Global Policy public lecture

The Haves and Have Nots

Branko Milanovic
Lead economist, World Bank's research division
Visiting fellow, All Souls College, Oxford

Professor Danny Quah
Chair, LSE
The haves and the have-nots: A short and idiosyncratic history of global inequality

Branko Milanovic
Winter 2010-11
“To determine the laws which regulate this distribution [into wages, profits and rent], is the principal problem in Political Economy.”

David Ricardo (1817), *Principles of Political Economy* (Preface)

“..of the tendencies that are harmful to sound economics, the most seductive, and …the most poisonous, is to focus on questions of distribution.”

0. Overview of the present and past of global inequality
Inequality 1950-2009
The mother of all inequality disputes

With new PPPs

Graph in interyd\do files\defines.do
BRICs and the US in percentiles
(year 2002; new PPPs)

Using world2002_centile.dta and michele_graph.do
A non-Marxist world

• Over the long run, decreasing importance of within-country inequalities despite some reversal in the last quarter century
• Increasing importance of between-country inequalities
• Global division between countries more than between classes
Composition of global inequality changed: from being mostly due to “class” (within-national), today it is mostly due to “location” (where people live; between-national).

Based on Bourguignon-Morrisson (2002) and Milanovic (2005)

From thepast.xls
1. Vignettes
1A. Marriage and Money
## Inequality 2 centuries ago & now: England

Elizabeth’s dilemma (from *Pride and Prejudice*)

<table>
<thead>
<tr>
<th></th>
<th>Income in 1810 (£ pa)</th>
<th>Approx. position in 1810 income distribution</th>
<th>Income in 2004 (£ pc pa)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mr. Darcy</td>
<td>10,000</td>
<td>Top 0.1%</td>
<td>400,000</td>
</tr>
<tr>
<td>Elizabeth’s family</td>
<td>3000/7~430</td>
<td>Top 1%</td>
<td>81,000</td>
</tr>
<tr>
<td>Elizabeth alone</td>
<td>50</td>
<td>Median</td>
<td>11,500</td>
</tr>
<tr>
<td>Gain</td>
<td>100 to 1</td>
<td></td>
<td>17 to 1</td>
</tr>
</tbody>
</table>

1810 position estimates based on Colquhoun 1801-3 data. 2004 UK data from LIS, and for 0.1% from Piketty (*Data-central*).
### Inequality 135 years ago & now: Russia

Anna’s 150-fold gain (from *Anna Karenina*)

<table>
<thead>
<tr>
<th></th>
<th>Income in 1875 (R pa)</th>
<th>Approx. position in 1875 income distribution</th>
<th>Income around 2005 (R pc pa)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Count Vronsky</td>
<td>100,000</td>
<td>Top 0.1%</td>
<td>3,000,000</td>
</tr>
<tr>
<td>Karenin and Anna</td>
<td>9000/3~3000</td>
<td>Top 1%</td>
<td>340,000</td>
</tr>
<tr>
<td>Anna’s parents</td>
<td>200</td>
<td>Mean (around 65\textsuperscript{th} percentile)</td>
<td>53,000</td>
</tr>
<tr>
<td>Gain</td>
<td>150 to 1</td>
<td></td>
<td>19 to 1</td>
</tr>
</tbody>
</table>

2005 data from surveysfor05\ECA\RUS2005_3.dta. For the top 0.1%. I take the maximum incomes (multiplied by 3).
Elizabeth Bennet and Anna Karenina

If Elizabeth loses the estate with Vronsky

If Elizabeth marries Mr. Darcy with Anna's family

The opening position in both novels

Incomes: Anna’s family

Alternative lives
Trade-off between inequality and love in marriage

Marital bliss vs. Country’s Gini coefficient

- Nick Diver, 1920
- Elizabeth Bennet, 1810
- Emma Rouault-Bovary, 1856
- Anna Karenina, 1875
1B. The three generations of Obamas
Obama’s three generations

Income

Obama’s grandfather: as high as he could get before reaching a colonial ceiling

Subsistence: 140 shillings

Europeans: 16,000 shillings on average!

