

Is there a Dark Side of Capitalism? The Effect of Income on Income Inequality – by Saeed Khodaverdian

Discussion by

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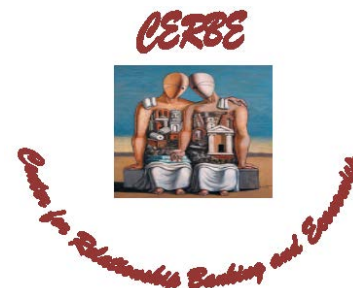
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3rd joint conference of European Central Bank & Central Bank of Republic of Turkey

Balanced and sustainable growth - operationalising the G20 framework

Session I: Sustainable economic performance

Thursday, 27 August 2015 – ECB Premises, Frankfurt am Main



Outline

❑ Main thrust of the paper:

- Inequality boosting growth only in rich but not in poor countries;
- Inequality lowering growth in Islamic countries;
- Conclusion: ideology (market fundamentalism?) matters.

❑ Some problems with data and methodology:

- The empirical strategy is very well accomplished but ...
- Problem of (many) missing Islamic countries;
- Better measures of Globalization?

❑ Which channels? Which ways out?

- Variety of capitalism: Are the poor lazy? Are the bankers “bangsters”?
- Financial capitalism vs. productive capitalism;
- Replacing the market fundamentalism ideology not capitalism;
- Any hope from “integral sustainability”?

Main thrust of the paper

- ❑ Inequality boosting growth only in rich but not in poor countries:
 - Since the 1980s inequality has increased in the rich but not in the poor countries;
 - The difference is more visible in the “market” than in the “net” Gini;
 - IV approach-causality Δ^+ growth $\rightarrow \Delta^+$ inequality (only in rich countries).

- ❑ Inequality lowering growth in Islamic countries:
 - Islamic religion may give anti-capitalist ideology (Campante & Yanagizawa-Drott 2015)
 - IV approach-causality Δ^+ growth $\rightarrow \Delta^-$ inequality (in Islamic countries).

- ❑ Conclusion: ideology (market fundamentalism?) matters:
 - To avoid rising inequality spoiling democracy, anti-capitalistic ideology may be needed (Khodaverdian 2015);
 - Theory of the “élites”.

Some problems with data and methodology – 1

❑ The empirical strategy is very well accomplished but ... two problems:

1. Many Islamic countries are missing:

- From Wikipedia we can count 49 Islamic countries (i.e., >50%) but in the paper there are only 36 Islamic countries
- Alas, the 13 missing Islamic countries could be very important: **Bahrain, Brunei, Kosovo, Kuwait, Libya, Oman, Palestine, Qatar, Saudi Arabia, Somalia, United Arab Emirates**, Western Sahara
- Actually the large majority of them are **oil producing mostly Mid-East countries**
- The Gini index is missing for these countries but ... oil rents could be a “**resource curse**” (Stiglitz 2006) and go with **high inequality** (Alvaredo & Picketty, 2014)
- Also Mid-East countries with missing Gini indices might feature particularly **high inequality** (Bibi & Nabli, 2010)
- Thus, there could be a **nasty self-selection problem** among the Islamic countries

