
***Development and Change* Distinguished Lecture 2018**

Behind the Seven Veils of Inequality. What if it's all about the Struggle within just One Half of the Population over just One Half of the National Income?**José Gabriel Palma**

ABSTRACT

This article addresses three main issues: why there is such a huge diversity of disposable income inequality across the world, why there is such a deterioration of market inequality among countries of the Organization for Economic Cooperation and Development (OECD), and why inequality seems to move in 'waves'. There are many underlying questions: does diversity reflect a variety of fundamentals, or a multiplicity of power structures and choice? Is rising market inequality the product of somehow 'exogenous' factors (e.g., $r > g$), or of complex interactions between political settlements and market failures? How do we get through the veils obscuring these interactions and distorting our vision of the often self-constructed nature of inequality? Has neoliberal globalization broadened the scope for 'distributional failures' by, for example, triggering a process of 'reverse catching-up' in the OECD, so that highly unequal middle-income countries like those in Latin America now embody the shape of things to come? Are we all converging towards features such as mobile élites creaming off the rewards of economic growth, and 'magic realist' politics that lack self-respect if not originality? Should I say, 'Welcome to the Third World'? In this paper I also develop a new approach for examining and measuring inequality (distance from distributive targets), and a new concept of 'distributional waves'. The article concludes that, to understand current distributive dynamics, what matters is to comprehend the forces determining the share of the rich — and, in terms of growth, what they choose to do with it (and how they are allowed to do it).

This article is the updated and expanded version of a paper that was first presented at the 2018 Development Studies Association Conference in Manchester, UK, as the *Development and Change* Distinguished Lecture. I am grateful to Alex Cobham and Andy Sumner for their contributions to my work on inequality, and also to many friends and colleagues, some of whom are mentioned in the Acknowledgements at the end of this essay. Interactions at an early stage in my career with Carlos Díaz-Alejandro, Tony Atkinson, Nicholas Kaldor, Joan Robinson, Joseph Stiglitz, and — especially — Charles Kindleberger were a great inspiration. Finally, above all, I would like to thank Ignês Sodré: as in *Far From the Madding Crowd*, whenever I looked up from the fire, there were you. The article was written while trying to cope with the long illness and death of a close relative, Maria Penco; I dedicate it to her.

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Inequality is a choice
Joseph Stiglitz

I am my choices
Jean-Paul Sartre

INTRODUCTION

Perhaps one of the most important analytical failings of current economic theory (despite recent significant progress) is our modest understanding of inequality, especially why there is such a huge diversity of inequality across the world, and why there has been such an enormous deterioration of market inequality among the OECD countries. Indeed, Krugman (2011) identified the latter as one of the two greatest analytical challenges today.¹ This lecture and article attempt to address these conundrums: is the vast diversity of disposable income inequality a reflection of a variety of fundamentals? Or is it mostly the outcome of a multiplicity of power structures and choice? Are contemporary patterns of rising market inequality the product of somehow ‘exogenous’ factors (e.g., stocks of assets, such as human capital and knowledge, and their degree of adaptability to the new technological paradigm, the impact of some ‘fundamental force of divergence’, such as $r > g$, or a new cycle of the ‘Kuznets waves’);² or are these patterns mainly the outcome of complex interactions between political settlements and market failures? And if the latter, how do we get through the set of veils which typically obscure these interactions, and could easily distort our vision of the often self-constructed nature of inequality? Finally, has the current neoliberal era broadened the scope for greater inequality by exacerbating ‘distributional failures’ around the world?

In order to address these questions, I shall look at nine distributional stylized facts of the current spectrum of inequality, five relating to disposable income inequality, and four to market inequality. After identifying several layers of misunderstanding, I shall categorize seven types of ‘distributional failures’, three relating to the former, and four to the latter. On the distribution of disposable income, I suggest that diversity mostly reflects a variety of outcomes in the distributional struggle in just one half of the population, over just one half of the national income, and that these outcomes can be broadly classified in seven categories of inequality.

1. Latin America’s perennial underperformance is the other (I give a tentative answer to this conundrum below). For recent contributions, see Atkinson (2015); Bourguignon (2015); Galbraith (2016); Milanovic (2016); Ocampo (2019); Palma (2011, 2016); Piketty (2014); Scheidel (2017); Taylor (forthcoming 2019).

2. r = return on capital; g = growth of income.

Regarding market inequality, I suggest that globalization and financialization³ triggered a new process of ‘unequalization’ across the OECD, which resembles a ‘reverse catching-up’ with highly unequal middle-income countries (such as those in Latin America), in the sense that the latter countries now seem to show the advanced ones the shape of things to come. We are all indeed converging in market inequality, but we are converging towards features typical of highly unequal countries, such as mobile élites creaming off the rewards of economic growth, and ‘magic realist’ politics that lack self-respect if not originality. I shall conclude that in order to understand distributive dynamics in either type of inequality, what really matters is to comprehend the share of the rich — and, in terms of economic growth, what they choose to do with that share, and how they are allowed to do it.

I also put forward a new approach for examining and measuring inequality — distance from distributive challenges — that is closely related to the index I suggested in Palma (2011) which was later christened the ‘Palma ratio’ by Alex Cobham and Andy Sumner, and I develop a new concept of ‘distributional waves’.⁴ I shall conclude that inequality is a particularly complex (and surely over-determined) phenomenon, which is often blurred by layers of distorting veils which sometimes make it resemble a hall of mirrors. These veils serve to conceal its frequent arbitrariness, and (in some cases) help in its idealization, and (in others) in its demonization. If this essay helps to make inequality more transparent by clarifying some of these layers of possible misunderstanding, it may hopefully help us take more responsibility as society for our distributional choices.⁵

THE DISTRIBUTION OF DISPOSABLE INCOME ACROSS THE WORLD

In examining the distribution of disposable income across the world according to survey data, five stylized facts and three ‘distributional failures’ can be identified.⁶

