

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

LSE events

gp global
POLICY



The haves and the have-nots:
A short and idiosyncratic history
of global inequality

Branko Milanovic
Winter 2010-11

The book's epigraph

“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)

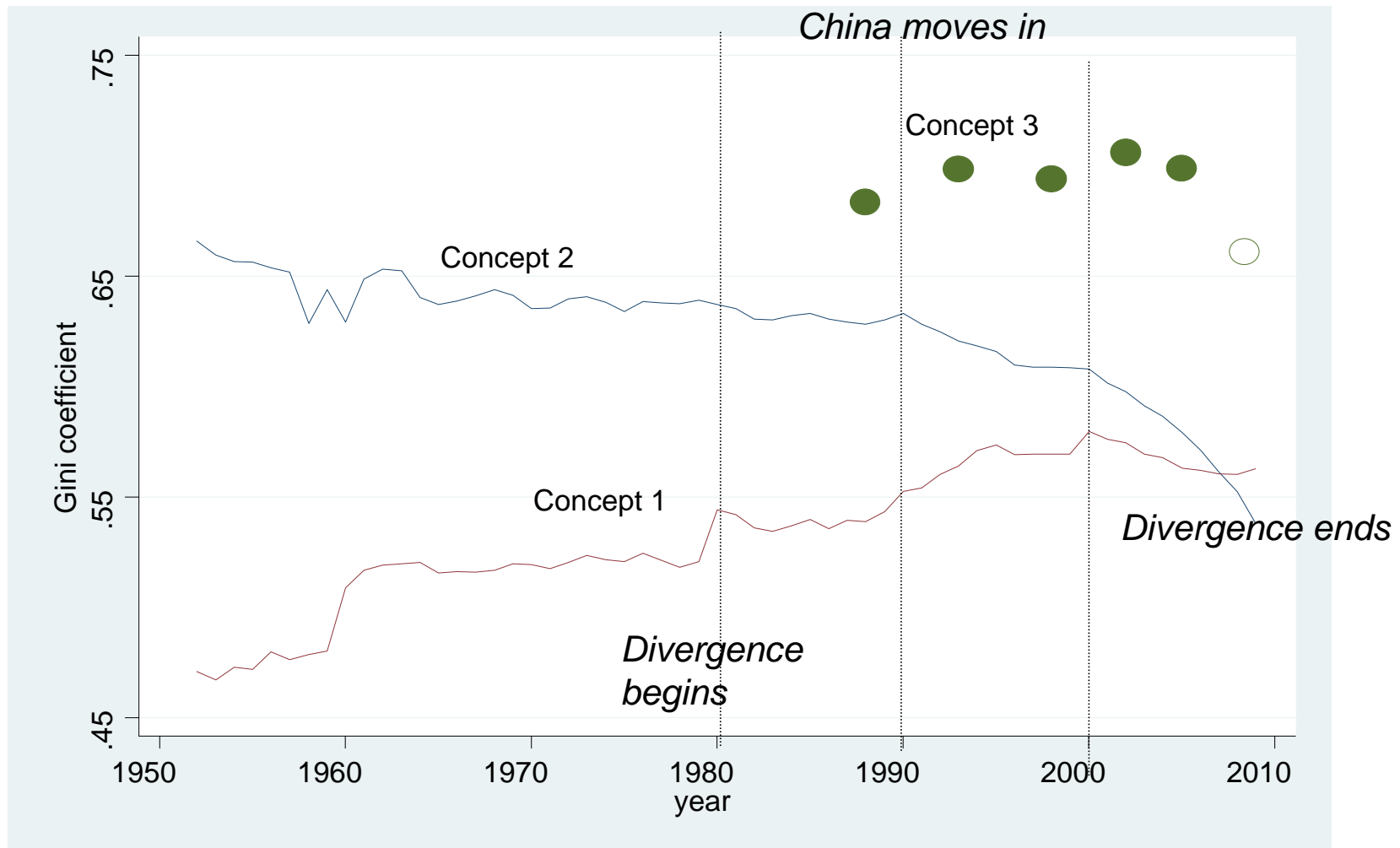
“..of the tendencies that are harmful to sound economics, the most seductive, and ...the most poisonous, is to focus on questions of distribution.”

Robert E. Lucas (2004), “The Industrial revolution: past and future”

0. Overview of the present and past of global inequality

Inequality 1950-2009

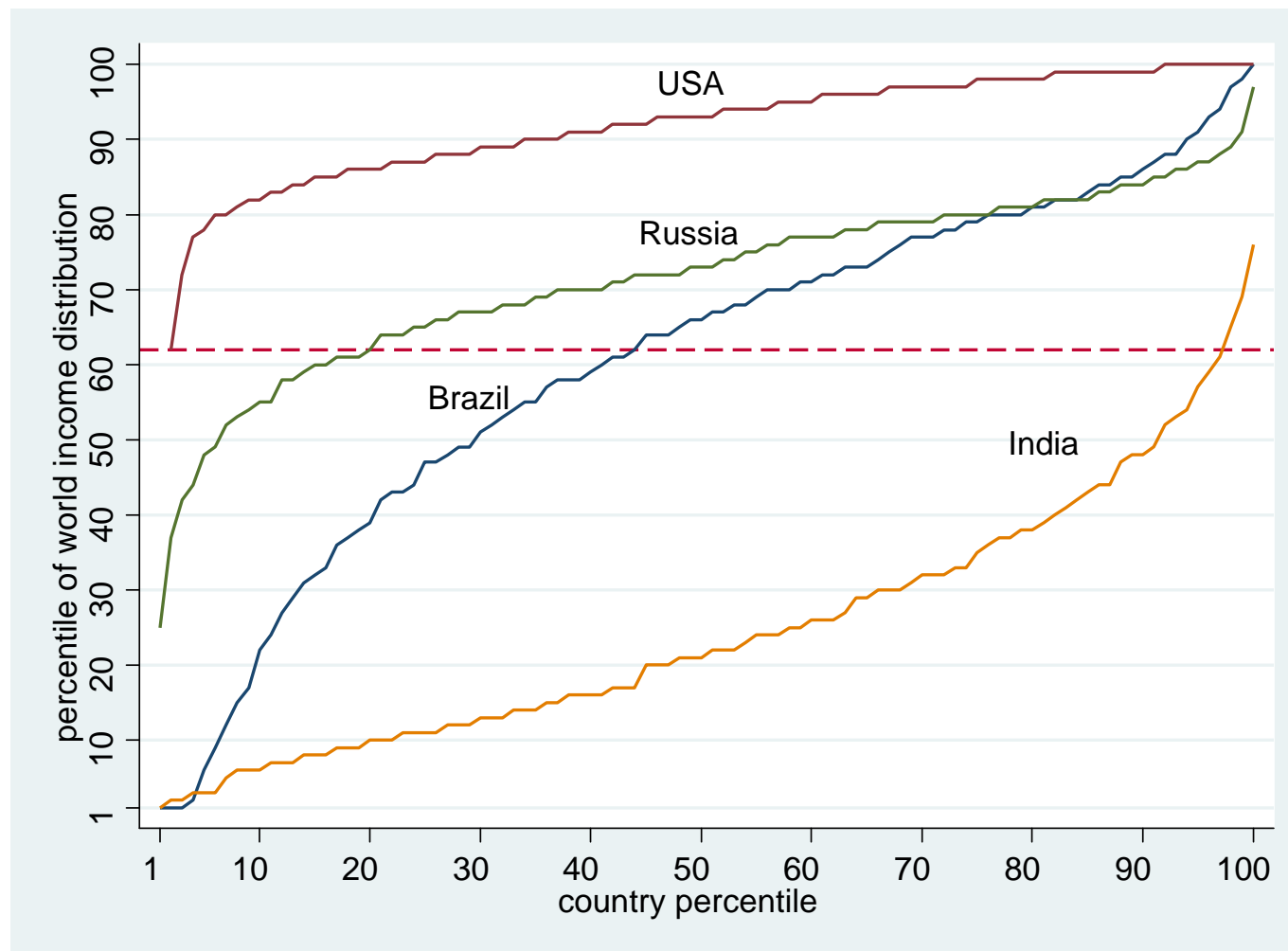
The mother of all inequality disputes



With new PPPs

Graph in interyd\dofiles\defines.do

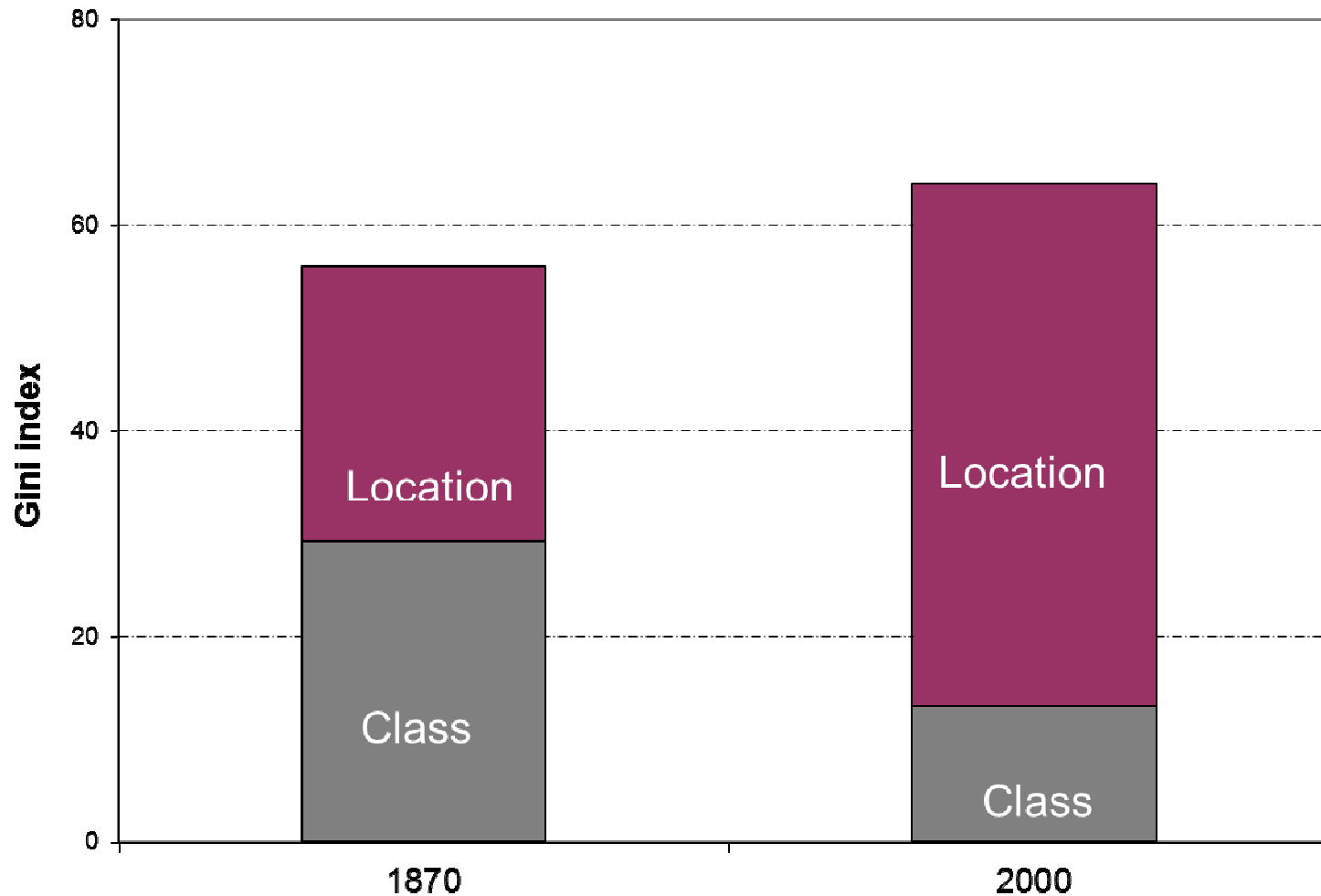
BRICs and the US in percentiles (year 2002; new PPPs)