Some problems with data and methodology – 2

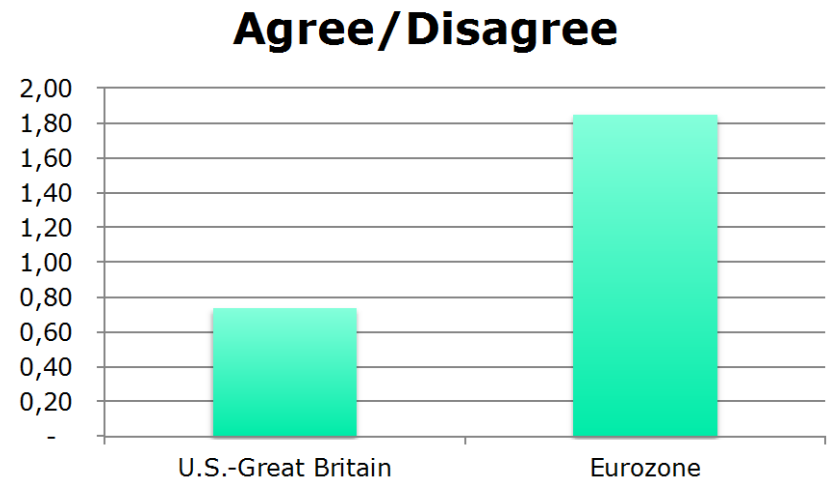
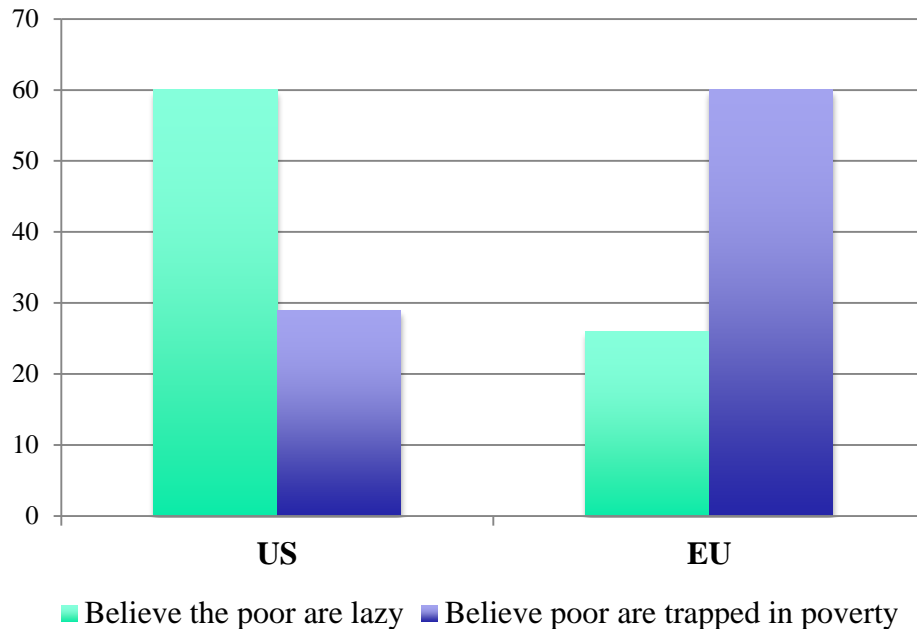
❑ The empirical strategy is very well accomplished but ... two problems:

2. Better measures of Globalization:

- Among the various controls for potential endogeneity, the author proxies for Globalization by means of Exports+Imports;
- This measure is not entirely satisfactory as Globalization entails dimensions other than trade (FDI, portfolio flows): use the KOF index (Dreher, 2006) or the more advanced NGI by Vujakovic (2009);
- This choice may be relevant: e.g., Vujakovic (2009) shows that moving from KOF to NGI reduces the rank of the 9 Islamic countries on average by more than two positions in the ladder.

Which channels? Which ways out? – 1

❑ Variety of capitalism: Are the poor lazy? Are the bankers “bangsters”?:



**“Success in life is pretty much determined by forces outside our control”:
Rich countries; U.S.-Great Britain vs Eurozone**

Which channels? Which ways out? – 2

❑ Variety of capitalism: Are the poor lazy? Are the bankers “bangsters”?:

Table 2. Misdoings related regulatory fines and settlements by bank's share (January 2010 -- October 2014) and incidence on tier 1 capital (Q2 2013)

	(A)		(B)		
	Settlements		Tier1 capital Q2 2013 (from FDIC)		(B)/(A)
	\$ billions	%	\$ billions		%
Bank of America	32.33	28.30	157		20.60
JPMorgan	14.43	12.63	164		8.80
BNP Paribas	8.90	7.79	100		8.90
Citigroup	7.09	6.21	144		4.92
UBS	5.53	4.84	42		13.15
Deutsche Bank	3.60	3.15	71		5.07
HSBC Holdings	2.72	2.38	150		1.81
Wells Fargo	1.76	1.54	133		1.33
Goldman Sachs	1.75	1.54	71		2.47
RBS	0.98	0.86	89		1.10
Barclays	0.75	0.66	80		0.94
Societe General	0.70	0.61	52		1.35
American Express	0.19	0.16			
Not allocated	33.50	29.32			
Total	114.25		1253		9.12

Source: own calculations on data derived from official announcements on the web (see the Appendix for details).

