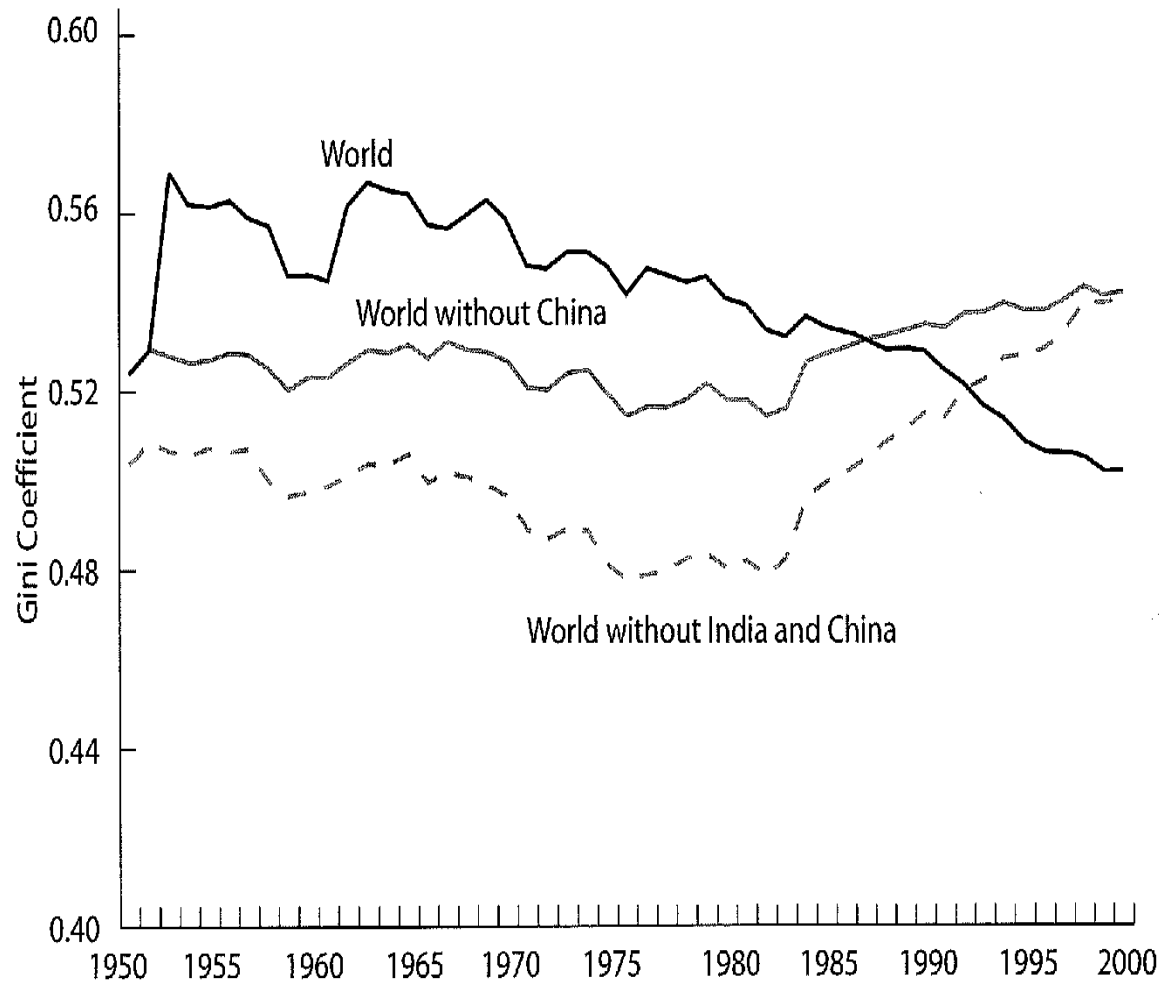
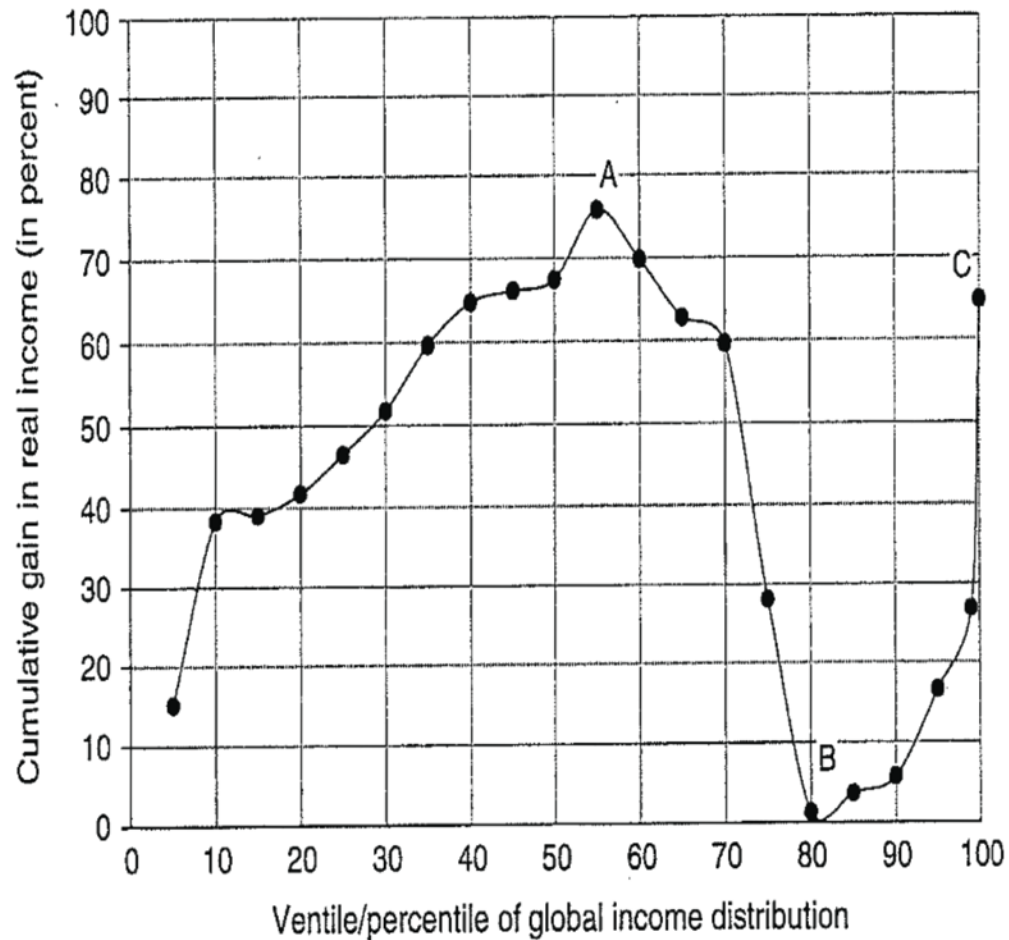


