BOOK REVIEW

Reflections on the issue of economic inequality in the world as described in James K. Galbraith's book "Inequality: What Everyone Needs to Know"[1]

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The author of this book, James K. Galbraith, is a renowned specialist in economic inequality, with at least 20 years of research in this field; he wrote a lot of articles and published some books on this subject: "Inequality : "Everyone Needs to Know" (Oxford University Press, 2016), "Inequality and Instability: A Study of the World Economy Just Before the Great Crisis" (Oxford University Press, 2012), "Created Unequal: (Free Press, 1998), "Inequality and Industrial Change: A Global View" (Cambridge University Press, 2001) co-edited with Maureen Berner. Galbraith leads the *University of Texas Inequality Project* (UTIP), a project that calculates an Estimated Household Income Inequality (EHII) for 149 countries and contains 3872 estimates of Gini coefficients over a period of more than 50 years.

This dataset is one of the few existing datasets in the world (besides the Deininger-Squire data set (DS), the Luxembourg Income Study (LIS) and the Standardized World Income Inequality Database (SWIID)) and has been described by economy historian Robert Skidelsky as "pioneering inequality measurement[2]." UTIP is also recognized for attempting to replace the Gini coefficient with Theil's T statistics when calculating inequality between groups, regions, and countries.

In addition, when inequality became again a major concern (after about 70 years), in the early 1980s, Galbraith served as CEO of the Joint Economic Committee of the United States Congress.

The book was published in the *What Everyone Needs to know* series of the prestigious Oxford University Press publishers, in which balanced opinions of recognized authorities on complex and up-to-date issues and situations are published. This is intended to be a rather in-depth study of the concept of inequality and of the many indicators used to measure it. Also, current and past debates on inequality are presented, along with some of the possible causes and measures to be taken in order to limit it, although the author does not have the objective of advocating any of the adverse parts of this debate. I believe that the ultimate goal of the book, to show the true meaning of inequality to the reader, as well as its effects and implications in different countries or regions of the world, is fulfilled.

The book is structured in five parts dealing with the following topics: a) a definition of economic inequality as well as the various types of indicators that measure inequality; b) an overview of the evolution of inequality in the history of economic thinking; c) causes of inequality variation in the US and the world; d) the consequences of inequality on economic growth, welfare, happiness; e) policies to reduce the inequality.

Considering that in this book the author examines a series of theories regarding the emergence and evolution of inequality, the types of inequality, the benefits and disadvantages of a certain level of inequality, the causes and the means of mitigation, trying, with few exceptions that I will comment, just to describe them, I will also analyze some of the concepts presented in the book which I consider fundamental for understanding the phenomenon and important enough to characterize the general level of the book.

First of all, it is obvious that there are two contradictory trends of thinking: one that considers inequality to be extremely harmful to human society and another that considers inequality as a natural process without which a society could not develop.

Among the problems that can result from the presence of a high level of inequality one may mention:

- Inequality can lead to the emergence of social problems, such as riots or rising crime rates;

- Unemployment, which can be considered a way of showing the failure of markets, meaning the inefficient allocation of resources in the free market;

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[1] James K. Galbraith, Inequality: What Everyone Needs to Know, Oxford University Press, 2016, 224 p.
[2] Skidelsky, Robert (2009). Keynes: The return of the Master. Allen Lane. pp. 124-125.

- The inheritance of considerable fortunes that give to persons in question an improperly assumed advantage in life which causes them to live only for spending these inheritances without making any effort to earn their living;

- As the marginal utility of income is decreasing, the increase in satisfaction is lower for a millionaire compared to a middle-income person, for example, when making an additional $ 1,000. Thus, by increasing revenue taxation, a better overall situation for the whole society can be achieved.

High inequality can lead to a number of advantages:

- The presence of inequality is mandatory for encouraging entrepreneurs to take risks and set up new businesses. This would not happen without the prospect of obtaining substantial gains;

- People's earnings must be directly proportional to their skills, level of training and experience. Here we are dealing with the principle of fairness;

- The incentive effect arises from the fact that rewarding hard work by offering higher wages will lead to an increase in total productivity for the benefit of all;

- Although it is a very controversial argument, the cascade effect is among the advantages of a high level of inequality: if a contractor enriches after assuming risks, he/she creates jobs and offers salaries to other people whose condition is improved compared to the situation of that entrepreneur's non-existence.

