

LS 812

Thomas Piketty  
Capital in the 21<sup>st</sup> Century

# Piketty:



- After earning his PhD, Piketty taught from 1993 to 1995 as an assistant professor in the Department of Economics at the Massachusetts Institute of Technology. In 1995, he joined the French National Centre for Scientific Research (CNRS) as a researcher, and in 2000 he became professor
- Piketty won the 2002 prize for the best young economist in France
- In 2006, he became the first head of the Paris School of Economics, which he helped set up.
- He left after a few months to serve as an economic advisor to Socialist Party candidate Ségolène Royal during the French presidential campaign. Piketty resumed teaching at the EHESS and Paris School of Economics in 2007.

# Piketty:

- Piketty's thesis did not arise suddenly with the writing of "Capital in the 21<sup>st</sup> Century", but rather over many years with the help of other (as he says "...several dozen...") scholars in the construction and analysis of a large database of historical data (income, wealth, taxes). The database covers over three centuries of data from over 20 countries.
- One element in his analysis of the cause of inequality is the 'formula' (itself an inequality):

$$r > g$$

Where:  $r$  = rate of return on capital  
 $g$  = growth rate of the economy (i.e. GDP)

- This inequality, in and of itself, does not explain income and wealth inequality. In fact, in a theoretical 'Steady State' where everyone starts with the same income and wealth, this formula could maintain the original steady state equality if everyone re-invested just enough of their return back into their capital 'stock' in order to maintain it.
- That's why there are at least two other components to his causal explanation for inequality:
  - Exogenous shocks
  - Policy, institutions, attitudes and mores, etc.

# Piketty:

- Exogenous shocks:
  - Political
    - Revolution
    - Wars
    - The 'welfare state' (e.g. the New Deal)
    - 'Reagonomics', 'Thatcherism', etc. and the changes they brought to the welfare state
  - Environmental/Ecological?
    - Will Climate Change bring about changes?
- Institutions, Policy, Attitudes
  - Piketty brings in a lot of examples from literature and movies to highlight the prevailing attitudes towards the distribution of income and wealth in different times and places
    - Balzac, Zola, Dickens, Austen, Titanic (if that doesn't lure in the GLS'ers I don't know what will 😊)
  - Taxation policy
    - Do we tax inheritances?
    - How progressive, or not, is our tax system?
  - Regulation

# Piketty:

- Institutions, Policy, Attitudes (cont.)
  - Education
    - Piketty is big on education, and equal access to it
  - Labour market rules
  - Minimum wage
  - Trade policies
  - Regulatory agencies (in the U.S. the EPA, FDA, SEC, etc.)
- Piketty's attitude towards mathematics/models in economics:
  - *“Models can contribute to clarifying logical relationships between particular assumptions and conclusions but only by oversimplifying the real world to an extreme point. Models can play a useful role but only if one does not overestimate the meaning of this kind of abstract operation. All economic concepts , irrespective of how “scientific” they pretend to be, are intellectual constructions that are socially and historically determined, and which are often used to promote certain views, values, or interests.”*

# Piketty:

- Attitudes to what capital is, and who should own and control it, have changed throughout time
  - Previous definitions of capital included slaves!
  - Today, there is pressure to extend the boundaries of commodification and capitalization:
    - Novel forms of financial assets (collateralized debt obligations, options, derivatives, etc.)
    - Capitalization of nature: forests, parcels of the ocean (for fishing), etc.
  - Branding
  - Knowledge

# Piketty:

- What's the prognosis?
  - $r - g$  might remain high in our century because of the unequal access to high financial returns...this is where the money is today!
  - The trend is away, not toward, regulation and progressive taxation (two of the most powerful antidotes to inequality)
  - We live in a globalized world now, where nation states must compete for capital. The flexibility that nation states had in the past to shape tax policy, regulation, and legal frameworks is being eroded (think EU)
  - However, Piketty admits that he is making a large assumption: that historical trends re. inequality will apply to the future (remember Hume?)