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-Morrison (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*)

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

1810 position estimates based on Colquhoun 1801-3 data. 2004 UK data from LIS, and for 0.1% from Piketty (*Data-central*).

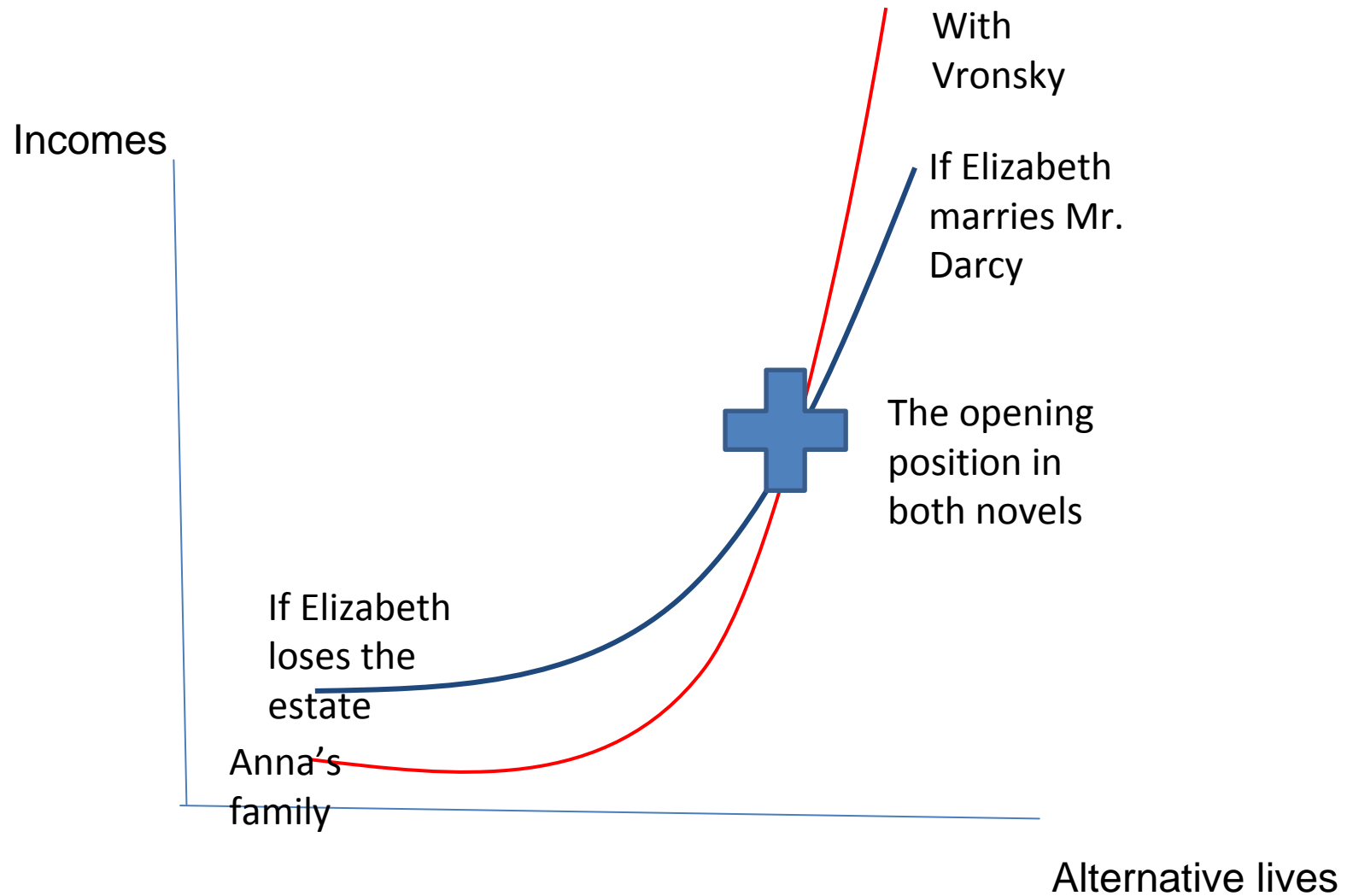
Inequality 135 years ago & now: Russia

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

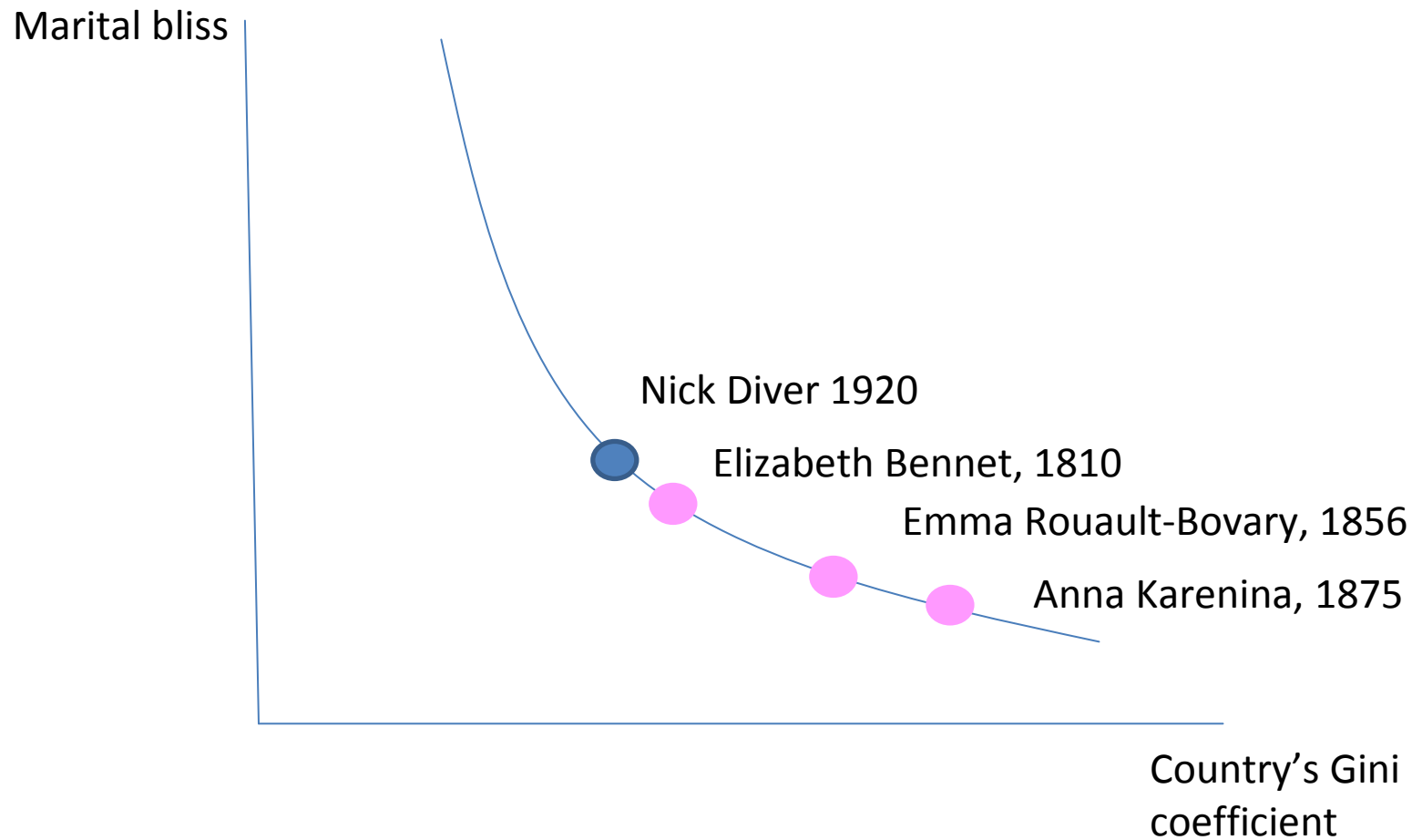
	Income in 1875 (R pa)	Approx. position in 1875 income distribution	Income around 2005 (R pc pa)
Count Vronsky	100,000	Top 0.1%	3,000,000
Karenin and Anna	9000/3~3000	Top 1%	340,000
Anna's parents	200	Mean (around 65 th percentile)	53,000
Gain	150 to 1		19 to 1