Secondly, although there are a number of indicators to measure the level of inequality, as well as enough data gathered over the past 50 years, there is no unanimity when assessing for example, whether the level of inequality has decreased or increased in the aftermath of the great economic crisis of 2007-2008: is inequality still rising in the late 2010s? Some measures indicate that it is. Others are not so clear. Measures of pay inequality in the United States, for example, seem to have peaked in the early 1990s and declined as the economy reached full employment in the late 1990s. Measures of income inequality - including dividends and realized capital gains, as well as the salaries and bonuses of top executives in finance and technology - reached a peak in 2000, with the end of the information-technology boom. Thereafter, these measures show a saw tooth pattern closely coinciding with asset price movements, notably the real estate finance bubble peaking and bursting in 2007, and the stock market recovery starting in 2010. Measures differ on whether the most recent values are slightly higher, or a little lower than in 2000. In any event, it is clear that the great rise of US income inequality became less secure and inexorable after 2000 than it was before. "

Thirdly, many thinkers and researchers have tried to understand the driving forces underpinning the fluctuation of inequality, especially during the economic development process, and to build a pattern of evolution of inequality. In the following paragraphs, we will present two contradictory opinions described by the author.

The one who managed to conduct a profound historical analysis and provided a simple model of industrial and structural change was the American economist of Russian origin, Nobel Laureate Simon Kuznetz. Kuznets's idea was based on his insight that the very important forces that determine the level of inequality in the process of economic development are not the specific public policies but the structural relations between different economic sectors. This process involves two forces: the relative share of high income and low-income sectors in the population, as well as the average difference between the incomes earned by people working in the different types of sectors. If the historical evolution of the level of inequality follows the trajectory described by Kuznetz, then it will take the form of an inverted U, with inequality rising at the beginning of the development process and then decreasing.

This model may undergo changes if the final conditions are historically different from those taken into consideration by Kuznets. For example, let's assume that in the present, some countries manage to take over leadership in certain border areas, such as advanced technologies, communications and/or financial services. In this case, the increase of the income of entrepreneurs in these areas will lead to an increased inequality in the respective countries. Consequently, the Kuznetz curve, which had experienced a decline during the industrialization process, will have a new inflection in the most developed countries during this new innovation phase and will flatten over time. This new curve was named the "Augmented Kuznetz Curve" by Pedro Conceiçao

and James K. Galbraith in an article in 2001[3]. The new model seems to cope with the simulations made by the above-mentioned authors using data for several countries, including the United States, Japan and the United Kingdom.

The view contrary to Kuznetz's ideas is presented by Thomas Piketty in his famous book, *The Capital in the Twenty-first Century*[4], which considers that a fundamental trend, determined by a profound feature of capitalism, is to increase the level of income inequality and, above all, the inequality of wealth. The historical trend of increasing inequality is based on two fundamental laws, according to Piketty. The first law states that the ownership of financial assets is very concentrated, so if income from financial assets grows faster than total income, then income inequality has to increase. In other words, $r > g$, where r represents the rate of profitability of the financial asset or what Piketty denotes capital, and g represents the growth rate of an economy. In his book, Piketty argues that in the long run, the value of r is around 5%, with g oscillating around 2%. Therefore, the previous inequality is almost always true.

Galbraith disagrees with this theory that the general trend of capitalism is to generate a continuous upward redistribution based on earnings from financial assets. This is demonstrated in a chapter in the book, written on the basis of the article published in 2014 as a review of Piketty's[5] book stating that the increasing trend of inequality is not clear for two reasons. The first is that the level of interest income taxation reduces the difference between r and g while spending on interest income can reduce the amount of available financial assets over time. The second reason is that most of the 20th century is an exception to the first law of Piketty. Between 1914 and 1980, when income taxation was implemented on a large scale and interest rates began to be controlled by central banks, r did not go beyond tax collection - and income inequality did not increase in the course of the process analyzed by Piketty.