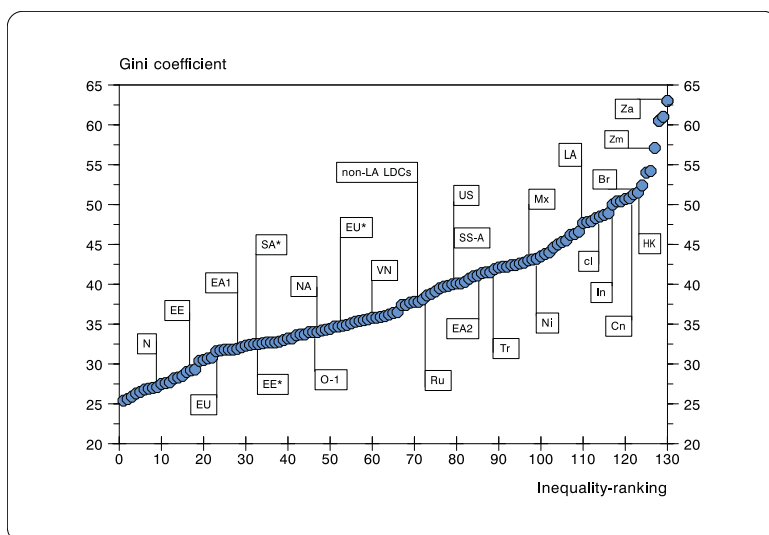
3. By ‘financialization’ I understand the rise in size and dominance of the financial sector relative to the non-financial sector, as well as the diversification towards financial activities in non-financial corporations.

4. See Cobham and Sumner (2013), and Cobham, Schlogl and Sumner (2015); see also Chang (2014); Green (2012). Following the logic of the Palma ratio, the World Bank (2016) coined a related statistic, the ‘Palma premium’ — an index resembling the first derivative of the Palma ratio (as it primarily tells us about its direction of change).

5. This article contains a large number of illustrative graphics: for colour renditions of all the Figures, the reader is directed to the online version of the article.

6. On problems with household surveys, see Meyer et al. (2015).

Figure 1. Gini Coefficient of the Distribution of Disposable Income in 130 countries, c. 2016



Notes:

The statistic used to measure centrality in regions is the harmonic mean. For the non-specialist, this is one of the three Pythagorean means. It is more appropriate for the average of ratios as it mitigates the impact of outliers; it also contains more information than the median. It is the reciprocal of the arithmetic mean of the reciprocals.

Country abbreviations are those for internet domains:

Br = Brazil; **cl** = Chile; **Cn** = China; **EA1** = Korea and Taiwan; **EA2** = Indonesia, Malaysia and Thailand; **EE** = Eastern Europe with GDP per capita above US\$ 20,000 (PPP); **EE*** = those below that; **EU*** = Mediterranean EU; **EU** = rest of Continental Europe; **HK** = Hong-Kong; **In** = India; **LA** = Latin America; **LDCs** = developing countries; **Mx** = Mexico; **N** = Nordic countries; **NA** = North Africa; **Ni** = Nigeria; **O-1** = non-US Anglophone OECD; **Ru** = Russia; **SA*** = South Asia, excluding India; **SS-A** = Sub-Saharan Africa; **Tr** = Turkey; **US** = United States; **VN** = Vietnam; **Za** = South Africa; and **Zm** = Zambia.

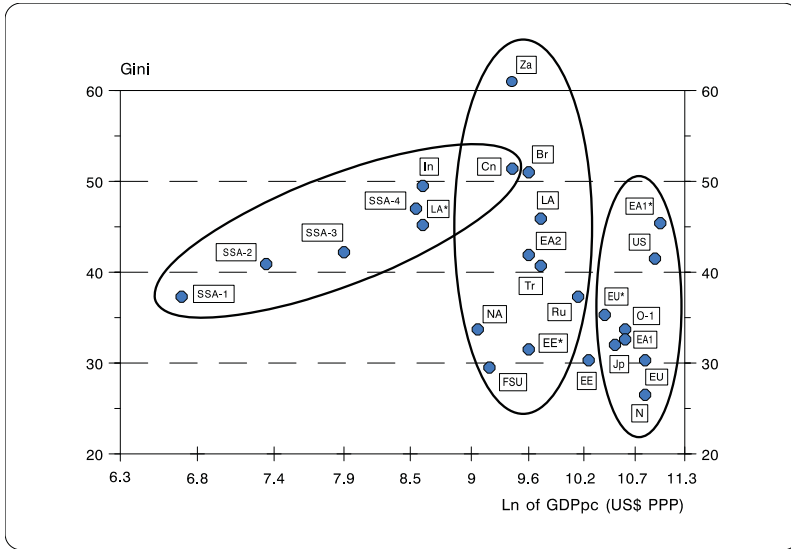
Sources: see Appendix 1.

Stylized Fact 1.1: Inequality is highly unequal across countries

This is the best known of the stylized facts, with some countries posting a disposable income Gini below 25, while for others the figure is nearly 65. In terms of the Palma ratio, the range spans from below 1 to 7. Figure 1 highlights this using the traditional Gini. As suggested above, the question that arises is whether this multiplicity of outcomes is the result of a ‘fundamentals-at-work’ scenario via fairly deterministic cause–effect interactions (such as Piketty’s neoclassical ‘ $r > g$ ’), or whether the diversity is mainly the outcome of different interactions between political settlements and market failures.⁷

7. Piketty (in his otherwise superb 2014 book) comes down on the side of the former, but later he argues that other (endogenous) factors may be more plausible explanations of inequality.

Figure 2. *The Geography of Inequality: Gini of Disposable Income and Log of GDP pc, c. 2016*



Notes:

Acronyms as above, and **FSU** = Former Soviet Union (excluding Russia); **Jp** = Japan; **LA*** = LA with GDPpc below US\$ 9,000 (PPP); **LA** = those above that; **SSA-1** = SS-A with GDPpc below US\$ 1,000 (PPP); **SSA-2** = those between US\$ 1,000 and US\$ 2,000; **SSA-3** = between US\$ 2,000 and US\$ 3,500; and **SSA-4** = above that.

South Africa (Gini = 63) is also a proxy for Botswana and Namibia.

The range of the horizontal axis is that of the sample. When I analyse income distribution across countries from the perspective of their GDPpc, I do so simply as a mechanism for visualizing the geometry of within-country inequality across the world; i.e., it is just a cross-sectional *description* of cross-country differences in inequality, when characterized by GDPpc.