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

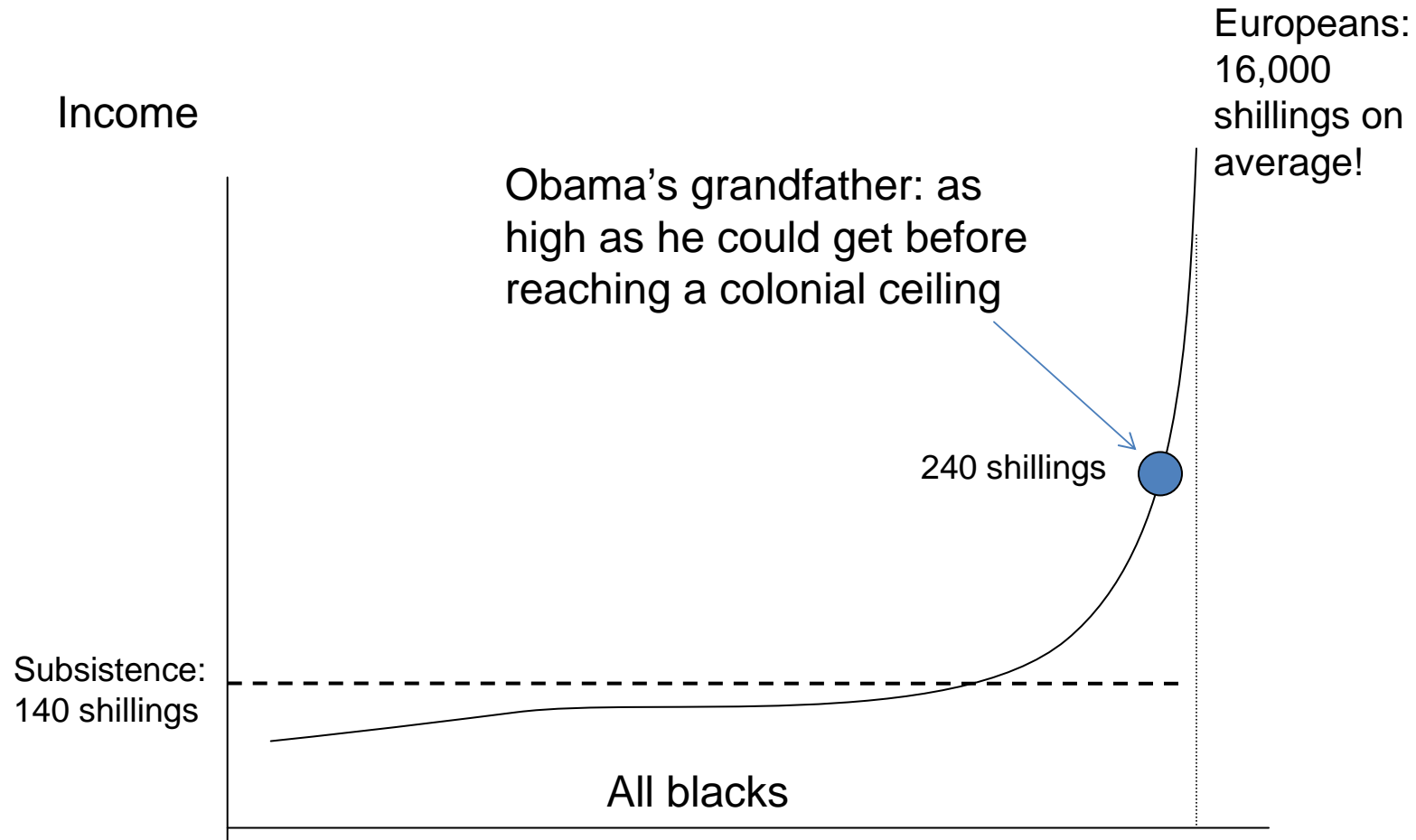


Trade-off between inequality and love in marriage

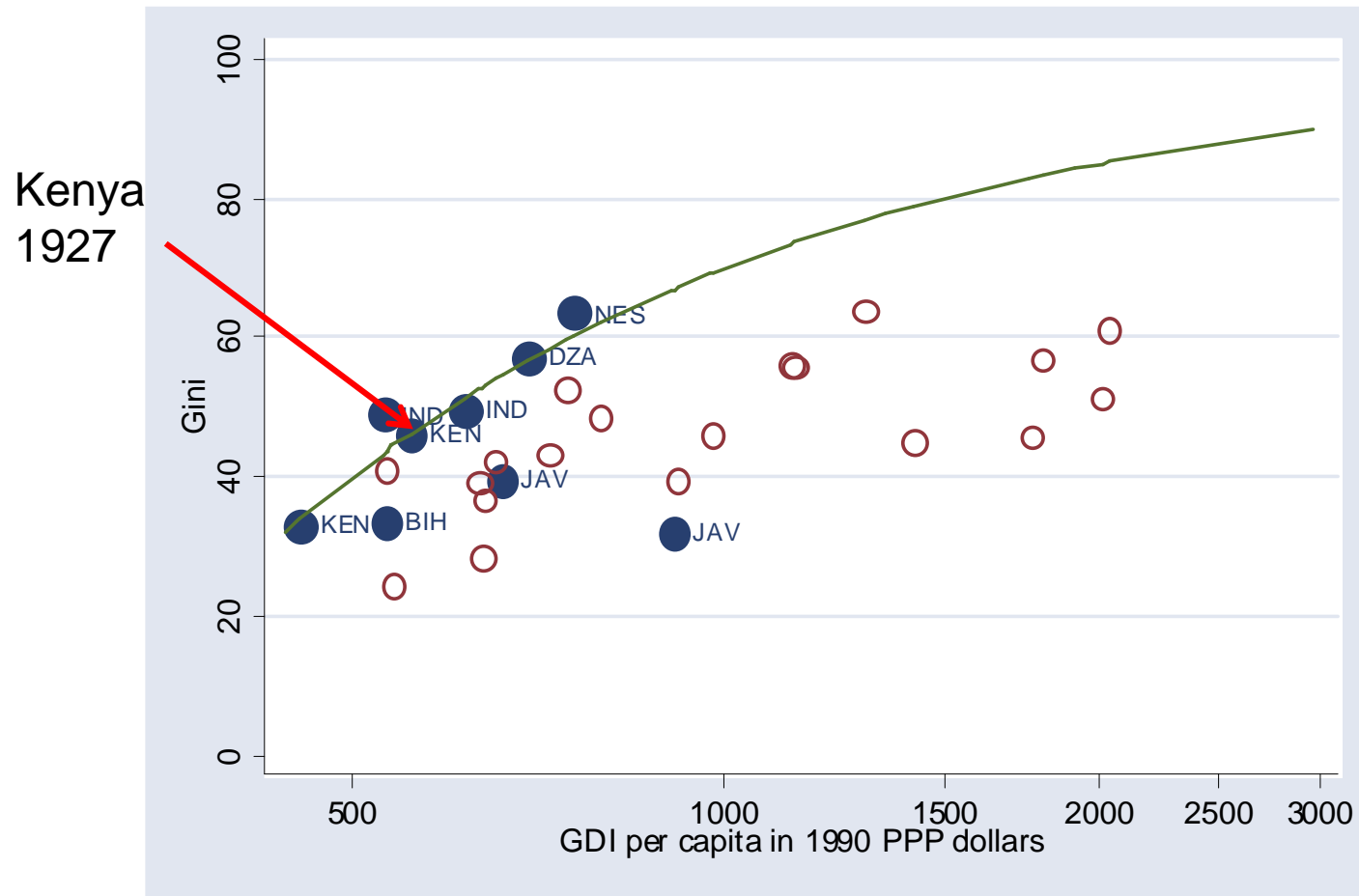


1B. The three generations of Obamas

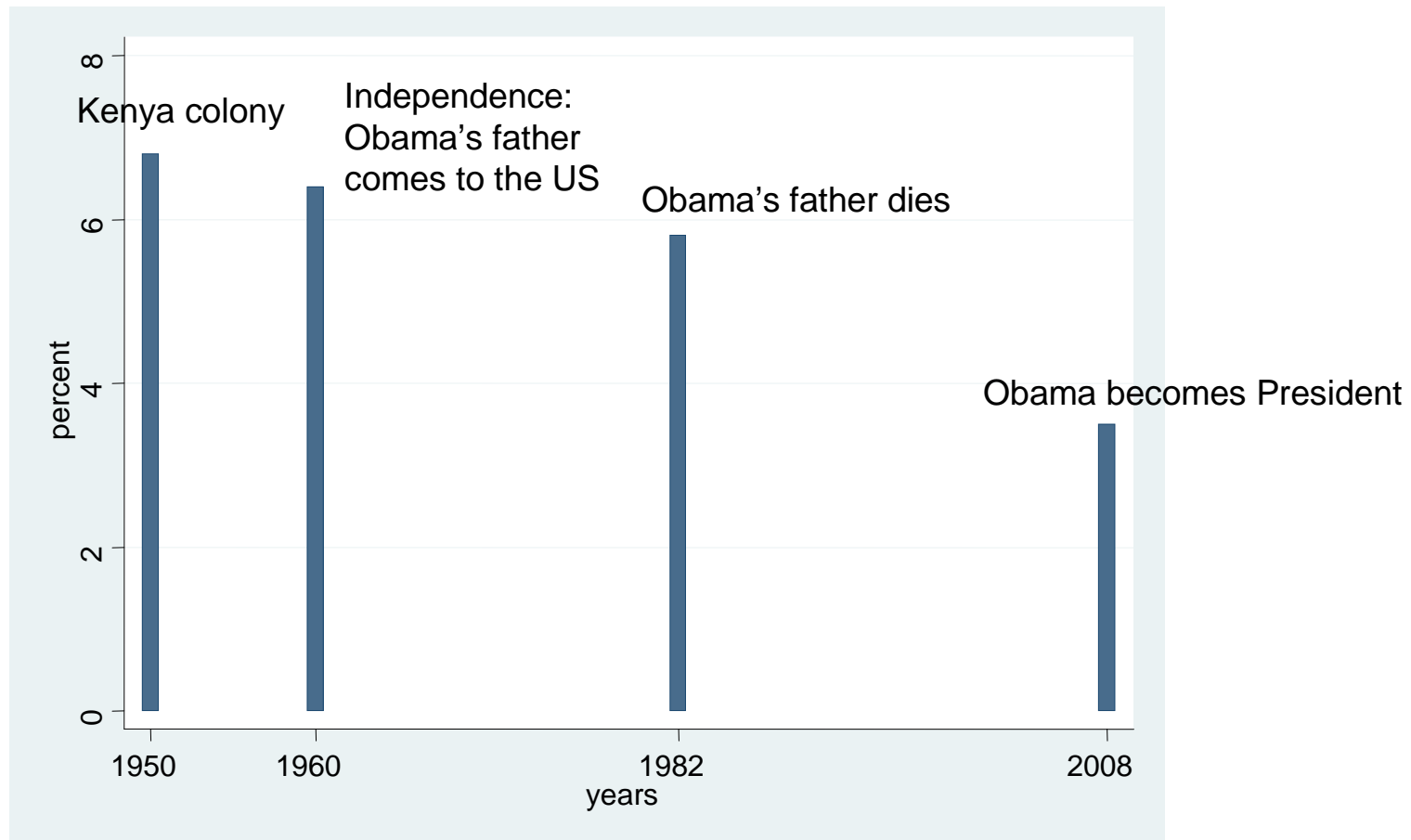
Obama's three generations



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

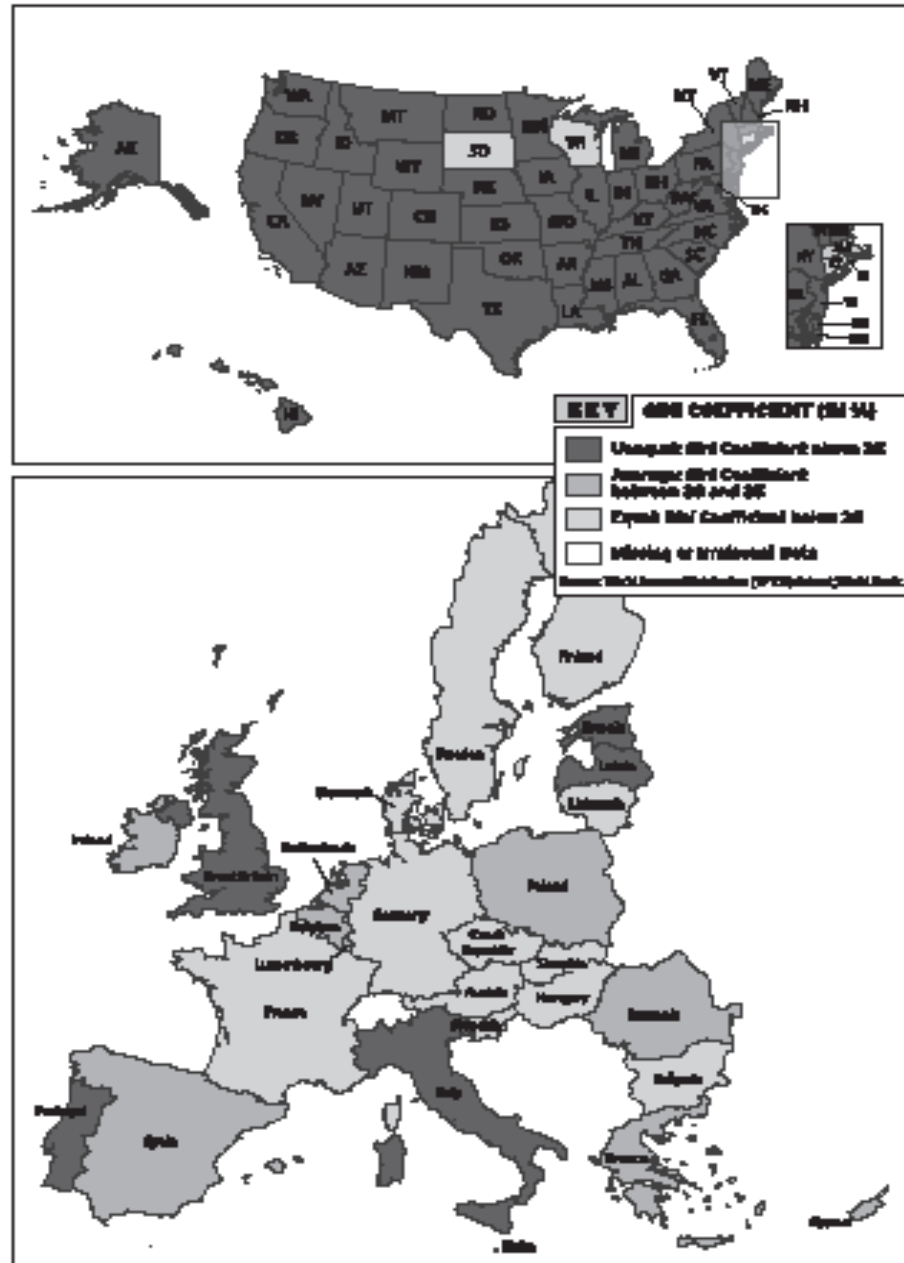
[My mother] had always encouraged my rapid acculturation in Indonesia...She had taught me to disdain the blend of ignorance and arrogance that too often characterized Americans abroad. But she now learned...the chasm that separated the life chances of an American from those of an Indonesian. She knew 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)

	Most equal	Average	Most unequal