All blacks

240 shillings
Because colonies pushed inequality to its maximum—and Kenya was not an exception
Independence’s dashed hopes:
Kenya’s GDP per capita as % of US GDP per capita

Based on Maddison’s data (in 1990 PPPs)
Citizenship premium (our next topic) in Obama’s own words

[My mother] had always encouraged my rapid acculturation in Indonesia...She had taught me to disdain the blend of ignorance and arrogance that too often characterized Americans abroad. But she now learned...the chasm that separated the life chances of an American from those of an Indonesian. She knew which side of the divide she wanted her child to be on. I was an American, she decided, and my true life lay elsewhere [outside of Indonesia].
1C. How different are the United States and the European Union?
Inequality in the United States and European Union constituent units (Gini points, around 2005)

<table>
<thead>
<tr>
<th></th>
<th>Most equal</th>
<th>Average</th>
<th>Most unequal</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>34</td>
<td>39</td>
<td>45</td>
</tr>
<tr>
<td></td>
<td>(South Dakota; Wisconsin)</td>
<td>(Delaware; Idaho)</td>
<td>(Texas; Tennessee)</td>
</tr>
<tr>
<td>European Union</td>
<td>24</td>
<td>31</td>
<td>38</td>
</tr>
<tr>
<td></td>
<td>(Hungary; Denmark)</td>
<td>(Netherlands)</td>
<td>(UK; Portugal)</td>
</tr>
<tr>
<td>Difference</td>
<td>10 points</td>
<td>8 points</td>
<td>7 points</td>
</tr>
</tbody>
</table>
Dark color = high inequality countries or states.
GDP per capita differences in the United States and European Union, around 2005

<table>
<thead>
<tr>
<th></th>
<th>Poorest</th>
<th>Average</th>
<th>Richest</th>
<th>Ratio top to bottom</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>66 (Mississippi; West Virginia)</td>
<td>100 (Rhode Island)</td>
<td>137 (Connecticut; Delaware)</td>
<td>2 to 1</td>
</tr>
<tr>
<td>European Union</td>
<td>36 (Bulgaria; Romania)</td>
<td>100 (Spain)</td>
<td>140 (Netherlands)</td>
<td>4 to 1</td>
</tr>
<tr>
<td>Difference</td>
<td>-30 points</td>
<td>0 points (by definition)</td>
<td>+3 points</td>
<td></td>
</tr>
</tbody>
</table>
GDP per capita in countries of the European Union and states of the USA (unweighted)
Ginis in countries of the European Union and states of the USA

Overall inter-personal Gini for both

Europe

USA

Gini

0

0.05

0.1

0.15

0.2

0.25

0.3

0.35

0.4

25

30

35

40

45

.kdensity gini if Deurope==1) (kdensity gini if Deurope==0, legend(off) xtitle((Gini) xline(31 38) xline(41, lwidth(thick)))
Using US_vs_EU.dta in c:\perseus\sources
## Between-unit and total inequality in selected countries, around year 2005

<table>
<thead>
<tr>
<th>Country</th>
<th>Gini: Between-states or countries</th>
<th>Gini total (between individuals)</th>
<th>Share of inter-state inequality in total (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA (50 states)</td>
<td>8</td>
<td>40+</td>
<td>~20</td>
</tr>
<tr>
<td>EU-15 countries (pre-enlargement)</td>
<td>10.2</td>
<td>33.4</td>
<td>30</td>
</tr>
<tr>
<td>EU-27 (post enlargement)</td>
<td>23.1</td>
<td>40.3</td>
<td>57</td>
</tr>
<tr>
<td>China (29 provinces)</td>
<td>24</td>
<td>40+</td>
<td>~60</td>
</tr>
<tr>
<td>EU-34 (all of Europe, incl. Turkey)</td>
<td>30.1</td>
<td>44.8</td>
<td>67</td>
</tr>
</tbody>
</table>

EU data calculated from world2002.dta US from the same source;
Two types of inequalities

• The American: all constituent units are unequal internally, but the differences in their mean incomes are small
• The European: constituent units are equal internally, but mean income differences between them are large
• In the American type, poverty is an individual attribute; in the European type, poverty is a collective attribute
• Policies must be different too: pro-poor in one case, “regional cohesion” in the other
Implications

• How far can EU’s expansion continue?
• With the last 2 expansions, EU has moved away from an American type of inequality
• With Turkey, EU’s Gini would exceed 45, so Europe would come to resemble Latin America: does this set a limit to EU expansion?
• China has a similar structure of inequality like Europe
• Such huge inter-national differences in mean incomes set also a limit to a possible political unity of Asia (leaving even aside the two giants): Asia is by far the most income heterogeneous continent
2. Citizenship rent and global inequality of opportunity
2A. *Les jeux sont faits* when you are born?
An example: global percentile positions (income levels in $PPP) in Denmark and selected African countries

Based on B. Milanovic, *Worlds Apart: Measuring International and Global Inequality*
Estimation

\[ y_{ij} = b_0 + b_1 m_j + b_2 G_j + b_3 C_{ij} + \varepsilon_{ij} \]

mj = mean country income
Gj = Gini coefficient
Cij = income class of i-th individual in j-th country

The issue: How to substitute parental income class \((C_{ij}^*)\) for own income class \((C_{ij})\), and thus have the entire regression account for the effect of circumstances only?

