Some Are More Unequal Than Others

By JOSEPH E. STIGLITZ

This election has rightly been characterized as one that will deeply affect the future direction of the country: Americans are being given a choice with potentially large consequences. One arena in which there are profound differences that has not been adequately debated is the future course of inequality.

Mitt Romney has been explicit: inequality should be talked about only in quiet voices behind closed doors. But with the normally conservative magazine The Economist publishing a special series showing the extremes to which American inequality has grown - joining a growing chorus (of which my book "The Price of Inequality" is an example) arguing that the extremes of American inequality, its nature and origins, are adversely affecting our economy - it is an issue that not even the Republicans can ignore. It is no longer just a moral issue, a question of social justice.

This perhaps provides part of the explanation for why inequality and poverty should suddenly appear as part of the Romney-Ryan makeover, as they attempt to portray themselves (to use a phrase of some 12 years ago) as compassionate conservatives. In Cleveland on Wednesday, Paul Ryan gave a speech that might lead one to conclude that the two Republican candidates were really concerned about poverty. But more revealing than oratory are budget numbers - like those actually contained in the Ryan budget. His budget proposal guts programs that serve those at the bottom, and little could have done more to enrich those at the top than his original tax proposals (like the elimination of capital gains taxes, a position from which he understandably has tried to distance himself). Every other advanced country has recognized the right of everyone to access to health care, and extending access was central to President Obama's health care reform. Romney and Ryan have criticized that reform, but have said nothing about how or whether they would ensure universal access. Most important, the macroeconomic consequences of the Romney-Ryan economic program would be devastating: growth would slow, unemployment would increase, and just as Americans would need the social protection of government more, the safety net would be weakened.

We'd all do well to pay a bit closer attention. That American inequality is at historic highs is undisputed. It's not just that the top 1 percent takes in about a fifth of the income, and controls more than a third of the wealth. America also has become the country (among the advanced industrial countries) with the least equality of opportunity. Meanwhile, those in the middle are faring badly, in every dimension, in security, in income, and in wealth - the wealth of the typical household is back to where it was in the 1990s. While the recession has made all of this worse, even before the recession they weren't faring well: in 2007, the income of the typical family was lower than it was at the end of the last century. While Obama may not have done as much as he should to counteract the steep downturn he inherited from George W. Bush upon taking office - and he underestimated the depth of the problems that had been passed along to him - he did far more than his predecessor. And he could have done far more, as the dimensions of the problem became clearer to everyone, had he not faced such strong opposition in...
Congress.

There are many forces giving rise to this high and rising inequality. But the fact that America's inequality is greater than other advanced countries' says that it's not just market forces. After all, other advanced countries are subjected to market forces much like those confronting us. Markets don't exist in a vacuum. Government policies - or their lack - have played a critical role in creating and maintaining these inequities.

Inequality in "market incomes" - what individuals receive apart from any transfers from the government - has increased as a result of ineffective enforcement of competition laws, inadequate financial regulation, deficiency in corporate governance laws, and "corporate welfare" - huge open and hidden subsidies to our corporations that reached new heights in the Bush administration. When, for instance, competition laws are not enforced, monopolies grow, and with them the income of monopolists. Competition, by contrast, drives profits down. What is disturbing about Romney and Ryan is that they have done so little to distance themselves from the economic policies of the Bush administration, which not only led to poor economic performance, but also to so much inequality. Understandably, perhaps, Romney has not explained why those, like him, in the hedge fund and equity fund business should be able to use a loophole in the tax law to pay 15 percent taxes on their earnings, when ordinary workers pay a far higher rate.

Our government does less to correct these inequalities than we did in the past, or than other countries do, and as disparities in "market" incomes have increased, its efforts have diminished. It's not just a matter of redistribution, as some suggest. It's in part a matter of ensuring that those at the top pay a fair share of their taxes. And it's in part a matter of ensuring that those at the bottom and in the middle get a fair start in life, through access to education, adequate nutrition and health, and not being exposed to the environmental hazards that have come to plague many of our poor neighborhoods.

But Romney's campaign likes to play tricks with numbers. When he unleashed a tirade against the bottom 47 percent of supposedly freeloading Americans (for which he has since apologized), he failed to note what should have been obvious and has been pointed out repeatedly since he made that remark: those Americans do pay large amounts in taxes. These include (and I'm hardly the first to point this out) payroll taxes, sales taxes, property taxes, excise taxes, and even part of the corporate income taxes that our major corporations manage to pass on to their customers. He failed to note, too, the many older Americans barely above poverty who receive social security payments, for which they contributed through a lifetime of work. Yes, the rich may pay a high and increasing share of the country's total tax revenue, but that's only because they have a high and increasing share of our national income- not because their rates have gone up.

Many of the very rich, like Romney, are avoiding taxes because of numerous loopholes that favor the rich, and capital gains taxes that are taxed at less than half the rate of other income. The 14 percent rate Romney reportedly paid on his income last year is well below that of Americans of comparable income who worked for their money doing things like creating a real business. Tax havens like the Cayman Islands (condemned by the Group20 and all economic experts) facilitate another level of tax avoidance. That the practice is legal is not an economic justification - the loopholes that allow it were put in place by the rich and the bankers, lawyers and lobbyists who serve them so well. We can be sure that the money is not in the Cayman Islands just because it grows faster in the bright sunshine there.
Putting all this together isn’t the politics of envy, as Romney’s camp likes to complain, or even about shaking a finger at the country’s real freeloaders. It’s about cold, hard economics. Tax avoidance and low rates on capital gains - and the inequality they amplify - are weakening our economy. Were the rich paying their fair share, our deficit would be smaller, and we would be able to invest more in infrastructure, technology and education - investments that would create jobs now and enhance growth in the future. While education is central to restoring America as a land of opportunity, all three of these are crucial for future growth and increases in living standards. Tax havens discourage investment in the United States. Taxing speculators at a lower rate encourages speculation and instability - and draws our most talented young people out of more productive endeavors. The result is a distorted, inefficient economy that grows more slowly than it should.

