

Hosted by the International Inequalities Institute
**The Evolution of Global Inequalities:
the impact on politics and the economy**

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EVENTS

Hashtag for Twitter users: #LSEBranko

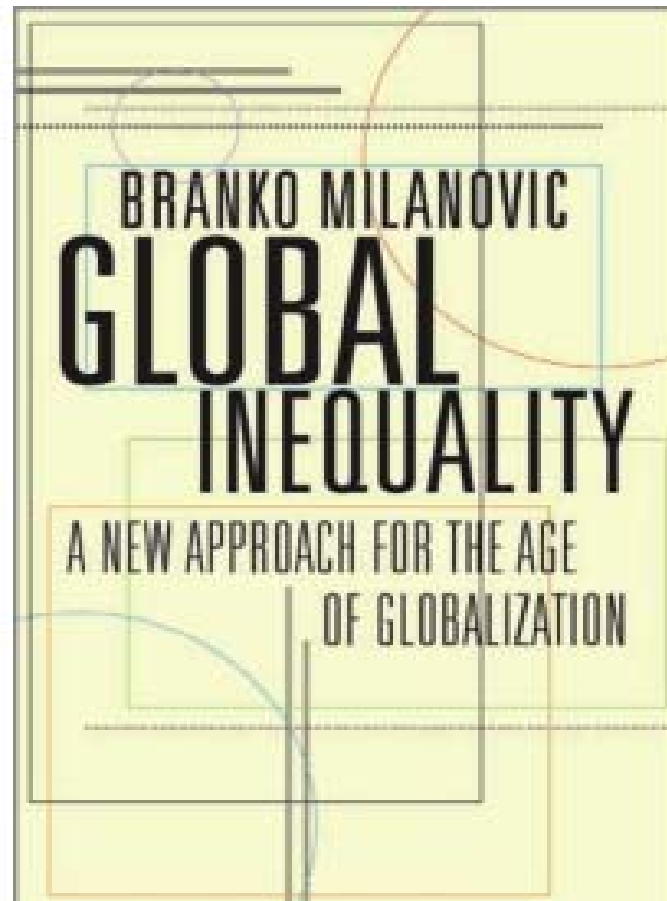
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Inequality in the age of globalization

Branko Milanovic
Spring/Summer 2017

Largely based on:

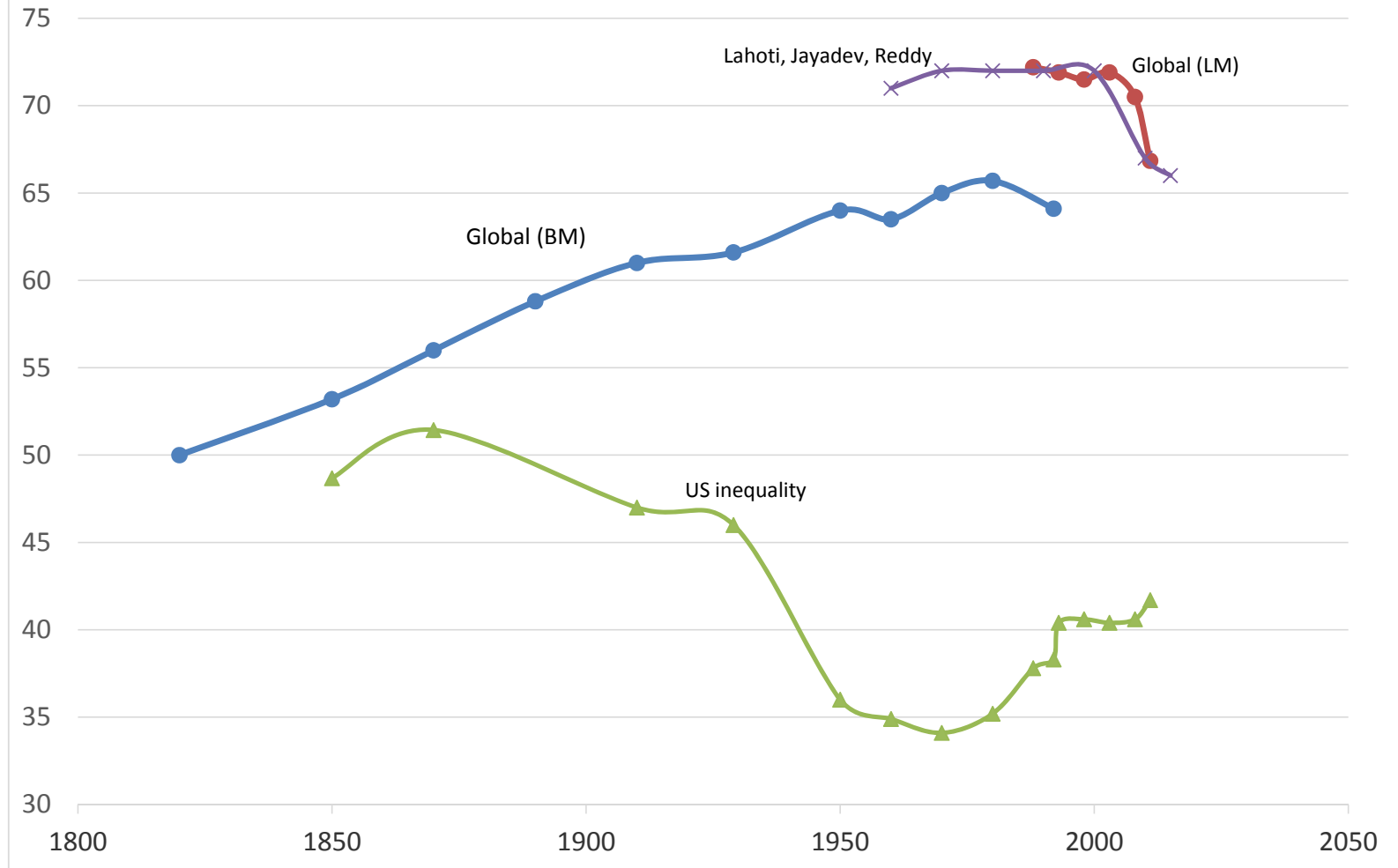


Brief structure of the talk

- Global inequality: in the past and now
- Technical problems of measurement
- How the world has changed between 1988 and 2013
- [Political implications of the changes]
- [Kuznets waves?]
- Issues of justice, politics and migration

1. Global inequality: key developments

Global and US Gini over two centuries



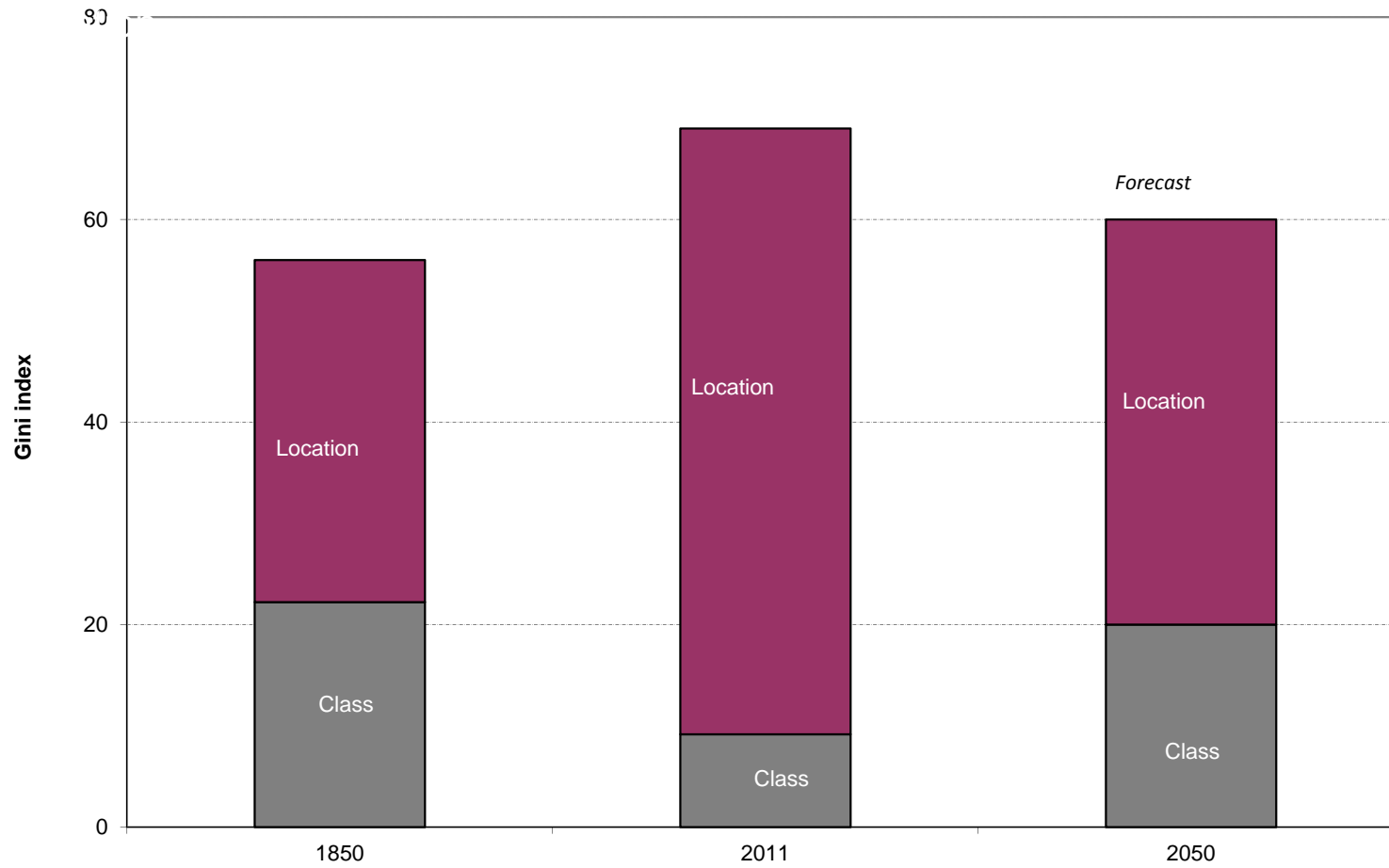
Lahoti, Jayadev, Reddy

Global (BM)

US inequality

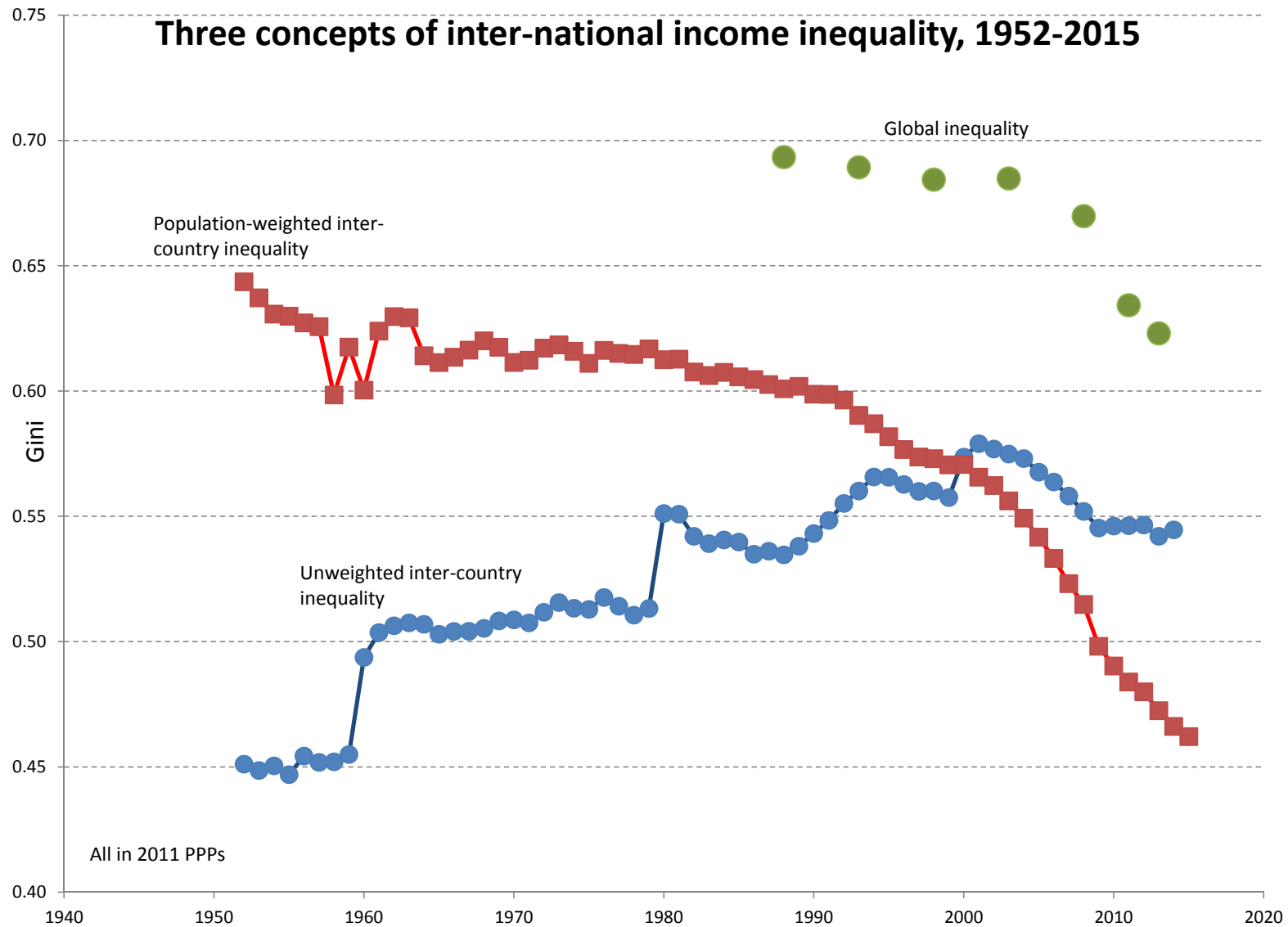
Global (LM)

La longue durée: From Karl Marx to Frantz Fanon and back to Marx?

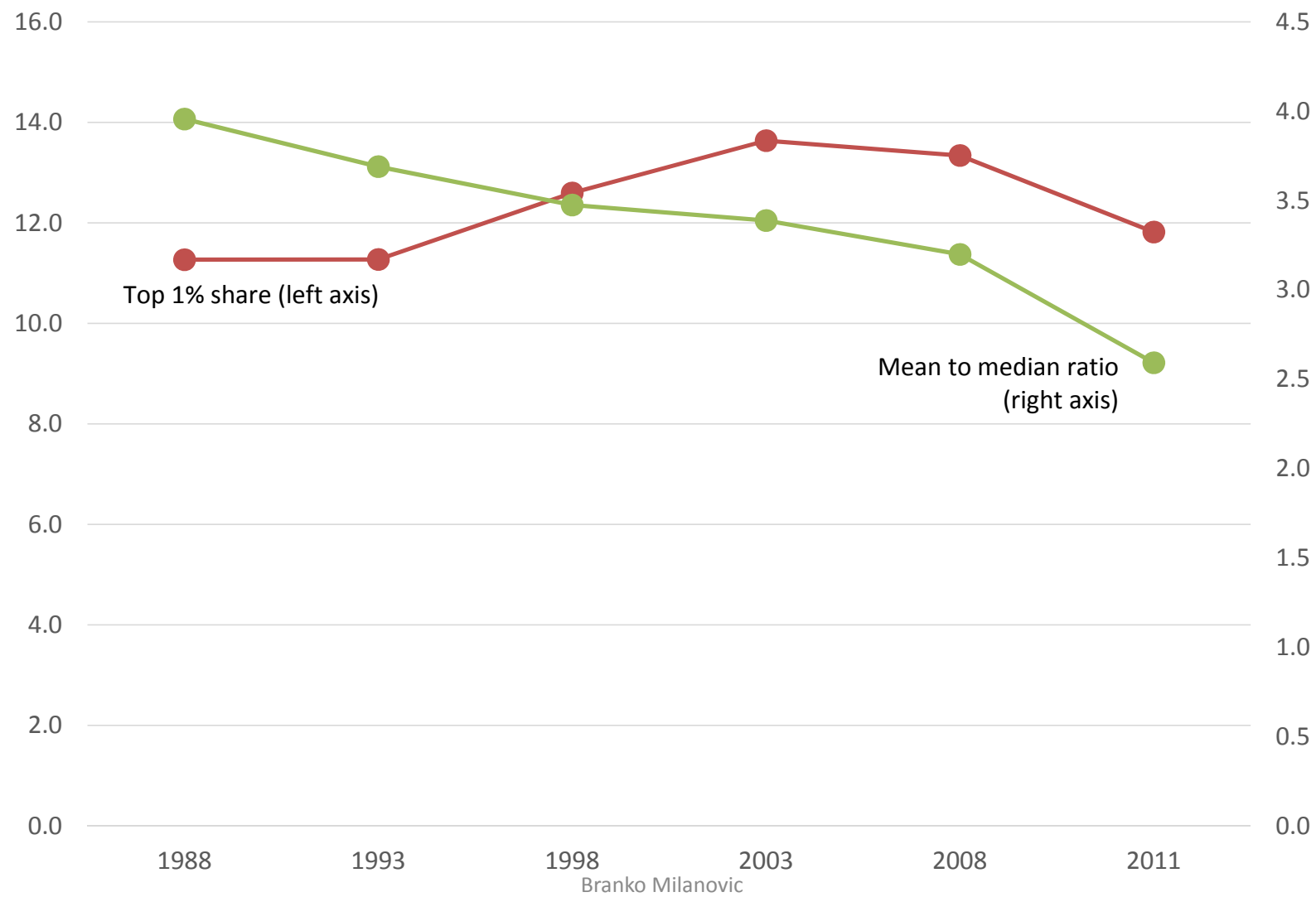


- In the *long-run* inequality is determined by the spread of the technological revolutions: the West in the 19th century, Asia today
- In the *medium-run* global inequality is determined by:
- What happens to within-country income distributions?
- Is there a catching up of poor countries?
- Are mean incomes of populous & large countries (China, India) growing faster or slower than the rich world?