Figure 8.3. Weighted international inequality without China and India.

Another way to see it:

Globally, which  
income groups  
have gained ground,  
and which have not?

Branko Milanovic,  
*Global Inequality*,  
Figure 1.1  
“the elephant graph”



**FIGURE 1.1.** Relative gain in real per capita income by global income level,  
1988–2008

1988 2008

One reason inequality has risen in many societies is the growth of the financial industry.

The financial industry has come to occupy a commanding share of corporate profits as economic activity has shifted out of the real economy and into finance.

The information-communications revolution has resulted in an enormous expansion driving up profits and wages in the financial industry.

This characterizes not just the US, but other countries as well, including Russia and China.

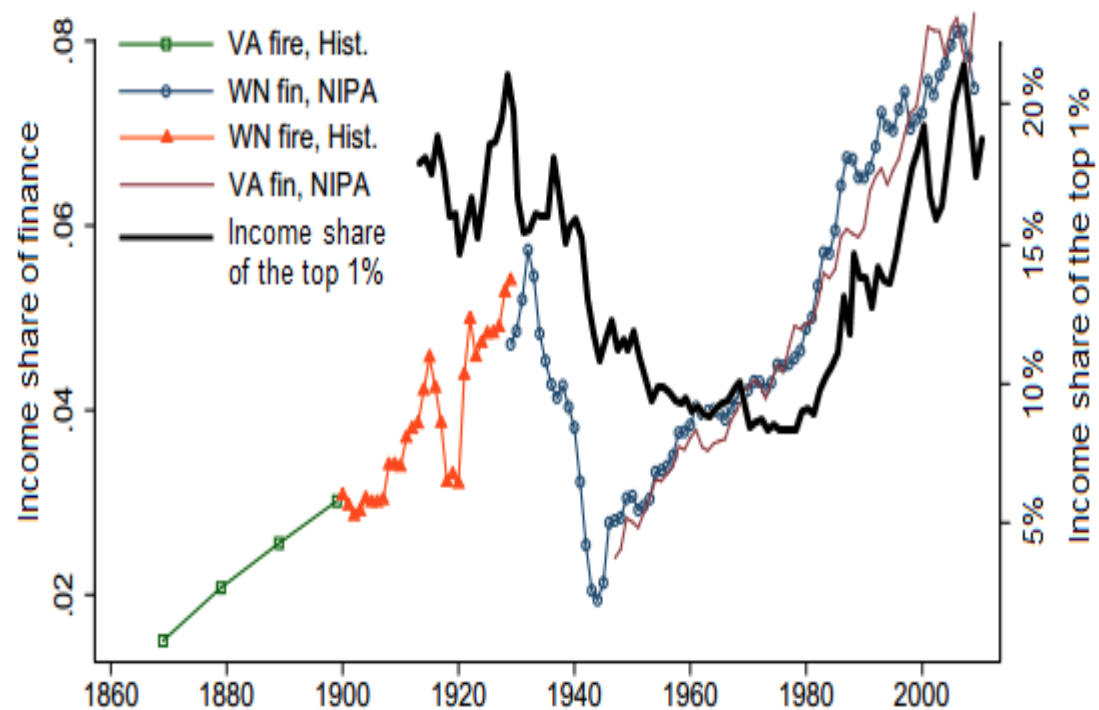
When government regulation of financial institutions is weak or corrupt, their control over the creation of credit gives them enormous opportunities to extract rents from society.

This helps explain the huge growth of profits and compensation levels in the financial industry in countries where competition and regulation are weak.

"A quarter of all American billionaires work in finance and investments, an industry that employs less than 1% of all workers." –*Economist*, March 5, 2016, p. 66.

## Economic data suggests a strong correlation between an expanding financial industry and rising income inequality

The United States:



Note: Original graph from Philippon (left scale) has been reformatted and overlaid with income share data including capital gains (right scale).

Original notes: VA is value added, WN is compensation of employees, "fin" means finance and insurance, "fire" means finance, insurance, and real estate. For "NIPA", the data source is the BEA, and for "Hist" the source is the Historical Statistics of the United States.

Source: Philippon (2012), Piketty and Saez

Source: <https://tcf.org/content/commentary/graph-how-the-financial-sector-consumed-a>

In Russia, the financial sector has seen the highest growth in average compensation—even more than oil and gas.