Run over income ventiles for 116 countries and 2320 (20 x 116) income levels \((y_{ij})\)
Global inequality of opportunity

- How much of variability of income globally can we explain with two circumstances (Roemer) only: person’s country of citizenship and income class of his/her parents?
  - Both circumstances basically given at birth
  - With citizenship person receives several public goods: income of country, its inequality level, and its intergenerational income mobility
- Use HS data to investigate that
• **Global equality of opportunity?** Country of citizenship explains almost 60% of variability in global income. (Estimated across representative individuals that have the mean income of their countries’ ventiles or percentiles). Citizenship and parental income class combined explain about 80%.

• **For comparison:** 4 circumstances (place of birth, parents, ethnicity, age) explain 40% of wage inequality in the US (N. Pistolesi, JofEI, 2009)
2B. Implications: migration; just international order
The XXI century trilemma

A. Globalization of ideas, knowledge, Communication, awareness of others’ living standards

B. Increasing differences in mean incomes among countries

C. No movement of people

If A and B, then no C. Migration is the outcome of current unequal globalization.
If B and C, then no A. Unequal globe can exist if people do not know much about each other’s living conditions or costs of transport are too high.
If A and C, then no B. Under globalization, people will not move if income differentials are small.
Growing inter-country income differences and migration:
Key seven borders today
The key borders today

• **First to fourth world**: Greece vs. Macedonia and Albania; Spain vs. Morocco (25km), Malaysia vs. Indonesia (3km)

• **First to third world**: US vs. Mexico

• The remaining three key borders walled-in or mined: N. Korea—S. Korea; Yemen—Saudi Arabia; Israel---Palestine

In 1960, the only key borders were Argentina and Uruguay (first) vs. Brazil, Paraguay and Bolivia (third world), and Australia (first) vs. Indonesia (fourth)
<table>
<thead>
<tr>
<th>Country/Region</th>
<th>Approximate % of foreign workers in labor force</th>
<th>Year 2007</th>
<th>Year 1980</th>
</tr>
</thead>
<tbody>
<tr>
<td>Greece (Macedonian/Albanians)</td>
<td>7.5</td>
<td>4 to 1</td>
<td>2.1 to 1</td>
</tr>
<tr>
<td>Spain (Moroccans)</td>
<td>14.4</td>
<td>7.4 to 1</td>
<td>6.5 to 1</td>
</tr>
<tr>
<td>United States (Mexicans)</td>
<td>15.6*</td>
<td>3.6 to 1</td>
<td>2.6 to 1</td>
</tr>
<tr>
<td>Malaysia (Indonesians)</td>
<td>18.0</td>
<td>3.7 to 1</td>
<td>3.6 to 1</td>
</tr>
</tbody>
</table>

Is citizenship a rent?

• If most of our income is determined by citizenship, then there is little equality of opportunity *globally* and citizenship is a rent (unrelated to individual desert or effort)

• How much is citizenship worth? Black-market UK passports sold for about £5,000; legally purchase citizenship for about $1m in investment.
The logic of the argument

- Global inequality between individuals in the world is very high (Gini=70)
- Most of that inequality is “explained” by differences in countries’ per capita incomes
- Citizenship “explains” some 60% of variability in personal incomes globally (assessed across national ventiles)
- This was not the case in the past (around 1850-70) when within-national inequalities “explained” most of global inequality
The questions to ask:

- Citizenship is a morally-arbitrary circumstance, independent of individual effort
- It can be regarded as a rent (shared by all members of a community)
- Is inter-generational transmission of collectively acquired wealth acceptable?
- Is it different from inter-generational transmission of family wealth? Why?
- Political philosophy arguments pro rent (social contract; statist theory; philia--Aristotle) and contra (cosmopolitan, justice as equality of opportunity)
3. Global inequality and the Rawlsian world
(also one of the vignettes)
Rawls on (a) inequality between countries and (b) global inequality

- Neither of them matters
- Concept 1 (divergence) is irrelevant if countries have liberal institutions; it *may* be relevant for liberal vs. burdened societies
- Irrelevance rooted in two key assumptions: (i) political institutions of liberalism are what matters; (ii) acquisition of wealth immaterial for both individuals and countries
- Global inequality between individuals similarly irrelevant once the background conditions of justice exist in all societies
- But within-national inequalities matter because the difference principle applies within each people (note however that the DP may allow for high inequality)
Rawls on irrelevance of material wealth for a “good society” and global optimum

• It is a mistake to believe that a just and good society must wait upon a high material standard of life. What men want is meaningful work in free associations with others, these associations regulating their relations to one another within a framework of just basic institutions. To achieve this state of things great wealth is not necessary. In fact, beyond some point it is more likely to be a positive hindrance, a meaningless distraction at best if not a temptation to indulgence and emptiness. (A Theory of Justice, Chapter V, §44, pp. 257-8).