The Romney campaign, however, has defended inequality or brushed it aside. To do so, it has employed a handful of economic myths. Here are a few of the most important:

(1) America is a land of opportunity. While rags-to-riches stories still grip our imagination, the fact of the matter is that the life chances of a young American are more dependent on the income and wealth of his parents than in any of the other advanced countries for which there is data. There is less upward mobility - and less downward mobility from the top - even than in Europe, and we're not just talking about Scandinavia.

(2) Trickle-down economics works (aka "a rising tide lifts all boats"). This idea suggests that further enriching the wealthy will make us all better off. America’s recent economic history shows the patent falsehood of this notion. The top has done very well. But median American incomes are lower than they were a decade and a half ago. Various groups - men and those without a college education - have fared even worse. Median income of a full-time male worker, for instance, is lower than it was four decades ago.

(3) The rich are the "job creators," so giving them more money leads to more and better jobs. This is really a subset of Myth 2. But Romney’s own private sector history gives it the lie. As we all know from the discussion of Bain Capital and other equity firms, many made their money not by creating jobs in America but by "restructuring," "downsizing" and moving jobs abroad, often using debt to bleed the companies of money needed for investment, and using the money to enrich themselves. But more generally, the rich are not the source of transformative innovations. Many, if not most of the crucial innovations in recent decades, from medicine to the Internet, have been based in large measure on government-financed research and development. The rich take their money where the returns are highest, and right now many see those high returns in emerging markets. It's not a surprise that Romney's trust fund invested in China, but it's hard to see how giving the rich more money - through more latitude to escape taxation, either through low taxes in the United States or Cayman Islands hide-aways - leads to a stronger American economy.

(4) The cost of reducing inequality is so great that, as much as idealists would like to do so, we would be killing the goose that lays the golden egg. In fact, the engine of our economic growth is the middle class. Inequality weakens aggregate demand, because those at the middle and bottom have to spend all or almost all of what that they get, while those at the top don't. The concentration of wealth in recent decades led to bubbles and instability, as the Fed tried to offset the effects of weak demand arising from our inequality by low interest rates and lax regulation. The irony is that the tax cuts for capital gains and
dividends that were supposed to spur investment by the wealthy alleged job creators didn't do so, even with record low interest rates: private sector job creation under Bush was dismal. Mainstream economic institutions like the International Monetary Fund now recognize the connection between inequality and a weak economy. To argue the contrary is a self-serving idea being promoted by the very wealthy.

(5) Markets are self-regulating and efficient, and any governmental interference with markets is a mistake. The 2008 crisis should have cured everyone of this fallacy, but anyone with a sense of history would realize that capitalism has been plagued with booms and busts since its origin. The only period in our history in which financial markets did not suffer from excesses was the period after the Great Depression, in which we put in place strong regulations that worked. It's worth noting that we grew much faster, and more stably, in the decades after World War II than in the period after 1980, when we started stripping away the regulations. And in the former period we grew together, in contrast to the latter, when we grew apart.

As I have explained in detail elsewhere, the cost of these myths goes far beyond the damage to our economy, now and in the future. The fabric of our society and democracy is suffering. The worry is that those at the top are investing their money not in real investments, in real innovations, but in political investments. Their big contributions to the presidential and Congressional campaigns are, too often, not charitable contributions. They expect, and have received, high returns from these political investments. These political investments, exemplified by those the financial institutions made, yielded far higher returns than anything else they did. The investments bought deregulation and a huge bailout - though they also brought the economy to the brink of ruin and are a source of much of our inequality.

Such political investments undermine and corrupt our democracy. But there are other manifestations: America is fast becoming a country marked not by justice for all, but by justice for those who can afford it. (Just one of many examples is that no banker has been prosecuted, let alone convicted, for banks' systematic lying to the court regarding the fraudulent practices that played so large a role in the 2008 crisis.) And with the increasing influence of money, especially notable in this election, the outcomes of our political process are becoming more like one dollar, one vote than one person, one vote. It's even worse, because political inequality leads to economic inequality, which leads in turn to more political inequality, in a vicious spiral undermining our economy and our democracy.

Recognizing all this is not class warfare. It is simply acknowledging the realities of life in the United States, which Romney has not done. That should be cause for concern: if you don't recognize that there is a problem, and if you don't understand the sources and consequences, you will never work to solve it.

Obama has at least touched on key elements: his education policies, from "the race to the top" to the reforms of student loan programs, will enhance opportunity. His tax proposals will do a little bit about the extremes at the top. His jobs and investment programs will expand growth now, and in the future, and these will be of enormous benefit to those in the middle. Romney and Ryan have tried a hard tack to the center in their rhetoric in recent weeks. But let no one be deceived: their tax policies will lead to even more inequality at the top, the continued hollowing out of the middle, and more poverty at the bottom. Worst of all, they will lead to a more divided society that endangers our future - our economy, our democracy and our sense of identity as a nation.

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