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Is the Growth of Inequality a Lasting or Transitory Feature of the Contemporary Process of Globalisation?

A Political Economy Perspective

One earmark of the economic development of the last two decades has been the rise of inequality across the board. The focus here is mainly on market income inequality.[1] In other words the distribution of primary incomes (e.g. before taxes and transfers) became more and more unequal.

In most developed economies this rise in inequality became a political issue. The attention paid to this problem was unable, however, to counter the downwards pressure on taxes and transfers set by a growing adhesion to political liberalism. Attempts to reduce taxes and restrict transfers have been continuous and more or less successful according to countries. The ensuing weakening of redistribution mechanisms in developed economies led in turn to an increase in the inequality of the distribution of net income (e.g. income after taxes and transfers).

A similar rise in inequality in income distribution has been observed in developing countries, although in some cases the overall growth of the economy helped to reduce considerably the level of absolute poverty, which somehow masked the rise in income inequality that went with it.

The most obvious factor explaining this general rise in income inequality is linked with the form of "globalisation" that our economies have been experiencing since the mid-1980s. The globalisation of finance, which puts pressure, directly and indirectly, on wage formation of both low skilled workers (downwards) and high skilled managers (upwards) is certainly part of the explanation. It is largely combined with the forms of work organisation accompanying the diffusion of information and communication technologies (see Nascio and Pianta in this issue), allowing among other things an unprecedented internationalisation of production chains.

Still, explaining the causes of the phenomenon requires a more detailed analysis. To understand how such an increase in inequality can develop in democratic societies without being met by strong political opposition requires a more comprehensive picture of the phenomenon. In the first place, inequality has many potential dimensions which all count in assessing how changes can take place or be resisted, if not reversed. Second, countries are different in terms of the institutional settings that govern the mix of social justice and economic efficiency that prevails in each of them.

Taking such a more comprehensive view should help us to assess whether and where the present trend of inequality will last or be reversed. In other words, will the global financial crisis help to bring an end to this rise in inequality or will it further develop in order to boost the economic recovery of countries badly struck by the financial crisis?

A Nexus of Inequalities

Income inequality is only one aspect of life, focusing mainly on the sphere of economic market activities where money plays a major role in transactions. Inequality can also be found in the other two spheres, namely the sphere of political activities and the sphere of domestic activities. Inequalities are not assessed there in monetary terms but in terms of rights or of the distribution of tasks. Still, no one would contest that equal rights to vote, to be represented in any respect (from unions to non-governmental associations), to be elected or to share domestic tasks are important issues that condition how income inequality is experienced. The trends in terms of inequality in these two other spheres of activity, namely political and domestic, are, however, difficult to assess at least in democratic developed economies. On the one hand there are obvious trends towards more equality

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[1] A comprehensive assessment of the trends in income inequality can be found in OECD: Growing unequal: income distribution and poverty in OECD countries, Paris 2008.

both in terms of the distribution of political rights and in terms of sharing domestic labour. But at the same time the permanent reconstruction of barriers can be observed, against migrants for instance but also regarding the number of people in custody.[2] On the other hand the division of labour within the domestic sphere of activities combines (relatively) slow trends towards more equal distribution of labour between males and females with a reduction in the size of the domestic sphere and an increase in single families, and more specifically of single mothers.[3]

Again these mixed situations in the political and domestic spheres of activities, that create inequalities among citizens, matter when one looks at the impacts of income inequalities.

It is clear for instance that these political and domestic inequalities facilitate the diffusion of economic inequalities. Wage formation is directly affected by the weakened positions of applicants, be it politically as in the case of unskilled illegal migrants or domestically as in the case of unskilled single mothers.

Moreover, changes in inequality do not have the same time-horizon nor the same volatility from one sphere to another. Economic inequalities may change more often than political inequalities, which may experience large moves at distant points in time when new rights are conceded. Changes in the distribution of tasks in the domestic sphere may take even more time. They are deeply rooted in customs and habits that are largely country-specific, representing a strong inertia even when policies tend to promote changes (as shown in most gender studies).

Inequalities are certainly somehow correlated between these spheres but much depends on how we measure them. We stressed above that forms of political and domestic inequalities fuel some economic inequalities. But conversely certain egalitarian characteristics in the political sphere or in the domestic sphere strongly change the impact of income inequality in the economic sphere. This is clearly the case, for instance, when the political situation has established a large base of public services, freely accessible whatever your income and knowledge. Many of these differences are indirectly accounted for when we distinguish various types of capitalism.

[2] In the case of the USA this policy of exclusion has risen to unprecedented levels (see S. Bowles, A. Jayadev: Garrison America, in: The Economists' Voice, http:www.bepress.com/ev, March 2007.

[3] Again a telling example is given by the situation of overworked single mothers in the USA. Cf. Juliet Schor: The Overworked American, New York 1996, Harper.

