

# **Econ 133 – Global Inequality and Growth**

## **Review and conclusion**

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## Roadmap:

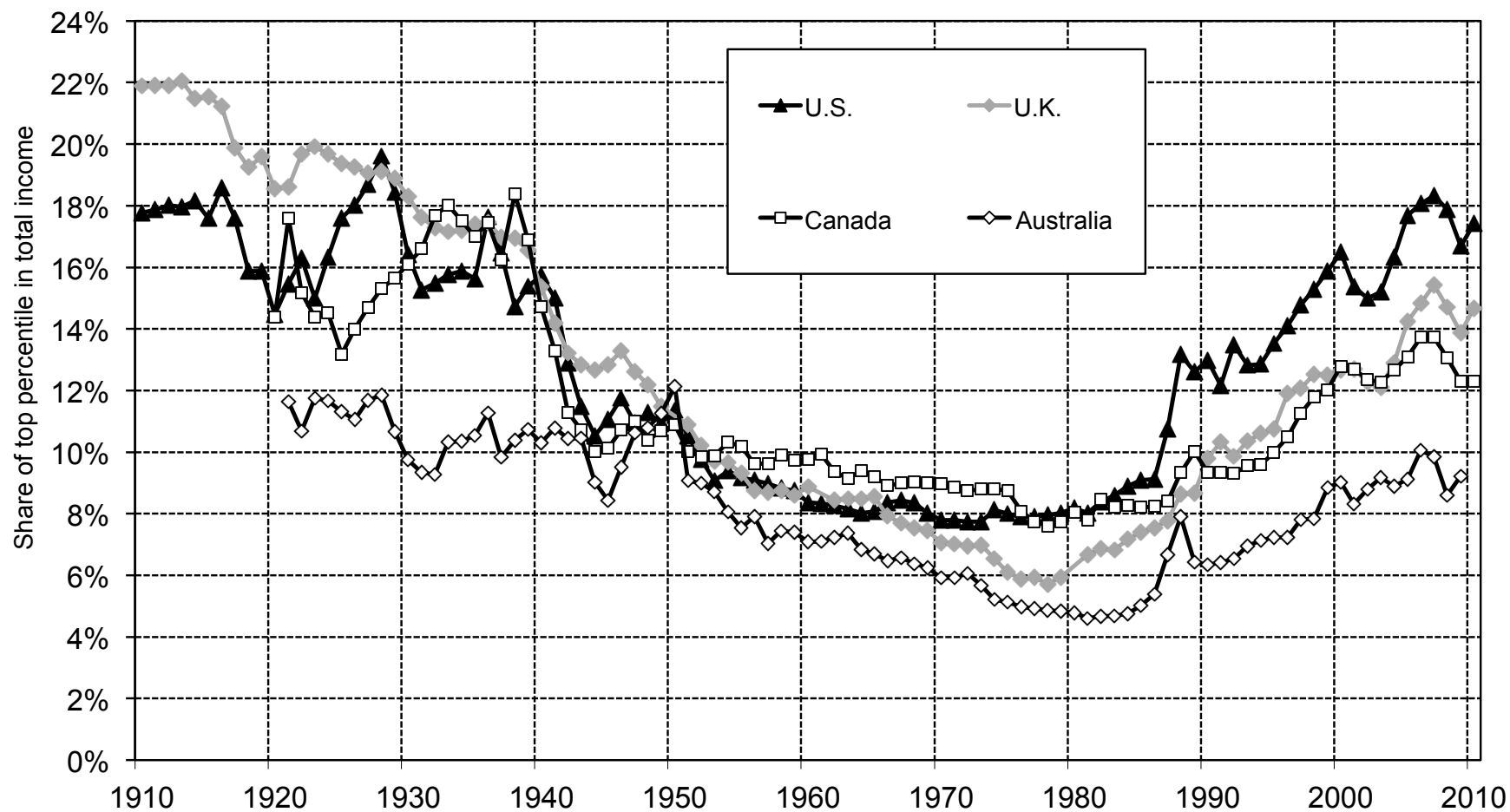
- There's nothing natural in the evolution of inequality: history and policies are key
- The reasons why inequality is rising in the US
- Forces of convergence and forces of divergence at the global level
- The policies that can promote equitable growth