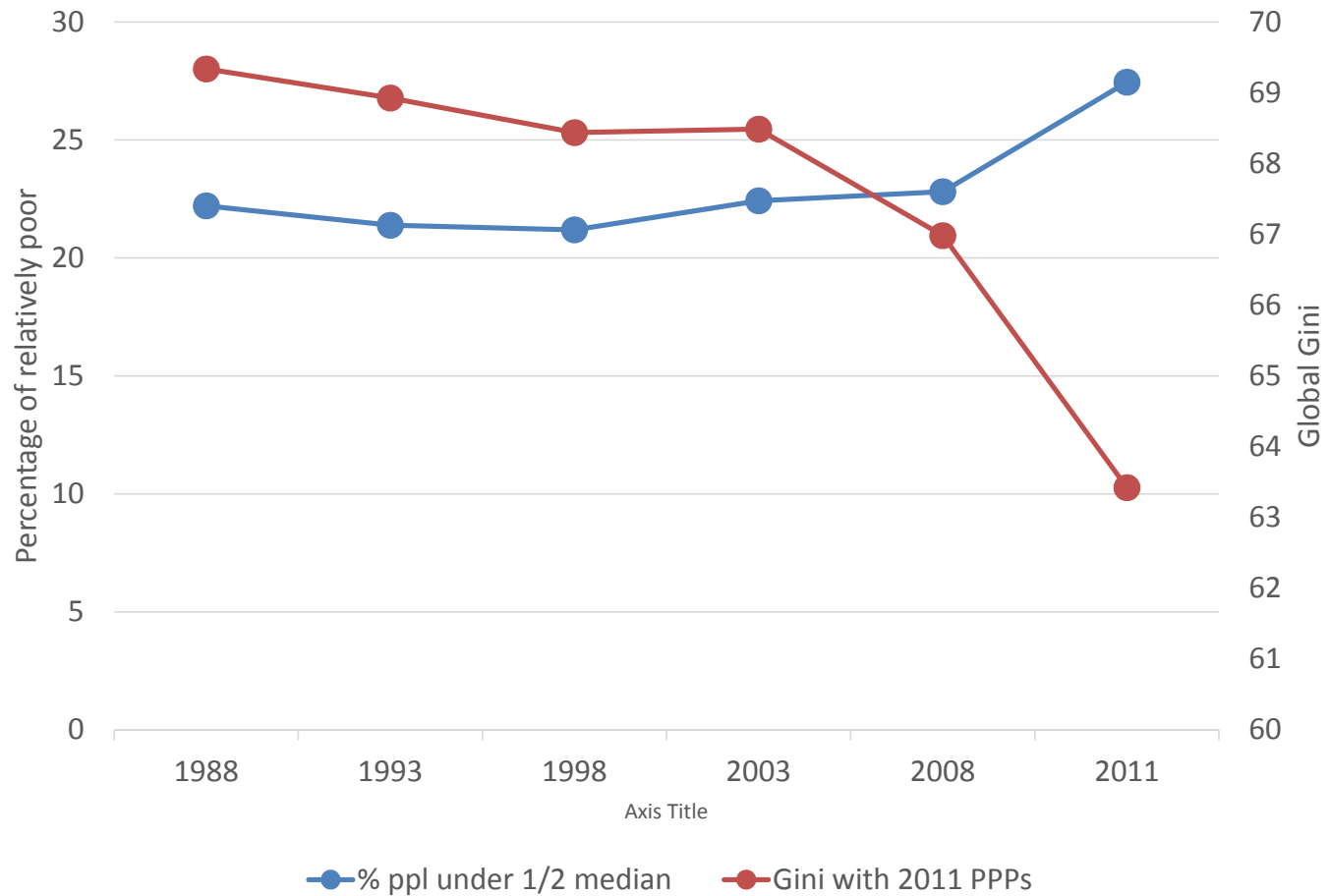
Three concepts of inter-national income inequality, 1952-2015

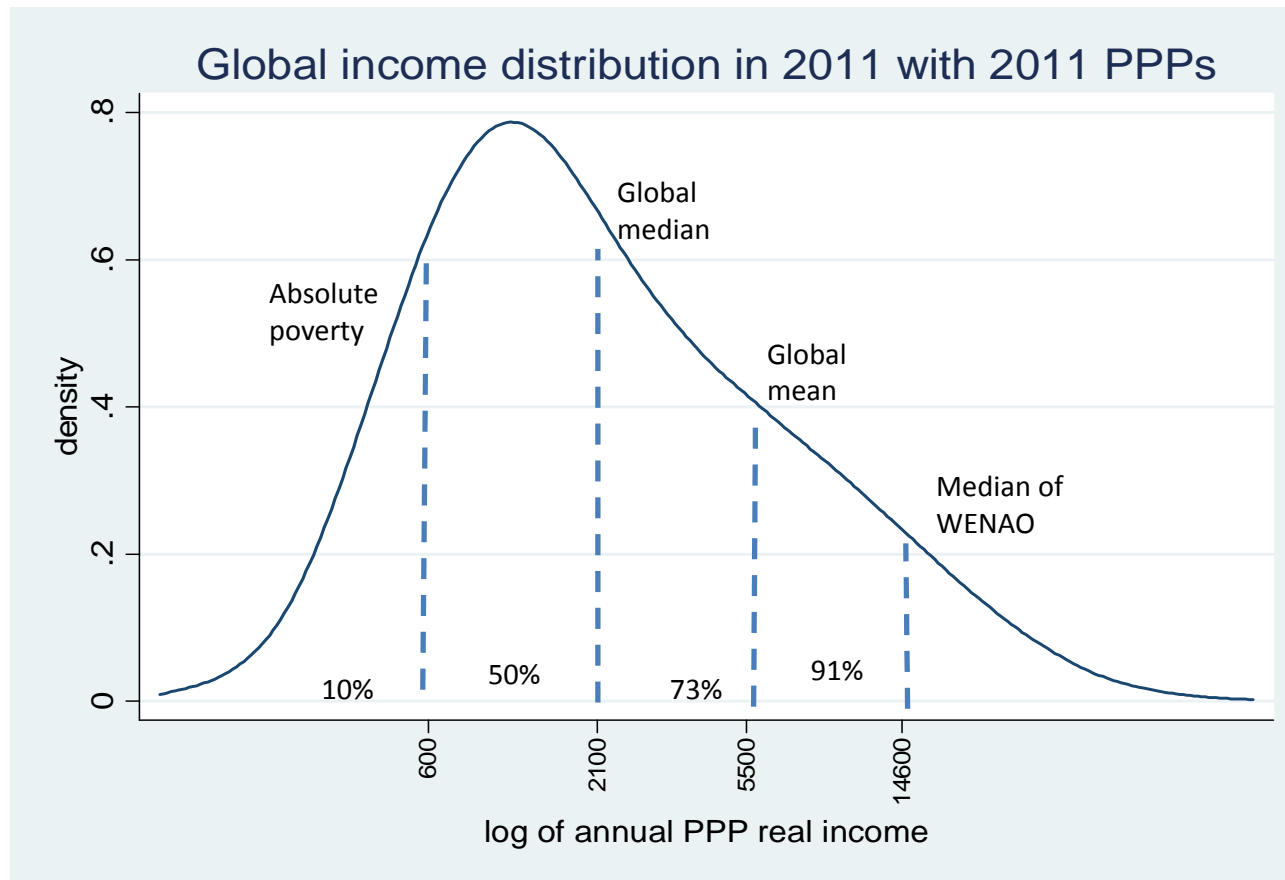


Key developments, 1988-2011



Gini and percentage of world population with income less than 1/2 global median, 1988-2011





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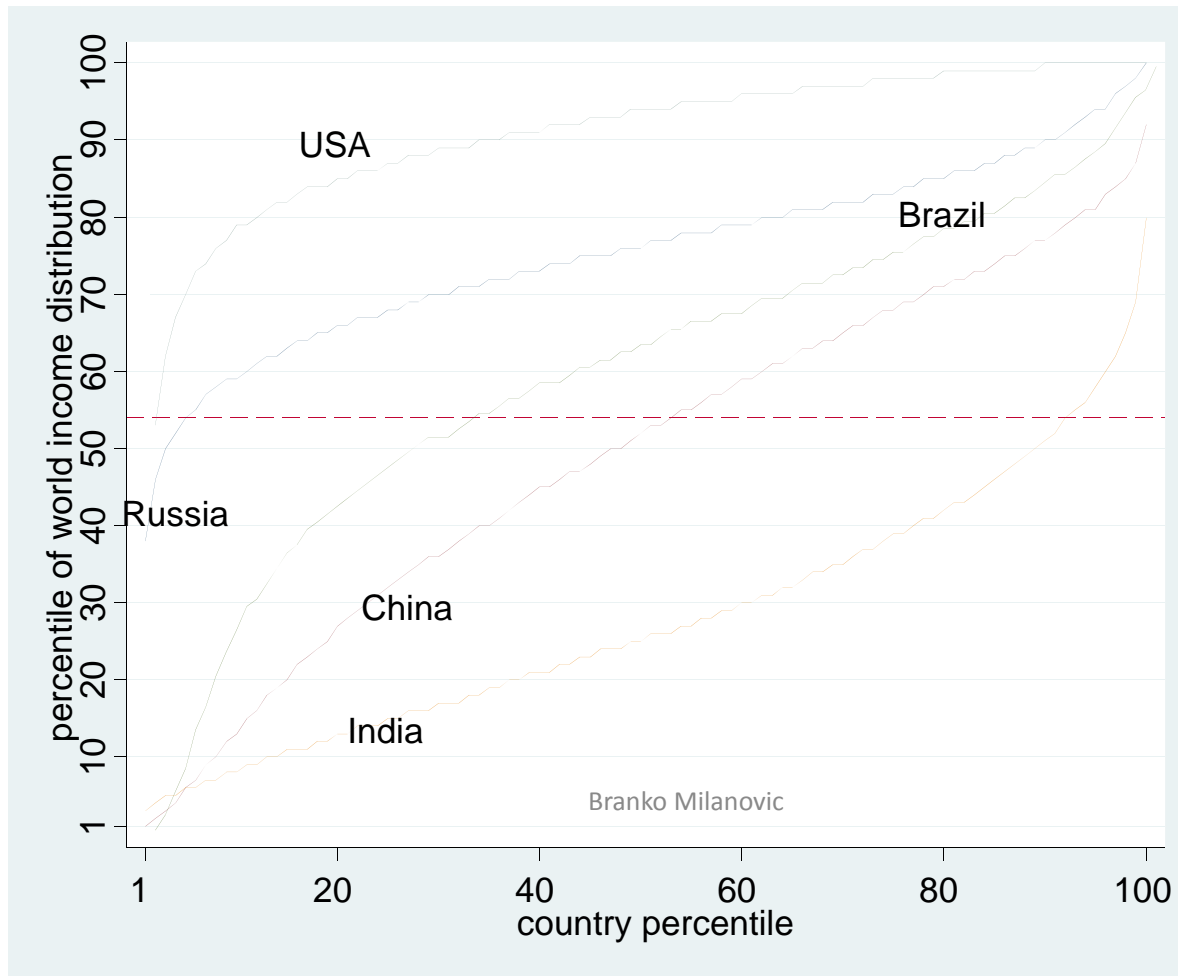
twoway (kdensity loginc_11_11 [w=popu] if loginc_11_11>2 & bin_year==2011, bwidth(0.2)) , legend(off) title(Global income distribution in 2011 with 2011
PPPs) xtitle(log of annual PPP real income) ytitle(density) xlabel(2.8"600" 3.3"2100" 3.74"5500" 4.2"14600", labsize(small) angle(90))
Using combine88_11.dta

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Large gaps in mean country incomes raise two important issues

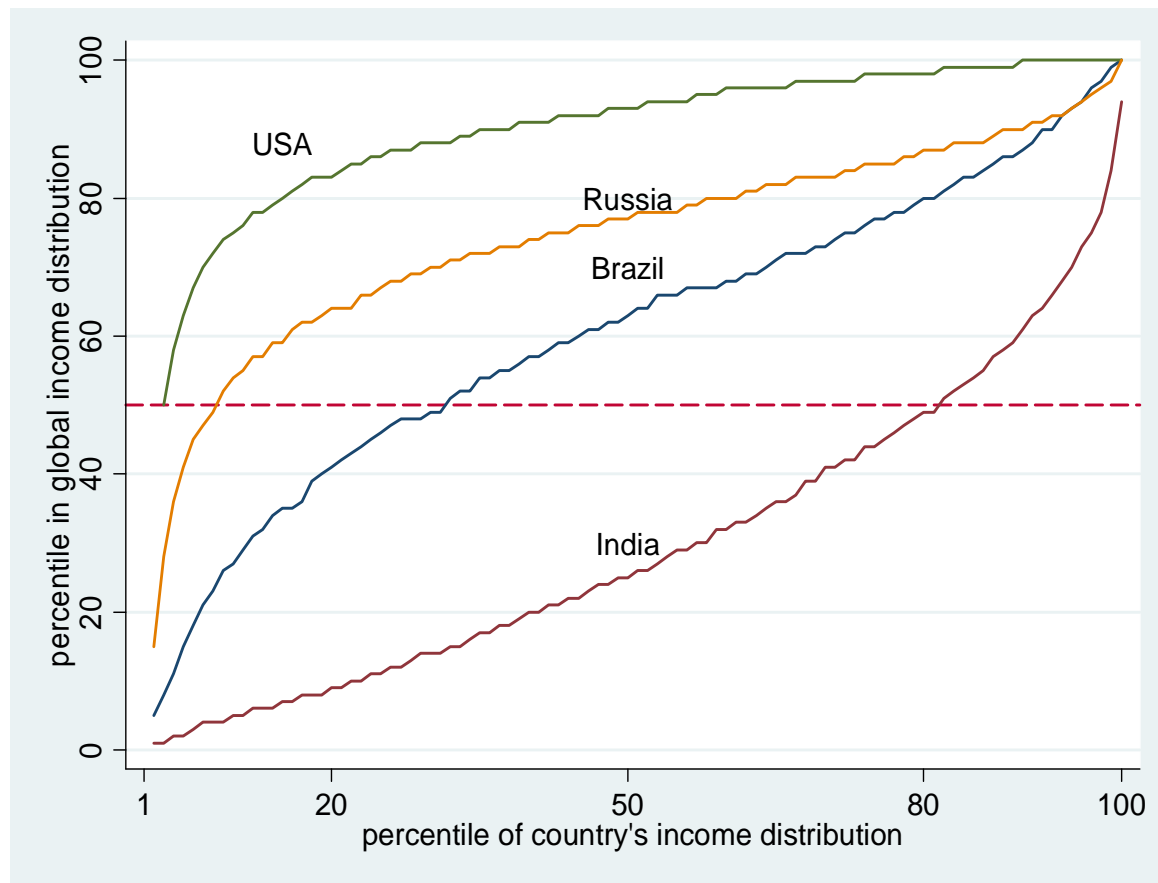
- Political philosophy: is the “citizenship rent” morally acceptable? Does global equality of opportunity matter?
- Global and national politics: Migration and national welfare state
- (will address both at the end)