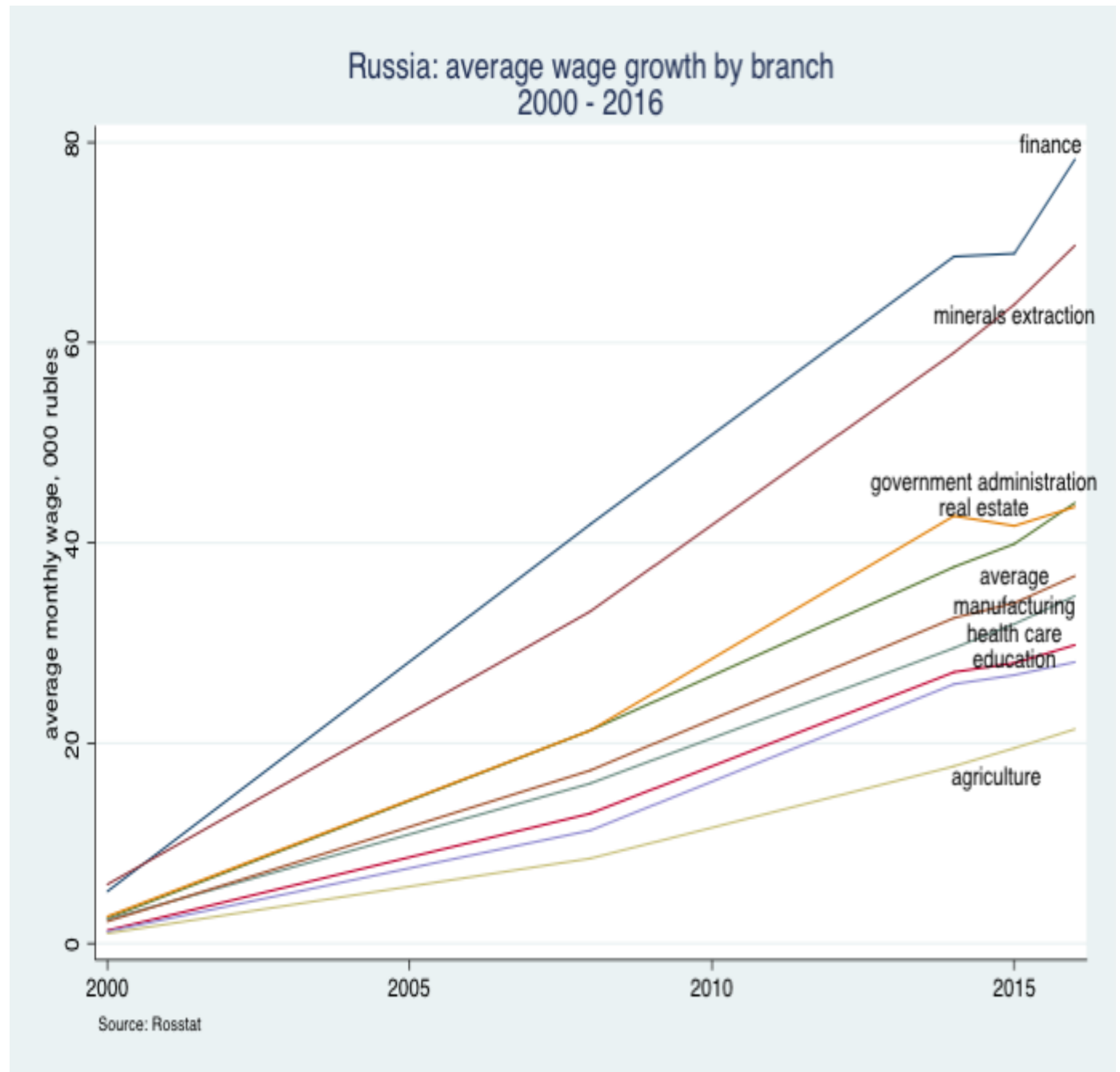
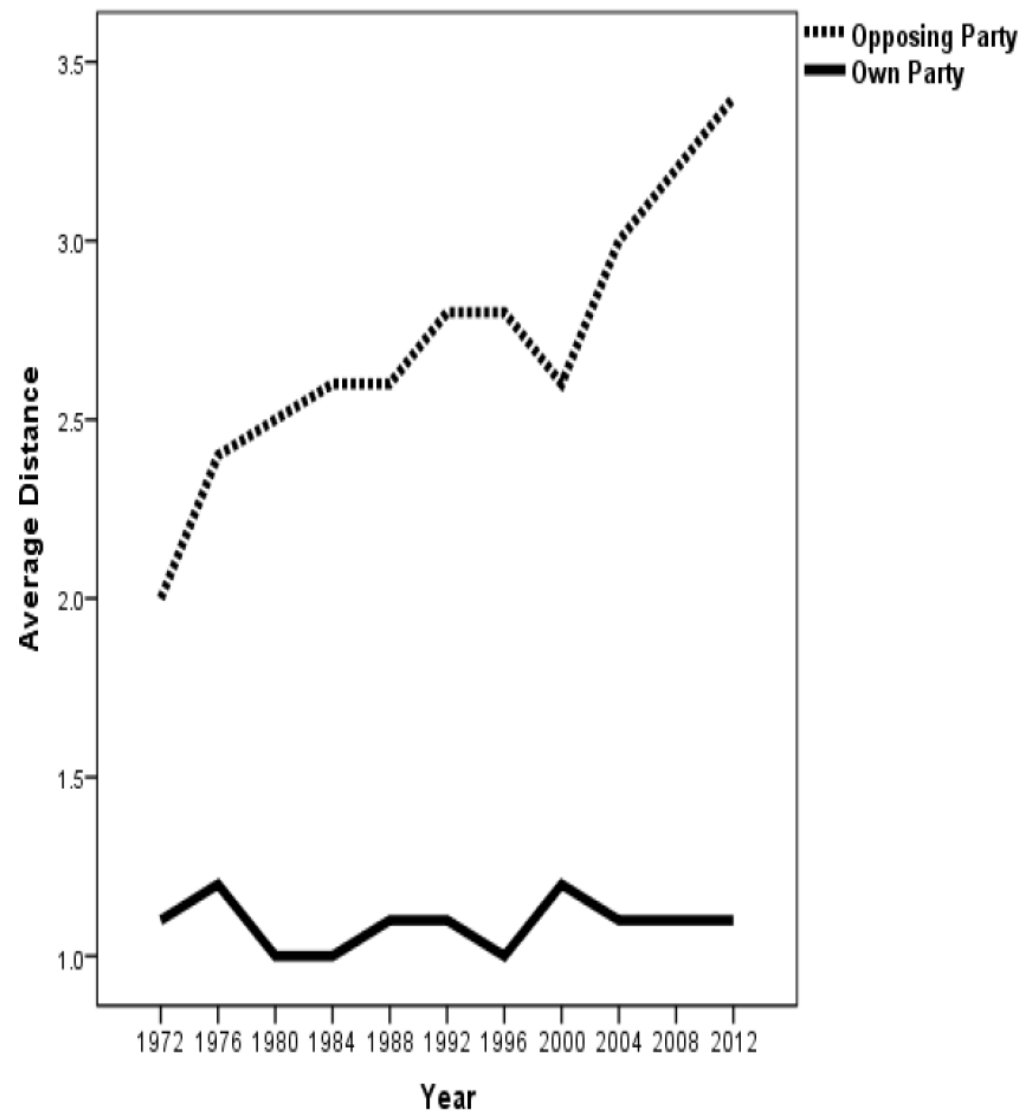