United States	34 (South Dakota; Wisconsin)	39 (Delaware; Idaho)	45 (Texas; Tennessee)
European Union	24 (Hungary; Denmark)	31 (Netherlands)	38 (UK; Portugal)
Difference	10 points	8 points	7 points

INCOME INEQUALITY IN THE UNITED STATES AND EUROPEAN UNION, AROUND 2008

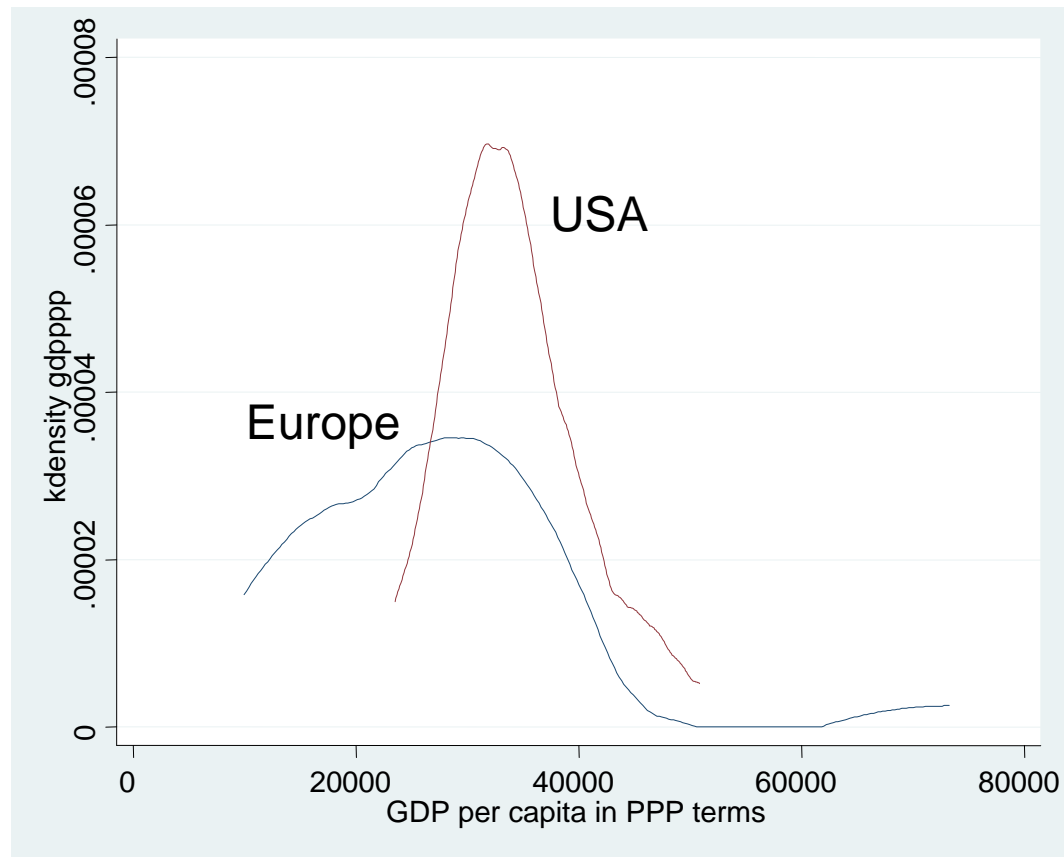


Dark color
= high
inequality
countries
or states

GDP per capita differences in the United States and European Union, around 2005

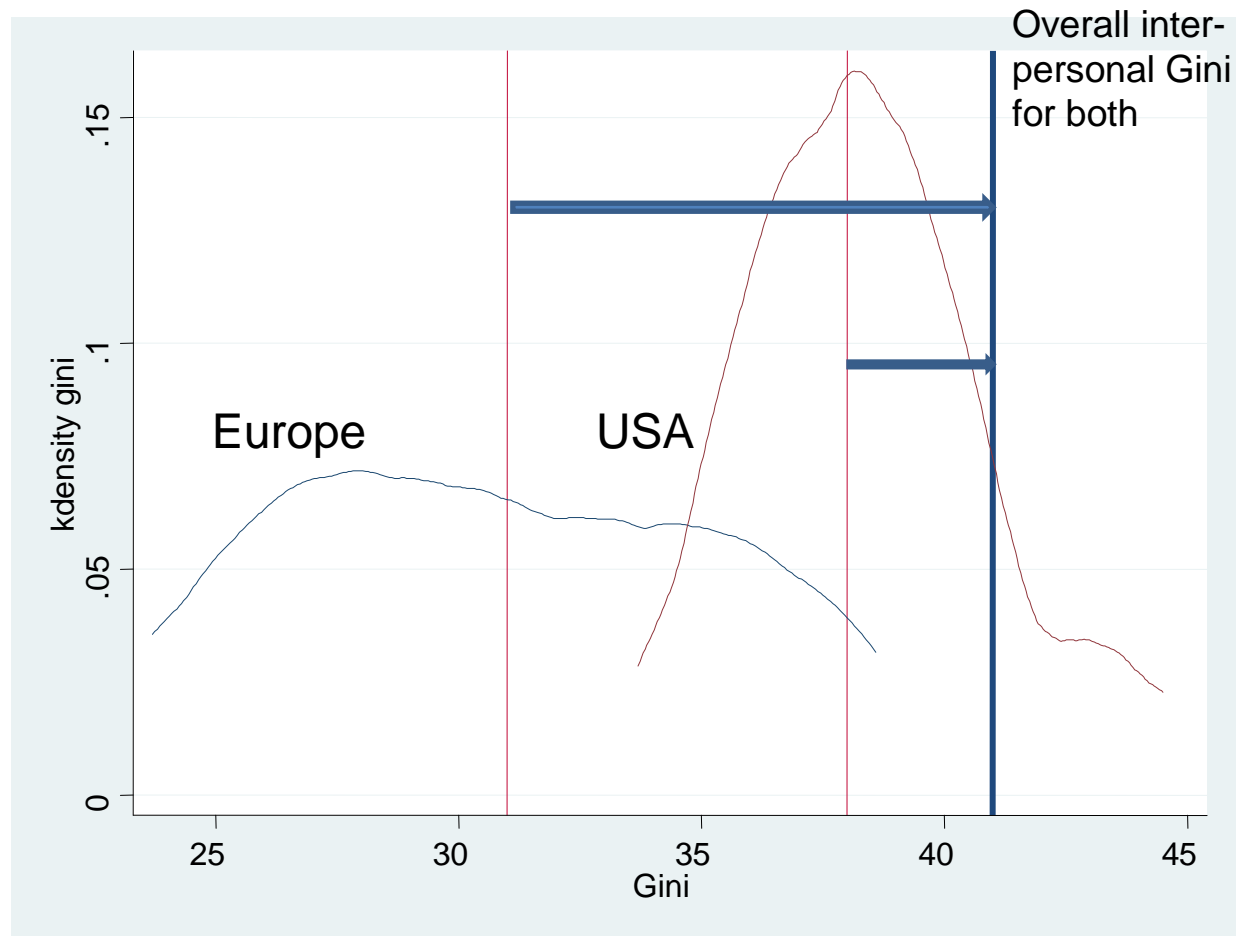
	Poorest	Average	Richest	Ratio top to bottom
United States	66 (Mississippi; West Virginia)	100 (Rhode Island)	137 (Connecticut; Delaware)	2 to 1
European Union	36 (Bulgaria; Romania)	100 (Spain)	140 (Netherlands)	4 to 1
Difference	-30 points	0 points (by definition)	+3 points	