Different countries and income classes in global income distribution in 2008



From calcu08.dta

Different countries and income classes in global income distribution in 2011

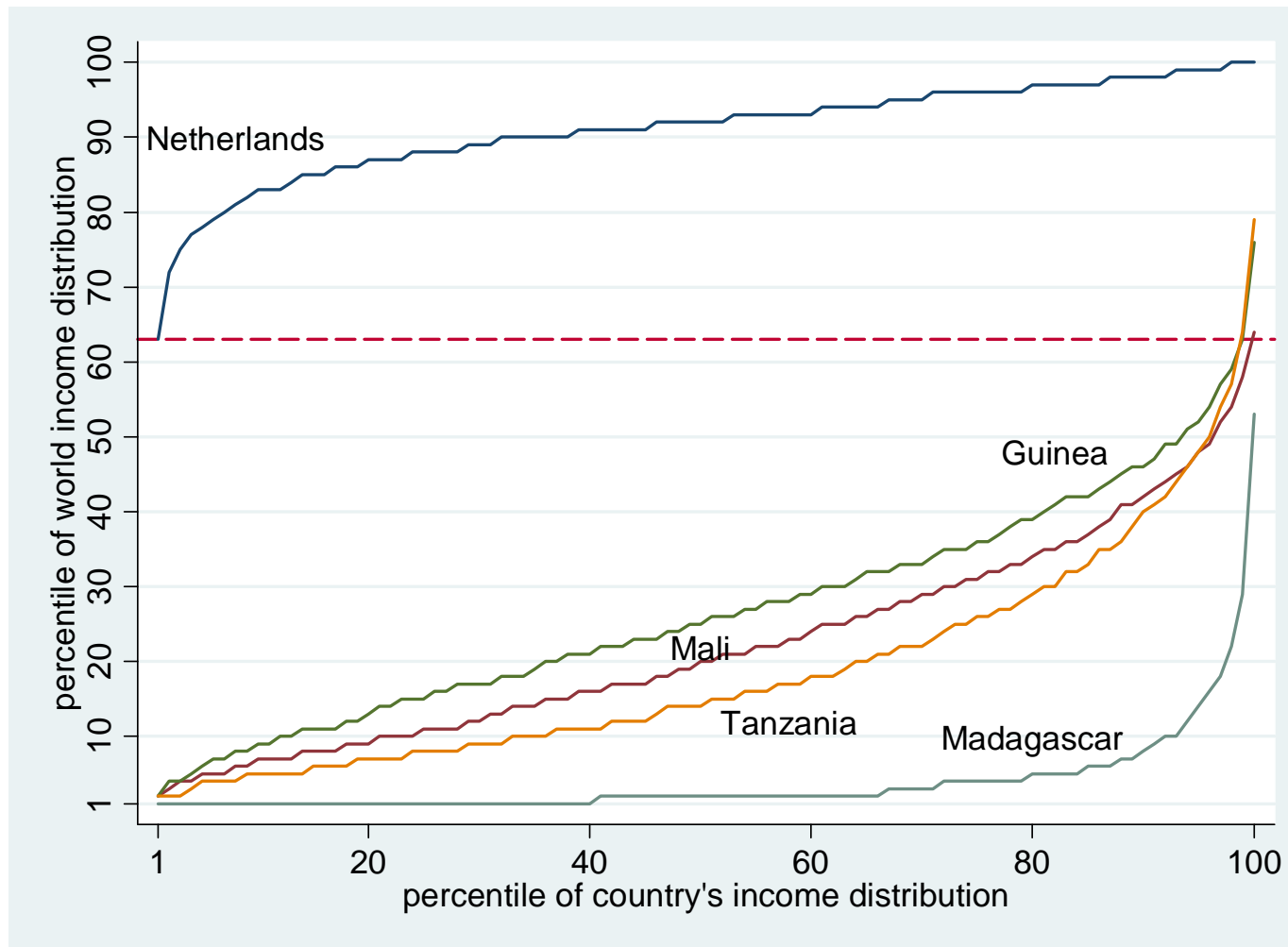


India with 2011 income data

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Final11.dta using michele_graph.do but with india consumption replaced by india income

Why international aid is unlikely to involve regressive transfers?



2. Technical issues in the measurement of global inequality

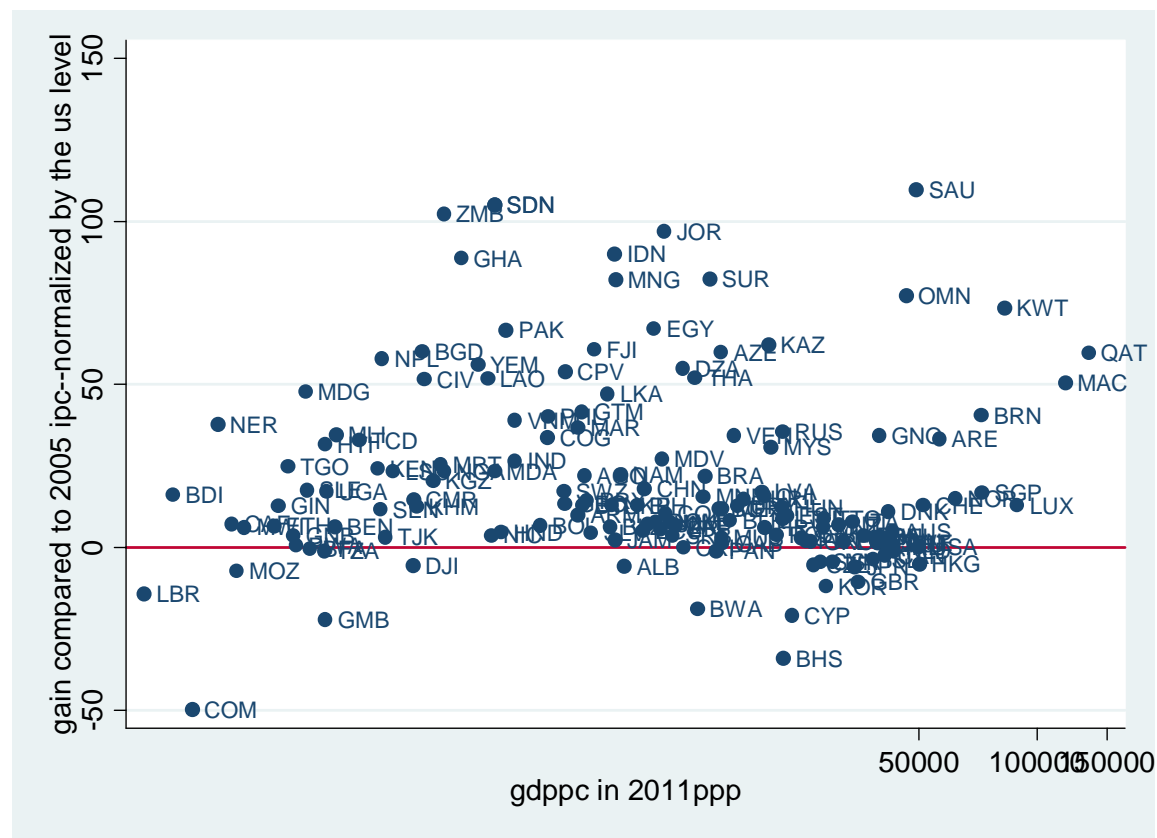
Three important technical issues in the measurement of global inequality

- The ever-changing PPPs in particular for populous countries like China and India
- The increasing discrepancy between GDP per capita and HS means, or more importantly consumption per capita and HS means
- Inadequate coverage of top 1% (related also to the previous point)

The issue of PPPs

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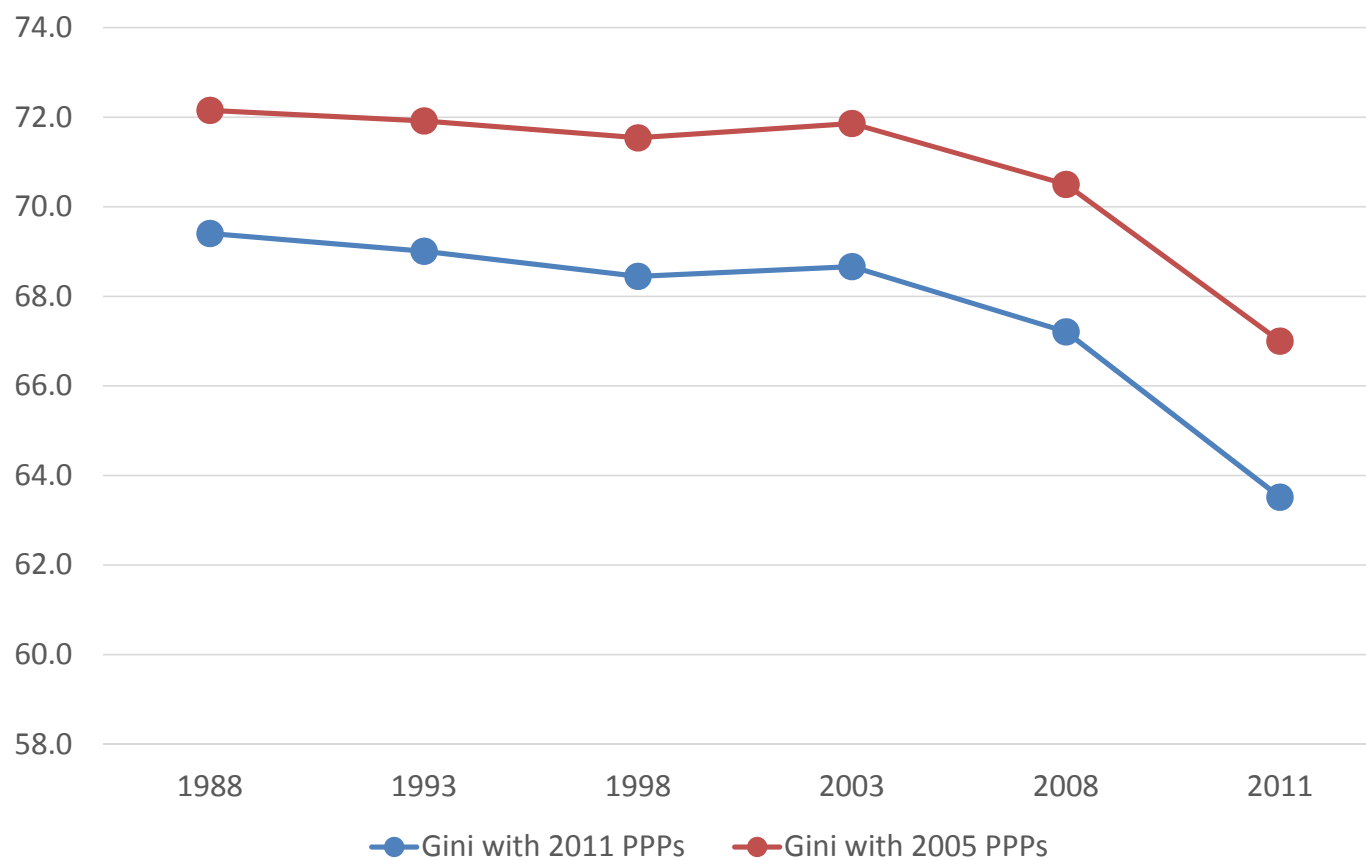
The effect of the new PPPs on countries' GDP per capita



The effect of new PPPs

Country	GDP per capita increase (in %)	GDP per capita increase population-weighted (in %)
Indonesia	90	---
Pakistan	66	---
Russia	35	---
India	26	---
China	17	---
Africa	23	32
Asia	48	33
Latin America	13	17
Eastern Europe	16	24
WENAO	3	2

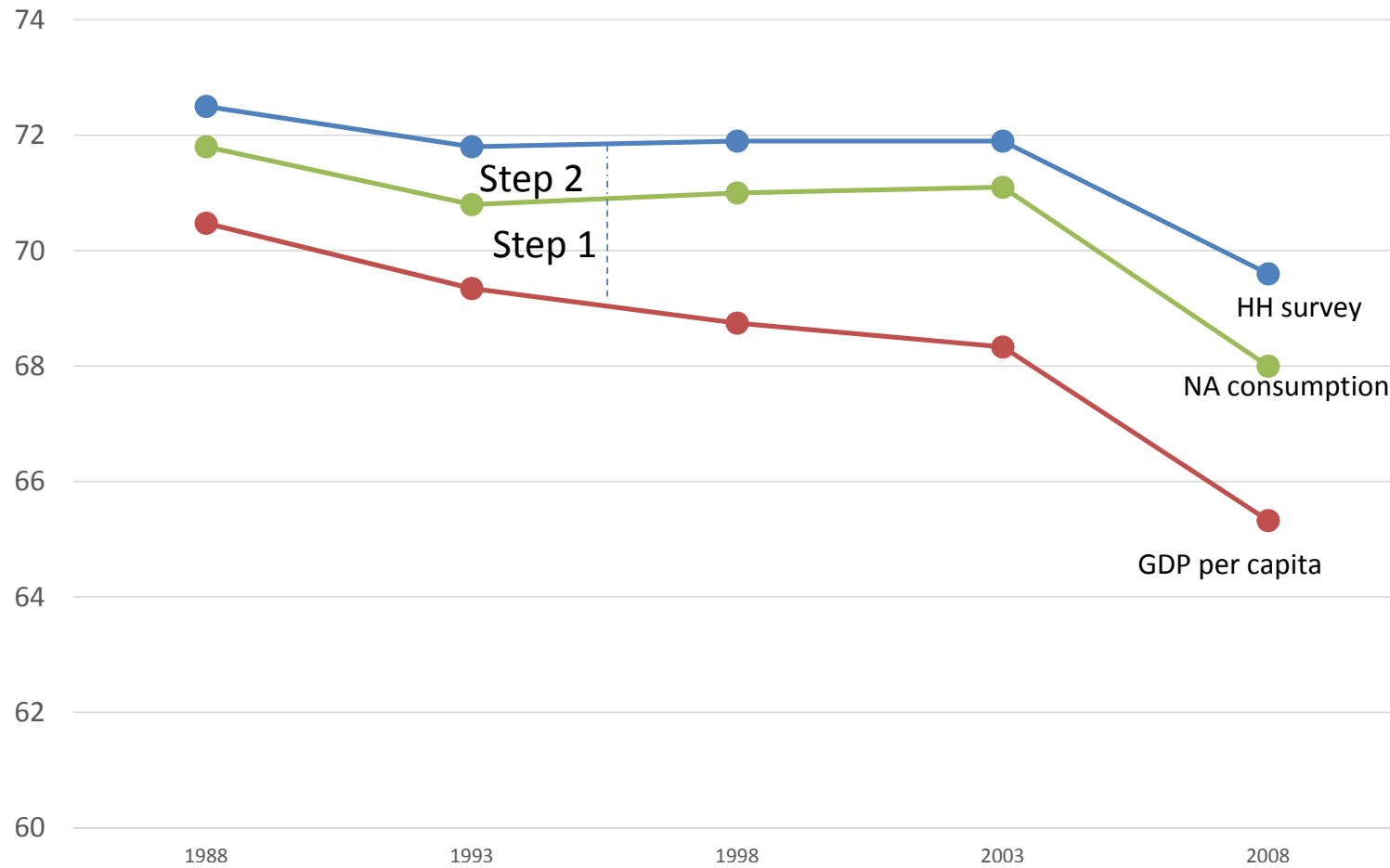
Use of 2011 PPPs reduces global inequality by about 3 Gini points but leaves the trends the same