# 1 There's nothing natural in the evolution of inequality

## 1.1 The Kuznets curve

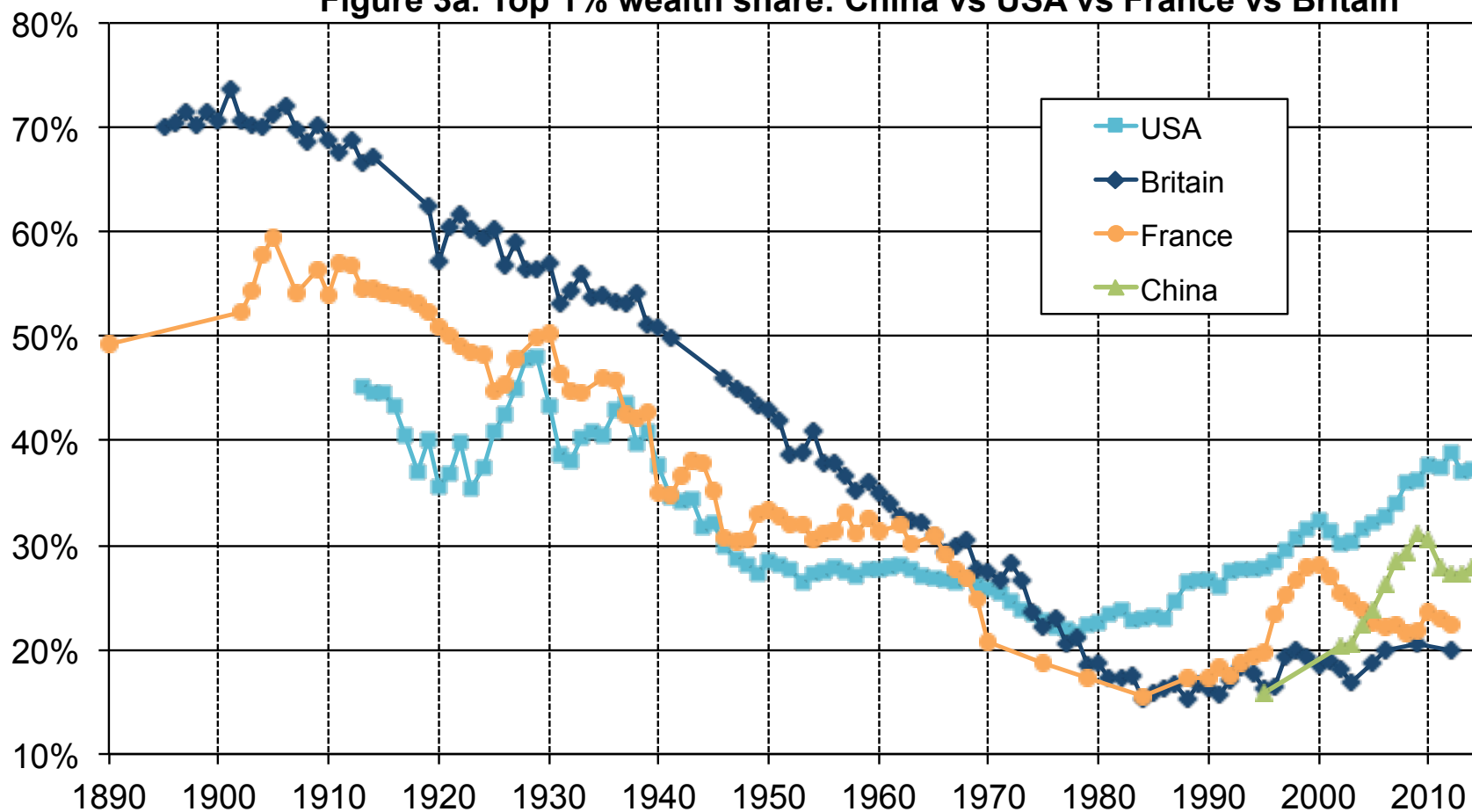
- Kuznets had an optimistic theory: inequality first rising, then naturally declining with growth
- With hindsight, this theory does not appear to be supported by the data