Sources: see Appendix 1; and PWT (2018).

Stylized Fact 1.2: Inequality is particularly disparate among middle-income countries, with some increasing diversity also found among high-income countries

Figure 2 shows the above distributional diversity when categorized by GDP per capita (GDPpc). The Figure confirms that middle-income countries are

He explains that although he does not actually believe in the deterministic neoclassical model he uses in the book, this 'is [just] a language that is important to use' (see *Potemkin Review*, 2014: 6). Unfortunately, his explanation of why it is so important to use a Ptolemaic language — such as the now obsolete neoclassical theory of factor shares of the Solow–Swan 1950s variety — is not convincing. Despite this ambiguity, his analysis of inequality makes at least three important contributions: it helps us to learn from history, it shifts the focus to capital, and it provides much needed new data. For more on this, see Appendix 2 below.

found across the whole distributional range (from Slovenia, 25, to South Africa, 63) as shown in the first vertical ellipse; so are high-income countries (from Iceland, 26, to Hong Kong, 52). It seems that this alone reveals a lot of choice. The distributional geometry of low-income countries is different (45-degree-angled ellipse), as inequality trends move upward vis-à-vis GDPpc from Mali and Liberia (33), to Zambia (57). This increasing trend is followed by India, lower-middle-income Latin America and China.

The huge middle-income diversity indicates that higher GDPpc countries are more able (and willing) to take advantage of the distributional range at their disposal — for better or for worse. This casts doubt not only on the Kuznets' 'Inverted-U', but also on deterministic theories — typical of the earlier Washington Consensus, although still influencing policy — which purport to explain why middle-income countries are bound to be unequal. These theories advocate patience and a hands-off attitude, with 'premature' falls in inequality dismissed as unsustainable, even counterproductive. This multiplicity of middle-income outcomes is highlighted by the contrast between high-inequality Southern Africa, Latin America, India and China, and low-inequality Eastern Europe and Former Soviet Union — although in the latter, oligarchs are trying to 'modernize' inequality.⁸ It also highlights the contrast between China and India, and low-inequality earlier East Asian industrializers, such as Korea and Taiwan.

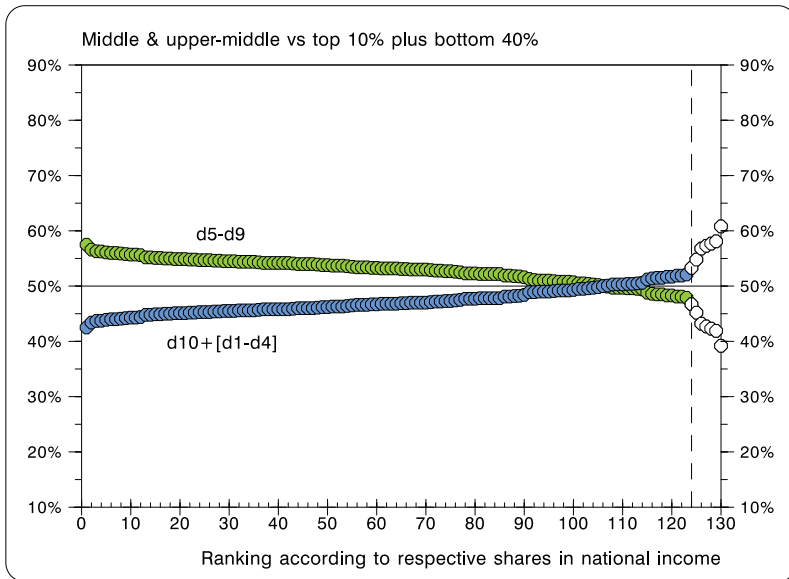
Paradoxically, some of the worst middle-income inequality appears in countries which have seen a recent consolidation of democracy, led by 'centre-left' coalitions (such as Latin America and South Africa) — countries where democracy has been achieved but is yet to be accomplished. Although many institutions have changed, the narrow interests of the élite have not. The comparative advantage of these oligarchies lies precisely in being able to use different institutions to achieve their fairly immutable goals, in part by co-opting key new members. Few have shown such skills for the 'persistence of elites' despite institutional change. The 'iron law of oligarchies' rules: dysfunctional institutions tend to rebuild (Acemoglu and Robinson, 2006).⁹

In turn, the growing spectrum of disposable income inequality among high-income countries (despite their convergence in terms of market inequality; see below) highlights the contrast between those defending pre-neoliberal reforms achievements (e.g., Nordic countries and some in Europe, both East and West), and those happier to sail along on unequalizing winds (e.g., Anglophone countries, Hong Kong and Singapore).

8. The oil-producing Middle East (for which no data are available) is likely to share the inequality heights of Southern Africa.

9. For an analysis of the changing strategies followed by the Chilean élite to accomplish this, see Palma (2011, Appendix 1). Had this élite shown the same skills in economic affairs, the country would not have been stuck in its middle-income trap for as long as it has been (Palma, 2010).

Figure 3. Percentage of Income Appropriated by Two Halves of the Populations, c. 2016



Notes:

d = decile.

Countries at the tail-end are from LA and Southern Africa.

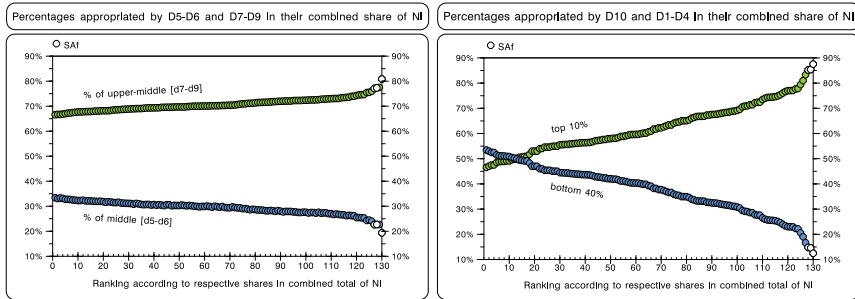
Sources: see Appendix 1.