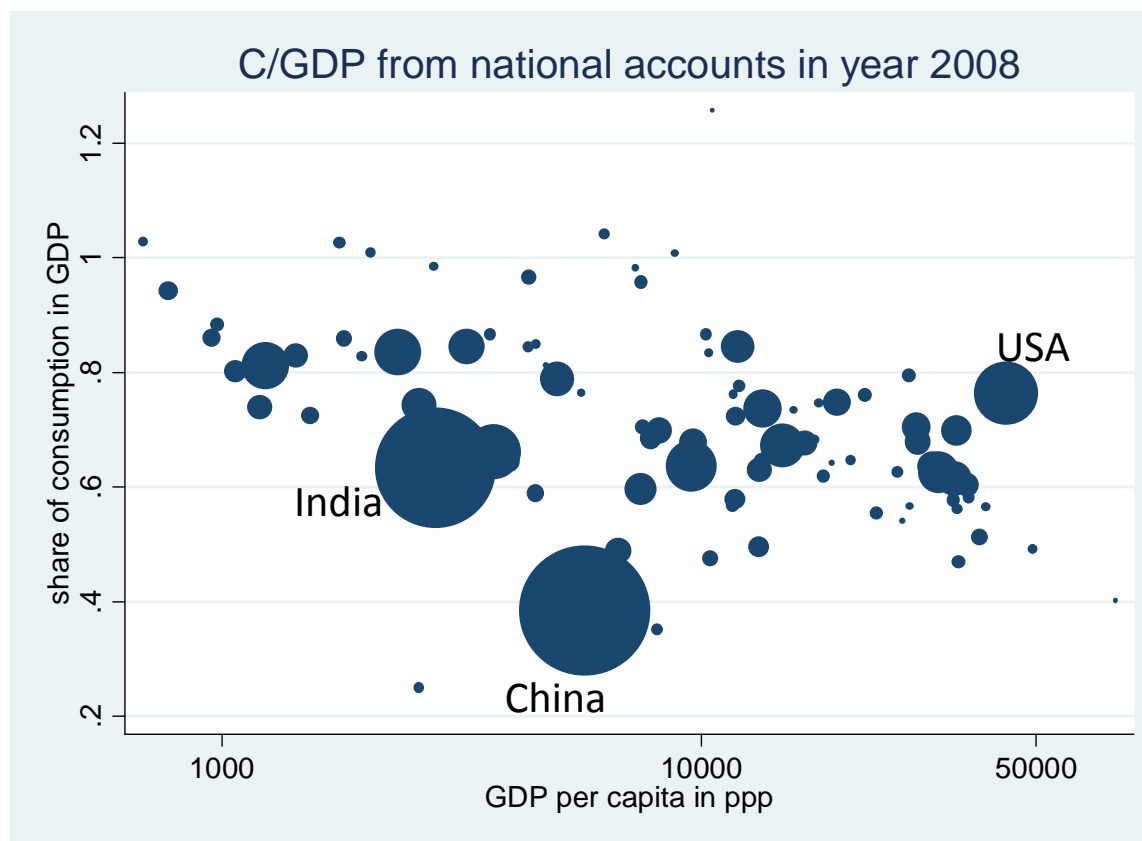
The gap between national accounts and household surveys

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Global Gini with different definitions of income



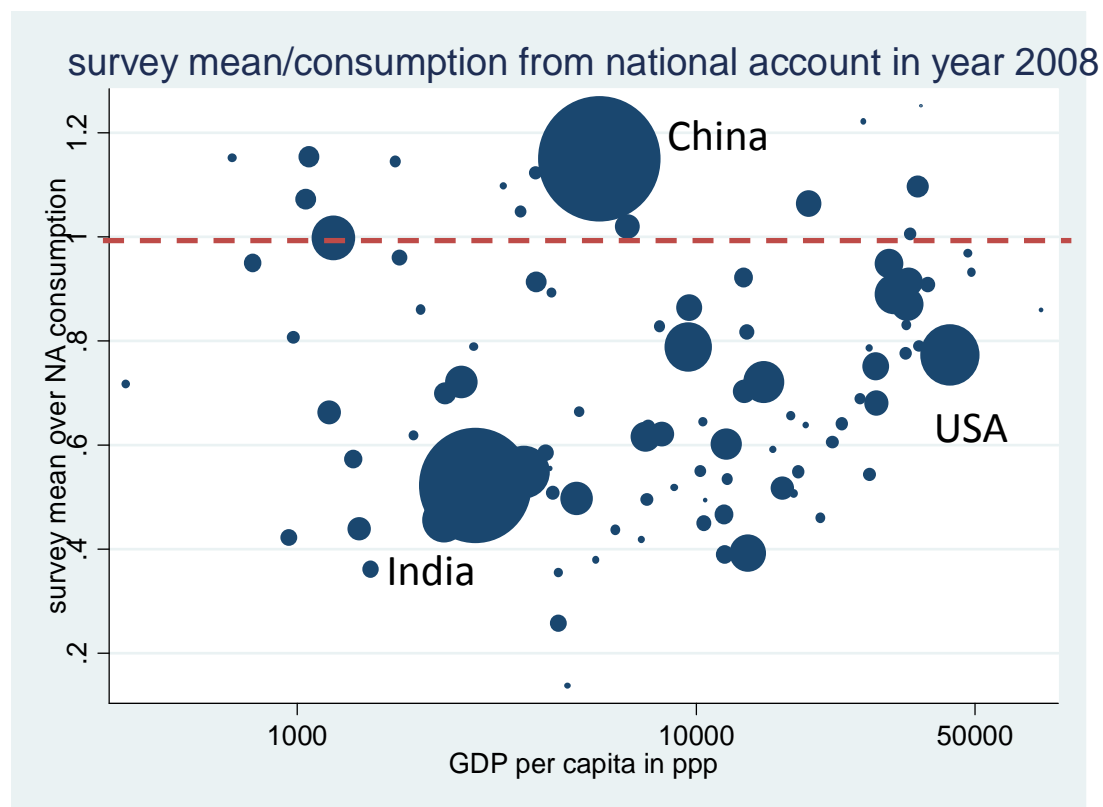
Step 1 driven by low consumption shares in China and India (although on an unweighted base C/GDP decreases with GDP)



```
twoway scatter cons_gdp gdpppp if group==1 & cons_gdp<1.4 [w=totpop], xscale(log) xtitle(GDP per capita in ppp) xlabel(1000 10000 50000)
yttitle(share of consumption in GDP) title(C/GDP from national accounts in year 2008)
using final08.dta
```