**Figure 9.2. Income inequality in Anglo-saxon countries, 1910-2010**

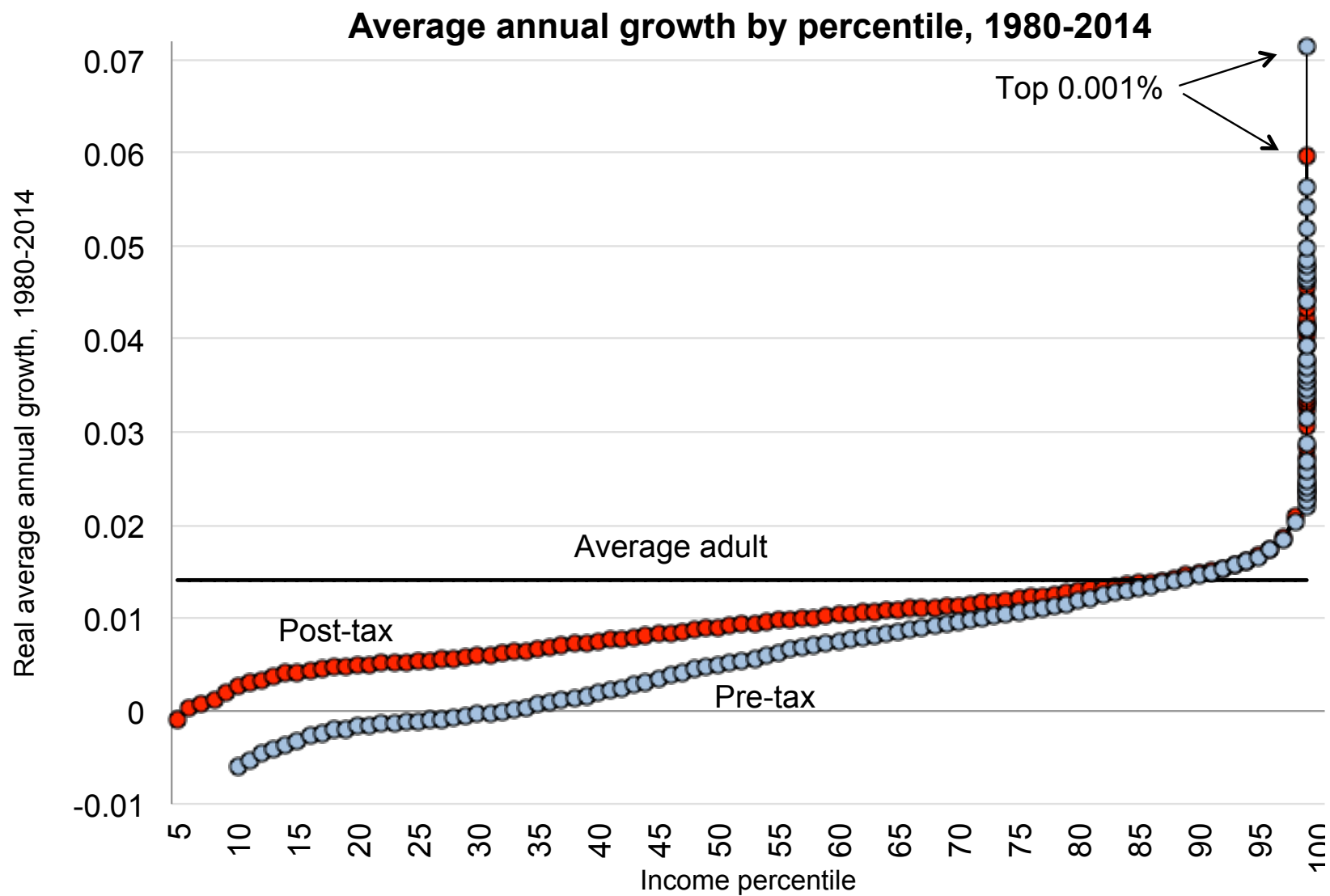


The share of top percentile in total income rose since the 1970s in all Anglo-saxon countries, but with different magnitudes. Sources and series: see [piketty.pse.ens.fr/capital21c](http://piketty.pse.ens.fr/capital21c).