Stylized Fact 1.3: The broad spectrum of cross-country distributional diversity suddenly changes when each country's population is divided into halves: the middle and upper-middle (deciles 5–9), and the top and bottom (deciles 10 and 1–4)

This stylized fact refers to the huge contrast between the multiplicity of outcomes when inequality refers to *the whole population* (as in the Gini above), and when it refers to the income shares of two halves of the population. This is clearly illustrated by Figure 3. The distributional contrast between Figure 3 and Figures 1 and 2 is remarkable. The diversity of the whole (Gini) turns into an amazing uniformity of the two halves! Furthermore, they divide the national income in a fairly 'equitable' way, getting roughly half each. Surprisingly, no-one seems to have noticed this before my previous work (e.g., Palma, 2006, 2011, 2016a).¹⁰ The exceptions to this rule, as always, are just a small number of countries in Latin America and Southern Africa.

10. Although, inevitably, one or two experts are now insisting that they knew all about it: they just forgot to mention it in their work. This common phenomenon is called 'hindsight bias'.

Figure 4. Percentages of Income Appropriated by Different Deciles



Note:
SAf = Southern Africa.
Sources: see Appendix 1.

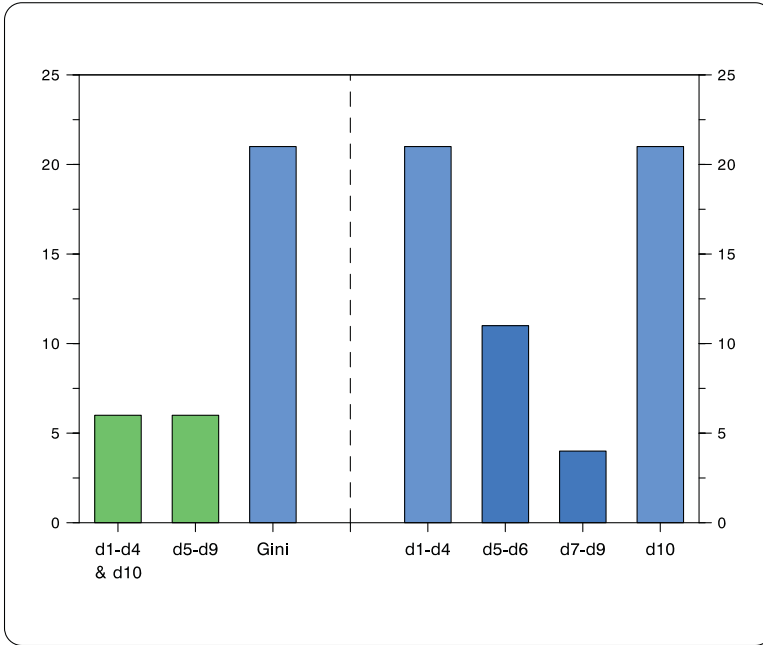
What is implied by this contrast between the whole and the halves — a first layer of possible misunderstanding — is that the diversity of the former must emerge from what happens distributionally *within* these two halves. That is, it must reflect the way in which each half divides its share among its members.

Stylized Fact 1.4: Although both halves of the population tend to get a similar income share across the world (about half), they divide it among their own constituents very differently

There are three aspects to this stylized fact. The first (we might call it ‘4a’) concerns the contrast between the *homogeneous* middle and upper-middle, and the *heterogeneous* tails. While D5–D9 distributes its half of the income pie uniformly between the middle (D5–D6) and the upper-middle (D7–D9), the opposite is the case for the top and bottom deciles. The left-hand panel of Figure 4 shows that (except for Southern Africa) there is little variation in how D5–D9 splits its share between its middle and upper-middle strata. The right-hand panel, meanwhile, indicates a huge diversity of outcomes in the distributional struggle between top and bottom: ranging from D10 getting *less* than D1–D4 (Finland), to D10 getting nearly nine-tenths of the combined shares (Southern Africa again . . .). That is, while the homogeneity of D5–D9 as a whole (hereafter — and just for analytical convenience — the ‘administrative classes’) is replicated in its parts, the homogeneity of the combined share of D10 and D1–D4 across the world, instead, becomes highly heterogeneous in terms of what each one gets.

Thus it appears that the diversity of inequalities shown by the Gini is basically a reflection of a tooth-and-nail distributional fight in *just one half* of the population, *for just one half* of the national income. Of all the veils

Figure 5. Coefficient of Variations: Gini, D1–D4 plus D10 vs D5–D9, c. 2016



Note:

Coefficients are multiplied by 100.

Sources: see Appendix 1.

obscuring our vision of inequality, this is probably the one that has led to most misunderstanding.

It seems, then, that the key aim of the administrative classes is to protect (as a group) their overall share of income, while in the other half of the population, the top 10 per cent is bent on enlarging its share at the expense of the bottom 40 per cent. One narrative of this remarkable contrast between the distributional dynamics of these two halves of the population can be found in Appendix 3 where, using simple game theory language, I argue that this contrast between what happens distributionally *within* the middle and upper-middle, and *within* the top and bottom deciles resembles the contrast between ‘coordination’ and ‘anti-coordination’ games. This is confirmed in Figure 5.

While the coefficients of variation of the shares of the two halves *when together* are very low, those of the two components of the tails *when separate* are remarkably high, and much larger than those of the two administrative strata.¹¹ In fact, D10 and D1–D4 individually have a coefficient of variation

11. Cobham et al. (2015) undertake a detailed statistical analysis of the stability of the income share of D5–D9.

that is almost four times larger than when combined.¹² This heterogeneity in the distributional outcomes at the tails is what dominates the Gini, as it ends up having *exactly* the same variability as them — implying that the Gini (despite its supposed statistical properties) turns out to be unmoved by the distributional homogeneity of the middle and upper-middle. That is, by mixing (homogeneous) pears with (heterogeneous) apples the Gini ends up being blind to the homogeneity of one half of the population. By contrast, the Palma ratio, *by design*, only attempts to measure the heterogeneity at the tails — that is, it measures inequality *at source* (see discussion on ‘4c’ below).