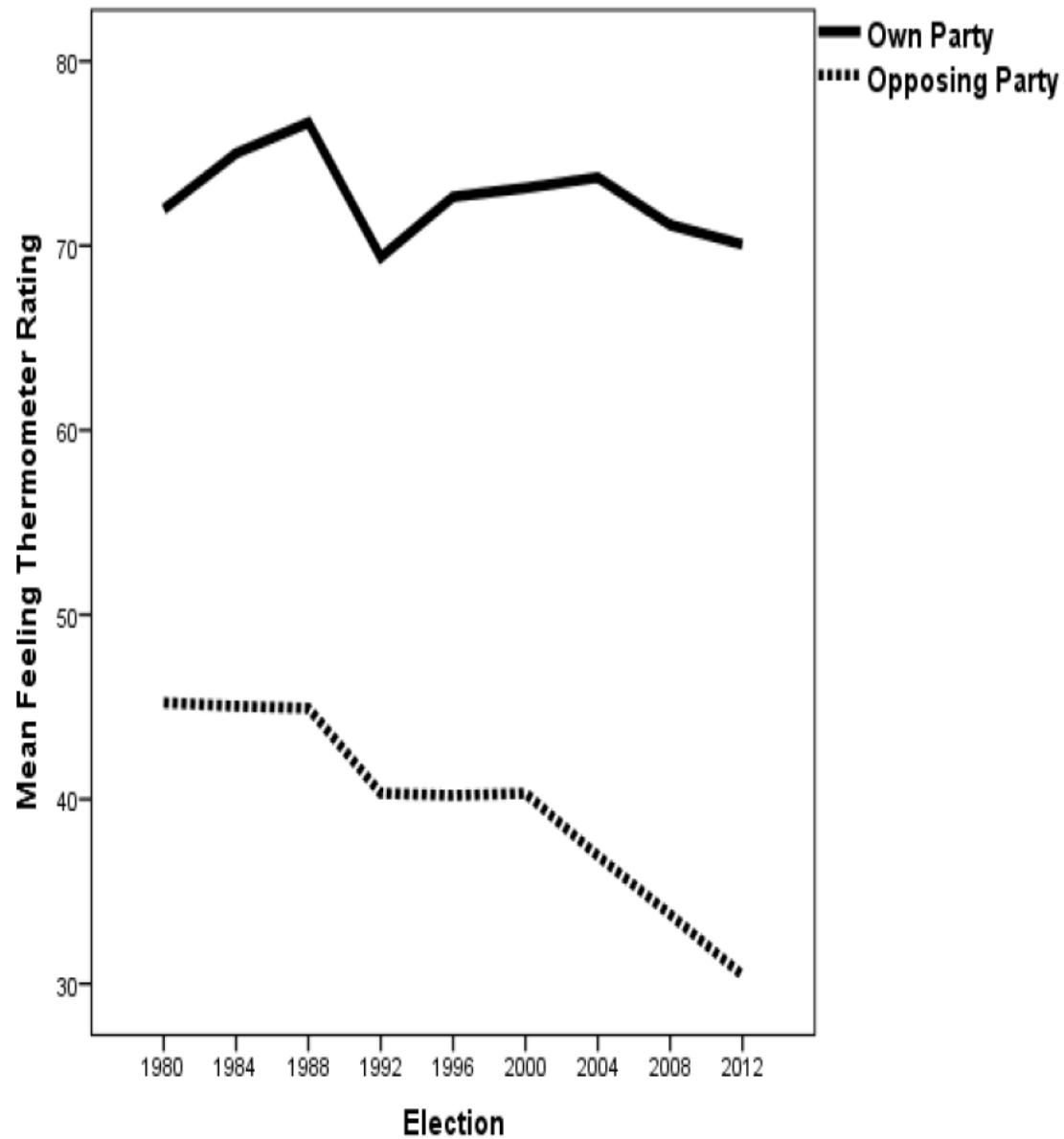