**Figure 3a. Top 1% wealth share: China vs USA vs France vs Britain**



Distribution of net personal wealth among adults. Corrected estimates (combining survey, fiscal, wealth and national accounts data). Equal-split-adults series (wealth of married couples divided by two). USA: Saez and Zucman (2016). Britain: Alvaredo, Atkinson and Morelli (2017). France: Garbinti, Goupille and Piketty (2016). China: Piketty, Yang and Zucman (2016).



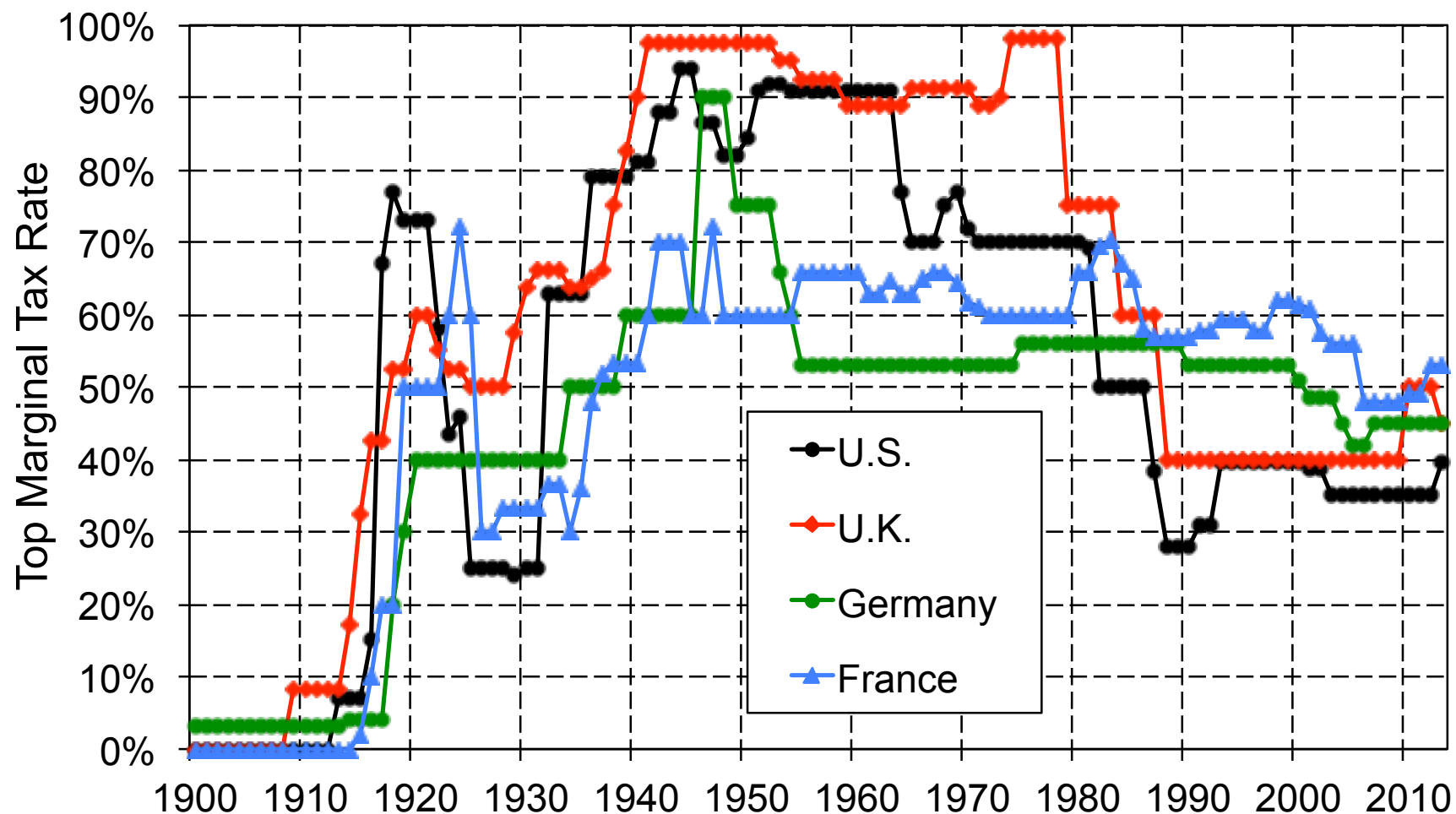
## 1.2 History and policies matter

- Diversity of national histories and representations:
  - US used to be more equal than Europe, now much more unequal
  - Booming top labor income mostly an Anglo-saxon phenomenon
  - The decline of wealth concentration during the 20th century: largely the result of wars, destructions, Depressions

- Dramatic changes in policies have played a key role in the history of inequality:
  - Non-tax policies: changes in bargaining power, unions, share of capital publicly owned,
  - Highly progressive taxation from 1940s to 1970s limited dynastic wealth
  - Decline in progressive taxation since the 1980s contributed to rising inequality



### Top marginal income tax rates, 1900-2013



## 1.3 The laws of inequality and what they mean

There are a number of laws that govern the evolution of inequality:

- $\alpha = r \cdot \beta$

- $\beta \rightarrow s/g$

- $r > g$

- But these laws do not imply that inequality is bound to rise or fall
- On the contrary:  $r$ ,  $g$ ,  $s$  are all functions of policies, institutions, shocks...
- Example:  $r$  depends on capital taxation, wars, social norm, technology, bargaining power
- So these laws are useful to think about the future, but nothing is set in stone

## 2 Why inequality is rising in the US

Fundamental distinction: inequality of labor income vs. inequality of capital income (or wealth)

### 2.1 Labor income inequality

- Rising skill premium, due to rapid increase in demand for skilled labor not matched by equivalent increase in skill supply
- Institutional change: decline in unions, decline of minimum wage,

rising market power

- Explosion of top wages, due to decline in top marginal tax rates and changes in social norms governing pay

## **2.2 Capital inequality**

- Rising labor income inequality and saving rate inequality
- Decline in capital taxation (estates, capital income, corporate tax)