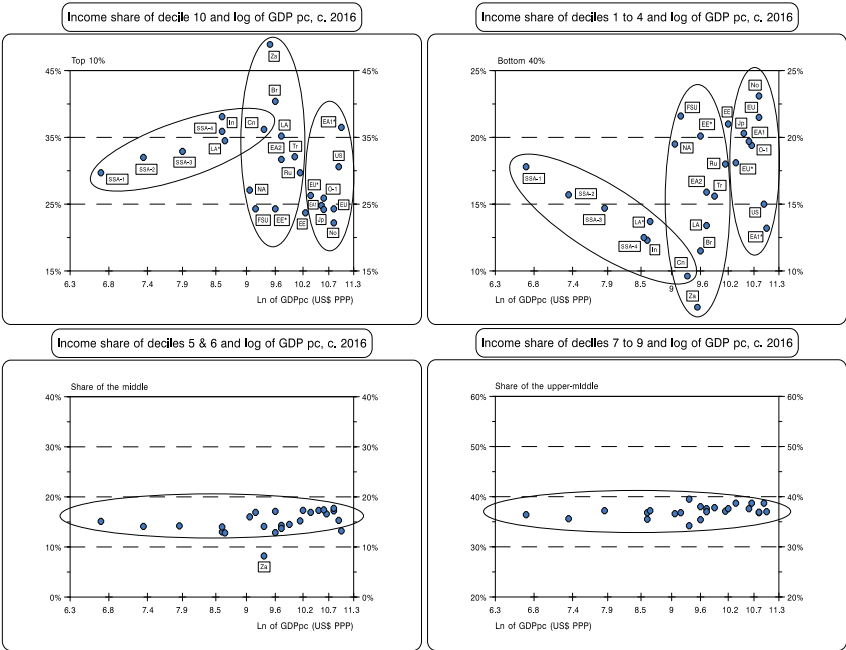
As these phenomena were not known before, the relevant literature — especially the econometric literature — by using indices such as the Gini, has failed to see that the huge diversity of inequality across the world is basically about the many outcomes of the struggle between the top 10 per cent and the bottom 40 per cent. In turn, neoclassical analysts need to explain how is it that if ‘ $r > g$ ’ rules, why would it all be in the tails? Why would this be a ‘fundamental force of divergence’ for only *one half* of the population?¹³

The second part of stylized fact 4 — we can call it ‘4b’ — takes the form of a question: *has the homogeneity of the middle and upper-middle been stable over time?* One controversy that followed my earlier findings was the issue of whether the current distributional homogeneity of D5–D9 has some ‘path-dependent’ roots. Has D5–D9 always been able to appropriate about half of national income — as a sort of ‘right’ — leaving the other half to be contested between D10 and D1–D4? The data available indicate that at least in OECD countries and in some middle-income countries there does seem to be a remarkable stability over time in the share of D5–D9, despite massive upheavals (see Appendix 4 below; see also Palma, 2014a). However, as the Chilean case in Appendix 4 indicates, those in D5–D9 are not immune from major political shocks — there is no ‘lack of history’ here. But, in general, those in D5–D9 are surprisingly successful in fighting for their ‘rightful’ half (irrespective, for example, of the amount and quality of their schooling; see below).

As Tony Atkinson remarked in his comments on a draft of my 2011 paper, another interesting implication of my findings is that if D5–D9 gets half the income, then the Gini is 1.5 times the share of the top 10 per cent, minus 15. In this case it has a maximum of 60, although it may be slightly larger on

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12. In this half of the population (the tails), while the difference between the mean and mode when together is 2.5 times that between mean and median, when separate this multiple jumps to over 9 times for D10 and 11 times for D1–D4. This does not happen in D5–D9, where this multiple is similar whether its two constituents are analysed together or separately.
 13. Perhaps Solow and Swan, by being concerned in their neoclassical (aggregate) production function with capital accumulation and technological progress, forgot all about the administrative classes — which often have little to do with either.

Figure 6. Income Shares and Logs of GDPpc



Note:
Countries and Regions in the bottom panels are the same as in the top. Acronyms as above (countries as internet domains).
Sources: see Appendix 1.

account of inequality within the groups, since this calculation linearizes the Lorenz curve.

The third part of stylized fact 4 (let's call it '4c') concerns heterogeneity at the tails and the Palma ratio. Figure 6 neatly shows the logic of the Palma ratio, which is based on this contrast between the heterogeneity in the top and bottom vs the homogeneity in the middle and upper-middle. Here the shares of the respective four groups are ordered according to GDPpc.

The high degree of homogeneity in the two components of D5–D9 (lower panels) is reflected in the fact that the measures of central tendency in this 130-country sample are almost identical.¹⁴ However, in the

14. For D5–D6, the harmonic mean is 15 per cent, the geometric mean is 15.2 per cent, the arithmetic mean is 15.3 per cent, the median is 15.7 per cent and the mode is 16.4 per cent. For D7–D9, the equivalent figures are 36.9 per cent, 36.9 per cent, 37 per cent, 37.4 per cent and 37.7 per cent, respectively.

top and bottom deciles these are rather different.¹⁵ The coefficients of variation in Figure 5 indicated the same. So, it seems that a schoolteacher, a mid-level civil servant, a young professional, a skilled worker, a middle-manager, or a taxi driver who owns a car, all tend to earn the same as each other across the world — as long as their incomes are normalized by respective GDPpc. That is certainly not true for the top 10 per cent and bottom 40 per cent.

Basically, in unequal middle-income countries, such as those in Latin America, the top 10 per cent has succeeded in getting an income similar *in absolute terms* to their counterparts in rich nations (often by artificially augmenting the value of their marginal productivity, and by directly appropriating a share of the income of others). Meanwhile D5–D9 has done so *in relative terms* (shares of income). The bottom 40 per cent, on the other hand, have an income more akin to the average income in sub-Saharan Africa, in part a result of the inability of labour to claim the value of its marginal productivity due to a lack of property rights over its energy and skills (Pagano, 1997).¹⁶ In other words, in so-called ‘middle-income countries’, only those in the middle have ‘middle-income’ earnings, as the top 10 per cent have prematurely caught up with their rich counterparts, while those in the bottom 40 per cent face a massive uphill struggle *just to get to ‘middle-income’ levels*. Per capita income convergence, therefore, seems far more complex than implied in neoclassical models.¹⁷ In sum, the broad spectrum of disposable income inequality across the world emerges basically from what happens within only one half of the population — the half mainly made up of the capitalist elite and their consiglieres at one end, and workers at the other.

