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INEQUALITY

A Dialogue for the Americas

by Kirsten Sehnbruch and Harley Shaiken

Inequality has emerged as a global crisis. “The problem is not only that the top income groups are getting a larger share of the economic pie,” Joseph Stiglitz writes, “but also that those in the middle are not sharing in economic growth, while in many countries poverty is increasing.”

Recent data in the United States has been striking. The country seems to be experiencing what one might call hyper-inequality: 93 percent of all income growth in 2010 flowed to the top 1 percent, with 37 percent of all income gains captured by the top .01 percent or 15,000 households. Meanwhile, median real family income slid almost 9 percent from 2000 to 2011.

The result of this dismal state of affairs, Stiglitz points out, is that “equality of opportunity has been exposed as a myth,” and the social mobility that this opportunity makes possible — the American dream — has been undermined. “Intergenerational mobility in the United States is now poor by international standards,” notes Harvard economist Larry Summers, “and, probably for the first time in U.S. history, is no longer improving.” Moreover, a sharp rise in inequality can depress broadly based demand, limiting growth. “Research by economists at the IMF,” *The Economist* magazine reports, “suggests that income inequality slows growth, causes financial crises and weakens demand.”

This extreme economic polarization can have corrosive political consequences across the globe. “Eventually, faith in democracy and the market economy will erode,” Stiglitz warns, “and the legitimacy of existing institutions and arrangements will be called into question.” The Economic Commission on Latin America and the Caribbean (ECLAC) reported that in 2011 “six out of every 10 Latin Americans reported having very little or no trust in political and state institutions; this is a very high percentage” linked to “high levels of inequality.”

Income inequality “remains one of the region’s main challenges,” according to ECLAC, despite modest progress in the last decade. “On average, the richest 10 percent of the Latin American population receives 32 percent of total income, while the poorest 40 percent receive just 15

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A homeless man in San Francisco.
Photo by Paula Steele.

percent of income” according to the most recent data for 18 countries. Ironically, the U.S. has now surpassed some Latin American countries such as Argentina in terms of unequal income distribution.

Since the challenges of inequality span the Americas, the Center for Latin American Studies (CLAS) sought to initiate a discussion across the hemisphere. In collaboration with the Universidad de Chile, CLAS held a series of four colloquia entitled “Inequality: A Dialogue for the Americas,” which used intercontinental video-conferencing to bring together scholars and policy makers from the United States and Latin America. The discussions were broadcast live to the Universidad de Chile in Santiago, where faculty members and students participated in the debate, and to Medellín, Colombia, where Sergio Fajardo, the governor of Antioquia province, was involved.

In the first colloquium, Chilean President Ricardo Lagos (2000-06) and UC Berkeley Professor of Public Policy Robert Reich contributed original perspectives and extensive policy experience to the discussion. Professor Reich argued that after World War II, a growing population and rapidly rising productivity fueled an expanding economy for three decades. These gains were broadly shared and allowed new investments in education and a social safety net. According to Reich, these programs acted like “trampolines,” propelling many working families into the middle class.

As the 1970s drew to a close, these economic gains began eroding, and for many, the economy took a “giant U-turn.” Despite economic growth and rising productivity, almost all the gains flowed to those at the very top, Reich maintained. In fact, real wages for large parts of society have either stagnated or even decreased since then, diminishing purchasing power and contributing to the economic crisis.

While inequality in the United States has recently become an issue, Latin America has long been plagued with highly unequal income distribution. Poverty, however, historically has been a more pressing concern, President Lagos argued.

Despite the lack of focus on inequality, between 2002 and 2007, the Gini coefficient, the indicator most commonly used to measure the distribution of income, declined moderately in 14 out of 17 Latin American countries. Recent studies argue that this trend can be attributed to both a reduction of the skill premium captured by highly qualified workers and to regional increases in social spending, particularly through conditional cash transfer programs to the poor.