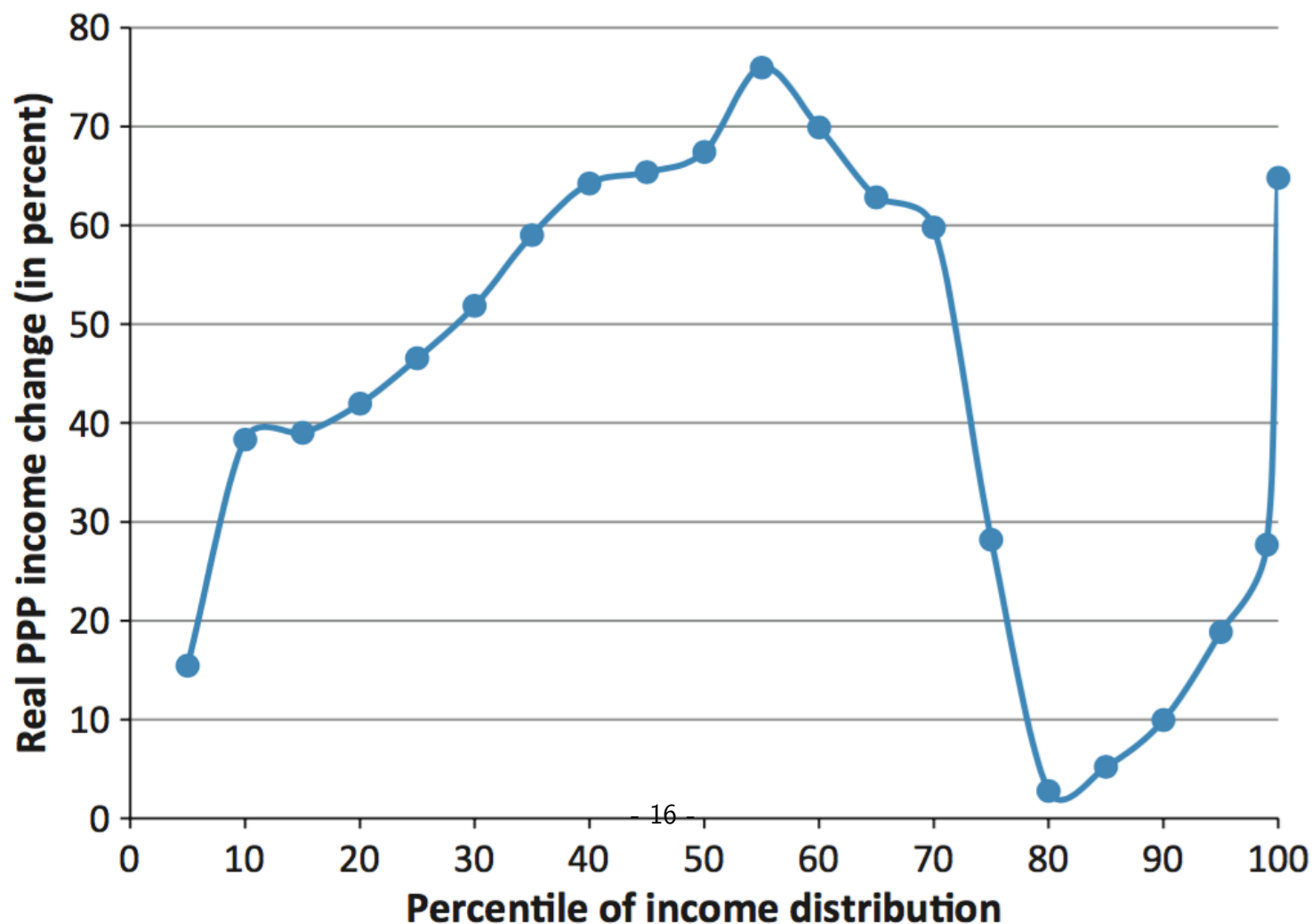
- $r > g$  will be key down the road
- Toward a new world where both super-managers and rentier co-exist at the top?

## **3 Global inequality: convergence or divergence?**

### **3.1 Forces of convergence**

- Catch-up growth in developing countries
- Technology diffusion through trade
- Migration from poor to rich countries

**Figure 4.** Change in real income between 1988 and 2008 at various percentiles of global income distribution (calculated in 2005 international dollars).





## 3.2 Forces of divergence

- Rise in top-end inequality within countries
- International tax competition and evasion (role of technology, policies & social norms, in particular in the financial sector)
- Decline in  $g$  (pop. + productivity)  $\rightarrow$  rise in inherited wealth. Has already started in Europe, might become global phenomenon