Among its many implications, this finding is relevant, for example, for the debate about the OECD’s ‘disappearing middle’. This debate has confused a declining relative level of welfare among the middle and upper-middle with D5–D9’s share stability (see Appendix 4). The huge increase in the cost of necessities (like health, education and housing), the accumulation of debts, meagre pensions, more regressive taxation, and so on, mean that despite the stability of the income share of D5–D9, this (stable) share is only able to provide a declining level of well-being.

Among the many other issues that need re-examining, the relationship between human capital and income distribution stands out, as *diversity* in

15. See footnote 12 above. Furthermore, since in D10 the mean > median > mode, while in D1–D4 it is the other way round, their distributions are skewed differently — one positively, one negatively. The skew in D5–D6 and D7–D9, instead, is not only very slight, but it also takes the same direction (negative).

16. This also distorts incentives to acquire skills among the bottom 40 per cent. What would be the point of making the effort in unequal middle-income countries if the *additional* output is bound to be appropriated by others?

17. The same is true for productivity convergence, due to huge diversity across sectors within countries (Palma, 2010).

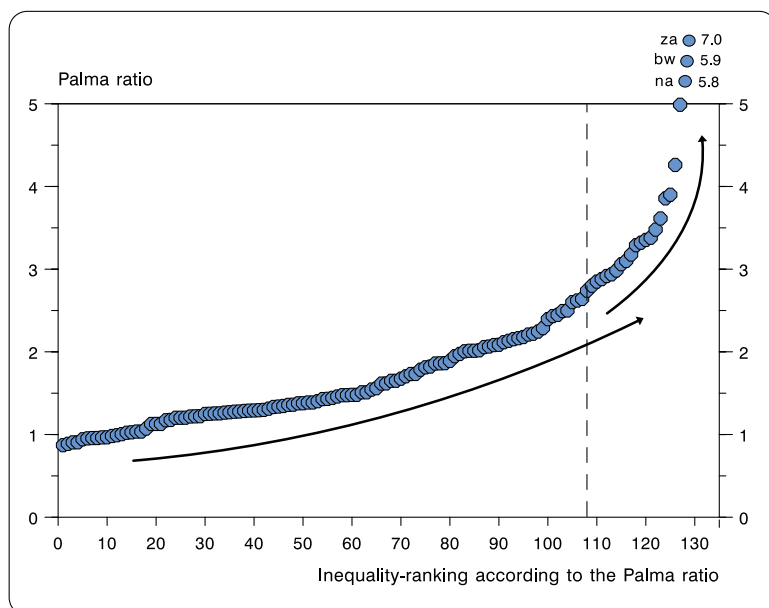
distribution is found among those with *uniformity* in education, and vice versa. While those at the top are able to buy a lot of ‘education’ everywhere, those at the bottom have access to little schooling or education of doubtful quality. However, this educational *uniformity* across the world (the top always having a lot, those at the other end similarly little) is associated with distributional *diversity*. The opposite is the case for D5–D9: although most of the world’s educational diversity (quantity and quality) is found among these deciles, they have *similar* income shares across the world, irrespective of their stock of human capital or any other recurrent factors in neoclassical models.¹⁸

This contrasting scenario in the two halves of the population also opens up huge analytical challenges for the growing econometric literature which tries to ‘explain’ the variance of the Gini. By regressing it in panels against a set of (ever more imaginative) explanatory variables — (hopefully ‘pre-determined’, if not at least weakly exogenous, even Granger causality) — what is ignored is that these variables are bound to relate statistically very differently to what is happening distributionally in the two halves of the population. By using the Gini (or similar) as a dependent variable, these economists are trying to explain *two contrasting distributional dynamics* at once, and with the same set of ‘explanatory’ variables, and this would be a specification error. It’s time to open up the Gini and start peering inside.

A different issue, of course, is whether one should still think of complex, over-determined, and surely ‘open’ subjects, such as inequality, in terms of methodologies that somehow resemble 19th century Newtonian physics — methodologies of mechanical determinism and simple causalities. Inevitably, the analysis that emerges from such econometrics is typified by ‘antecedent causation’ and ‘inert consequences’. The priority of exogenous over endogenous factors is established (via *unidirectional* cause–effect interactions), thus almost metaphysically separating the two sides of the opposition and thereby losing the notion of movement through the dynamics of the interaction and contradictions between them. Furthermore, any factor that may interact with inequality can only do so within *specific* institutional dynamics. In addition, ‘over-determination’ complicates the standard counterfactual understanding of causation.¹⁹

18. For example, tertiary enrolment in Chile (90 per cent) is very different from that in Uganda, Kenya, Tanzania or Malawi (5 per cent or less), but the income shares of D7–D9 are identical — despite this group in Chile overflowing with ‘education’ (WDI, 2018). This also helps us understand the spurious nature of the ‘skill-biased technical change’ type explanation for increased inequality (for a critique, see Atkinson, 1997). A different issue, of course, is that this extra education may well have significant positive externalities (not reflected in the income of those in this group), as externalities accruing to society from increased government investment in educating the children of the poor. From the perspective of this article, the key issue is who pockets the benefits of those externalities.

19. An analysis of these major methodological and social ontological issues is well beyond the scope of this article, but see, for example, Lawson (2015).

Figure 7. *Palma Ratios of the Distribution of Disposable Income, c. 2016*

Notes:

bw = Botswana; **na** = Namibia; **za** = South Africa.

Sources: see Appendix 1.

