


Opinions

April 30, 2014

The World Economy in the Era of Rising Inequality



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During his State of the Union Address on January 28, 2014, President Obama put forth resolving economic inequality as the nation's priority agenda and introduced proposals to raise minimum wage and improvement of retirement pension. Christine Lagarde, managing director of International Monetary Fund, also pointed out in her speech on February 2, 2014, that "economists have underestimated the importance of inequality," warning that "a severely skewed income distribution harms the pace and sustainability of growth over the longer term." So why has inequality, again, become a global issue?

Inequality is a human condition closest to the state of nature. From birth some are endowed with certain gifts while others

may be afflicted with disabilities. One cannot choose one's parents or mother country. Everything in the state of nature has an unequal starting point owing to destiny. Wild animals that we see on nature documentaries find equilibrium amidst this inequality, but the human race has no tolerance for such conditions.

One of the axes of the discourse on economic inequality is “efficiency” and “fairness”. The operating principles for our capitalistic system underscore “competition”. It has been demonstrated over the course of several decades that capitalism's competitive regime is more “efficient” than the socialist regime with which equality was comparatively emphasized further. So far, countries that have adopted the capitalist system have had a more rapid growth compared to socialist countries, and based on such fast growth, they have been capable of expanding welfare. However the question as to whether this race, where the starting point for each individual differs, is truly “fair” still remains. Moreover, the discourse has thus far been focused on achieving ethical fairness at the cost of economic efficiency. The philosopher John Rawls' ethical perspective was that a society where even the worst off member is guaranteed the fundamentals to lead a humane life by maximizing the minimum rank of items (maxmin) is a just society. This may be regarded as the Maginot Line that our civilized society can expect from welfare.

One development economics perspective on economic inequality is the famous inverted U hypothesis of Simon Kuznets. According to this theory, the degree of inequality is low at underdeveloped stage and reaches its peak at the developing stage and moderates again at the “developed” stage. This theory seemed persuasive considering how Latin America, during its developing stages in the 70s and 80s, had a high degree of inequality and most developed European countries have low degree of inequality. Also, according to this theory, the issue of economic inequality was a by-product of a development process and there was the expectation that it could be solved once a country attains the “developed” stage.

However, a new kind of concern has arisen recently in economics with respect to inequality. It postulates that inequality is not only an issue of fairness but it also hurts efficiency; it does not become resolved automatically in step with economic development. Although there has been many mixed results with respect to the effects of inequality on economic growth, the empirical research, verified through the recently accumulated data, tend to show all that the worsening of inequality hampers economic growth. The IMF and the KIEP have also reported that their studies showed that the higher the degree of economic

inequality as expressed by the Gini index, the more negative effect it has on the economy. The worsening of the economic inequality not only damages harmony among the members of the society and increases political burden, but it also could increase economic costs. Moreover, some studies seek the cause of the subprime crisis in the heightening of degree of inequality in income, and assert that income inequality tends to lead to banking crisis. According to these hypotheses, the problems of efficiency and fairness are not conflicting but are rather in the same vein. The results of the research suggest that alleviating the degree of economic inequality is not only desirable for a fair society, but it can also raise economic efficiency.

Another observation receiving attention from economists is that the degree of inequality does not become resolved spontaneously in accordance with economic development. Over the past decades, the degree of income inequality in the world economy has increased on average. It deteriorated in developed countries that are relatively better off, and it became even worse in developing countries that were relatively worse off. It is only just a few European countries with sound welfare systems, such as Norway, Denmark, and Sweden that maintain the acceptable degree of income inequality.

This makes the issue even clearer. To sum up, the degree of income inequality has been worsening over the past decades in both developed and developing countries alike, hindering economic progress. It has become particularly severer after going through the full onset of the 2009 global crisis, causing the decline in domestic consumption and delay in economic recovery. Now, it has become a situation where it is not only a matter of fairness, but also one that cannot be overlooked for the sake of national economy. This is why President Obama and Director Lagarde are touting resolution of economic inequality as this year's main economic issue.

The global economy is rapidly integrating due to the development of transportation technology and IT. The increase in the volume of international trade is accelerating and the international financial integration is also progressing rapidly. One country's problem is no longer isolated to that country alone. It now affects other countries and regions through various channels. Now that we know that the ailment afflicting the global economy is income inequality, it is high time to research and discuss its cure and near-possible preventive measures. I hope that countries around the world will work together through international economic cooperative bodies, such as the G20, and that reasonable solution could be found.

Through this, the global economy will be able to escape from the long economic downturn that followed the global financial crisis and laid the groundwork for sustainable growth. 