## 4 Policies that can promote equitable growth

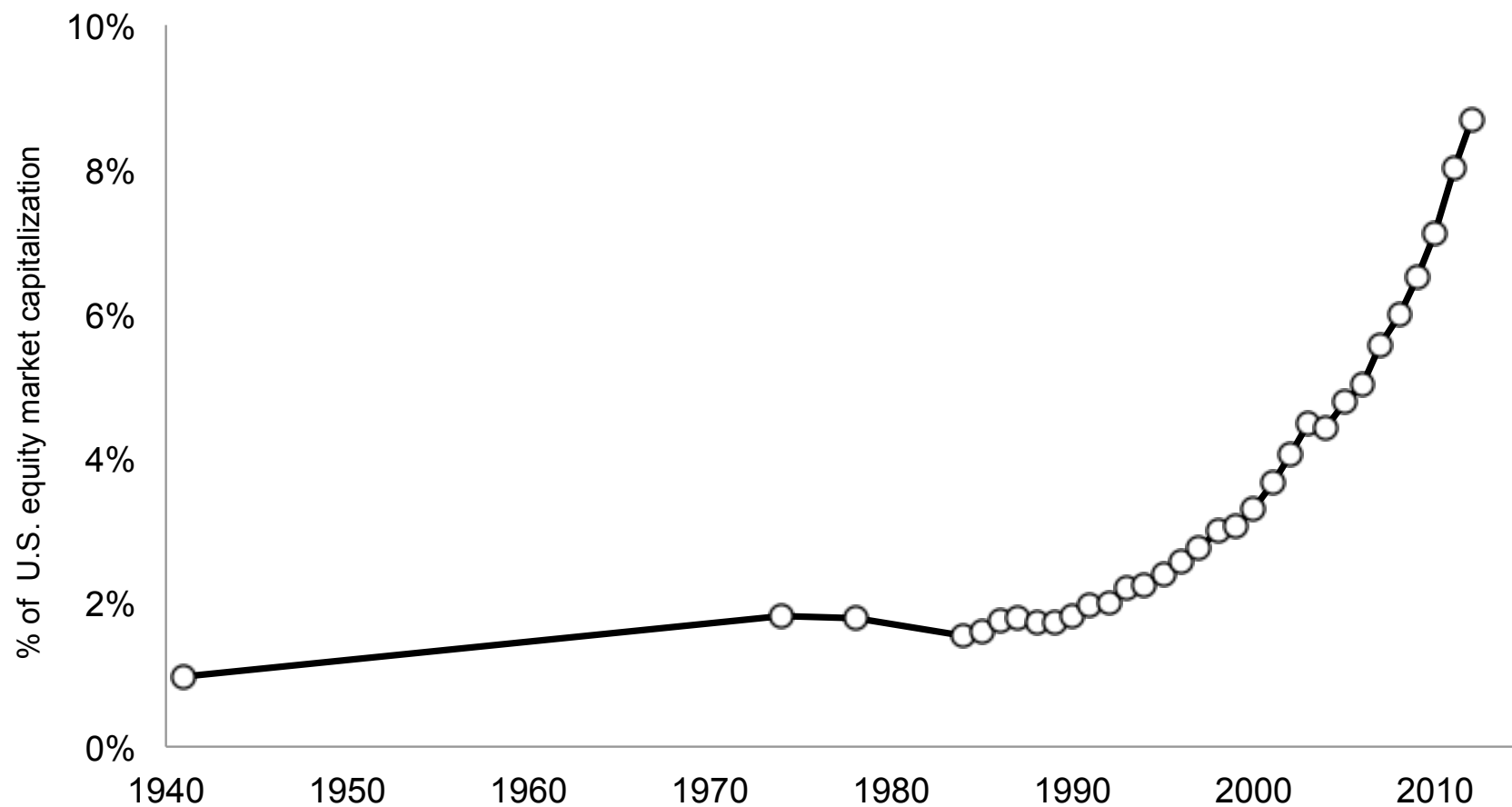
### 4.1 Policies that worked in the past

- Progressive income and wealth taxation
- Investment in access to education: reduces skill premium and makes it possible to increase minimum wage
- Strong social safety net and transfers to make it possible for poor & middle class to accumulate wealth

## 4.2 Institutions and policies always need to be reinvented

- World is more globalized → limits unilateral policy changes
- Technological change → may hurt labor more than in the past
- Rise of algorithms, patents, etc. → need to find new ways to regulate capital
- Global demo. transition, climate change → may lead to low  $g$

### U.S. equities held by tax haven firms and individuals



In 2012, 9% of the U.S. listed equity market capitalization was held by tax haven investors (hedge funds in the Cayman Islands, banks in Switzerland, mutual funds in Luxembourg, individuals in Monaco, etc.). Source: author's computations using US TIC data

Key policy challenges for the future involve inventing:

- New ways to grow: e.g., through green energy industrial revolution
- New ways to regulate inequality: e.g., global wealth taxation and financial transparency; patent regulation
- New ways to produce: corporation with sole goal of max. shareholder value not always best way to organize econ activity