• For Rawls, global optimum distribution of income is simply a sum of national optimal income distributions (my interpretation)
Go back to our definition of global inequality

- In Gini terms:

\[
\sum_{i=1}^{n} G_i \mu + \frac{1}{\mu} \sum_{i}^{n} \sum_{j>i}^{n} (y_j - y_i) p_i p_j + L
\]

Term 1

Term 2

Rawls would insist on the minimization of each individual Gini (G_i) so that Term 1 (within-inequality) would be minimized. But differences in mean incomes between the countries can take any value. Term 2 (between inequality) could be very high.

And this is exactly what we observe in real life. Term 2 accounts for 85% of global Gini.
<table>
<thead>
<tr>
<th>Mean country incomes</th>
<th>All equal</th>
<th>Different (as now)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual incomes within country</td>
<td>All equal</td>
<td>0</td>
</tr>
<tr>
<td>Different (as now)</td>
<td>45.6 (all mean incomes same; all country Ginis as now)</td>
<td>69.7</td>
</tr>
</tbody>
</table>
Conclusion and 21st century policy issues

- To reduce significantly global inequality (and poverty) and citizenship rent there are two ways:
  - A slow and sustainable way: higher growth rate of poorer countries
  - A fast and possibly politically tumultuous way: increase migration

- Either poor countries will have to become richer or poor people will move to rich countries.

- Should migrants be taxed additionally to pay native population’s losers and those remaining in their countries of origin?
EXTRAS. Should the whole world be composed of gated communities
Passages and death at average annual rates

<table>
<thead>
<tr>
<th></th>
<th>Estimated successful illegal passages</th>
<th>Number of arrests</th>
<th>Deaths</th>
<th>Death rate</th>
<th>Relative death rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Berlin Wall</td>
<td>~200*</td>
<td>115</td>
<td>~7</td>
<td>2.2%</td>
<td>100</td>
</tr>
<tr>
<td>Mexican Wall</td>
<td>200,000</td>
<td>About 1 million</td>
<td>400-500</td>
<td>0.05%</td>
<td>2</td>
</tr>
<tr>
<td>Africa/EU</td>
<td>200,000</td>
<td>Around 1000</td>
<td>0.5%</td>
<td>23</td>
<td></td>
</tr>
</tbody>
</table>

* Most of the successful passages before the consolidation of the Wall.
A debate about inequality: come prepared

• The Economist (January 2011): “Remember: Envy is a deadly sin!” (List made in 4th century, envy introduced on the list in the 7th)

• “Again I tell you, it is easier for a camel to go through the eye of a needle than for a rich man to enter the kingdom of God.”

• "If you want to be perfect, go, sell your possessions and give to the poor, and you will have treasure in heaven.” (in Mark, Luke and Matthew)
China
China (1980-2000)

Red: fast growth (1σ above the mean)
Yellow: average
Light yellow: slow (1σ below the mean)

North to South
Shandong
Jiangsu
Zhejiang
Fujian
Guangdong
China’s Gang of Eleven: 5 maritime provinces + 4 city provinces + Hong Kong and Macao: almost 60% of GDP by a third of the population

Provinces are from N to S: Shanong, Jiansu, Zhejiang, Fujian, Guangdong
India and China Ginis, 1950-2004

twoway (scatter Giniall year if contcod=="IND" & Di==0 & Dhh==0, connect(l)) (scatter Giniall year if contcod=="CHN" & Di==1 & Dhh==0 & year<2005, connect(l)), legend(off) text(33 1970 "India") text(40 1990 "China")

From igdppppreg.dta
Where are the BRICS compared to the United States (year 2005, new PPPs)?

Using world2002_2005dta and michele_graph.do
BRICs and the US in percentiles (year 2002; new PPPs)

Using world2002_centile.dta and michele_graph.do
Chinese and American income distributions, 2005

From world2002_2005.dta
The crisis
Rich man’s crisis? 2008 GDP per capita against growth rate in 2009 (with population weights)
Plutocratic and democratic real global growth rate, 1990-2009

twoway (scatter gdpROG year if contcod=="USA" & year>1990, connect(l) yline(0) legend(off)) (scatter gdprog year if contcod=="USA" & year>1990, connect(l) text(0.01 2002 "global plutocratic growth rate") text(0.06 2002 "people global growth rate"))
From gdppp preg.dta
Global Policy public lecture

The Haves and Have Nots

Branko Milanovic
Lead economist, World Bank's research division
Visiting fellow, All Souls College, Oxford,

Professor Danny Quah
Chair, LSE