Nonetheless, inequality remains a potent political issue and a critical social and economic question. President Lagos emphasized that once per capita income reaches a threshold of approximately US\$20,000 per year (at purchasing power

parity), improvements in social indicators such as life expectancy, infant mortality, and crime rates are strongly associated with more equal distribution of income. Since several countries in the region are expected to cross this threshold within the next five to eight years, improving income distribution will become the region’s new priority. Therefore, the appropriate measure of development will no longer be average per capita income, but rather “how this income is distributed.”

While Latin America has seen modest improvement on measures of inequality in recent years, studies of income distribution in the United States by Berkeley professor Emmanuel Saez show a sharp increase in earnings of the top 1 percent and 0.1 percent since the 1980s, which reflect that country’s worsening income distribution. This analysis is based on tax data, which is both reliable and precise. In Latin America, by contrast, tax data is not readily available to analysts. Instead, researchers use household survey data, which is known to significantly underestimate the income of the highest percentiles. This means that although official Gini indicators have improved, it is likely that Latin American tax data would show similar trends to those observed in the United States.

In the second colloquium, professors Bradford DeLong from UC Berkeley and Oscar Landerretche from the Universidad de Chile discussed the economic aspects of inequality. DeLong outlined three fundamental dimensions of inequality: first, global and historical inequalities between nations, which generally reflect whether or not a country industrialized early; second, inequality between persons, which principally reflects differences in educational opportunities; and third, the explosive increase of income among the top 1 percent of earners. DeLong argued that recent developments in the United States reflect the distancing of a select upper-class from the rest of society, which could lead to a plutocracy that erodes the democratic ideal of equity. “Political decisions helped to create the super-elite in the first place,” former Financial Times journalist Chrystia Freeland observes, “and as the economic might of the super-elite grows, so does its political muscle.”

Overall, the United States has witnessed a major transfer of income from wages and salaries to profits, particularly over the last three decades. In 2012, the St. Louis Federal Reserve reported that wages and salaries accounted for 43.5 percent of the gross domestic product (GDP), the smallest share since World War II, down from a peak of 53.5 percent in 1969. In contrast, after-tax corporate profits reached 11.1 percent of GDP last year, the largest share since World War II.



Photo by Jim Block.

Ricardo Lagos and Robert Reich draw a packed house at the Berkeley Law School.

Professor Landerretche brought the perspective of developing countries to the discussion, analyzing income distribution from five different angles: the distribution of productivity and education; the distribution of negotiating capacity; the productive structure of the country; its fiscal policies; and finally, direct transfers and acquired social rights. Landerretche recognized that Chile has not made significant progress in any of these dimensions, which leads to the important question: Why aren't aggressive public policies enacted to tackle inequality? He explained that in every one of these five dimensions powerful interest groups would lose out if more aggressive structural reforms were implemented. Therefore, elite groups are motivated to put up a highly coordinated resistance to any change in the status quo. On the other hand, the people who would gain from such policies are not organized and do not form an effective pressure group.

The arguments of professors DeLong and Landerretche both lead to a crucial conclusion: behind the economics of policymaking lies the distribution of political power. The third colloquium in the series focused on the politics of inequality by bringing together professors Paul Pierson from UC Berkeley and Daniel Hojman from the Universidad de Chile.

Taking up the theme raised by DeLong, Pierson, a political scientist, began by asking whether the United States is turning into an oligarchy. The evidence he offered in support of this thesis was striking. First, the 15,000 richest households in the United States have increased their income by 600 percent during recent decades. The inequality generated by these gains is a historical novelty, and its long-term political consequences remain unknown. Second, a small group of people invest large sums in financing political campaigns in the United States, which suggests an outside influence on politics. As Freeland writes, "The feedback loop between money, politics, and ideas is both cause and consequence of the rise of the super-elite." Finally, the United States increasingly resembles an extractive society, similar to what has traditionally been seen in Latin American countries, where powerful minorities control the political and economic system and extract resources from both the country and its people for their own benefit.