# Piketty:

- Solutions(?):
  - Enigmatically, one of Piketty's main solutions is education. This certainly helps, but in an already unequal society, access to education and public funding of education, seems to be pointing in the direction of more inequality, not less.
  - Progressive taxation along with a highly punitive, one-time tax on wealth! (how's that gonna go over?). High (maybe 100%?) tax on inherited wealth.
  - Stronger regulation, particularly in the financial markets
  - Put institutions back at the centre of economics!
    - Alternative forms of property arrangement/ownership
    - Participatory governance (even at the level of the firm)



# Acemoglu/Robinson:

- Their main critique of Piketty is the search for “...general laws of capitalism”
  - A reliance on general laws misleads Piketty just as it misled Marx
- Inequality is affected more by the political and cultural contingencies of time and place than by economic fundamentals.
  - In fact, Marx’s general laws, as well as the general laws of any school of economics, are drawn from the data and experiences of a particular time and place and extrapolated (or projected) out to the future
  - Their position, then, is very much a ‘social construction’ view of the economy
- Their position is that what really matters is the evolution of technology and of institutions.

# Acemoglu/Robinson:

- They argue for a more nuanced view of the causes of inequality and do so by means of a comparison between Sweden and South Africa
  - After Apartheid ended, inequality actually rose! This was because a different dynamic shaped South African socio-economic reality: white mine -owners, blue and white-collar workers, and farmers (i.e. a mix of socio-economics classes) united against industrialists to protect white labour wages.
  - After Apartheid, the artificial restrictions on labour were lifted thus putting the emphasis on capital investment, which led to lower wages and increased inequality.
  - In Sweden, social democracy united businessmen and unskilled workers against the middle class and skilled workers. Swedish economic institutions thus compressed wage differences, which led to greater equality.

# McCloskey:



- Professor of economics, history, English and communication at the University of Illinois at Chicago, and visiting professor of philosophy at Erasmus University in Rotterdam.
- Her major contributions have been in the field of economic history, the rhetoric of economics, virtue ethics, the role of mathematics in economic analysis.
- She began her life as male and transitioned to female at the age of 53.
- She describes herself as follows:

“literary, quantitative, postmodern, free-market, progressive Episcopalian, Midwestern woman from Boston who was once a man. Not ‘conservative’! I’m a Christian Libertarian.”

# McCloskey:

- Agrees with Piketty's approach in the following ways:
  - Not infatuated with the empirical tools (e.g. regression analysis, general equilibrium, non-cooperative game theory...doesn't betray "physics-envy")
  - Is an "...honest and massively researched book..."
- After obligatory praise, she then proceeds to give him a good thrashing:
  - Piketty's book just another instance of a "long series..." of "leftish worries" about capitalism's role in the rich getting richer
  - Instead of "capitalism" McCloskey's prefers the term "market-tested betterment" (as a good rhetorician would)
  - Her main argument is that "market-tested enrichment" has led to incredible amounts of wealth creation and betterment. She calls it the "Great Enrichment"

# McCloskey:

- Good thrashing (cont.):
  - Goes through laundry list of leftist worries:
    - Greed
    - Alienation
    - Consumerism
    - Market imperfections
    - Exploitation
    - Externalities
  - McCloskey is a Nozickian libertarian:
    - Government intervention is a type of “violence”
    - McCloskey says that the combined effect of all market “malfunctionings” (see above) do not nullify the offsetting “market-tested betterment”
  - McCloskey believes that criticisms of capitalism persist because “pessimism” sells

# McCloskey:

- Good thrashing (cont.):
  - Piketty's definition of capital excludes "human capital"
  - McCloskey is critical of Piketty's focus on 'relative wealth', as are many on the right. It's a leftish strategy to discount the "Great Betterment".
  - She quotes Matt Ridley: a good part of inequality in the U.K., for example, is because of government intervention.
  - Uses example of Sam Walton (Wal-Mart) to bring in the concept of "social value":
    - Sure the Waltons are multi-billionaires, but their wealth is but 2% of the total "social value" created by Wal-Mart (similar to U.S. Republican "job creators" rhetoric)