Figure 3  
Mean Distance from Own Party and Opposing Party on Liberal-Conservative  
Scale, 1972-2012



Source: American National Election Studies Cumulative File

Figure 5  
Feeling Thermometer Ratings of Own Party and Opposing Party, 1980-2012



Source: American National Election Studies Cumulative File



FIGURE 1

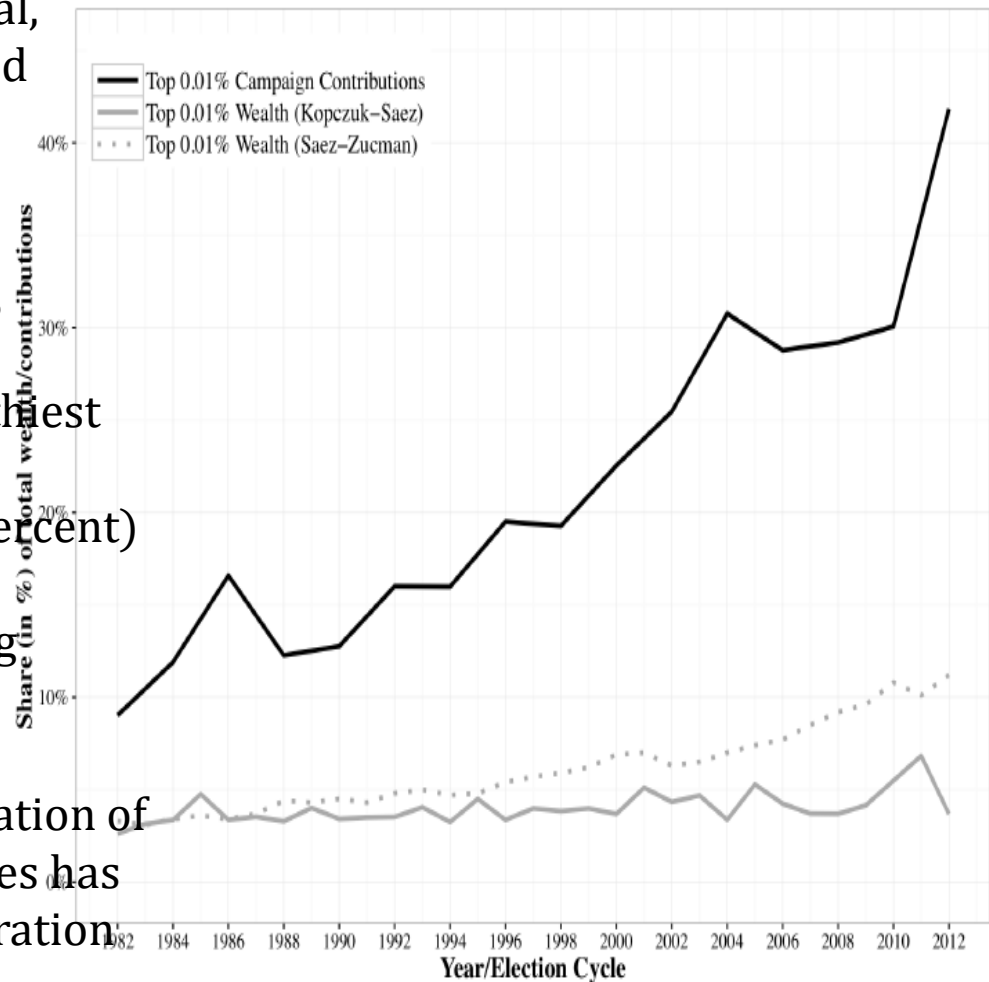
*Concentration of Wealth and Campaign Contributions in the Top 0.01 Percent of Households and Voting Age Population.*

Adam Bonica and Howard Rosenthal, "Increasing Inequality in Wealth and the Political Contributions of Billionaires," unpublished paper.

The dark line shows that over time, the share of total campaign contributions donated by the wealthiest .01% of voting age population (ie the top one-hundredth of one percent)

The lower lines show the increasing concentration of wealth in the US.

The graph shows that the concentration of political contributions by billionaires has risen much faster than the concentration of wealth.



Note: The dark line tracks the share of campaign contributions in federal elections given by the top 0.01 percent of the voting age population. See Bonica et al. (2013) for details on how the trend was constructed. The shaded lines track the share of total private wealth owned by the top 0.01 percent of households as measured by Saez and Zucman (2016) by capitalizing income tax data (solid line) and by Kopczuk and Saez (2004) estimated from estate tax returns (dashed line). The Kopczuk and Saez (2004) series was extended to 2012 by Saez and Zucman (2016). Both measures were obtained from <http://eml.berkeley.edu/~saez/>.

Inequality also blocks social mobility.

As the gap in income and wealth between rich and poor grows, family background becomes an increasingly important determinant of the life chances of the next generation.

Katz & Krueger,  
“Documenting Decline in US  
Economic Mobility,”  
*Science* (April 2017)

Top line shows Chetty et al.  
calculations of absolute income  
mobility rates for successive  
birth cohorts;  
bottom line shows gap in median  
earnings of childrens’ and parents  
generations over succesive  
cohorts

### Mobility and child-parent income gap, linked over time

(Top) From online table 1, column CY, of Chetty et al. (see [www.equality-of-opportunity.org/data/](http://www.equality-of-opportunity.org/data/));  
(bottom) from table S1 in Chetty et al. (1). Based on authors’ calculations (see SM).

