

## The Great Divide\*

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Joseph E. Stiglitz:

*The Great Divide: Unequal Societies and What We Can Do About Them*

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Recipient of the Nobel prize in economics, *Joseph Stiglitz*, has dealt with the phenomenon of increasing income differences for years. His work entitled “*The Price of Inequality*” was published in 2013 by Norton & Norton Co. and according to the New York Times it was the best-seller of that year. In 2015, he published another book on this subject (“*The Great Divide*”), partially repeating and further developing the ideas of his 2013 work.

Indeed, *The Great Divide* can perhaps more aptly be described a volume of essays, since he publishes his articles presented in various papers and Internet forums, arranged into topics. He essentially addresses two subjects: What is the explanation for the increasing gap between poor and rich people in America and throughout the world? Can solutions be found for this phenomenon whereby liberal capitalism retains its advantages, yet it eliminates its effects which hinder growth?

As an economist, Stiglitz approaches the issue of poverty versus wealth not from the aspect of moral theology. He is not only bothered by the fact that the distribution of incomes between capital and labour, among the people already possessing wealth and those living only from their wages and salaries, is unfair – although naturally this bothers him as well. He states it in the most precise way that this “great divide” is – and will be – detrimental to the growth of the economy. I.e. *in the long run this is not advantageous to anyone!*

He does not agree with the standpoint of Piketty that the so-called period of Ford growth after World War II was *only a deviation*, since the differentiation of incomes and the concentration of wealth is *in the nature of* capitalism. After all, this would mean that the economic-social system must be rejected if we intend to

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terminate this phenomenon! According to Stiglitz, however, in the 1930s *capitalism was capable of self-correcting itself*, and this made such further development possible for capitalism which increased the performance of the developed world to an amazingly high level. Only Reaganomics, the return to the fundamentalism, the radical decrease in taxes and the resulting indebtedness of the state and the population can be considered as deviations from the line of development.

*He denies the essence of neo-liberal philosophy, according to which it is good if the differences in incomes are great.* According to this view, the profit of the rich “trickles down” to the poor. “It creates jobs and employment and increases salaries”. This is the ideology. That is, capital owners becoming rich is in the interest of the workers... According to the data, however, *this is not true at all!* Over the last almost four decades, the income of the poorest *has increased by almost zero*, whereas that of the upper decile, especially the richest 1 per cent, *has increased like a rocket!* Where is “trickle down” here?

He already pointed this out in detail in his work published in 2013. (Hence the title: *“Price of inequality”*. According to Stiglitz, this fact has and will have a serious economic price.) He launches his work on the Great Divide by highlighting the contrast between the 1 per cent vs. 99 per cent. He presents that the American belief *in the equality of chances is only a myth*. No doubt, this is not verified in today’s USA. Poor people cannot break out from their hopeless situation. These days only education can provide an opportunity for this, but even this is less and less affordable for the average American. Thus, it is only a fairy tale that the small shoeshine boy will become a millionaire. Young people who understand this challenge and attempt to find money for further education are trapped by student loans. According to Stiglitz, young people in America are tragically indebted and the labour market opportunities are far below their expectations. Moreover, the handling of the collapse of student loans is even more difficult than that of mortgages. This would only be improved if state education financing (and health care) became much more extensive! He is not alone with this idea. Of the financial economists, R. Rajan, professor at the University of Chicago, ex-chief economist at the IMF, and ex-governor of the Bank of India, also emphasised this (already in his book *“Fault Lines”* published in 2010).

One of the basic messages of Stiglitz is that even the so-called social expenditures of the state do not only serve social purposes. Ultimately, conservative, fundamentalist capitalists must understand that solidarity with the poor *is in their interests* as well, because *there is no market of appropriate size without these people!* Moreover, poorly educated and paid labour is less efficient both as a consumer and as a producer. There is no appropriate labour supply if we finance education and health care based on the residual principle and we do not raise talented people from all parts of society. Hence, we essentially *waste human capital* and thus reduce the

market potentials of our own national economy. It has always been the *profitable co-operation of the market and the state that has made the US big!* There is no enterprise or enterprise empire of large success in America whose foundations were created not by state infrastructure developments and state-financed research.