GDP per capita in countries of the European Union and states of the USA (unweighted)



```
twoway (kdensity gdp PPP if Deurope_inc==1) (kdensity gdp PPP if Deurope_inc==0, legend(off) xtitle(GDP per capita in PPP terms))  
Using sources\US_EU\US_vs_EU.dta
```


Ginis in countries of the European Union and states of the USA



```
. twoway (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

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

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

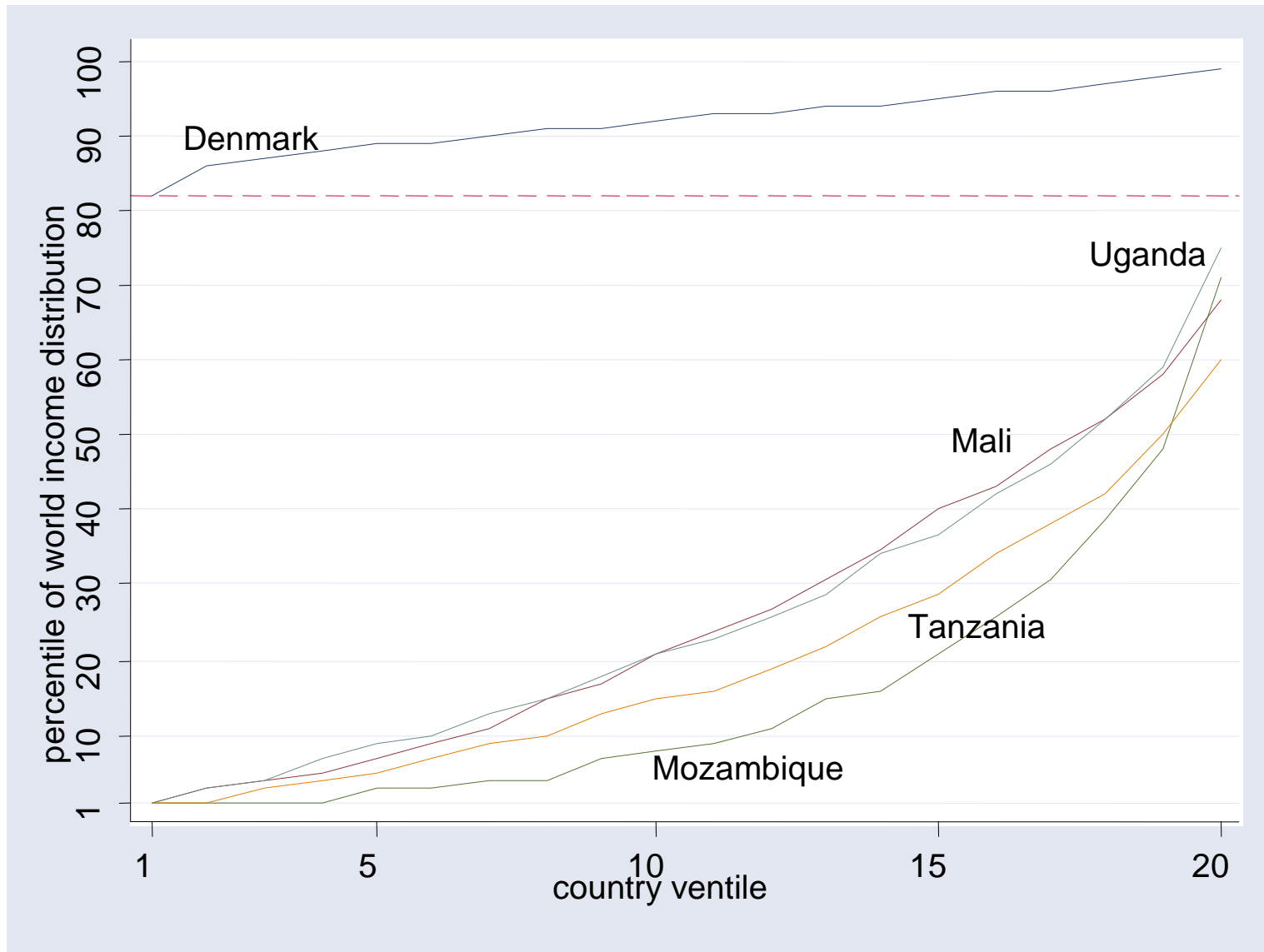
Implications

- 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

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

m_j = mean country income

G_j = Gini coefficient

C_{ij} = 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})

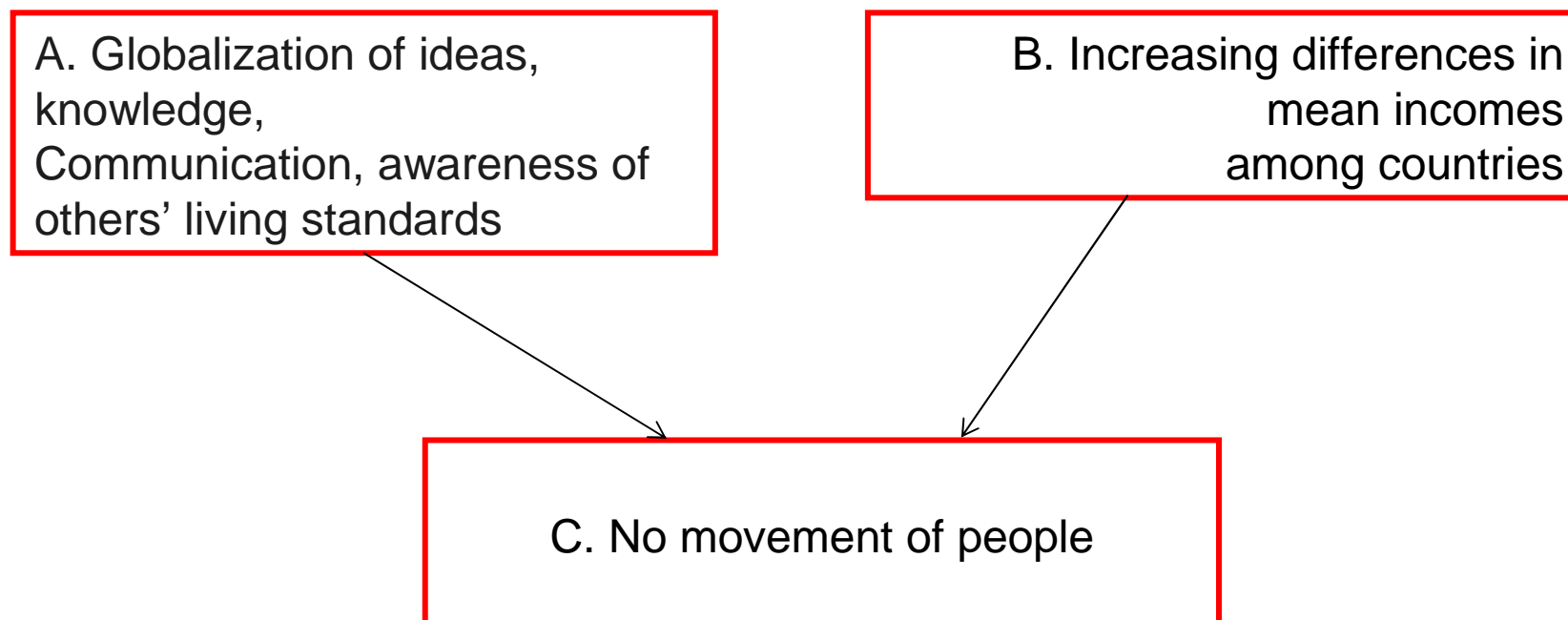
Global inequality of opportunity

- 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. Pistoiesi, JofEI, 2009)

2B. Implications: migration; just
international order

The XXI century trilemma



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)

		Year 2007	Year 1980
	Approximate % of foreign workers in labor force	Ratio of real GDI per capita	
Greece (Macedonian/ Albanians)	7.5	4 to 1	2.1 to 1