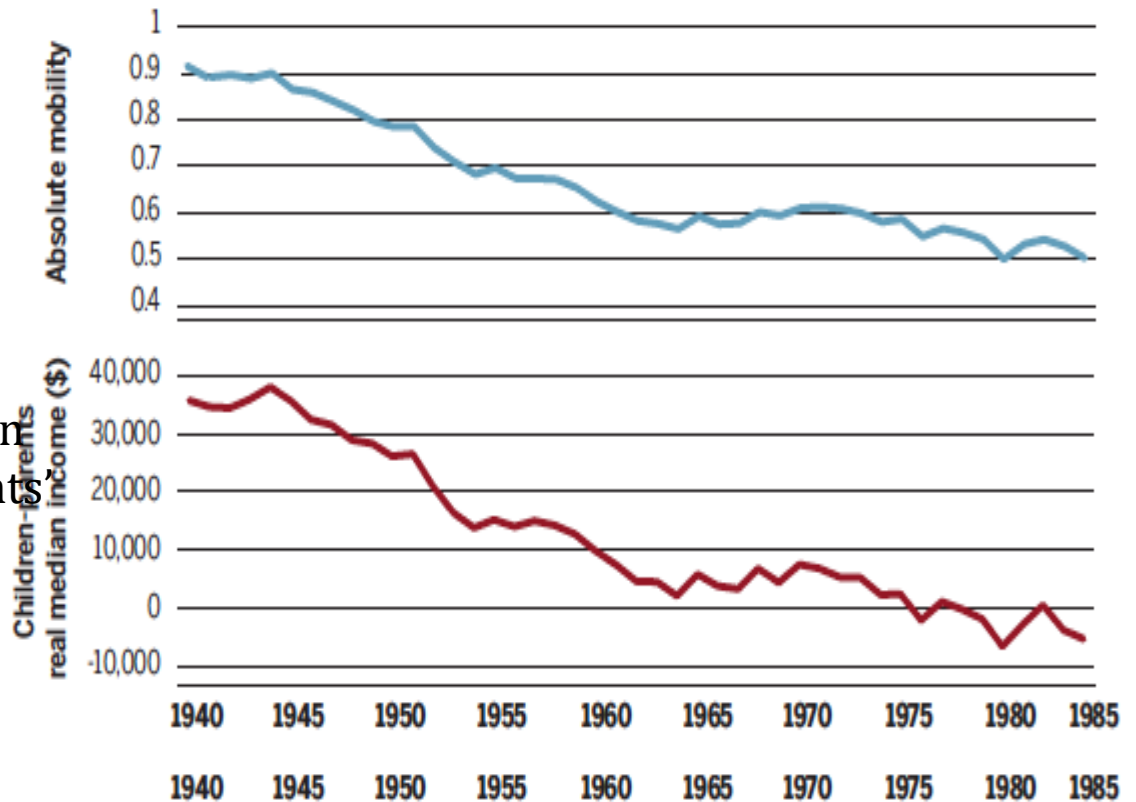
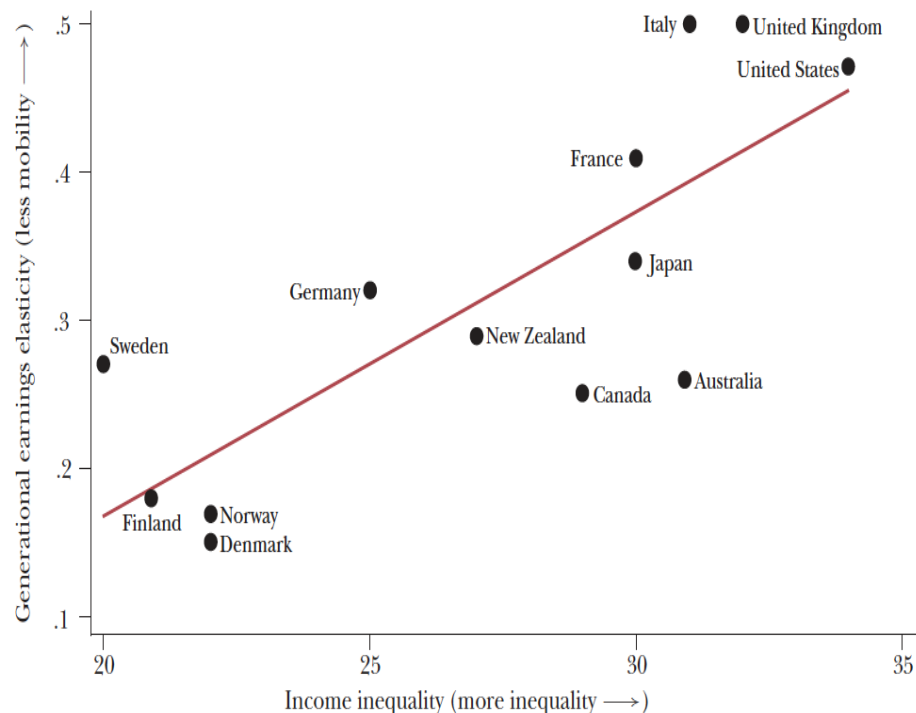