The Diversity of Capitalism

The history of modern capitalism lends itself to some broad periodisation in which the three decades following World War II play a predominant role. This period has been named the golden years of capitalism.[4] Indeed, the welfare states that developed in occidental economies at that time seemed to achieve a good compromise between the interests of labour and those of capital, which had been fiercely opposed in the first part of the twentieth century. When one looks at these welfare states, differences appear precisely in the way in which the three spheres were organised and interacted. Esping Andersen[5] thus distinguished the Mediterranean model, in which much of the welfare was directly supported by the organisation of the domestic sphere, from the Scandinavian model, where welfare depended to a specific extent on the organisation of the political sphere caring precisely and at the local level for the welfare of all citizens. In the third type of welfare state (which concerns countries of the North of Continental Europe) the political organisation had a broad approach, mainly mediated by money transfers, to the provision of welfare. In the early 1980s, following the crisis of the mid-1970s, the rise of political liberalism tended to blur these distinctions and, chiefly, to introduce a new division according to the place given to market mechanisms in the governance of the economic sphere. This distinction between market and coordinated economies popularised the notion of diversity of capitalism.[6] All of which led to the splitting into four categories of the western economies under review. Clearly, East Asian economies like Japan and Korea constituted a fifth distinct species in that respect. Our contention is that the dynamics of inequalities differ among these countries. We mean that inequalities are felt differently, that the possibilities to reduce them or to increase them differ. We have already stressed the importance of public domains and services in that respect.

Another characteristic is tied to the time-horizon in which these inequalities are considered. Inequalities are thought of and experienced differently depending on whether they are seen as lasting or transitory. The idea that situations may change in a not too distant time-horizon helps those badly positioned to endure

[4] S. Marglin, J. Schor (eds.): The golden age of capitalism, New York 1990, Sage.

[5] G. Esping Andersen: The three worlds of welfare capitalism, Cambridge 1990, Polity Press.

[6] Following the work of P. Hall and D. Soskice: Varieties of capitalism: the institutional foundations of competitive advantage, Oxford 2001, Oxford University Press.

waiting for a better future and those highly positioned not to take too much advantage of a position that life could reverse. Societies in which unequal positions in some domains are seen as transitory or reversible are believed to show a higher social mobility.

Finally, whether inequalities are considered lasting or transitory is a major element of the stand that societies take regarding inequalities. Such stands are themselves important components of the conventions that structure the political domain of societies. France and the USA give two opposite examples in that respect. In the USA the frontier spirit, that deeply marks the political terrain, led to legitimising Obama's "yes we can" campaign slogan, implying that one can be at the bottom of a ladder at one point in time and still climb to the top thanks to one's own will and work. By experience, such a society is ready to put up with high levels of inequality. In France, on the contrary, the revolution of the late 18th century introduced a more demanding principle of equality into the core of political convention. In this context inequalities have little legitimacy. Even the application of meritocratic principles, tied to education, has to stay within limits: privileges should remain attached to positions, not to persons. These two examples of France and the USA are not the most polar cases. India shows a more extreme case of adjustment to inequalities than the USA in the name of a redistribution of roles to take place in another world. Scandinavian countries have more egalitarian principles than France. One should not conclude, however, that the status of inequality is forever fixed in any country. These statuses are products of history and may change with it. The strong Scandinavian stand on inequality dates from the interwar period.

What we have experienced in the last two decades with the universal rise in income inequality across countries somehow affected these statuses. In all countries it became a political issue with partisans and adversaries. The balance between them tilted at some elections, weakening or reinforcing the "traditional" political stand on the issue in the country concerned. Scandinavian countries provided examples of such changes. The universal rise in income inequality observed across the board of all countries certainly was accompanied by a weakening of the political willingness to contain inequality.

The question then, is, whether or not such a universal move is reversible. Are the current levels of inequality going to last or will the move be only a transitory deviation? Looking at the distribution of income over a long period of time may help to transform how getting back to normal is seen. Picketty and Saez[7] thus showed how over the whole 20th century it is finally the postwar period, the three decades of golden capitalism in the USA, that looks like a special phase of compression. Similar evolutions are obvious in other English speaking (market driven) economies such as the UK and Canada. In this context the rise of income inequality of the last two decades looks like a catching up with the levels of inequality prevailing in the early 20th century.[8]

No Natural Rate of Inequality

There is no reason why there should be a specific long-term level of income inequality, some kind of natural rate of inequality to which societies would return after a while. The rise in inequality certainly occurred along with the decline at the turn of the 1980s of the Keynesian macro-conventions that were established in the aftermath of World War II. These conventions were as diverse as the types of capitalism. Each focused on specific political objectives and policy tools. All stemmed from a similar fear that an unreconstructed capitalism would lead again to huge economic crises and wars. In that respect the global financial crisis of 2008, which saw a near-collapse of the world financial system, can have acted as a global warning, likely to lead to deep changes in politics and policies. Indeed the main question is whether the state interventions to save the financial system will bring a rebound of interventionism, boosting more redistributive and egalitarian policies.