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Step 2. No clear (weighted) relationship between survey capture and NA consumption



```
twoway scatter scale2 gdpppp if group==1 & scale2<1.5 [w=totpop], xscale(log) xtitle(GDP per capita in ppp) xlabel(1000 10000 50000) ytitle(survey mean over NA consumption) title(survey mean/consumption from national account in year 2008)
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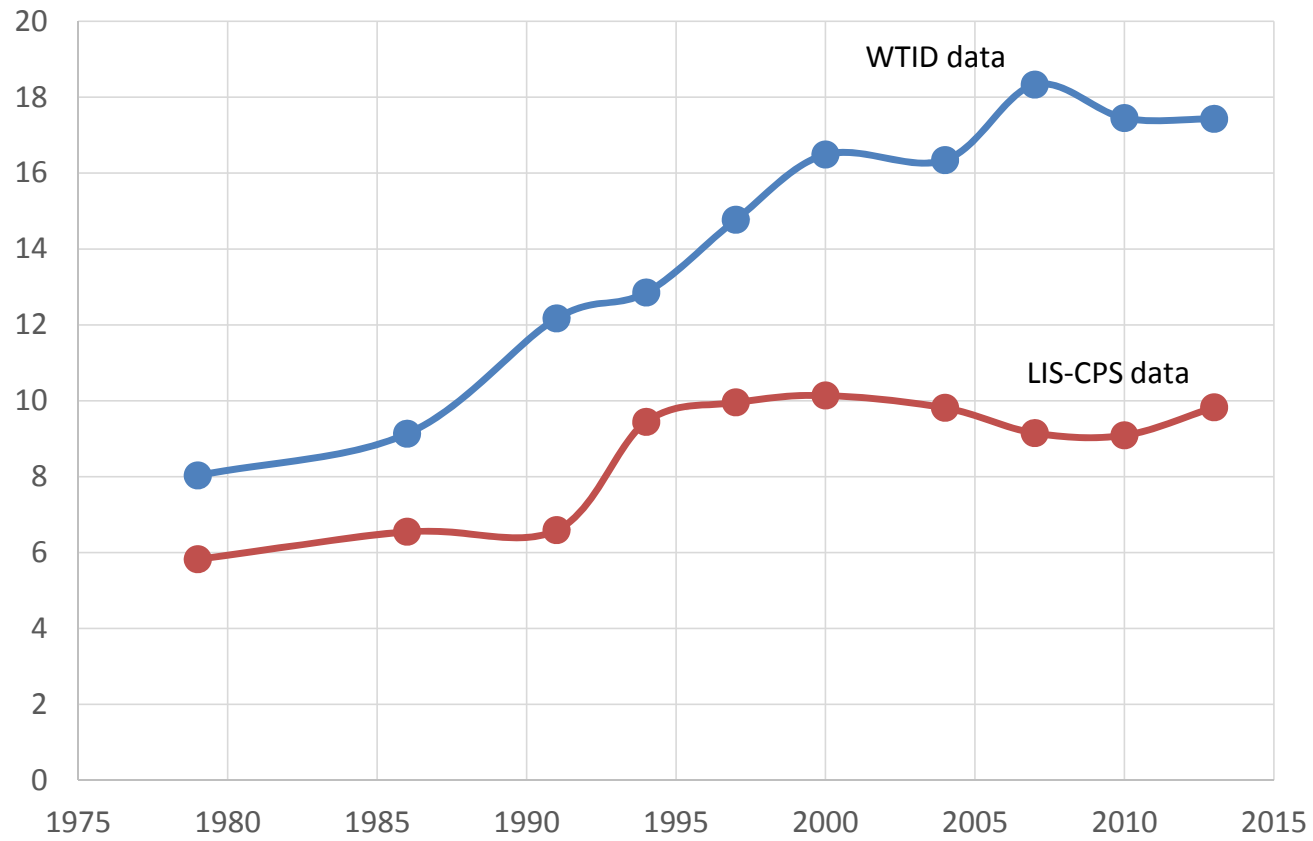
The issue of top underestimation

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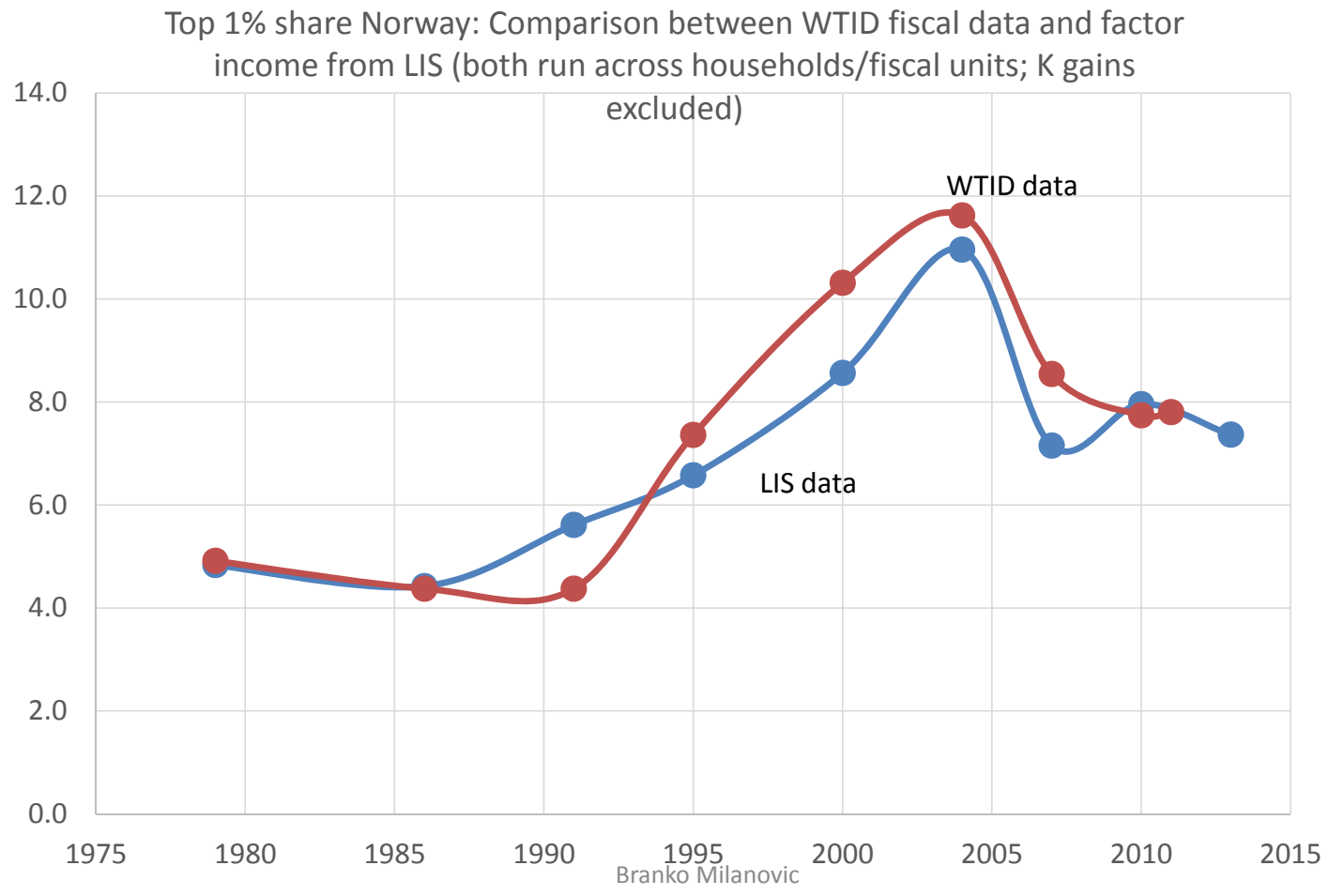
Rising NAC/HS gap and top underestimation

- If these two problems are really just one & the same problem.
- Assign the entire positive (NA consumption – HS mean) gap to national top deciles
- Use Pareto interpolation to “elongate” the distribution
- No *a priori* guarantee that global Gini will increase

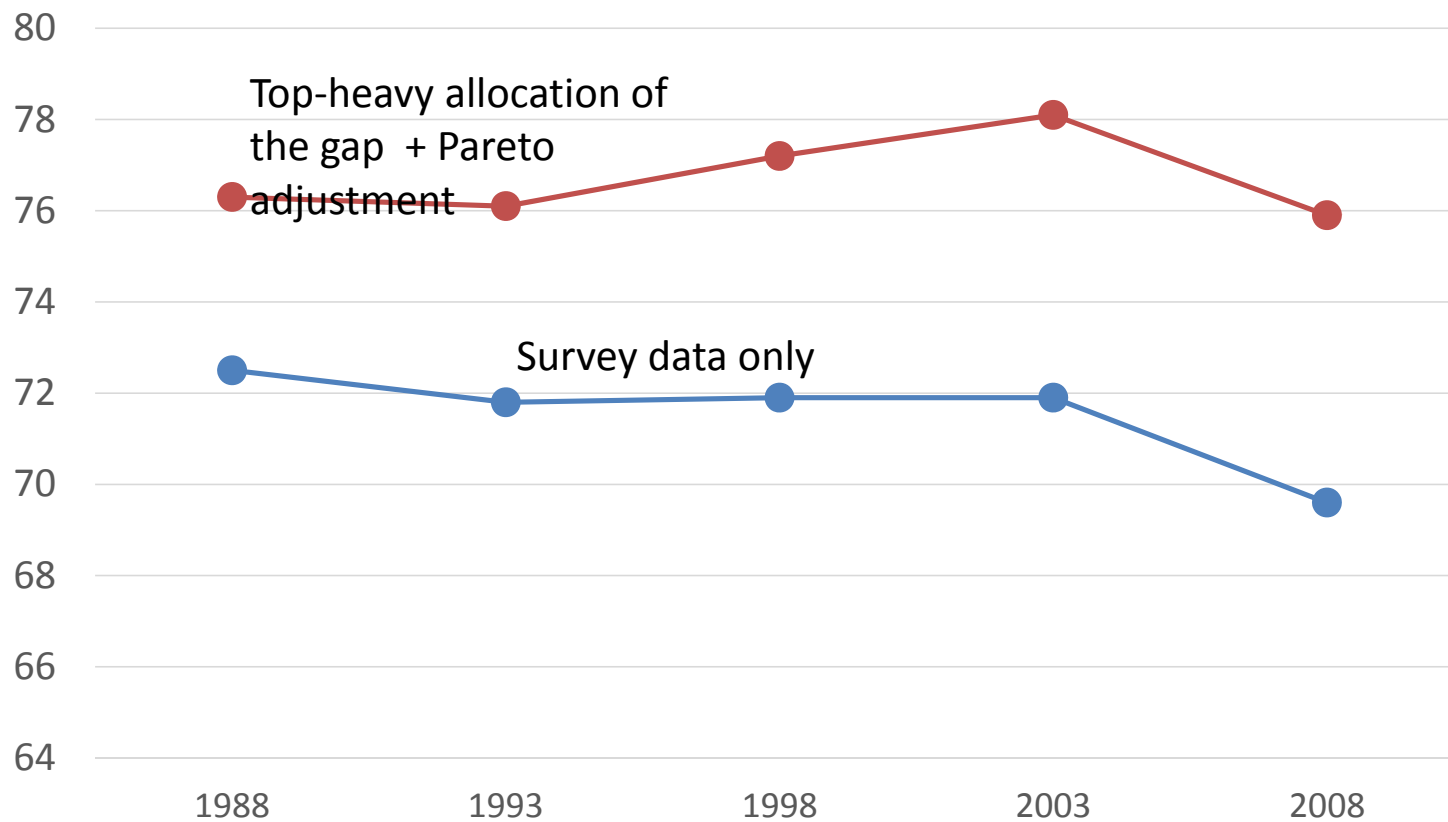
Top 1% share in US: Comparison between WTID fiscal data and factor income from LIS (both run across households/fiscal units; K gains excluded)



But the rising gap between fiscal and HS income is not universal



With full adjustment (allocation to the top 10% + Pareto) Gini decline almost vanishes



3. How has the world changed between the fall of the Berlin Wall and the Great Recession

[based on joint work with Christoph Lakner]

Number of surveys

	1988	1993	1998	2002	2005	2008	2011
Africa	14	30	24	29	32	23	30
Asia	19	26	28	26	23	27	22
E.Europe	27	22	27	25	27	27	24
LAC	19	20	22	21	18	18	18
WENAO	23	23	21	21	22	23	21
World	102	121	122	122	122	118	115

Population coverage

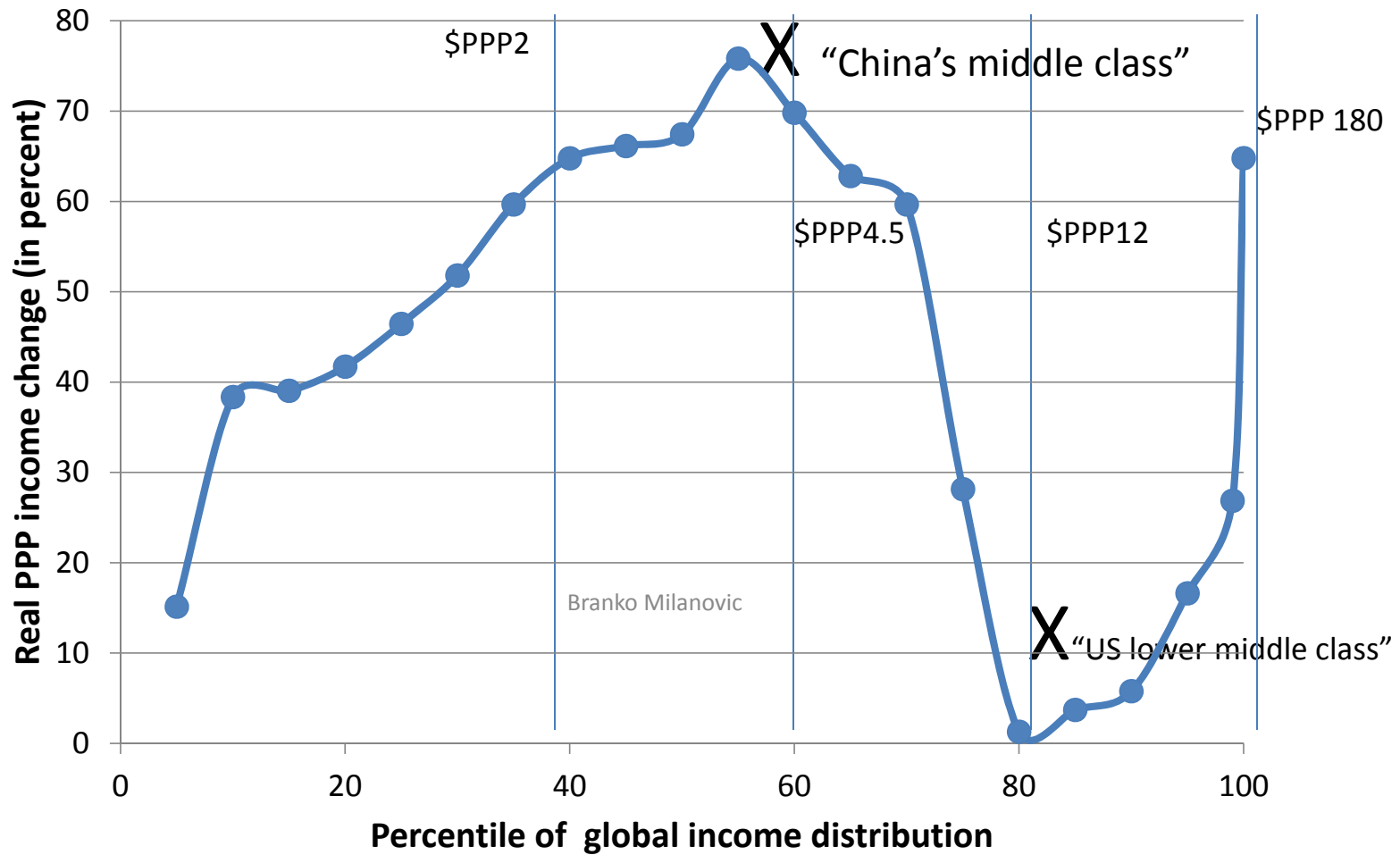
	1988	1993	1998	2002	2005	2008	2011
Africa	48	76	67	77	78	78	70
Asia	93	95	94	96	94	98	96
E.Europe	99	95	100	97	93	92	87
LAC	87	92	93	96	96	97	97
WENAO	92	95	97	99	99	97	96
World	87	92	92	94	93	94	92

Non-triviality of the omitted countries

GDI (US dollar) coverage

	1988	1993	1998	2002	2005	2008	2011
Africa	49	85	71	71	70	71	63
Asia	94	93	96	95	90	93	83
E. Europe	99	96	100	99	99	98	94
LAC	90	93	95	95	98	98	94
WENAO	99	96	96	100	100	97	95
World	96	95	96	98	97	95	90

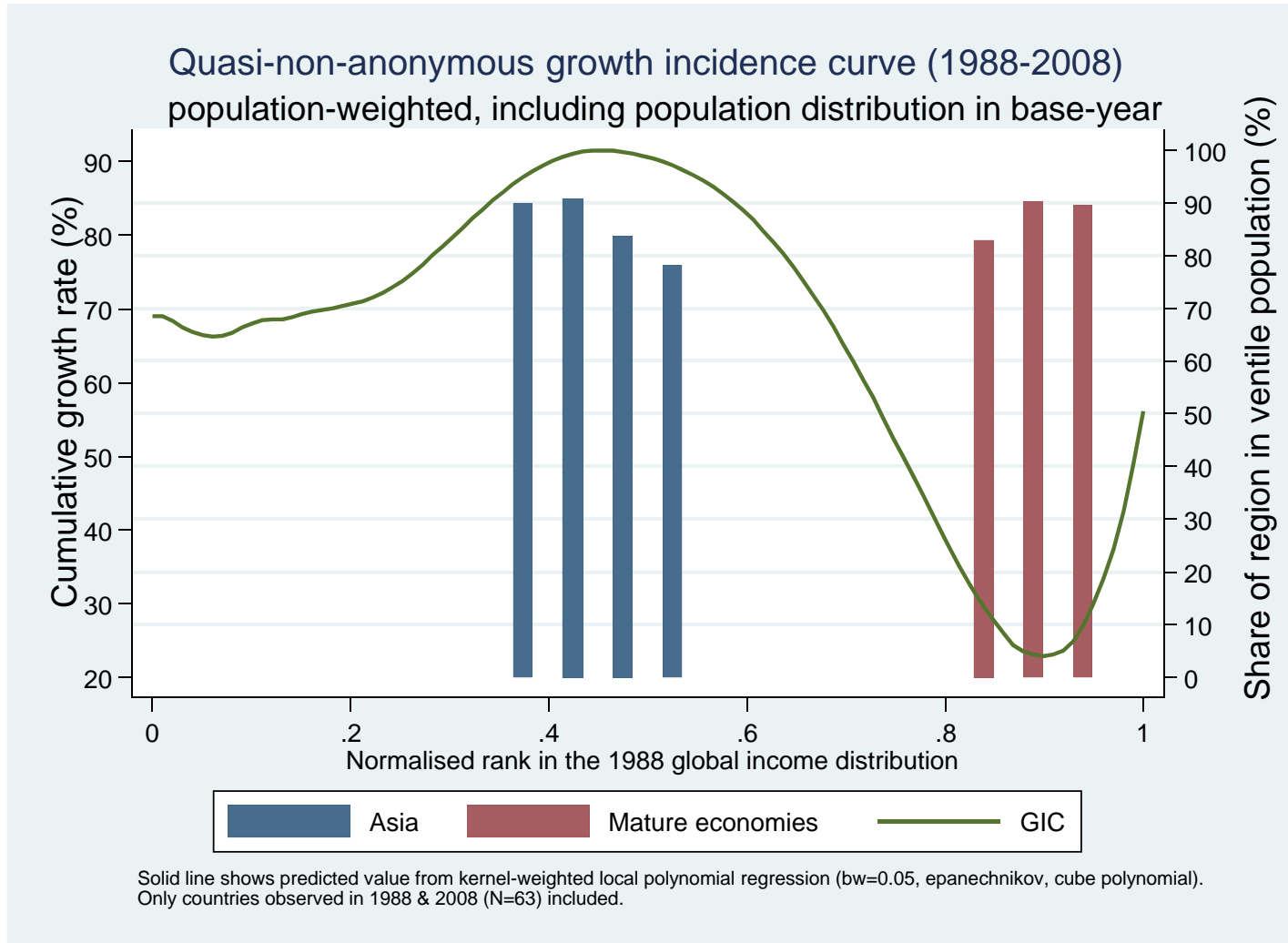
Real income growth at various percentiles of global income distribution, 1988-2008 (in 2005 PPPs)



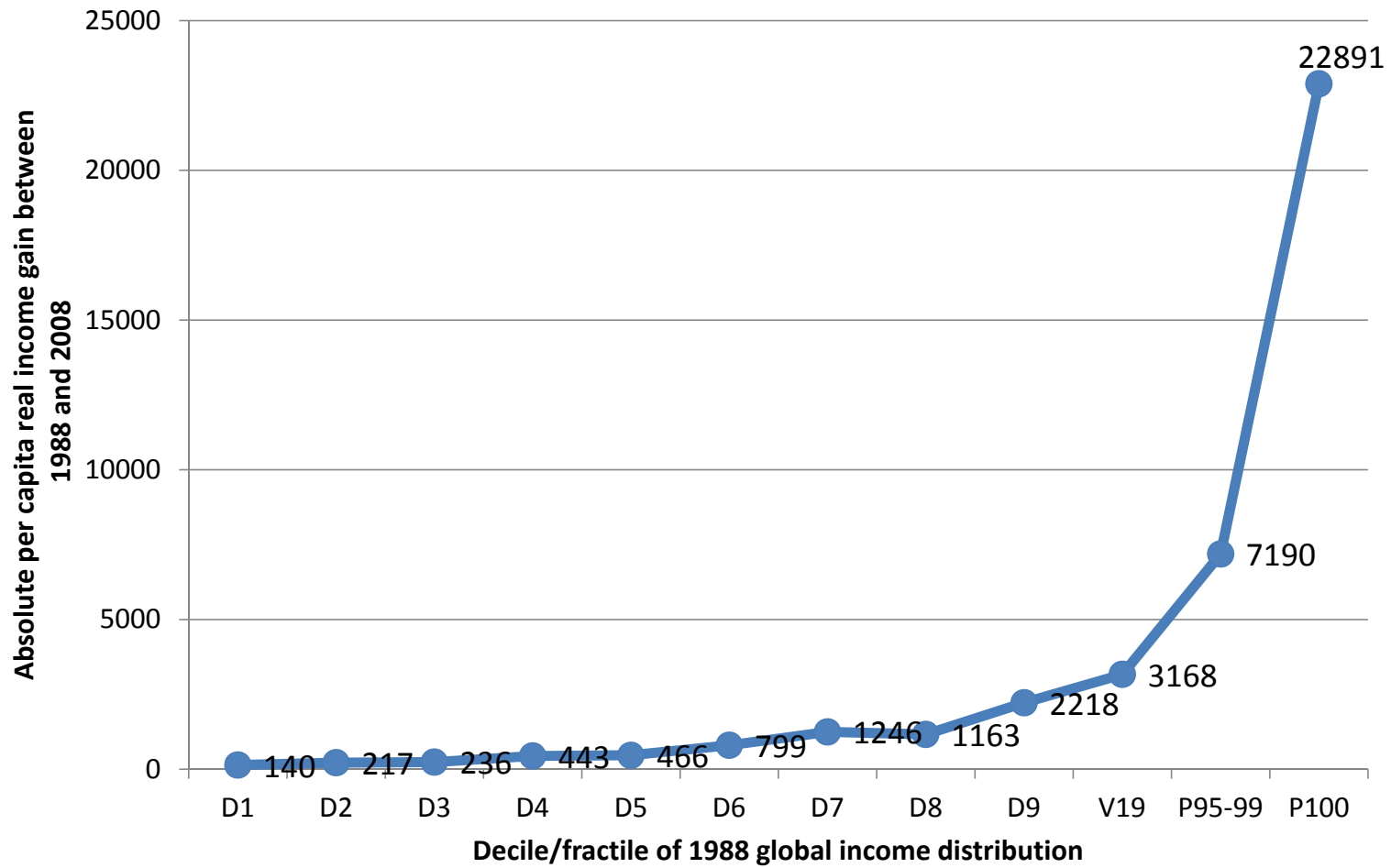
From twenty_years\final\summary_data

Estimated at mean-over-mean

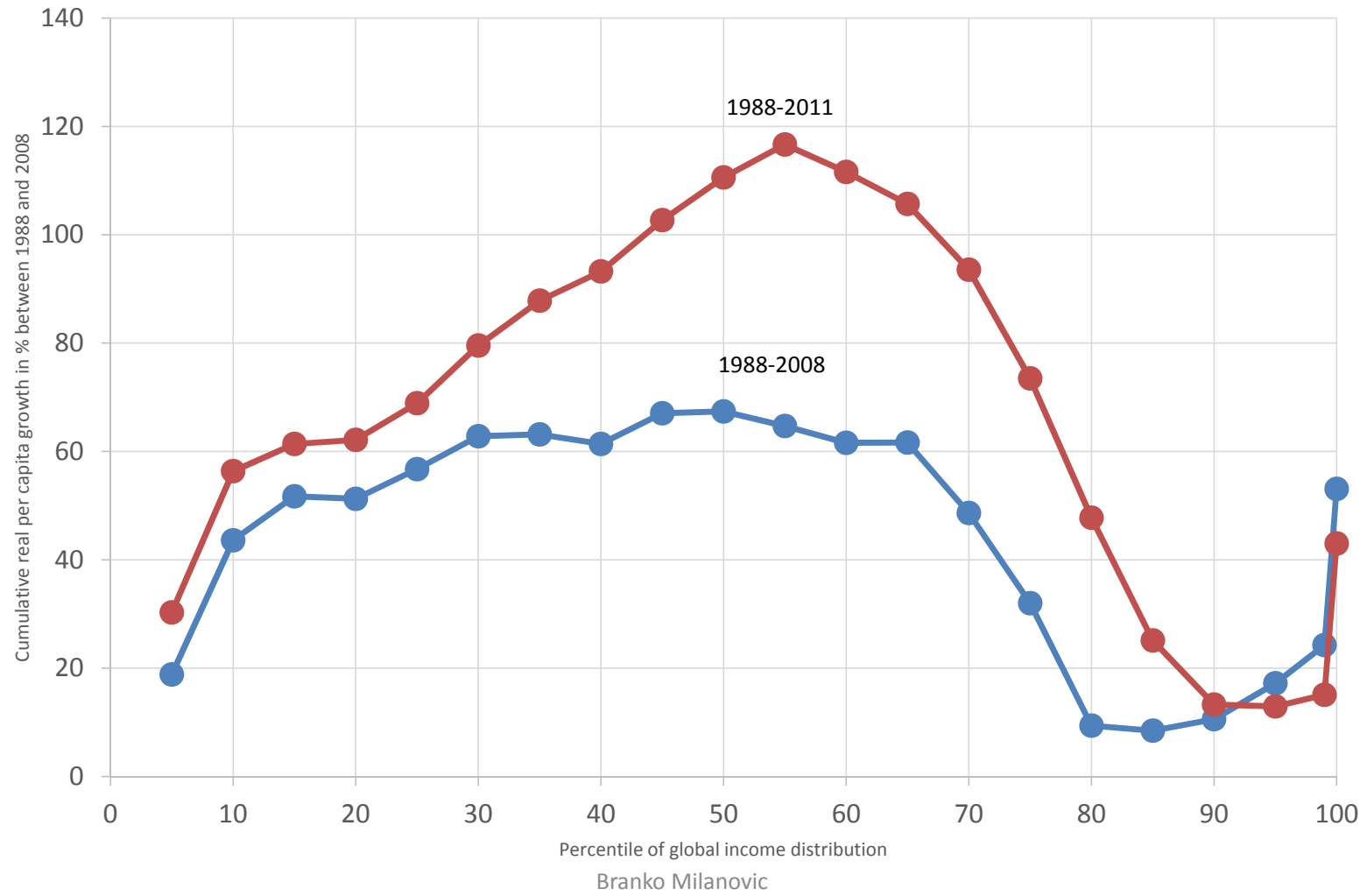
Parts of the distribution that gained the most are dominantly from Asia, parts that stagnated are mostly from mature economies



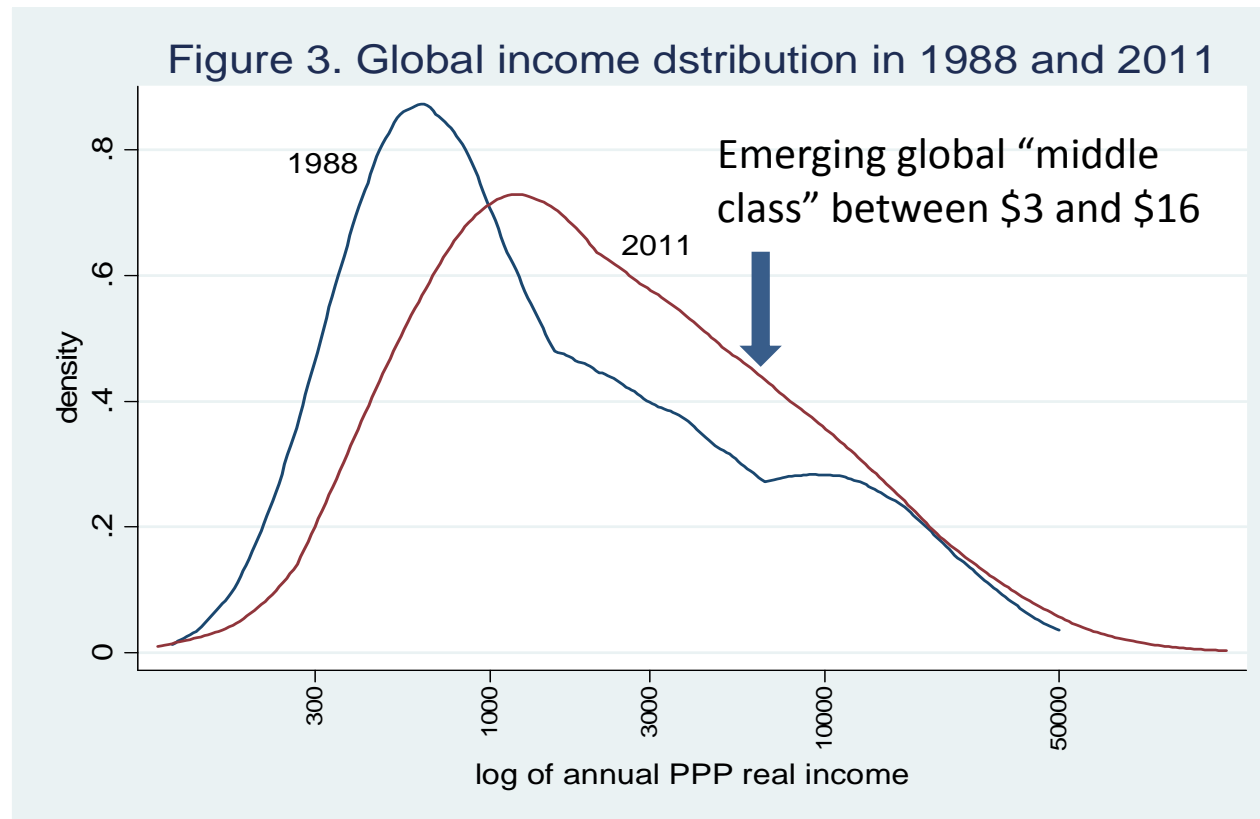
Quasi non-anonymous growth between 1988 and 2008: real absolute per capita gains at different fractiles of the **1988** distribution



Real income growth over 1988-2008 and 1988-2011 (based on 2011 PPPs)



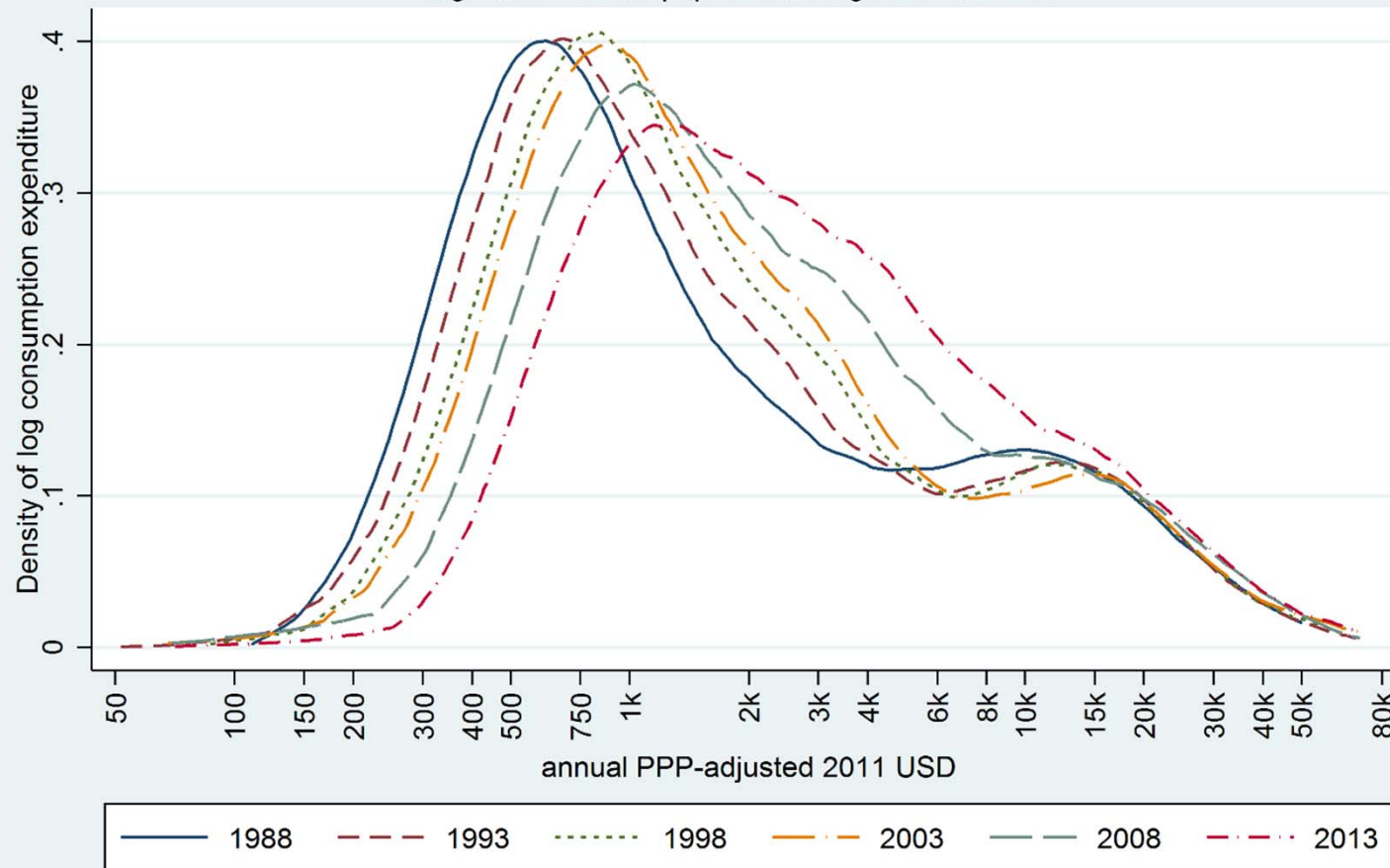
Global income distributions in 1988 and 2011



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(kdensity loginc_11_11 [w=popu] if loginc_11_11>2 & bin_year==2011, bwidth(0.2)) , legend(off) xtitle(log of annual PPP real income) ytitle(density) text(0.78 2.5
"1988") text(0.65 3.5 "2011") xlabel(2.477"300" 3"1000" 3.477"3000" 4"10000" 4.699"50000", lsize(small) angle(90))
Using Branko\Income_inequality\final11\combine88_08_11_new.dta
    
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The global distribution of consumption expenditure over time
logarithmic scale, population-weighted, 2011 PPP



From Christoph Lakner

4. Political implications