# McCloskey:

- Good thrashing (cont.):
  - The wealthy got their wealth by sheer merit:
    - More intelligent, hard working, less risk-averse, more productive
    - Wilt Chamberlain argument brought in from Robert Nozick
- What's so bad about inequality, anyway?
  - Maybe it represents a 'state of nature'
  - Maybe it's the price we pay for 'progress' and 'wealth generation' (one of McCloskey's arguments)
  - Maybe we should be content with the "pretty good"
  - Those lower on the socio-economic ladder are better served by allowing the market to freely generate wealth, which "lifts all boats"
  - To insist on equality, society would be "cutting down the tall poppies"

# McCloskey:

- What is McCloskey's alternative solution?
  - Promote "Bourgeois Virtues":
    - Hard work
    - Fairness
    - Justice
    - Freedom!
  - In this sense, she is anti-institutionalist:
    - It's not the government or other societal institutions that must guide behavior, it's an appeal to morality and virtue.



# McCloskey:

- Anti-institutionalist (cont.):
  - Here's a quote from her article "Tow Cheers for Corruption":

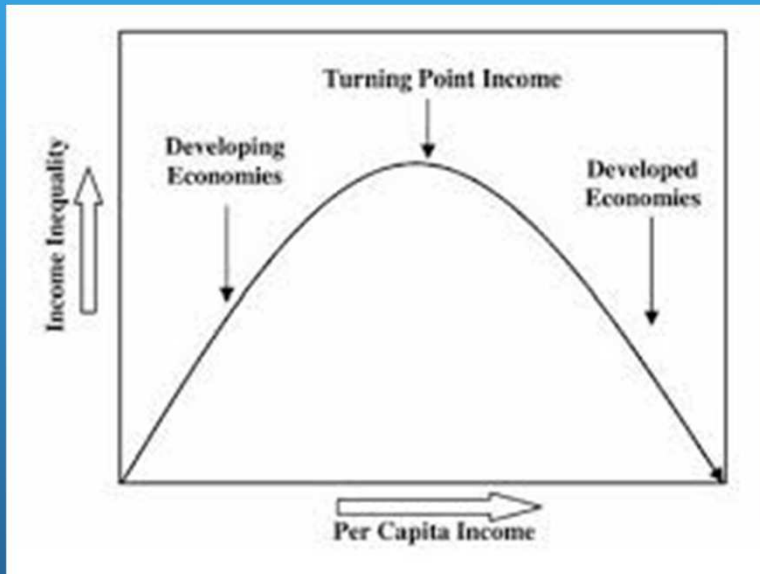
*"But corruption can be efficient and just too. It can be good for efficiency if, say, bribes are paid to get around bad laws...or to smooth the course of sales by U.S. businesses to the Egyptian military. And the turkey at Christmas supplied by Tammany Hall justly helped the poor - if they voted right."*
- In the past, she has urged people to consider CEO's who commit felonies as our heroes: their bribes, extortion, and fraud often produce a more just and efficient world\*
- In the end, we have a clash of values:
  - Piketty: ?
  - McCloskey: ?
- <http://neweconomicperspectives.org/2015/03/mccloskeys-plea-for-an-unethical-ethical-response-to-corporate-bribery.html>

# Singh Grewal:

- Bias alert!...my favourite paper of the bunch
- His review is generally sympathetic to Piketty, and if anything, pushes for a more radical interpretation of inequality.
- Piketty's work, if nothing else, has given us the empirical evidence for the existence of inequality, and has called for an interdisciplinary discussion (philosophy, politics, economics, history, sociology)