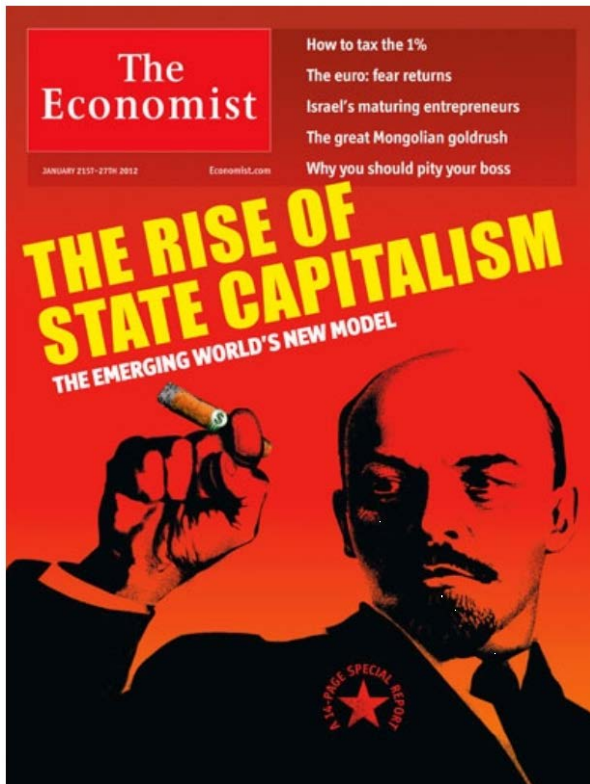
Table 3. Misdoings related regulatory fines/settlements by allegation (Jan 2010 – Oct 2014)

	\$ billions	%
misselling MBS to investors	39.05	34.18
discriminatory lending + foreclosure abuses + fraud on consumers	35.10	30.72
misselling MBS to Fannie Mae/Freddie Mac	18.33	16.04
breaking US sanctions + money-laundering + fraudulent tax shelters	12.25	10.73
rigging markets (interest rates; forex; municipal bonds; electricity)	6.85	6.00
others	2.67	2.34

Source: own grouping on data derived from official announcements on the web (see the Appendix for details).

Which channels? Which ways out? – 3

❑ Variety of capitalism: Are the poor lazy? Are the bankers “bangsters”?:



State capitalism is distorted by pervasive political interference – because of the remaining elements of command economy – and cannot insure individual freedom

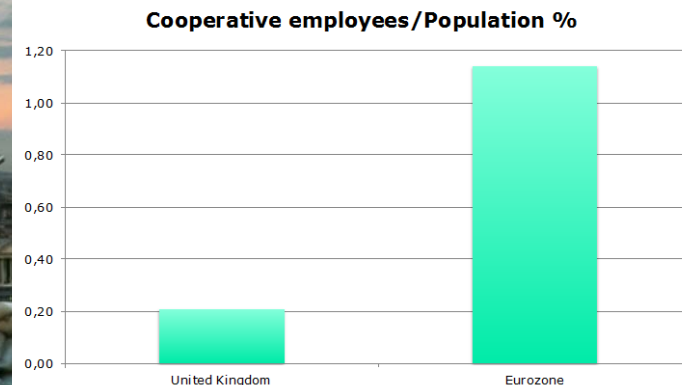
Being based only on individualistic motivations (utility, profit, rent), financial capitalism is unstable, it builds bubbles in the prices of assets, over-indebtedness, global imbalances; it destroys social capital.



Continental European capitalism differs from both models: it secures individual freedom but it features mechanisms aimed to common goods as well, e.g.:

- relatively large **welfare state**;
- large **role of the no-profit sector**;
- vast **incidence of cooperatives** (mission to serve communities);
- **Social market economy** (in some countries);
- high **frequency of family businesses** (with longer-term/community sensitive objectives);
- size and nature of **trade unions**

Importance of Cooperative: Eurozone vs. UK



Which channels? Which ways out? – 4

□ Financial capitalism vs. productive capitalism:

from Philippon-Reschef, 2009

Figure 11: Historical Excess Wage in the Financial Sector



Which channels? Which ways out? – 5

❑ Replacing the market fundamentalism ideology not capitalism:

- Working on the “élites” theory may be fruitful but that’s exactly where also Keynes and, after all, FDR stood (Rahman, 2012, Democracy and Productivity: The Glass-Steagall Act and the Shifting Discourse of Financial Regulation).

❑ Any hope from “integral sustainability”?

- And, maybe, we should also remind that a big challenge to the financial capitalism ideology comes from the issue of sustainability;
- Not by chance, various criticisms came out, especially in the US, after Pope Francis recently sent out his encyclical letter “Laudato si’” (*Thou be lauded*) invoking the spirit of St Francis of Assisi and proposing the idea of “Integral sustainability”;
- In other words, the concept of Social Sustainability (caring for the poor) and that of Environmental Sustainability (caring for life on planet Earth) are intertwined: *There will be no peace between humans and nature if there is no peace between human and human!*