The contradiction of inequality changes during Globalization II

- Most countries displayed an upward sloping GIC (US, China, India urban, Indonesia...)
- Perception that the rich are doing better than anybody else (true)
- But growth rates of countries are uneven; those that grew the fastest were in the lower middle of global income distribution, and they were also most populous
- This led to the “elephant-shaped” global GIC and decreasing global inequality

The issues

- Are growth (1) along the entire Chinese income distribution and (2) stagnation around the median in the rich world as well as stagnation across most of income distribution in E. Europe and LAC, related?
- In other words, is the hump in middle related to the dip around the 70-80th percentile?
- Marching of China and India through the ranks reduces global inequality and the importance of the between-country component in global inequality
- But it might “cause” increases in within-national inequalities (thus offsetting global inequality decline)
- Can democracy survive if rich countries’ middle classes are hollowed out?

Back to Mandeville...

- Can something that is bad nationally (increased inequality) be good globally (decreased inequality) ?
- Can national vices produce global virtue?

Political implications

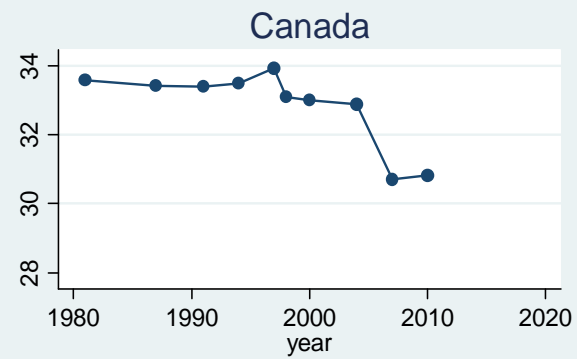
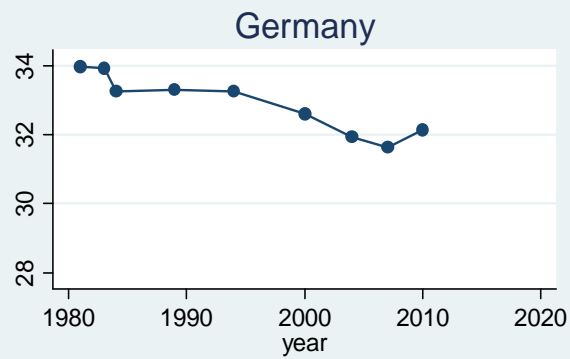
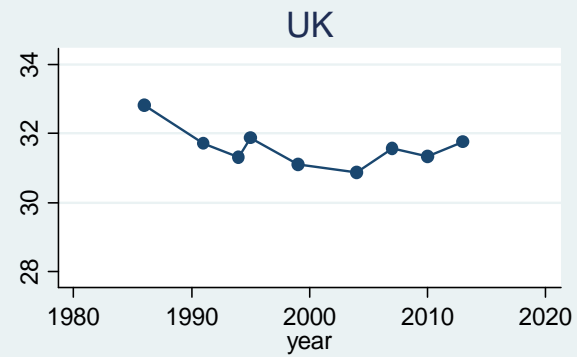
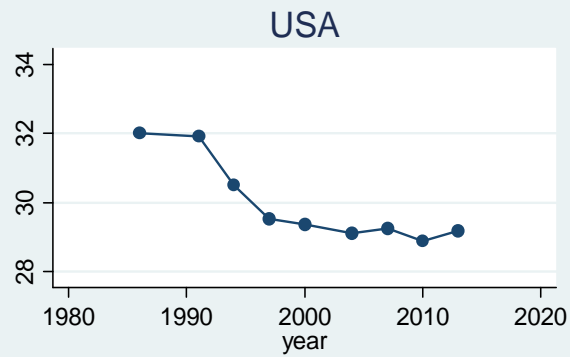
- Possible crowding out of national middle classes, and the creation of a global one
- But the middle class is presumably a force for stability when there is a political community. There is no political community at the global level. What does *global* middle class mean?
- Would global middle class create a global polity?
- Or, global plutocracy: in the longer-term, reversal to the pre World War I situation

Are we at the end of capitalism's long “el periodo especial” or going upward the second modern era Kuznets curve?

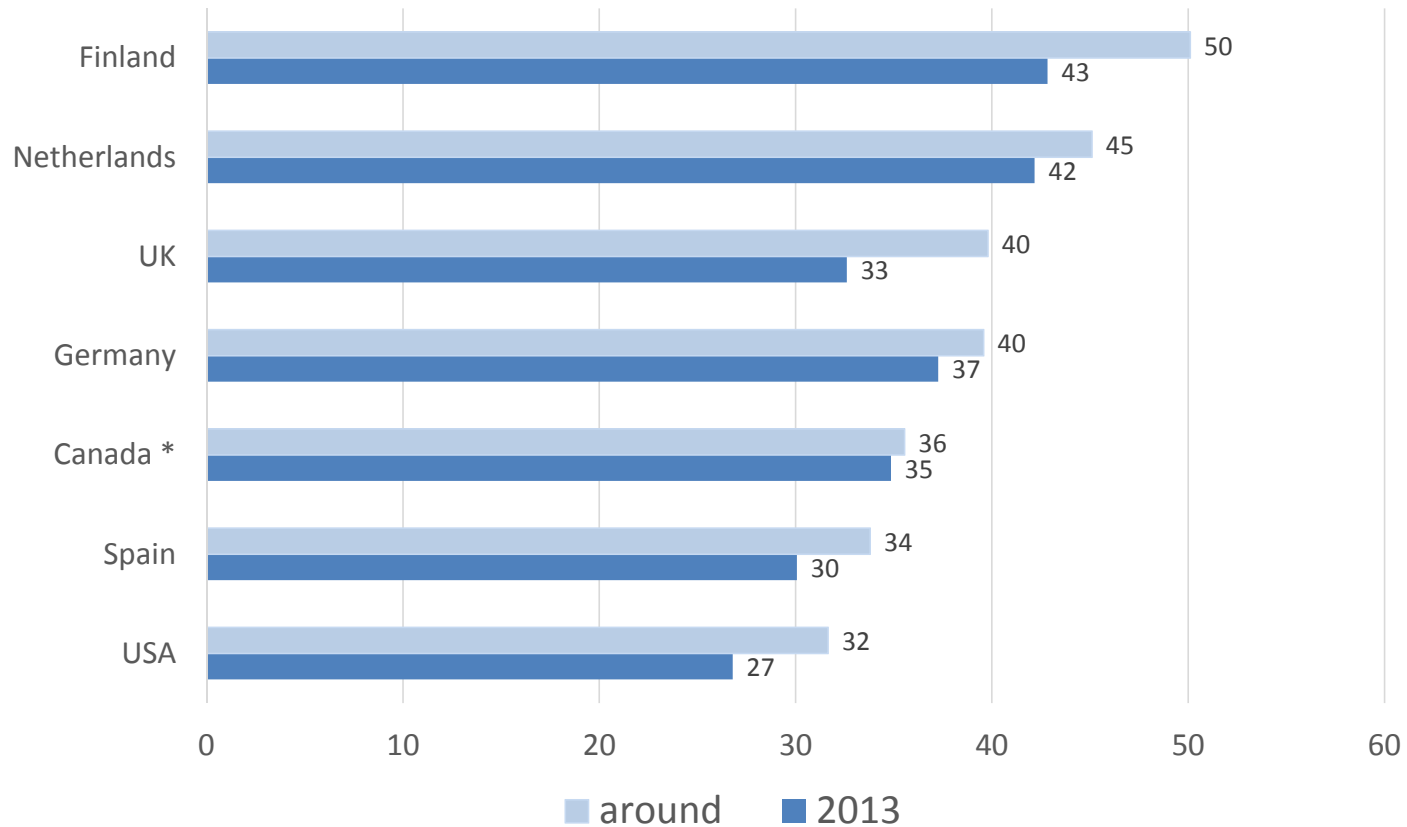
- Three challengers to global capitalism were beaten off in the 20th century: depression (by reinventing gov't), war (by marshalling resources), Communism (through Welfare State)
- Neither of these threats is any longer present; so is this the reason capitalism is becoming more unequal?
- Or is the period after 1980, the second modern era Kuznets curve driven by the technological revolution and globalization?

Focus on point B of the
“elephant graph”
(income stagnation and erosion
of the middle class in advanced
economies)

Income share of the middle four deciles 1980-2013 in percent



Percentage of population considered middle class in early 1980s and 2013



The middle class defined as population with income between +/-25% of national median income (all in per capita basis; disposable income; LIS data)

US real median after-tax household per capita income 1979-2013



5. How to think of within-national inequalities: Introducing the Kuznets waves

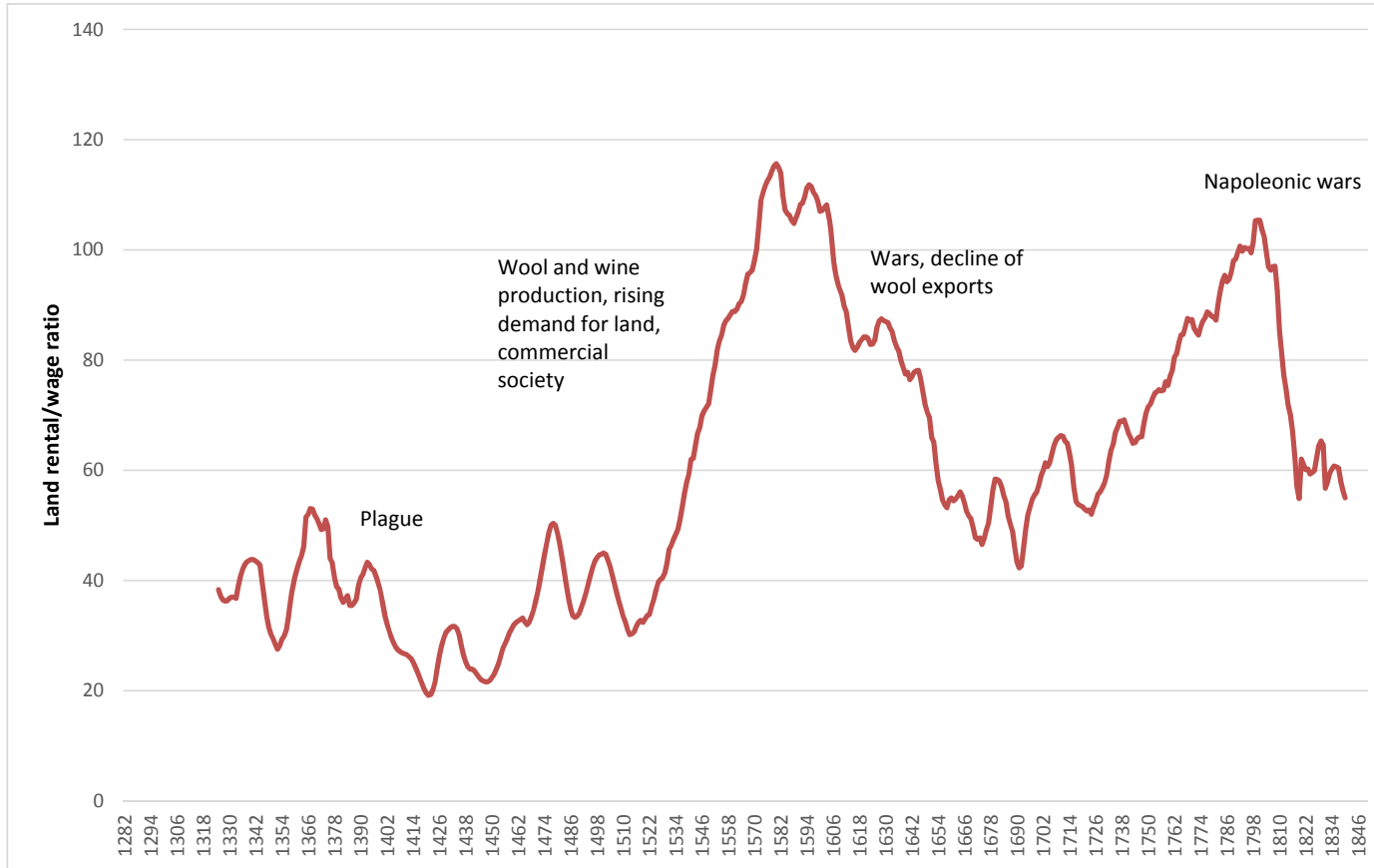
Kuznets waves defined

- Kuznets saw just one curve. We now know there may be many more.
- Distinguish the waves in pre-industrial and modern societies (those with sustained increase in mean income)
- Kuznets waves in pre-industrial societies are visible when plotted against time only (because mean income is stagnant)
- Kuznets cycles in industrial societies are visible when plotted against income per capita=> proxy for structural changes