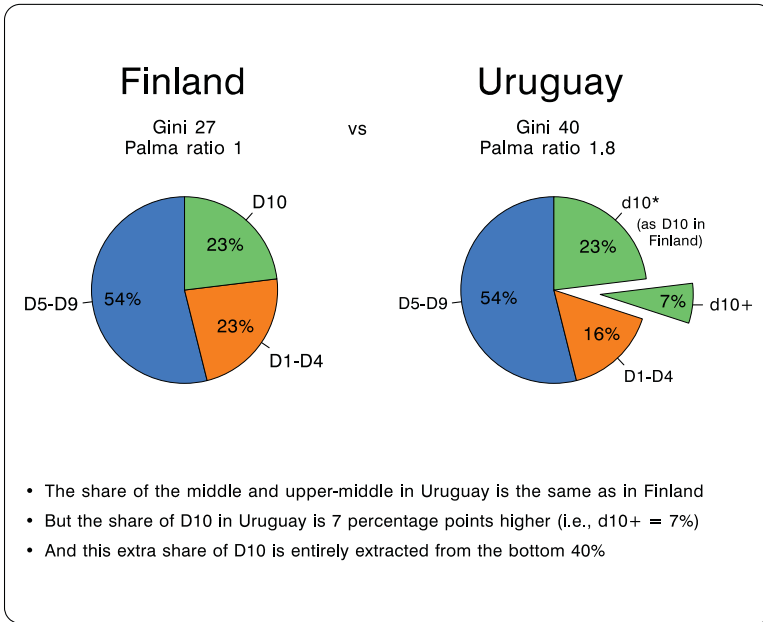
Figure 6 helps demonstrate the logic of the Palma ratio as an index of inequality. By dividing the top 10 per cent's share with that of the bottom 40 per cent, it aims to measure inequality where it exists — 'at source'.²⁰ In the case of the Gini, the geography of inequality ends up being only a mirror image of the distributional diversity of D10 and D1–D4.²¹ The Palma ratio, meanwhile, attempts to make the *actual* distributional struggles more transparent.

According to the Palma ratio, inequality increases first relatively slowly, and almost linearly, only to switch gear at the tail-end of the distribution (around ranking 110), when it starts increasing rapidly and eventually geometrically (Figure 7). In fact, as the lower arrow on Figure 7 indicates, had the 'steady pace' of deterioration in inequality found in the first

20. Cobham et al. (2015: 1–2) indicate that: 'Data for the Palma Ratio is now listed and updated as standard measure of inequality in the OECD database, ... the UNDP Human Development Report, ... as well as by some national statistical offices, e.g. the UK Further, interest in the Palma Ratio is evident among NGOs and international agencies alike'.

21. As Cobham et al. (2015: 8) remark: 'We know that by construction the Gini is over-sensitive to the middle; but in practice ... tells us nothing about it If you want to know about the middle, the Gini seems to be little good to you — but may fool you that it is'.

Figure 8. 'D10+', or the 'Extra' Share of D10: The Key to Differences in Inequality



Sources: see Appendix 1.

(approximately) 110 countries continued, the most unequal country (South Africa) would have posted a Palma ratio barely higher than 3. Instead, it has a ratio of 7. This unveils another layer of possible misunderstanding, as this rapid deterioration of inequality at the tail-end — only 14 countries post a Palma ratio of 3 or above — inevitably casts doubts on traditional theories of inequality which have little to say about this sudden surge of inequality in just a few countries (which are also located in two specific regions). It would even be tempting to say that these countries should probably be the subject of 'extreme value analysis' (of the type that focuses on values above a threshold). I will take on this challenge in the next subsection.

A clear example of the logic that underpins the Palma ratio is found in the comparison of Finland and Uruguay (Figure 8). According to their Gini (27 and 40) they don't have much in common. However, the Palma ratio — and a new simple statistic of inequality that I am introducing here, and calling 'd10+' — point in a different direction, which is characterized by as many similarities as contrasts.

The apparent considerable distributional difference between them (13 Gini percentage points) is all about the extra share of the rich in Uruguay (d10+) — gained *entirely* at the expense of the bottom 40 per cent. The

actual size of d10+ will of course vary according to the benchmark. The benchmark I suggest is what is necessary in order to achieve a Palma ratio of 1 (as in Finland) — that is, what must be transferred from D10 to D1–D4 in order to achieve this. Following Pigou (1920: 81), this transfer should be welfare-improving since:

[It] is evident that any transference of income from a rich to a relatively poor man of similar temperament, since it enables more intense wants to be satisfied at the expense of less intense wants, must increase the aggregate sum of satisfaction. The old ‘law of diminishing utility’ thus leads securely to the proposition: Any cause which increases the absolute share of real income in the hands of the poor . . . will, in general, increase economic welfare.

Figure 8 also shows how the information provided by d10+ complements that of the Palma ratio, as both statistics together provide fairly comprehensive information regarding a given country’s degree of inequality. While it is not intuitively clear where Uruguay’s extra Gini inequality comes from, knowing that its Palma ratio is almost twice that of Finland, and that its d10+ is 7 per cent of national income, tells a much more focused, transparent and informative story. And (with very few tail-end exceptions) its thrust is that the distributive struggle relates mostly to D10 trying to appropriate an extra income share by shrinking D1–D4’s share (that is, by increasing d10+). Therefore, the size of d10+ is also a proxy for the capacity or otherwise of D1–D4 to resist D10’s insatiable appetite.

As suggested above, the 64,000 dollar question is obviously whether the size of d10+ in Uruguay is the fairly inevitable outcome of its ‘fundamentals’, or whether d10+ is *self-constructed*, reflecting *choice* and the nature of a more unfair political settlement, characterized by Uruguay’s greater tolerance for inequality. If the former, as discussed above, this would still require an explanation for why these fundamentals impact only on the income share of one half of the population. If, alternatively, what really matters is the nature of political settlements and the (often) ‘tailor-made’ market failures supporting them, then d10+ would reflect the specificity of Uruguay’s political economy and (convenient) inequality-driving market failures.

The distributional information provided jointly by the Palma ratio and d10+ — especially by focusing the distributional struggle on a fairly specific arena, a phenomenon that is blurred by all those veils obscuring our vision of inequality — can help illuminate this message, while also helping to create awareness of the dimensions *and specificity* of inequality. This can be very useful for policy making, since with these two indicators it becomes evident where inequality is located, *and what must be done* if one wants to eradicate the ‘extra’ inequality (i.e., that above a Palma ratio of 1) in countries such as Uruguay. In other words, its minimalism — purposely avoiding all the algebraic sophistication of alternative inequality statistics — becomes its main strength, as transparent information such as this can be crucial. As

Gramsci rightly said, more often than not battles of this kind are won or lost on the field of ideology (something triumphant 1970s' neoliberals know better than anyone).