Spain (Moroccans)	14.4	7.4 to 1	6.5 to 1
United States (Mexicans)	15.6*	3.6 to 1	2.6 to 1
Malaysia (Indonesians)	18.0	3.7 to 1	3.6 to 1

* BLS, News Release March 2009; data for 2008 inclusive of undocumented aliens.

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:

$$\underbrace{\sum_{i=1}^n G_i p_i \pi_i}_{\text{Term 1}} + \underbrace{\frac{1}{\mu} \sum_{i=1}^n \sum_{j>i}^n (y_j - y_i) p_i p_j}_{\text{Term 2}} + L$$

Rawls would insist of 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.

Global Ginis in Real World, Rawlsian World, Convergence World...and Shangri-La World

<div>Mean country incomes</div> <div>Individual incomes within country</div>	All equal	Different (as now)
All equal	0	61.5 (all country Ginis=0)
Different (as now)	45.6 (all mean incomes same; all country Ginis as now)	69.7

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

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

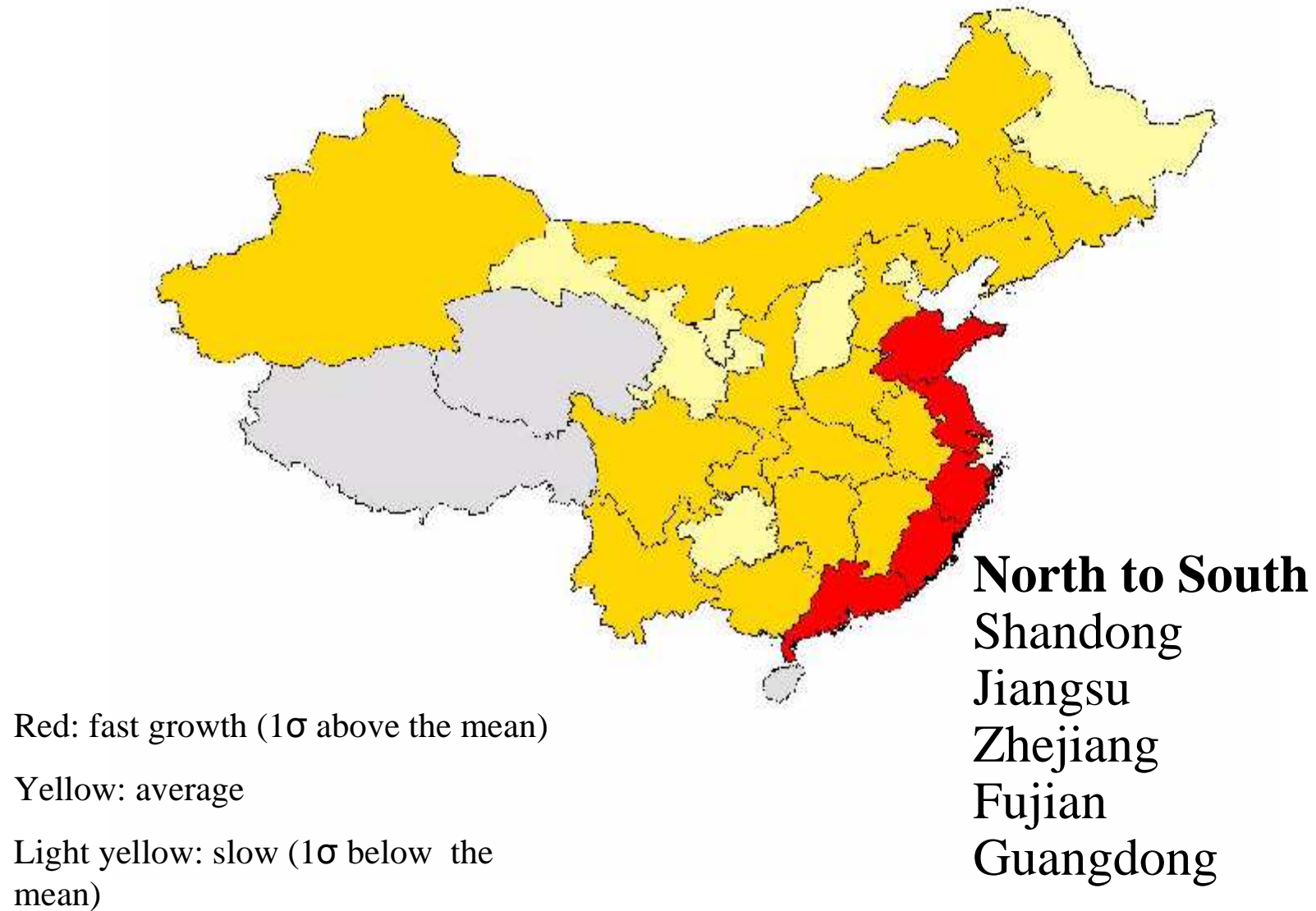
* Most of the successful passages before the consolidation of the Wall.

A debate about inequality: come prepared

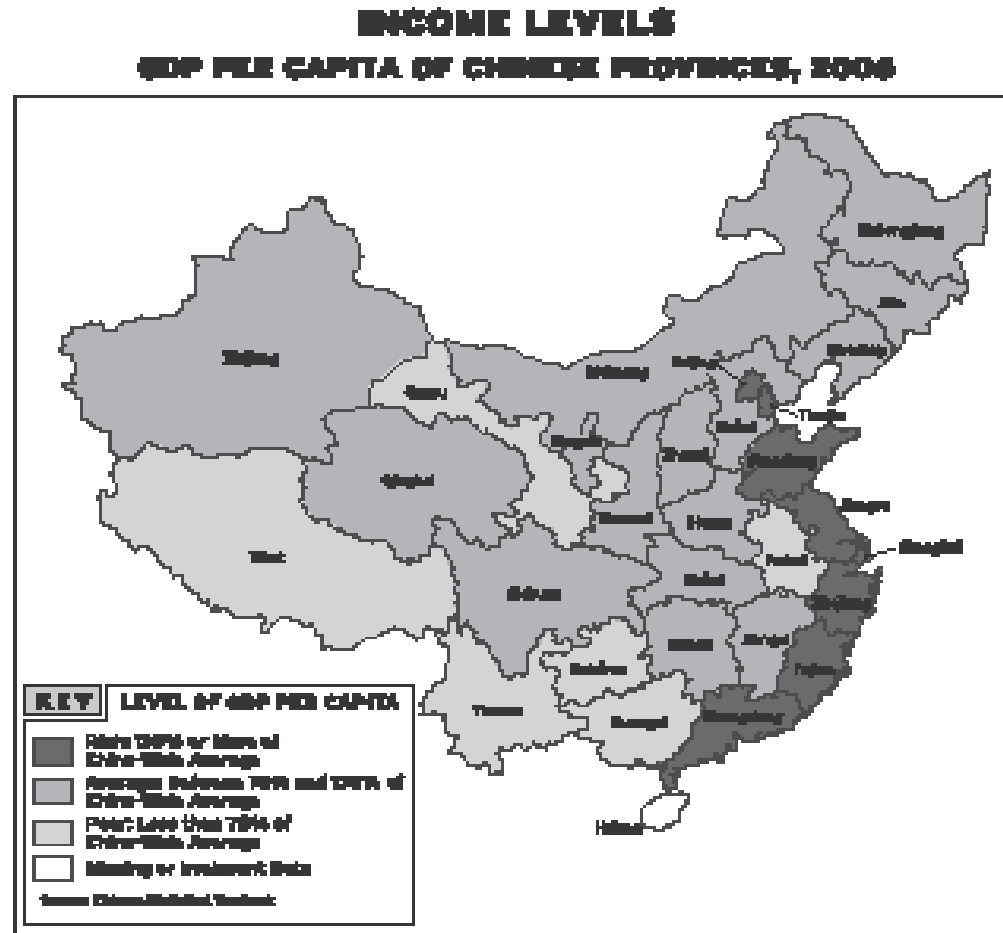
- *The Economist* (January 2011): “Remember: Envy is a deadly sin!” (List made in 4th century, envy introduced on the list in the 7th)