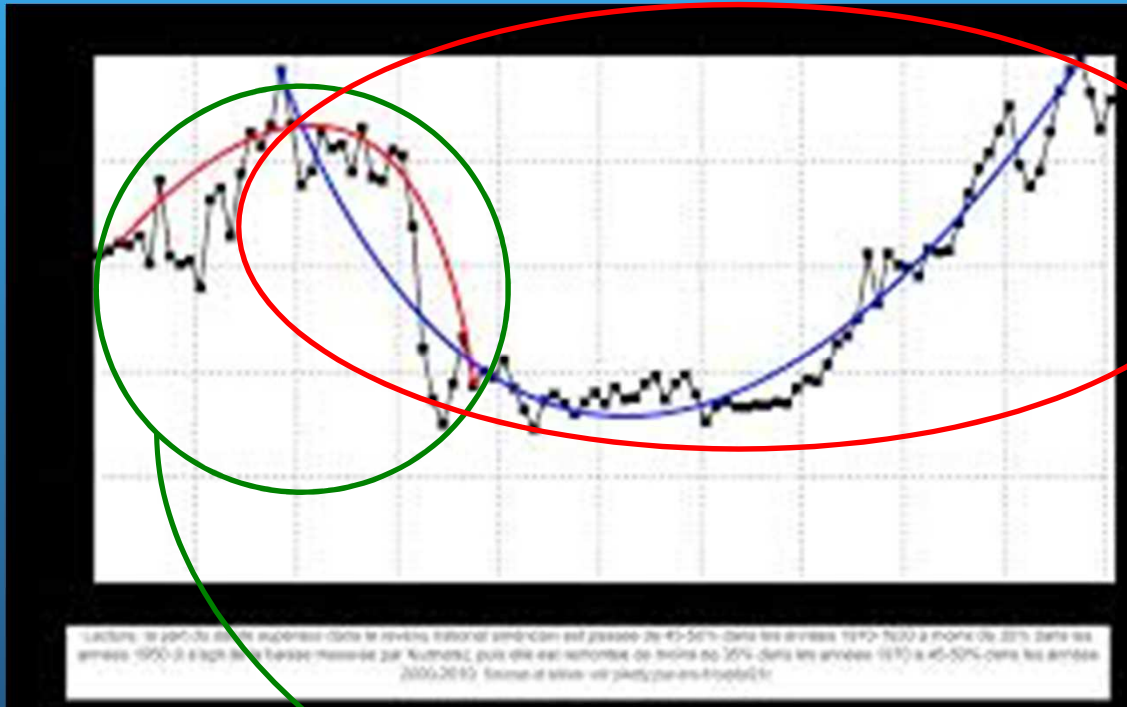
# Singh Grewal:

- Kuznets curve:



# Singh Grewal:

- Piketty's reassessment of the Kuznets curve :



1925 - 2005:  
Not-so-Kuznets

1910 - 1945: Kuznets

# Singh Grewal:

- “Piketty’s comprehensive reassessment of Kuznet’s data has unsettled the confidence that the market will “self-correct” in terms of inequality...”
- But this critique of the Kuznets curve has also been made in regards to its application to the other areas where it is used to demonstrate the self-correcting nature of the free market (e.g. the ‘Environmental Kuznets Curve’).
- One of the main points that Singh Grewal brings out is the effect that inequality has on democracy itself (see page 640).
- Singh Grewal also challenges Piketty’s reliance on single index number for GDP. The reliance on a single index obscures the complexity, dynamics and even the normative applicability of the index and its components.

# Singh Grewal:

- Singh Grewal criticizes Piketty's lack of discussion regarding why inequality is undesirable.
- However, Piketty does (rightly in his view) discuss the implications for two value systems:
  - *Democratic*: inequality obstructs the “articulation and realization of collective goals”
  - *Meritocratic*: Emphasis on merit is a bourgeois obsession that rewards thrift, hard work, talent and is meant to protect the asset-owning middle class. Meritocracy is a form of prejudice and can clash with democratic values.
- Finally, Singh Grewal challenges Piketty's emphasis on up-front taxation: “...it may be only through structural changes to the economy...that an electorate becomes capable of demanding higher tax rates.”