Figure 1

### The Great Gatsby Curve: More Inequality is Associated with Less Mobility across the Generations

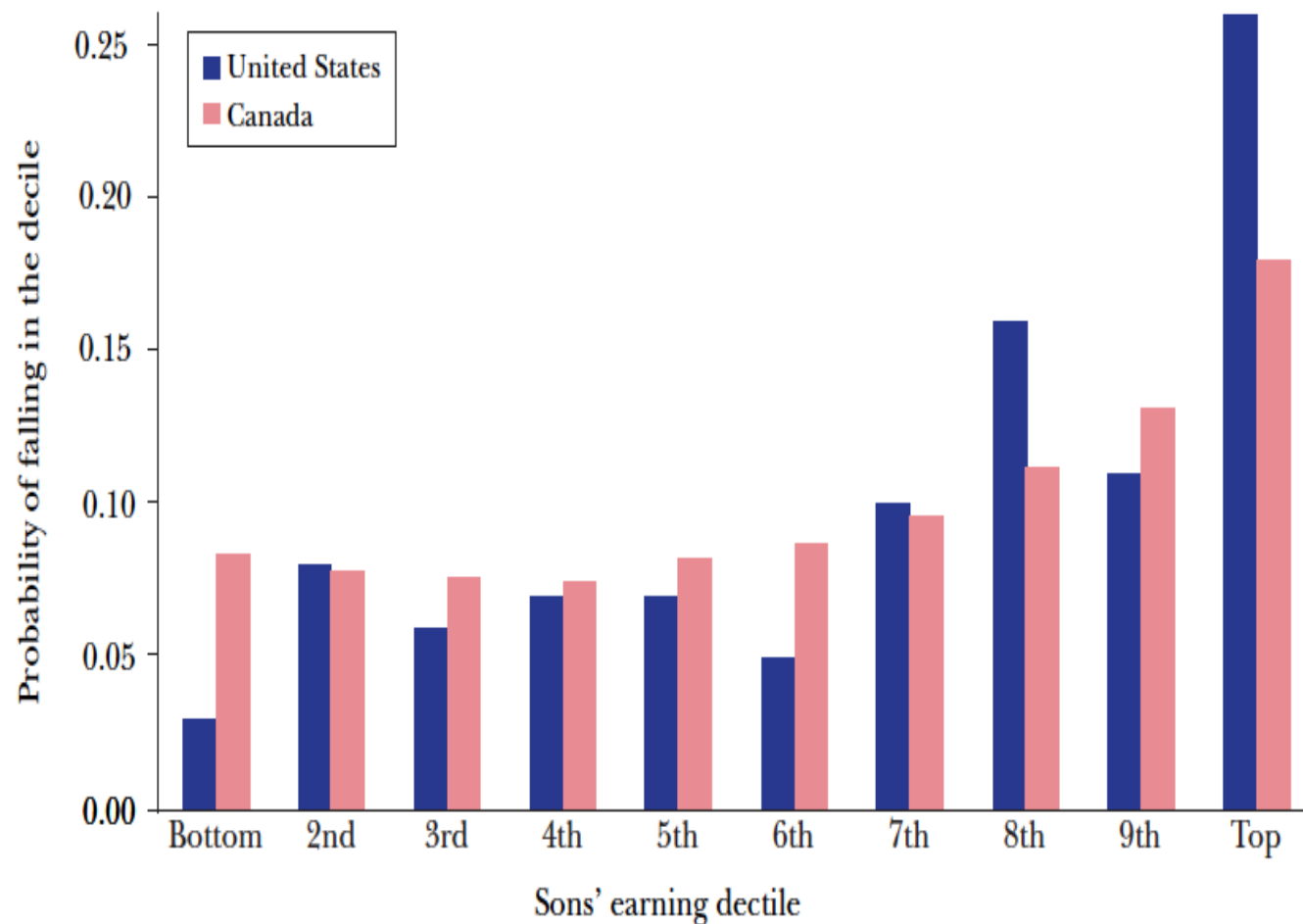


Source: Corak (2013) and OECD.

Notes: Income inequality is measured as the Gini coefficient, using disposable household income for about 1985 as provided by the OECD. Intergenerational economic mobility is measured as the elasticity between paternal earnings and a son's adult earnings, using data on a cohort of children born, roughly speaking, during the early to mid 1960s and measuring their adult outcomes in the mid to late 1990s. The estimates of the intergenerational earnings elasticity are derived from published studies, adjusted for methodological comparability in a way that I describe in the appendix to Corak (2006), updated with a more recent literature review reported in Corak (2013), where I also offer estimates for a total of 22 countries. I only use estimates derived from data that are nationally representative of the population and which are rich enough to make comparisons across generations within the same family. In addition, I only use studies that correct for the type of measurement errors described by Atkinson, Maynard, and Trinder (1983), Solon (1992), and Zimmerman (1992), which means deriving permanent earnings by either averaging annual data over several years or by using instrumental variables.