The second law refers to the effect of savings on financial wealth, claiming that a higher rate of savings by wealthy people strengthens their advantage over the rest of the population and increases their income at a faster pace. This argument can be counter-balanced in the same way: taxes and inflation can decrease the value of accumulated wealth compared to the newly realized revenues.

In another article on inequality[6], Galbraith argues that the publication of Piketty's book has helped spread the idea that the rise in inequality is due to economic growth rates, interest rates, exchange rates, trade conditions and other macroeconomic phenomena that affect all economies in a systematic and general way. But reducing this phenomenon only to interest rates, growth rates, and savings is unconvincing. For example, in the case of the United States, the relationship between capital asset bubbles and income inequality is not taken into account. This link is clearly highlighted by existing data and has nothing to do with high-interest rates or savings. Rather, we are dealing with the reallocation of incomes from some rich people to others, meaning there have been price increases in capital assets in certain sectors (finance, technology), while other sectors have been endangered (manufacturing industries old). The rise in inequality was due to the fact that a handful of new capitalists became the winners of this game, while a significantly larger group - along with their employees - disappeared from the business.

Fourth and finally, one of the last chapters lists the policies that can be implemented to reduce the level of regional and global inequality. Even though the entire book wishes (and even succeeds, in our opinion) to be a balanced navigation between the two contradictory views presented at the beginning of the review, the mere presence of this chapter represents the author's enrolling among supporters of reducing the level of inequality, regardless of its type. This chapter lists the most important policies that can be implemented to reduce inequality, along with the author's view of the impact of implementing each of these policies in light of the experience and calculations made by the author. We will look at some of these policies in the following sentences.

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[3] Conceição, P. , Galbraith, J.K.: Toward a New Kuznets Hypothesis: Theory and Evidence on Growth and Inequality, in Galbraith , J.K., Berner, M. (eds.): Inequality and Industrial Change: A Global View, New York 2001, Cambridge University Press, pp. 139-160.

[4] Piketty, T.: Capital in the Twenty-First Century, Cambridge 2014, Harvard University Press.

[5]Galbraith, J.K.: *Kapital for the Twenty-First Century?* available at https://www.dissentmagazine.org/article/kapital-for-the-twenty-first-century

[6] Galbraith, J.K.: Causes of Changing Inequality in the World, Intereconomics, 2016 (2), available at https://www.ceps.eu/system/files/IEForum22016_2.pdf

The antitrust policy was probably the first major egalitarian policy of the modern age. It is hard to find any proof that the dissolution of most trusts in order to eliminate monopolies on the American market has led to the fall of inequality.

It is assumed that trade liberalization reduces monopolistic profits or economic rents and leads to a general increase in welfare. Even if, following the Second World War, the world has moved towards a more open trade, the continuation of free trade agreements (which, through the few thousand pages each has, are in fact detailed regulations of trade control and investment freedom) cannot make us measure the intensity of the correlation between trade liberalization and inequality in an empirical way.

Progressive taxation of income has different effects depending on different models of market economy: for advanced social-democratic countries, the effect is between 10% and 15%, in the case of the United States it was around 20%, and for most developing countries, the effect is roughly zero, since tax does not significantly reduce the wealthy benefits of the wealthy people over the middle class and the poor class.

Countries with strong trade unions and laws that provide high minimum wage levels - with average country productivity - have a lower degree of inequality than those in the opposite position. The few countries where there are national wage negotiations have enjoyed some of the lowest levels of inequality.

To conclude, it does not take much effort to find out that the author is a believer in reducing inequality (at least to the possible extent). However, I think Mr. Galbraith did a very good job of writing an objective description of inequality and its evolution, and has managed to explain these issues without getting too far into the technicalities. All these things make this book understandable for many people who want to learn more about this controversial issue, but do not have a specialist's background in economics. Also, it can be a good starting point for anyone interested in learning more about the vast inequality issues humanity faced and continues to face.