- Inequality waves are too complex for formal modelling => need to use inductive reasoning and analytic narrative
- The waves in modern era reflect economic forces of technological innovation and structural transformation. But also wars and policy changes.

Malign and benign forces reducing inequality (downward portion of the Kuznets wave)

	Malign	Benign
Societies with stagnant mean income	Idiosyncratic events: wars (though destruction), epidemics, civil conflict	Cultural and ideological (e.g. Christianity?)
Societies with a rising mean income	Wars (through destruction and higher taxation: <i>War and Welfare</i>), civil conflict	<ul style="list-style-type: none"> •Widespread education (reflecting changing returns) •Social pressure through politics (socialism, trade unions) •Aging (demand for social protection) •Low-skill biased TC •Cultural and ideological (pay norms?)

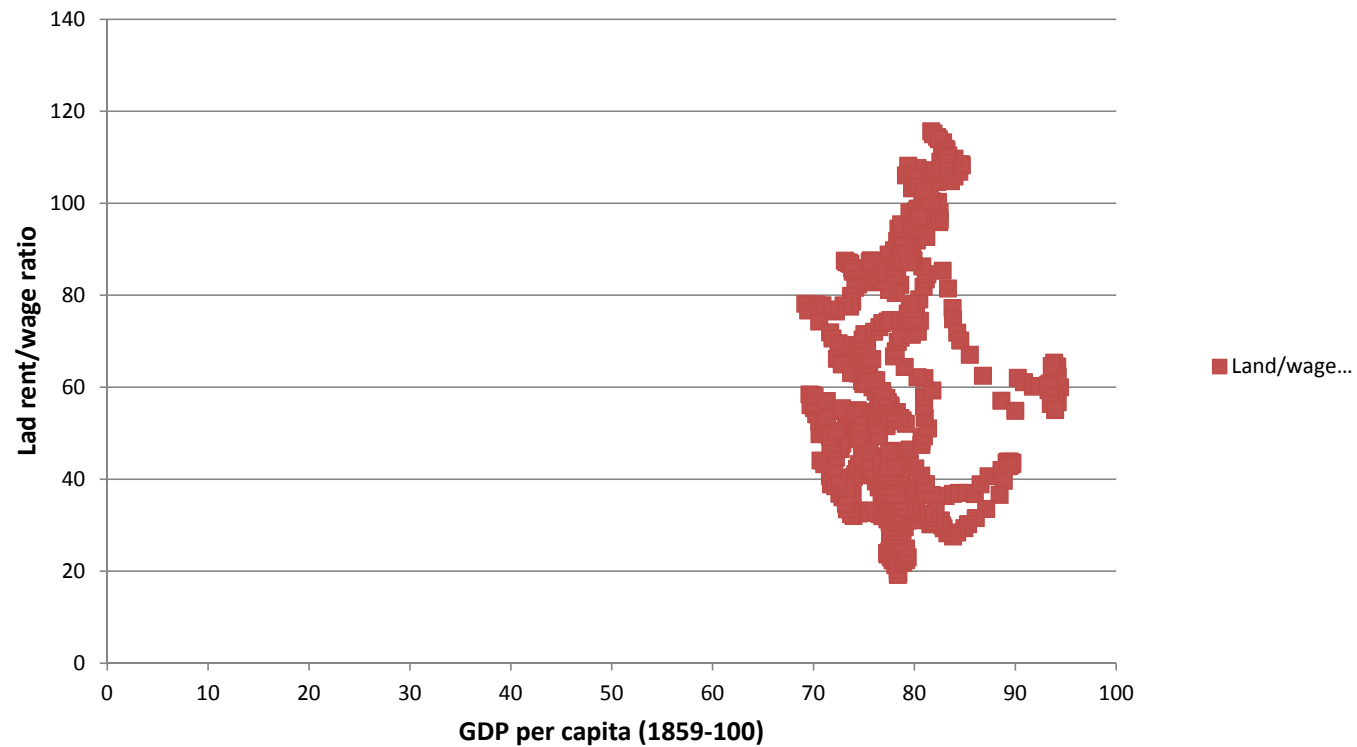
Cyclical nature of the Kuznets curve:
Land rental/wage ratio over the long-term in Spain, 1282-1842



From Prados de la Escosura & Alvarez-Nogal, "The rise and fall of Spain 800-1850"

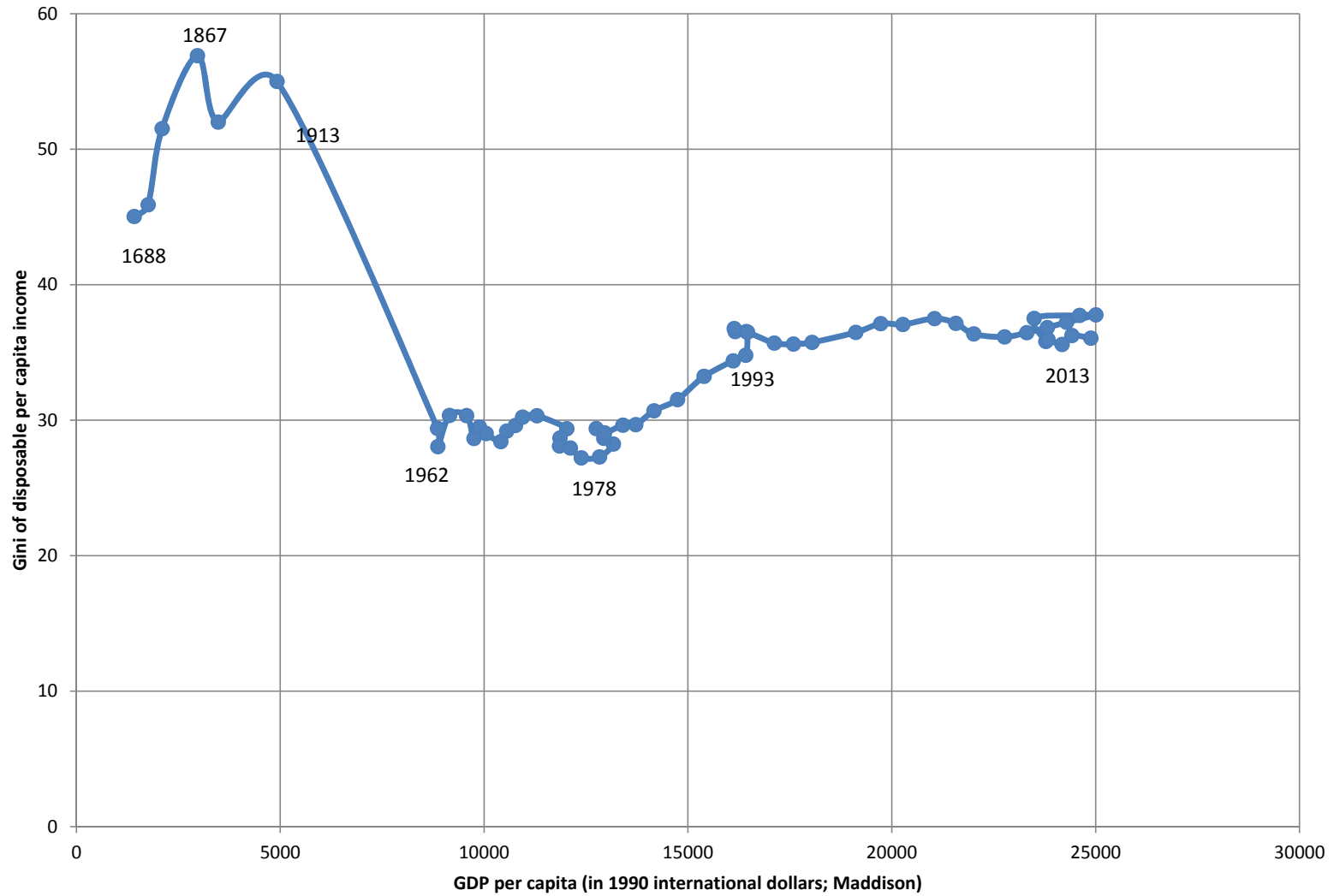
Kuznets curve here? No.

GDP per capita and rent-wage ratio: Spain 1325-1840

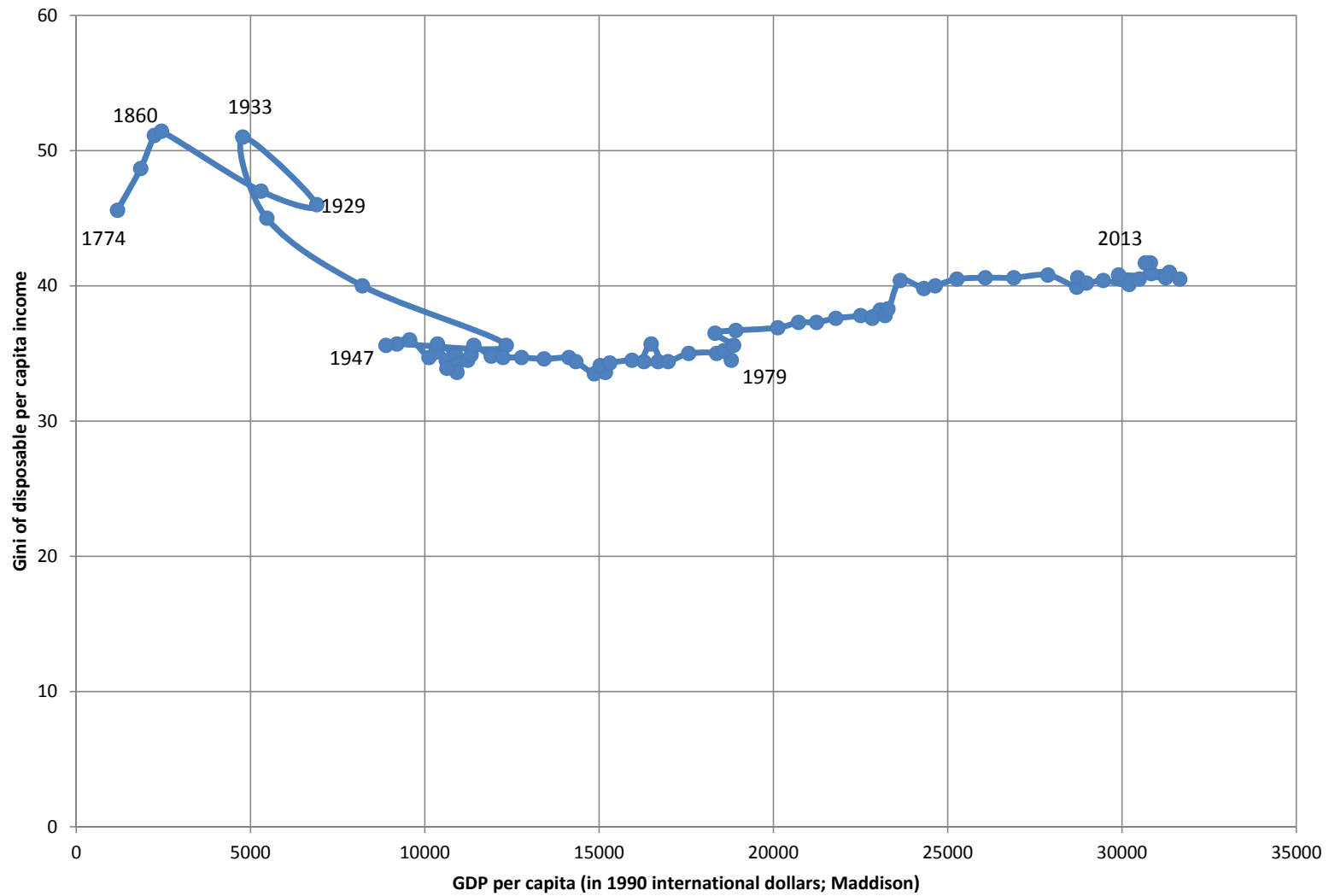


From Prados de la Escosura & Alvarez-Nogal, "The rise and fall of Spain 800-1850"

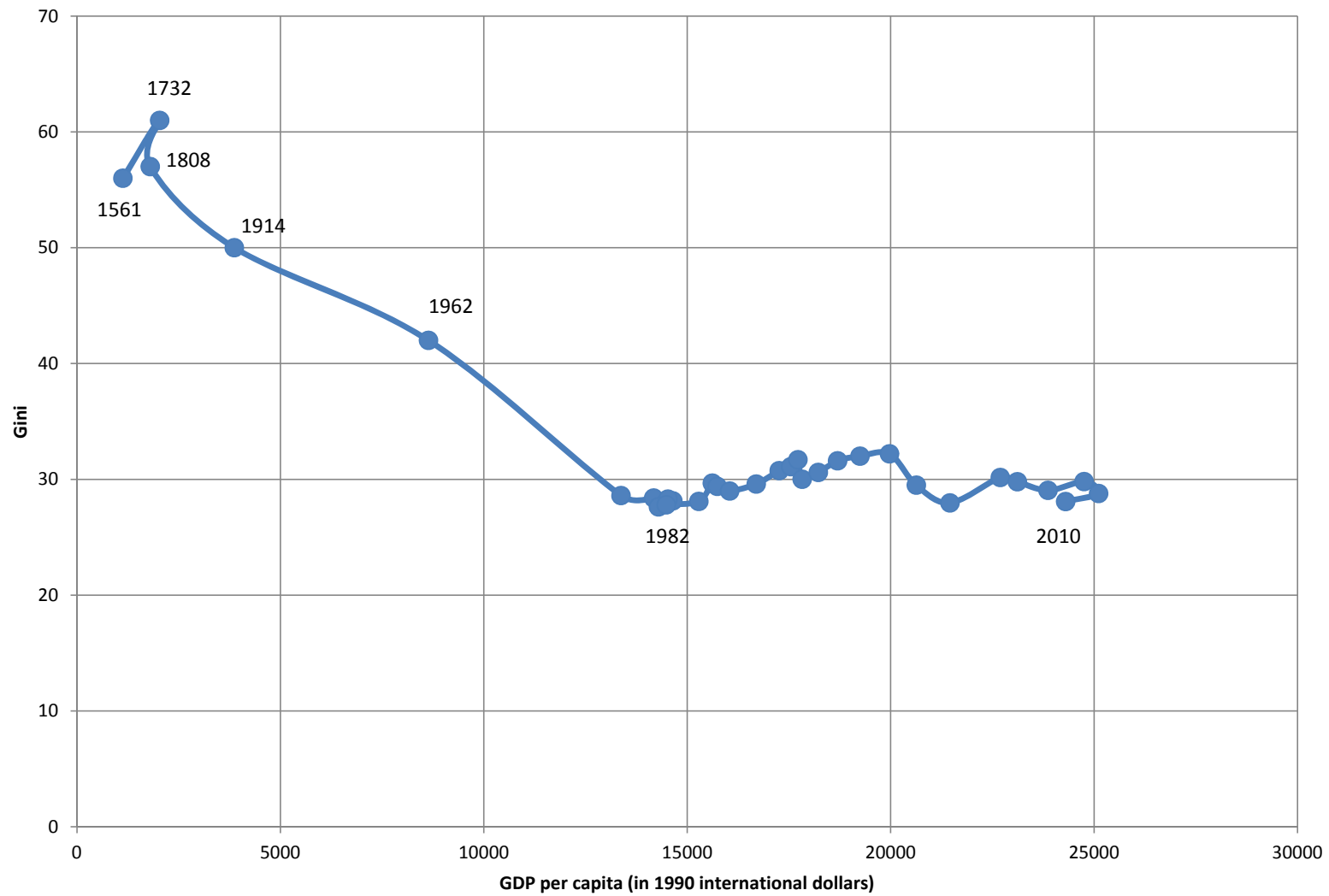
Kuznets relationship for the UK, 1688-2014



Kuznets relationship for the United States, 1774-2013



The Kuznets relationship for the Netherlands, 1561-2010

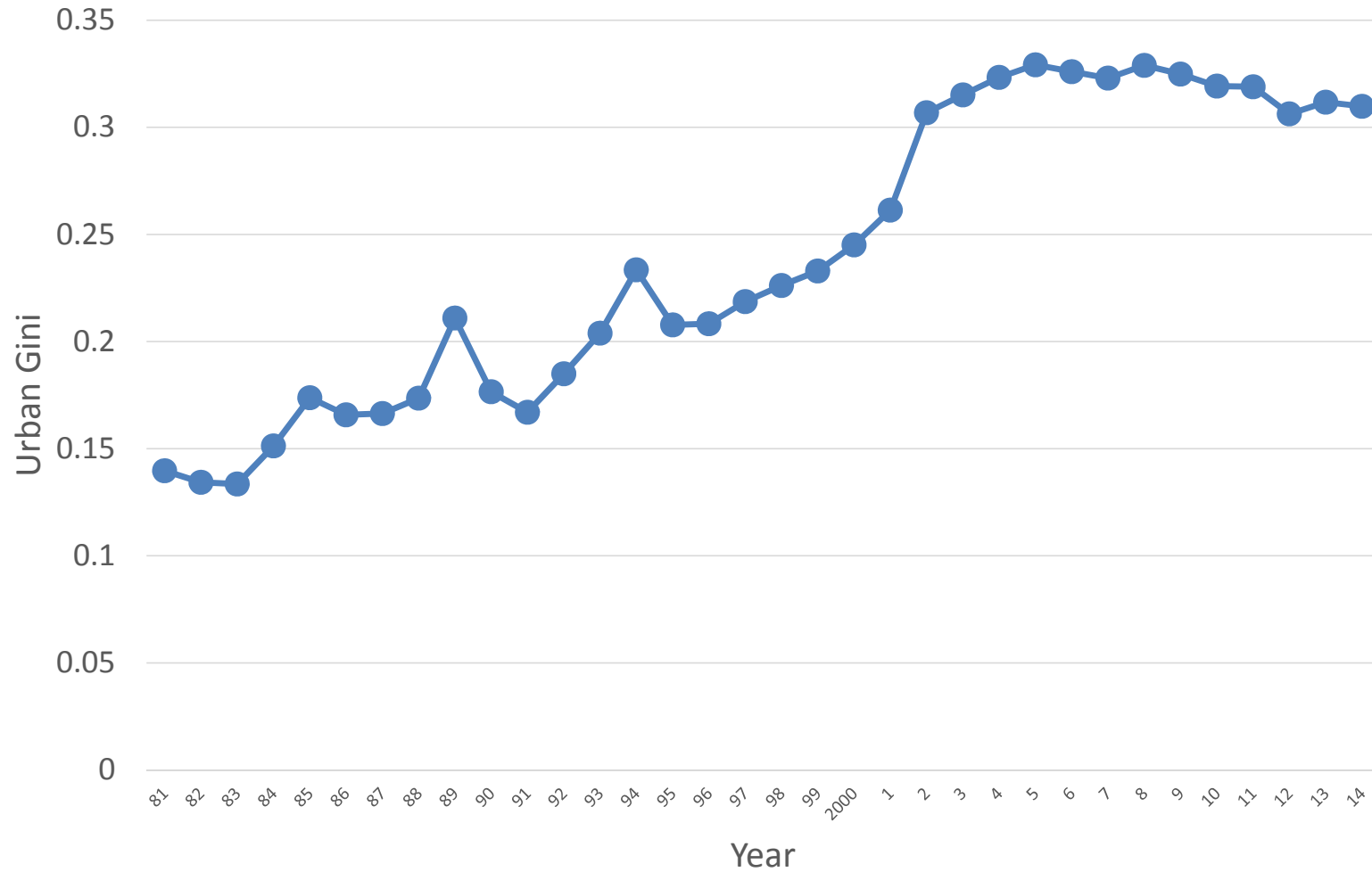


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Downswing of Kuznets first wave and upswing of the second Kuznets wave in advanced economies

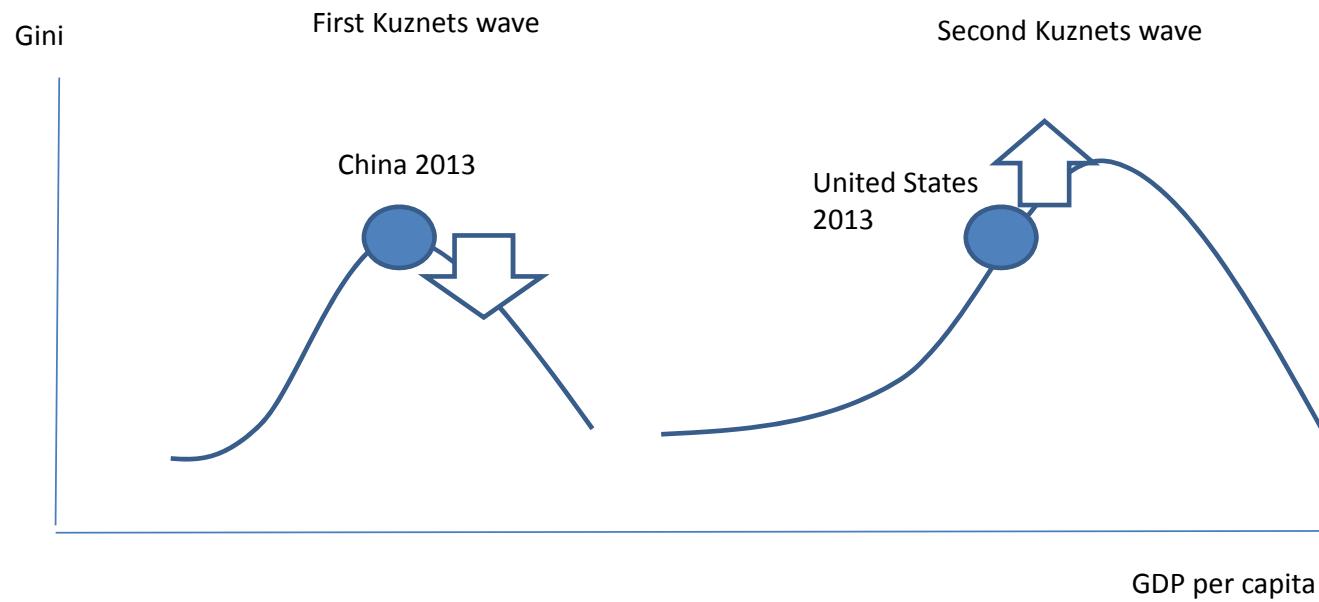
	Level of maximum inequality (peak of Wave 1) Gini points (year)	Level of minimum inequality (trough of Wave 1) (year)	Approximate number of years of downswing of the Kuznets wave	Reduction in inequality (Gini points)	GDP increased (how many times) during the downswing	The second Kuznets wave (increase in Gini points)
United States	51 (1933)	35 (1979)	50	16	4	Strong (+8)
UK	57 (1867)	27 (1978)	110	30	>4	Strong (+11)
Spain	53 (1918)	31 (1985)	70	22	<5	Modest (+3)
Italy	51 (1851)	30 (1983)	120	21	<9	Strong (+5)
Japan	55 (1937)	31 (1981)	45	24	6	Modest (+1)
Netherlands	61 (1732)	28 (1982)	250	33	7	Modest(+2)

Urban Gini in China: 1981-2014 (based on official household surveys)



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Where are now China and the US?



What might drive the 2nd Kuznets cycle down?

- Progressive political change (endogenous: political demand)
- Dissipation of innovation rents
- Low-skilled biased technological progress (endogenous)
- Reduced gap in education (but it is not a silver bullet)
- Global income convergence: Chinese wages catch up with American wages: the hollowing-out process stops
- Note that all are all endogenous

6. Issues of justice and politics

1. Citizenship rent
2. Migration and national welfare state
3. Hollowing out of the rich countries' middle classes

Global inequality of opportunity

- Regressing (log) average incomes of 118 countries' percentiles (11,800 data points) against country dummies “explains” 77% of variability of income percentiles
- Where you live is the most important determinant of your income; for 97% of people in the world: birth=citizenship.
- Citizenship rent.

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, effort)