Figure 2

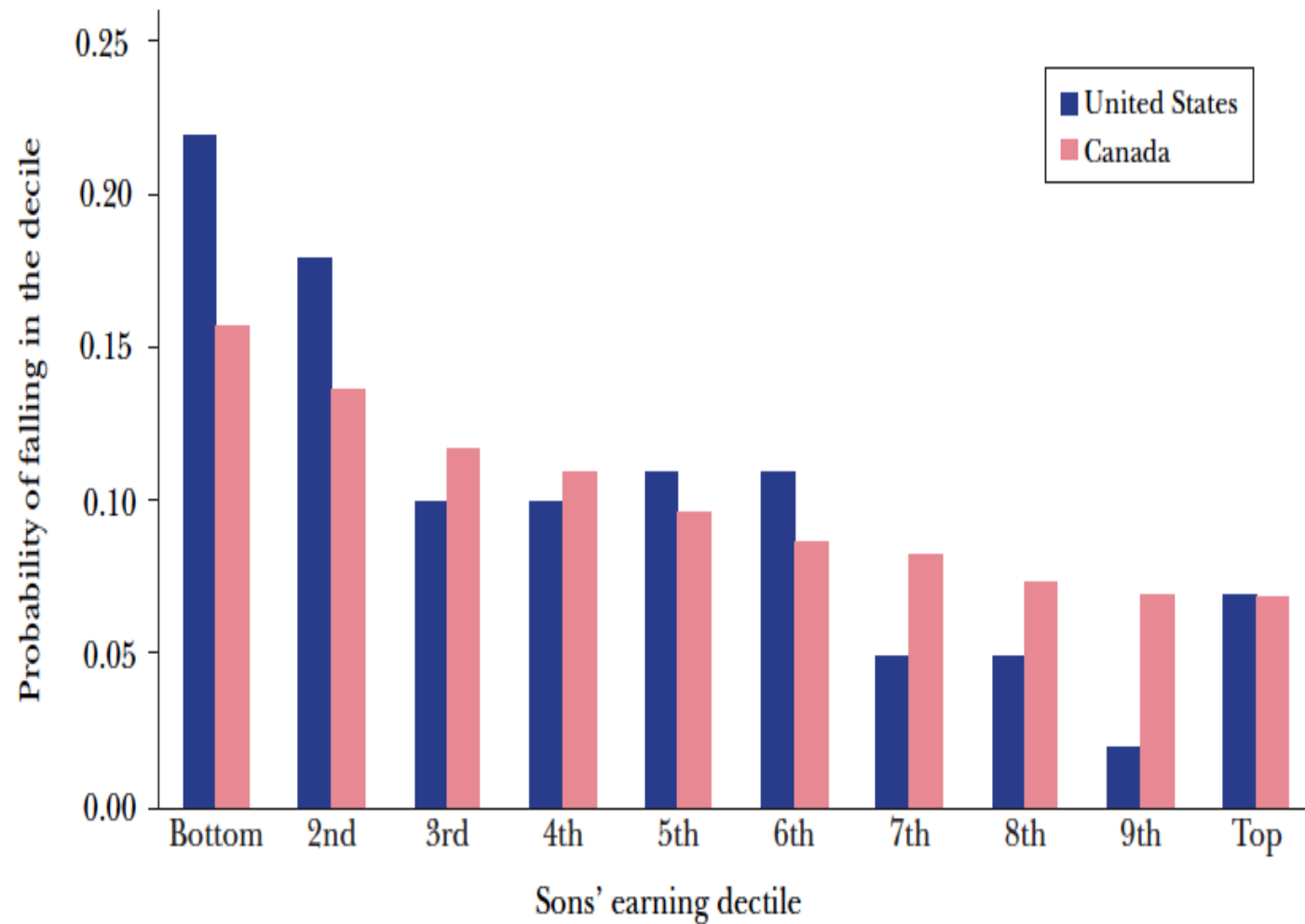
## Earnings Deciles of Sons Born to Top Decile Fathers: United States and Canada



Source: Corak and Heisz (1999, table 6); Mazumder (2005, table 2.2).

*Figure 3*

**Earnings Deciles of Sons Born to Bottom Decile Fathers: United States and Canada**



*Source:* Corak and Heisz (1999, table 6); Mazumder (2005, table 2.2).

## What are the consequences for international relations?

- Turns intra-national distributional conflicts into inter-national ones
  - Globalizes conflicts over allocation of cost to alleviate negative externalities of economic activity (eg environmental pollution) because policy solutions to global problems require national consent
  - Shorter time horizons mean unwillingness to solve long-term problems, such as global climate change
- Milanovic: we are moving to a world without a middle class (only 17% of world live on incomes between 75 and 125% of the world median. --Milanovic, *Worlds Apart*, p. 130.)
- Lowers willingness to cooperate in solving common-pool resource problems (common pool resources are non-excludable but rivalrous, ie it is hard to keep people from exploiting them but they can be depleted by overuse, eg overfishing in oceans)
  - Solutions to common pool resource problems take cooperation typically based on trust among groups capable of monitoring behavior of members and sanctioning abuse
  - Many international conflicts stem from intra-national or cross-national failures to stop overuse of common pool resources

Thomas Piketty proposed a global tax on wealth.

The purpose is not only to collect revenues that could be used to generate more inclusion.  
But also to ensure worldwide registration of wealth.

His associate, Gabriel Zucman, estimates that at least 8% of the world's household wealth is  
hidden in offshore accounts, three quarters of it unrecorded.



What are some other possible policy remedies if a global wealth tax is not feasible?

- Fiscal and social policies within societies aimed at reducing intra-national inequality:
  - Tax system: progressive income tax; reduce regressive consumption taxes
  - Transfers to reduce market-derived inequality
  - Pooled risk: public and private financing of social insurance against risks of loss of income due to retirement, disability, unemployment, maternity
    - Multi-tier systems of social insurance financing can be progressive
    - Broad access to health care, financed through social insurance pools
- Joint investment in public goods by labor, capital, government
  - Wider use of public-private partnerships to pool investments in and benefits of human capital
  - Infra-structure (transportation, communications, sanitation)
  - Security
  - Civil administration
- Policies aimed at stimulating broad-based economic growth (ie growth not based on financial services and resource rents); broad-based growth expands middle class

Policies addressing the crisis of inequality within societies will help to mitigate the c  
of inequality for international society.