The chances of this are small considering, a year after the peak of the financial crisis, the limits met by public intervention to contain the bonuses and high salaries of CEOs. The persistence of tax reduction policies, especially the will to reduce the progressivity of taxes, points in another direction. So far the crisis does not seem to have forged new political compromises that would help to reduce income inequality and other inequalities.

This does not mean, though, that it is definitively ruled out. There are two good reasons for this. First the crisis is not over. The first phase of the crisis had an essentially financial dimension and was solved by massive public refinancing of the surviving financial institutions. A second phase is still to come that will

[7] T. Picketty, E. Saez: The Evolution of Top Incomes: A Historical and International Perspective, in: American Economic Review, AEA Papers and Proceedings, May 2006.

[8] One can also note that Picketty and Saez, ibid., do not find the same result when looking at the share of the top income decile in France and Japan, where these statistics do not show such a marked catching up in the early 2000s with pre-1930 levels.

show how other activities have been able to cope with the shock and to restore their market in the long run. Automobile industries and construction industries, for instance, have been hard hit and whether the new order will help them to recover and develop safely is an open issue. It follows that the development of unemployment still strongly conditions the outcome of the 2008 crisis. We learned from 1929 that the detrimental consequences of major crises can come in successive waves. A worsening of economic and social conditions could then lead to new political compromises in favour of more egalitarian societies.

The second reason has to do with the climate threat and the other environmental hazards with which our societies are confronted. This challenge is pressing, even if the urgency of financial issues provokes some postponements. International negotiations around these issues are difficult and take time. But public opinion and series of natural catastrophes will exert pressure to put them back at the top of the agenda. The magnitude of the efforts required will become more and more obvious. If one follows the 2007 report of the IPCC (Intergovernmental Panel on Climate Change[9]) developed economies should reduce their CO_2 emissions to a quarter of the present level by 2050. Such objectives, implying deep changes in ways of life in the developed economies under review, can only be attained in societies with a positive attitude towards collective interests and solidarity. This requirement should act as an incentive for countries to reverse the current trend of increasing inequality. But whether there will be a major effort to counter the degradation of our environment will also depend on the policies followed in less developed economies. In these countries the dynamics of inequality may be different, however, which would possibly undermine their incentive to reduce inequality.

On Inequality and Development

We have already stressed that sustained economic growth in some countries, especially in the so-called emerging economies such as India and China, led to an absolute reduction of poverty, which in turn masked the rise in income inequality that occurred at the same time.

The reason these countries paid less attention to inequality lies in the belief that the very process of development, with the expansion of high productivity sectors, increases income inequality, which then recesses when this structural change comes to concern a majority of agents within the developing economy under review. Kuznets[10] stressed that development was bound to be associated with an inverted U curve of inequality, rising in a first phase and declining afterwards. This scheme seemed a priori to fit well with development paths moving activities from agriculture to manufacturing and services. Yet the development trajectories observed in the last two or three decades do not validate Kuznets's hypothesis. Clearly the specificities of local political situations matter. In developing countries political and economic inequalities are entangled in specific ways, forged by history, which limits the possibility of any type of general relationship between inequality and growth. The nature of the elites and of the international linkages of the country are clearly important. In open economies, development may benefit certain classes and regions long-term which are directly linked to the form of international integration in the world economy of the country in question, while other groups get only a very small share of the gross income generated. Inequality may even be aggravated when development implies major changes in ways of life, like peasants becoming workers in manufacturing or services. Their qualitative dimensions of well-being, such as access to health care, housing, education and social relations, may deteriorate. Active social and redistribution policies are then needed to avoid a strongly biased irreversible development path. Emerging economies, e.g. large developing economies strongly engaged in international trade, are facing such challenges. These policies have, moreover, to take into account the measures required by their shares of the environmental objectives. Their importance in the global economy is such that their responses influence the path that more developed economies can take in favour of a more equal growth process. It will not only set the tone but also release some pressures on developed economies and help post-crisis recovery policies to engage clearly in reversing the past trends which have fuelled inequality. A key issue in this respect is that such universal demand-oriented policies must include the taming of globalised finance.

At this moment in history the fairness of developments in Northern and Southern countries are entangled in new specific ways. How they will manage to get out of the financial crisis and face the environmental threat in a more or less cooperative way is a key issue for any reversal of the past trend of increasing inequality.

[9] See the website of the panel http://www.ipcc.ch.

[10] S. Kuznets: Economic Growth and Income Inequality, in: American Economic Review, Vol. 45, 1955, pp. 1-28.