- ***Key issue:*** *Is global equality of opportunity something that we ought to be concerned or not?*
- Does national self-determination dispenses with the need to worry about GEO?

The logic of the argument

- Citizenship is a morally-arbitrary circumstance, independent of individual effort
- It can be regarded as a rent (shared by all members of a community)
- Are citizenship rents globally acceptable or not?
- Political philosophy arguments *pro* (social contract; statist theory; self-determination) and *contra* (cosmopolitan approach)

Rawls' views on inter-generational transmission of wealth

Group	Inter-generational transmission of collectively acquired wealth	Argument	Policy
Family	Not acceptable Or at least to be limited	Threatens equality of citizens	Moderate to very high inheritance tax
Nation	Acceptable	Affirms national self-determination (moral hazard)	International aid

The Rawlsian world

- For Rawls, global optimum distribution of income is simply a sum of national optimal income distributions
- Why Rawlsian world will remain unequal?

Global inequality in Real World, Rawlsian World, Convergence World...and Shangri-La World (Theil 0; year 2011)

Mean country incomes Individual incomes within country	All equal	Different (as now)
All equal	0	54 (all country Theils=0; all mean incomes as now)
Different (as now)	23 (all mean incomes equalized; all country Ginis as now)	77

Conclusion

- Working on equalization of within-national inequalities will not be sufficient to significantly reduce global inequality
- Faster growth of poorer countries is key and also...

Migration....

Migration: a different way to reduce global inequality and citizenship rent

- How to view development: Development is increased income for poor people regardless of where they live, in their countries of birth or elsewhere
- Migration and LDC growth thus become two equivalent instruments for development

Growing inter-country income differences and migration: Key seven borders today



The logic of the migration argument

- Population in rich countries enjoys the citizenship premium
- They are unwilling to share, and thus possibly reduce (at least “locally”) this premium with migrants
- Currently, the premium is full or 0 because citizenship is (in terms of rights as well as financially) a binary variable
- Introduce various levels of citizenship (tax discrimination of migrants; obligation to return; no family etc.) to reduce the premium
- Temporary work
- Doing this should make native population more acceptant of migrants

Trade-off between citizenship rights and extent of migration



* People who would like to migrate according to a world-wide Gallup poll

Political issue: Global vs. national level

- Our income and employment is increasingly determined by global forces
- But political decision-making still takes place at the level of the nation-state
- If stagnation of income of rich countries' middle classes continues, will they continue to support globalization?
- Two dangers: populism and plutocracy
- To avert both, need for within-national redistributions: those who lose have to be helped

Final conclusion

- To reduce global inequality: fast growth of poor countries + migration
- To have migration, discriminate the migrants
- To preserve good aspects of globalization: reduced inequality within rich countries via equalization of human and financial assets (i.e. focus on pre-redistribution)

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Chair, LSE

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