- “Again I tell you, it is easier for a camel to go through the eye of a needle than for a rich man to enter the kingdom of God.”
- “If you want to be perfect, go, sell your possessions and give to the poor, and you will have treasure in heaven.” (in Mark, Luke and Matthew)

China

China (1980-2000)

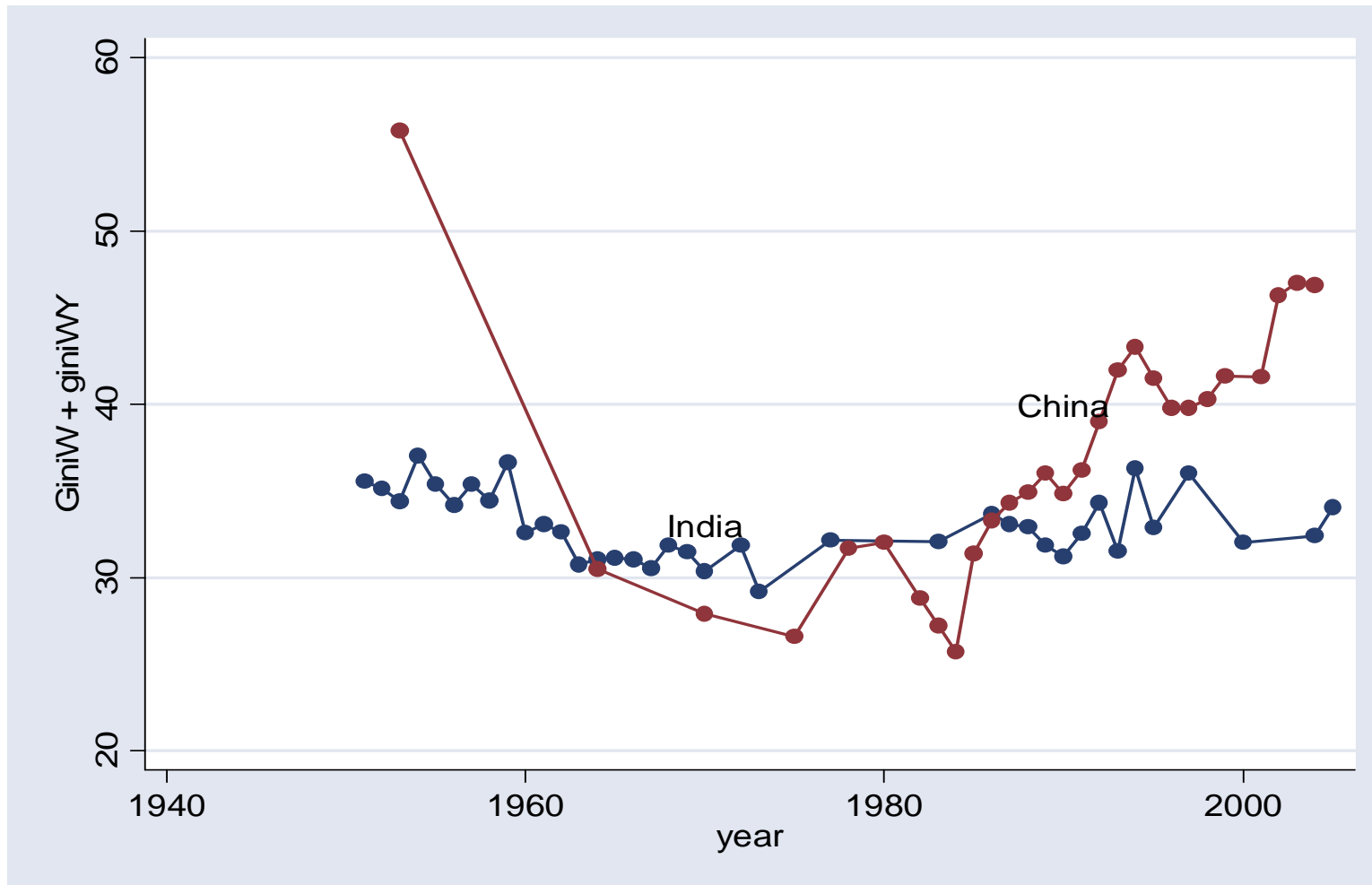


China's Gang of Eleven: 5 maritime provinces + 4 city provinces + Hong Kong and Macao: almost 60% of GDP by a third of the population



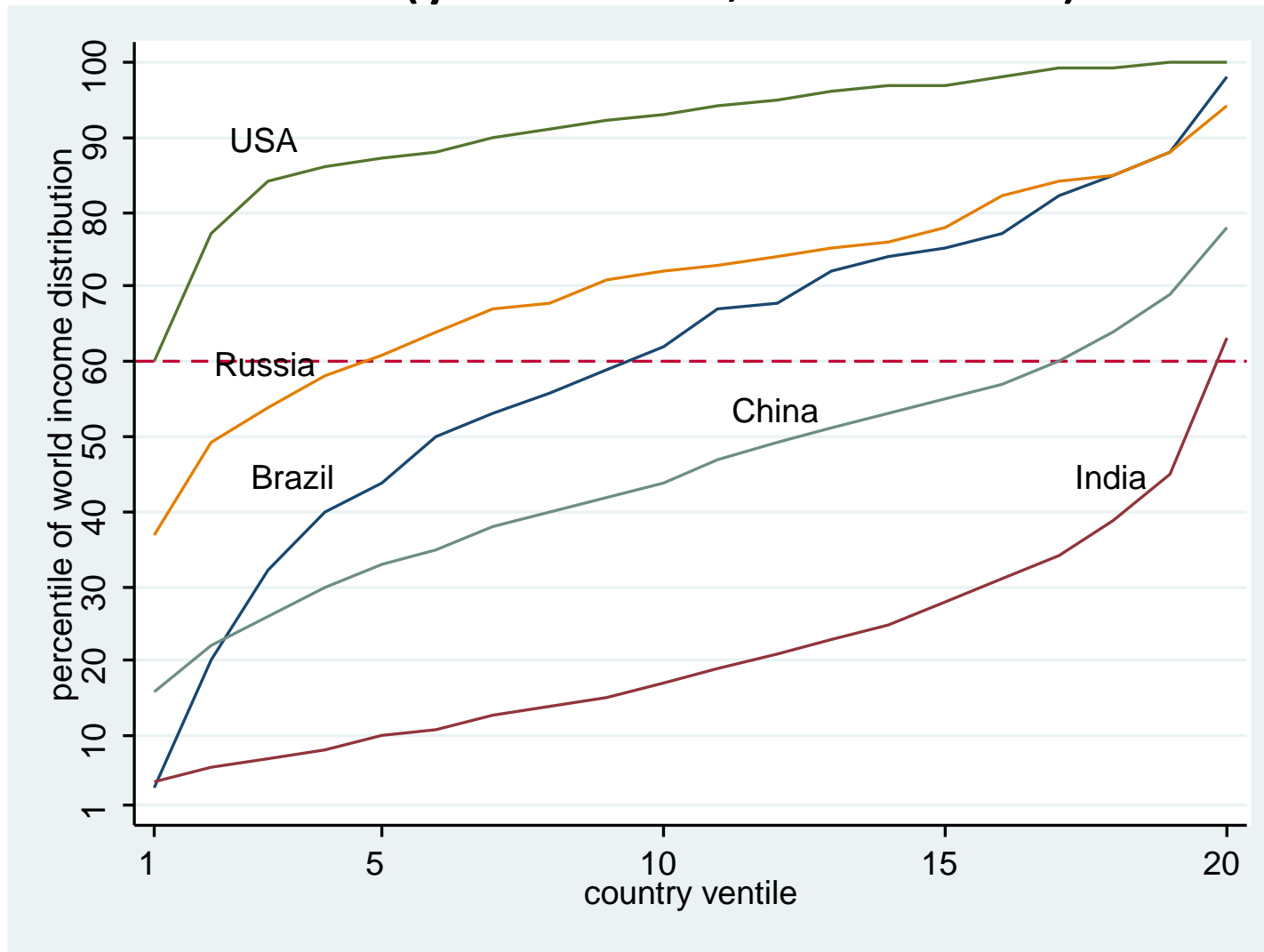
Provinces are from N to S: Shanong, Jiansu,Zhejiang, Fujian,Guangdong

India and China Ginis, 1950-2004

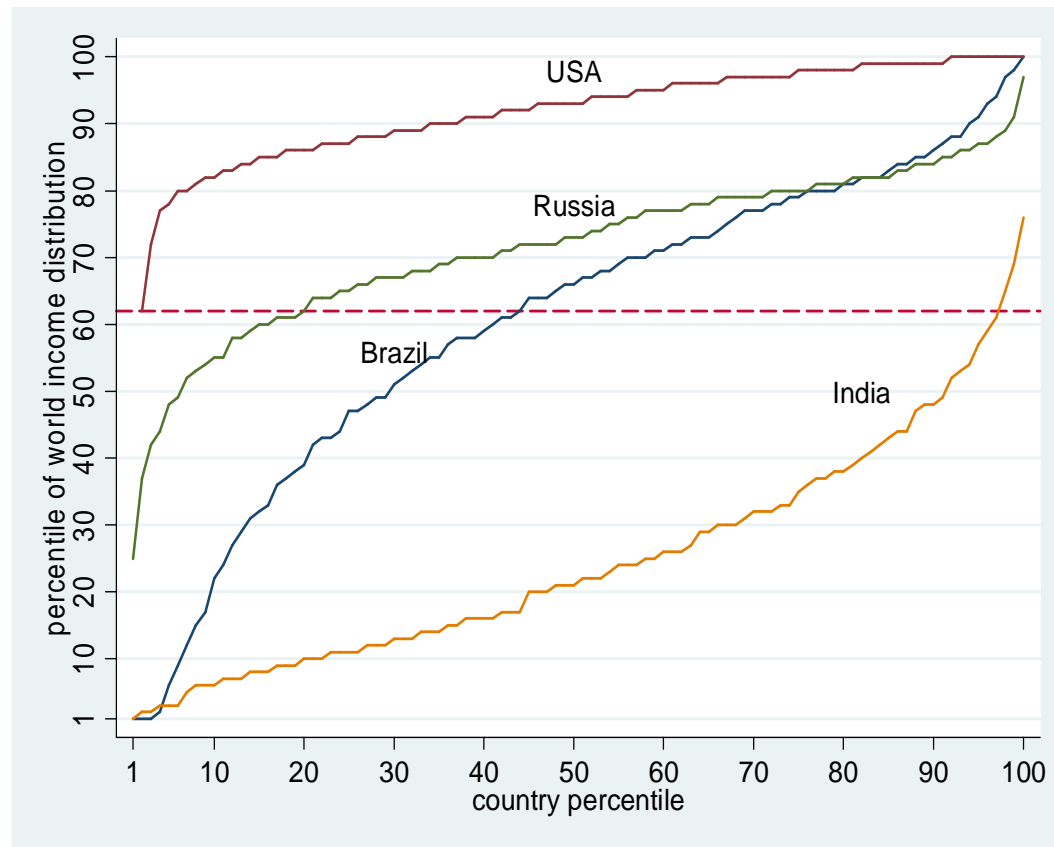


`twoway (scatter Giniall year if contcod=="IND" & Di==0 & Dhh==0, connect(l)) (scatter Giniall year if contcod=="CHN" & Di==1 & Dhh==0 & year<2005, connect(l)), legend(off) text(33 1970 "India") text(40 1990 "China")`
From igdppppreg.dta

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

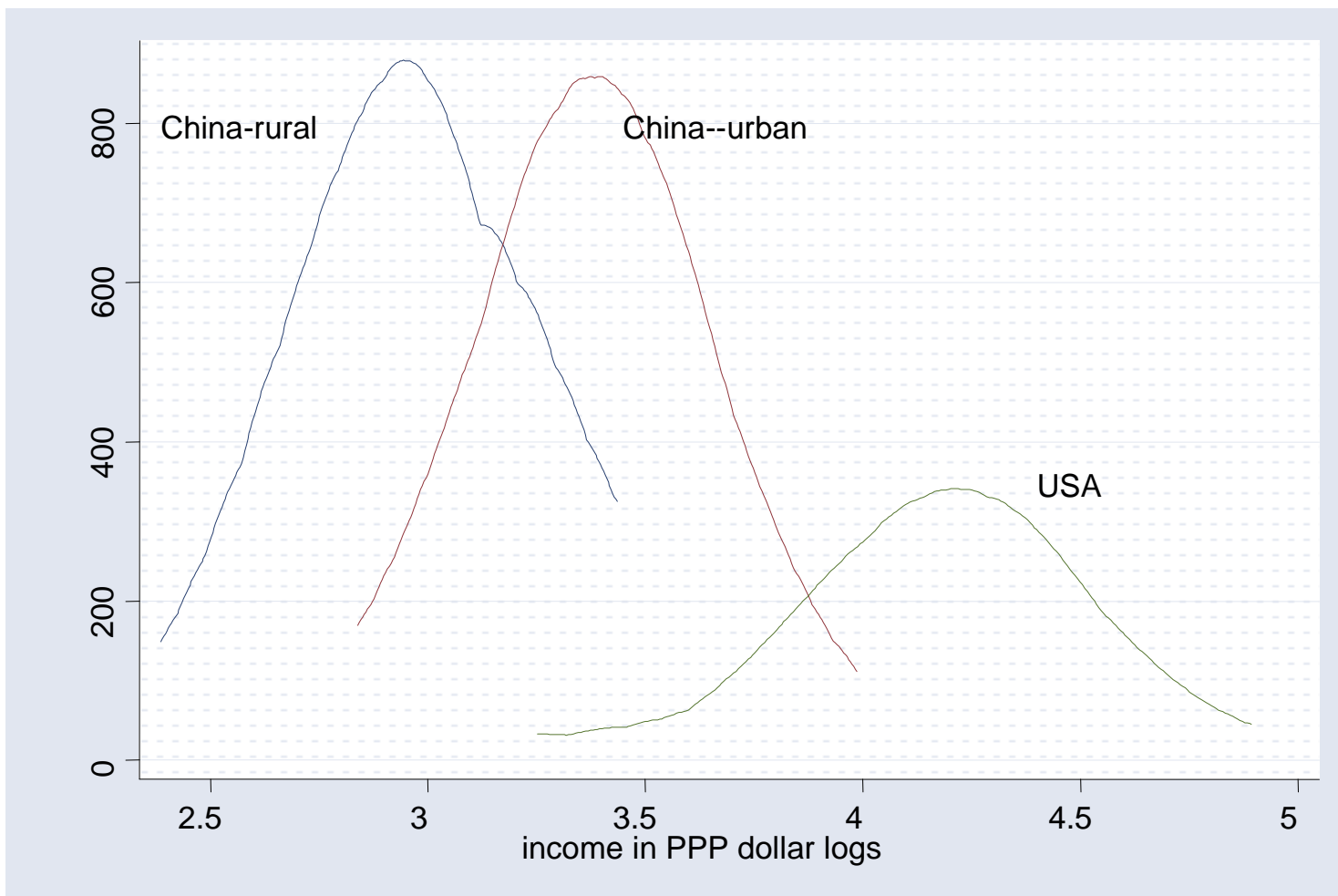


BRICs and the US in percentiles (year 2002; new PPPs)



Using world2002_centile.dta and michele_graph.do

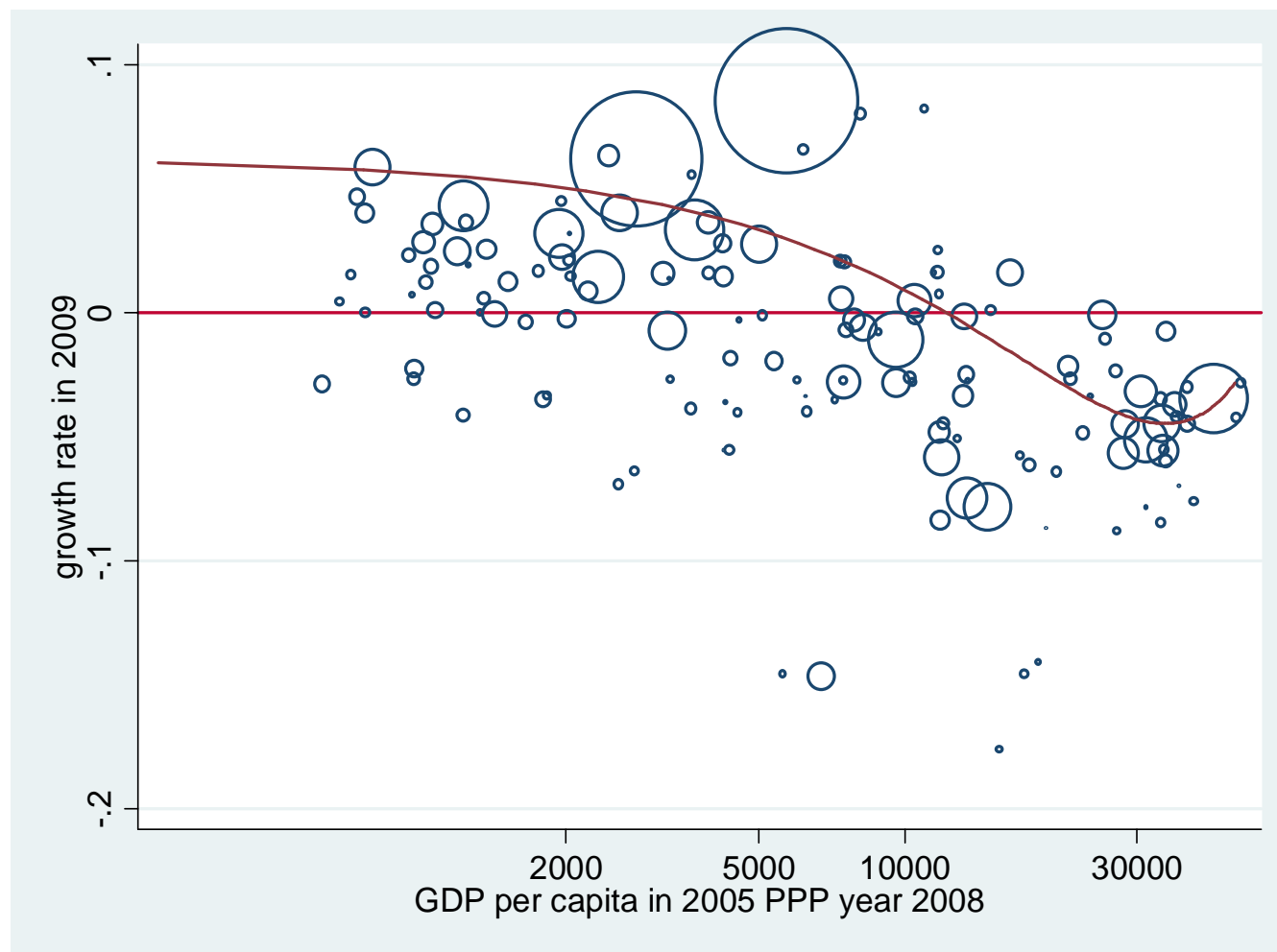
Chinese and American income distributions, 2005