Yet, incomes are also necessary for expenditures!

Stiglitz deals with the issue of taxes intensively. He states that the decrease in tax rates in the US clearly favoured richer people. However, it is not possible to stimulate the economy endlessly by decreasing taxes, since the state would then have no sufficient tools for assisting the economy. He mentions that the current American taxation is extremely *unfair*, as already noted in his earlier work in 2013. The rich *pay a much smaller proportion* of their declared income as tax than less rich people, and their declared income is often just a fraction of their real income. He disputes that it is not worth taxing the rich more than the middle class, since this supposedly “does not result in a lot of money” ... He writes that this is no longer so today. Indeed, the progressive tax income from the rich can be significant, exactly as a result of the large differentiation of incomes that has occurred up until now. However, he sees that the reforms planned up to now are more and more aimed at terminating the benefits assisting the middle class, for example the deductibility of mortgage interests and health care provided by employers. Stiglitz acknowledges that these indeed decrease the tax base and their gradual elimination could in fact be justified, all the more so because the deductibility of mortgage interest rates assists the rich more than the middle class... However, now that the real estate market is on the ground after the crisis, he does not deem it practical to eliminate the benefit in one step. Although this tool is essentially condemned in the hand of the state, since this also contributed to the previous, overly brisk construction industry demand (the housing boom).

Stiglitz says that a well-organised tax system is not only capable of raising the necessary amounts for the government, but it is also capable of *economic policy orientation*. It is better to tax harmful activities than useful activities. It is more practical to impose taxes on environmental pollution and speculation than on human labour and savings. It is more rational to tax things that cannot be taken away (such as land, oil and other natural resources), in contrast to profits, whose realisation can be cleverly relocated to tax havens. And yes: the stimulating effect of taxes does also matter. He considers it correct if the state encourages domestic investments that create jobs. According to him, it would be good if multinational companies were taxed on the basis of how much they produce and sell in the US. This is because the possibility of reorganising incomes to countries with low taxation is currently very popular... He also says that the additional taxation of the banking sector is justified, since as a result of its “innovations”, it indeed realised additional incomes in the period leading to the crisis (pp. 123–124).

According to the author, the main objective of tax reforms cannot primarily be the realisation of higher budget income. Their effect on steering the economy is more important. Therefore, he favours “tiered” taxes. As regards the so-called carbon tax, the punitive tax on emissions, he thinks that it is clearly justifiable in terms of economics, since the damage caused has to be compensated to society. As the environment is indeed our scarcest resource, which we have to guard to a greater extent!

The author puts great emphasis on the importance of the war against corruption and the links between the private sphere and the state. The privatisation of benefits and the nationalisation of losses is an extensive practice in the US. There is a “revolving door system”, whereby certain people find themselves in well paying positions of large companies at the end of an election cycle in return for their services in the state administration. Moreover, as a result of the elections, the leaders of companies may obtain positions of power, where they can again assist business sector enormously by establishing through regulation, monopolist benefits, and with state orders. In his 2015 work (similarly in 2013), Stiglitz emphasised that the problem of the established system is primarily not of economic, but of *political nature*. Namely, it is the *distortion of democracy* that it is not the “one man – one vote” principle, that prevails in reality, but the “one dollar – one vote” principle, *because of the campaign support system...* (The US Supreme Court has rejected the upper limit of campaign funds transferred by corporations.) This also means that those with the opportunity of establishing statutory regulation can spend larger amounts on the campaign, including buying the media empires as well. As we already pointed out, these influence the average voter to such an extent that he/she is inclined to not see his/her own interests... But both main parties in the US are the hostages of enormous business conglomerates, and thus it is not expected that there will be a major difference in the programmes regarding the equalisation of incomes.

The author emphasises that the future is not predetermined, we have the power to change it, but *political will* is necessary for this. More democracy, more transparency, more civil activity. All of this has to be accompanied with assisting actions of the state, since the poorest people are unable to rise solely on the basis of market rules of the game, and a downward spiral can develop in society.

Stiglitz has confidence in the strength of the civil sector and the viability of liberal capitalism. The future will answer the question to what extent this can be implemented during the term of the new US Administration.

## References

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