Professor Hojman took up Paul Pierson's arguments, adding that high inequality erodes the public good, which in turn leads to social unease, illustrated by the increased activity of social movements across Latin America, not least in Chile, where the student movement firmly put the issue of inequality on the public policy agenda.

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SPEAKERS IN THE SERIES
 "INEQUALITY: A DIALOGUE FOR THE AMERICAS"

Ricardo Lagos was president of Chile from 2000 to 2006 and is president of the Fundación Democracia y Desarrollo.

Robert Reich is the Chancellor's Professor of Public Policy at UC Berkeley.

Bradford DeLong is a professor of Economics at UC Berkeley.

Oscar Landerretche is the director of the School of Economics and Business at the Universidad de Chile.

Paul Pierson is the John Gross Professor of Political Science at UC Berkeley.

Daniel Hojman is a professor of Economics at the Universidad de Chile and at Harvard University's Kennedy School of Government.

Emmanuel Saez is the E. Morris Cox Professor of Economics and the director of the Center for Equitable Growth at UC Berkeley.

Sergio Fajardo Valderrama is the governor of Antioquia, Colombia.

Hojman attributed the political unease in Chile to several factors: while inequality increased significantly during the dictatorship, subsequent democratic governments led by the center-left Concertación coalition did not manage to reverse this trend in a significant way. In addition, the market is the main mechanism that distributes resources and governs social interaction in Chile. Again, this is an inheritance from the dictatorship that the Concertación could only moderate with increased social expenditure. The legacy of the dictatorship therefore produced a significant concentration of wealth and political power in the hands of a rich oligarchy. In addition, these elites are geographically isolated from the general population, further contributing to their political insularity. The only factor that has to some extent relieved social unease and counteracted this political polarization is the increase in consumption produced by relatively high levels of economic growth. Lower- and middle-income families have begun to satisfy their basic needs since the transition to democracy. While economic growth in Chile has certainly not been redistributive, it has at least increased everyone's income.

In the final colloquium, Economics professor Emmanuel Saez, who directs the Center for Equitable Growth at UC Berkeley, engaged with Governor Sergio Fajardo on the issues that inequality raises from different, though complementary, perspectives. Saez presented a broad overview of his path-breaking research on income inequality and put these findings in historical perspective. He compared the sharp rise of pre-tax income inequality in the United States over the past three decades to what the country experienced in the early 1900s, the Gilded Age. Overall, he pointed out that public policy — particularly on taxes — was a key determinant in exacerbating U.S. income inequality.

Saez presented a graph that showed U.S. income inequality surpassing that of Argentina between 2000 and 2010 and approaching that of Colombia, one of the most unequal countries in Latin America.

As governor of Antioquia, the most unequal province in Colombia, Fajardo has put inequality at the top of his agenda and laid out the importance of addressing it in a comprehensive way. For him, education is a central component of any meaningful, long-term change. Fajardo emphasized that progress in education requires major improvements in infrastructure, schools, technology, culture, and the state. While well aware of the enormity of the challenge, Fajardo viewed it as critical and not insurmountable. He brings to the task a highly-regarded track record as mayor of Medellín, where he was able to enact innovative reforms in a very difficult context.

One conclusion to be drawn from these colloquia is the striking parallel between the United States and Latin America when one compares both the causes of inequality and its consequences. As the colloquia participants explained, the concentration of economic power has led to the concentration of political power in both regions. In turn, this political power has perpetuated the vicious circle of inequality. The United States has traditionally tolerated higher levels of income inequality than other developed countries in exchange for the promise of earnings growth, while Latin America has simply suffered the consequences of its historically high levels of inequality. Effectively addressing this issue could prove critical for economic success and democratic values going forward.

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Harley Shaiken is the Class of 1930 Professor of Letters and Science and chair of the Center for Latin American Studies. He is a faculty member in the Graduate School of Education and the Department of Geography.