```
twoway (kdensity loginc [w=popu] if year==2005 & loginc>1 & contcod=="CHN-R", area(678)) (kdensity loginc [w=popu] if year==2005 & loginc>1 & contcod=="CHN-U", area(626)) (kdensity loginc [w=popu] if year==2005 & loginc>1 & contcod=="USA", area(296)), legend(off) xtitle(income in PPP dollar logs) text(800 2.6 "China-rural") text(800 3.7 "China--urban") text(350 4.5 "USA")
From world2002_2005.dta
```

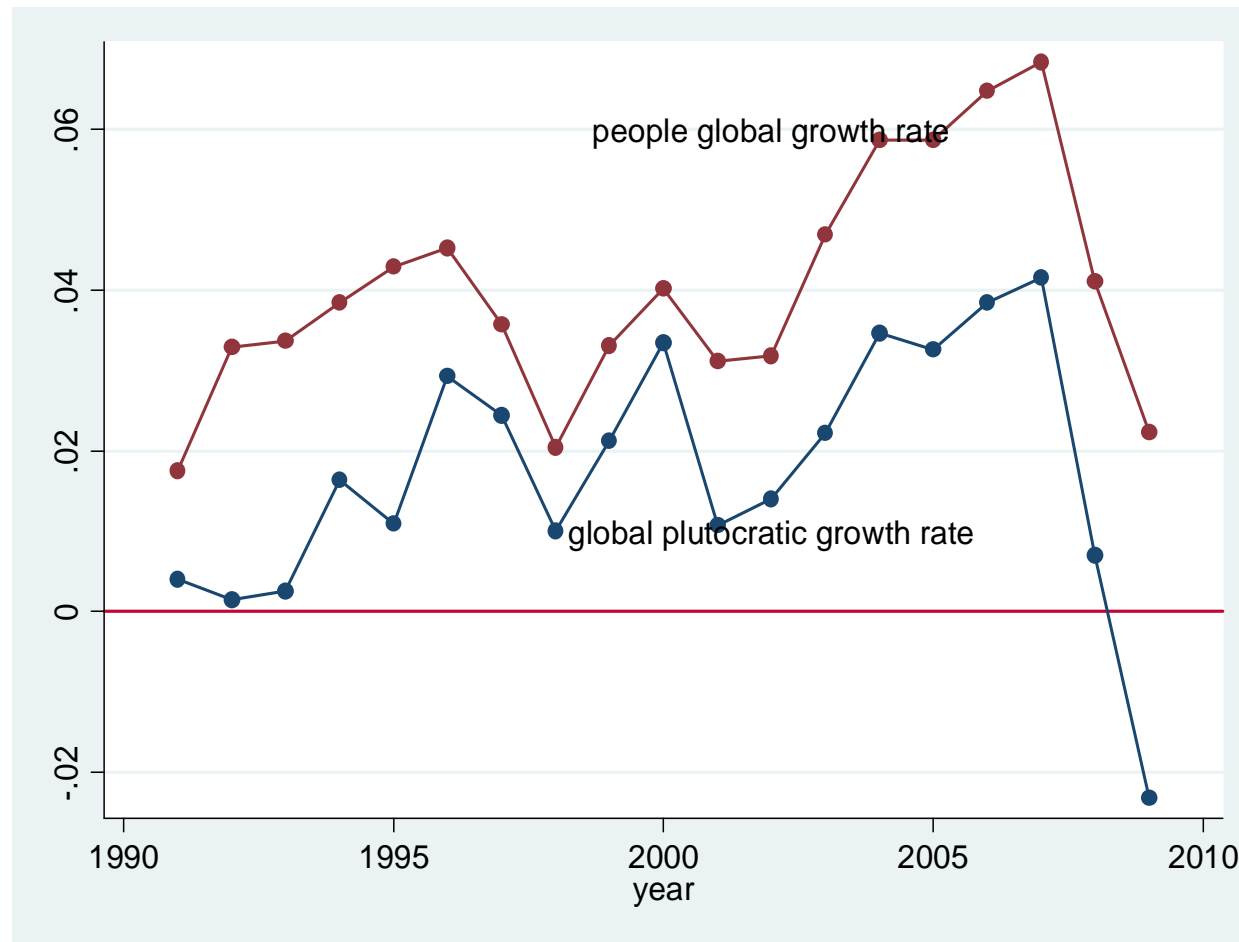
The crisis

Rich man's crisis? 2008 GDP per capita against growth rate in 2009 (with population weights)



```
twoway (scatter gdpgrth lgdpppp [w=pop] if year==2009 & gdpppp<50000 & gdpppp>500, yline(0) xscale(log) xlabel( 2000 5000 10000 30000) msymbol(circle_hollow))  
(qfit gdpgrth gdpppp [w=pop] if year==2009 & gdpppp<50000, legend(off) xtitle(GDP per capita in 2005 PPP year 2008) ytitle(growth rate in 2009))  
Using gdpppp.dta
```

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 gdp PPP reg.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

LSE events

gp global
POLICY