Consequently, I would likewise venture that d10+ is also a proxy for the size of Uruguay's 'distributional failure', as I cannot see any (positive or normative) reason why a country such as this should have a level of disposable income inequality greater than a Palma ratio of 1. That is, I see d10+ as a 'distortion'; therefore, I shall henceforth call d10+ 'distributional failure 1'. This new evidence suggests that we all still have some analytical work to do — especially those who argue that the 'extra' inequality, such as Uruguay's, somehow reflects the inevitable outcome of its (given) inputs. And even more work is required from those who still support high inequality from an economic efficiency point of view.

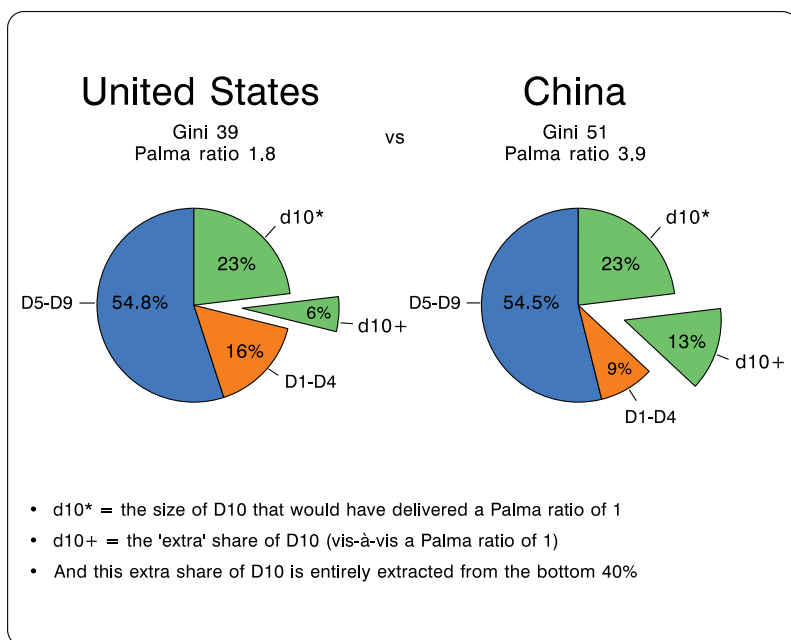
Of course, as in any other area of economics, one can always construct a suitable shopping list of potential fundamentals that might be statistically associated in a significant way (from an econometric point of view) with the very different levels of inequality found across the world, and then speculate about how (say) globalization might have impacted on them (keeping everything else constant, of course). But even in this scenario, some explanation is required as to why they affect the two halves of the population so differently.²² At the same time, an explanation is also required as to why only some governments are willing and able to tackle market inequality systematically via taxes and transfers and whether, when they do so, they are violating some distributional order of the universe, at the cost of efficiency (see more on this below).

For a long time analysts (especially those justifying higher levels of inequality) were reluctant to study the share of the rich, the most likely driver of inequality. This was the trademark of the classical Washington Consensus. As John Kenneth Galbraith remarked: 'Of all classes the rich are the most noticed and the least studied' (Galbraith, 1977: 44). Fortunately, it is beginning to look as though a certain cat is finally out of a certain bag. In fact, since the sum of all shares has to be equal to 100, and given the distributional homogeneity of *and within* D5–D9, the share of decile 10 alone could be a very simple but highly informative statistic for *the whole distribution*.

In sum, according to survey data, and with the sole exception of a few extremely unequal countries, the size of d10+ can explain the essence of the difference in within-nation inequality, even in countries that have little else in common, such as the USA and China (Figure 9).

22. One guess could be that the administrative classes may be less affected by the transformations brought about by globalization, such as the breakdown of the value-chain, increased capital (and labour) mobility, and so on.

Figure 9. US vs China: 'd10+' Is What Diversity of Inequality Is Basically About



Note: percentages may not add up to 100% due to rounding.

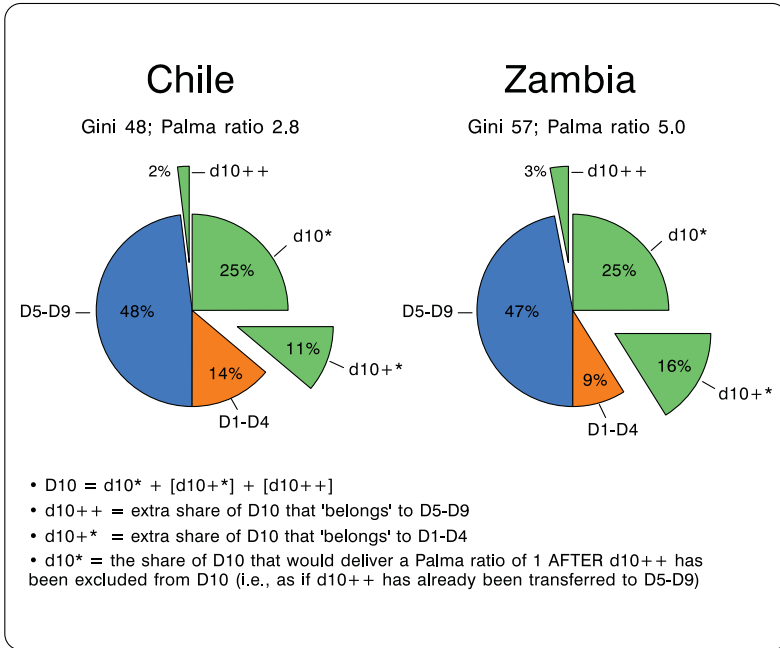
Sources: see Appendix 1.

Stylized Fact 1.5: In a few countries inequality becomes extreme because D10 is not only able to squeeze D1–D4 even further, but it also can bring the share of D5–D9 into play: The emergence of 'd10++'

The next issue for analysis is what happens at the tail-end of the distribution, where the explosion of inequality takes place — the analytical challenge mentioned above.

At the tail-end of the distribution, increased inequality is not only about an even larger d10+, but there's an added twist: in a small number of countries (mostly in Latin America and Southern Africa), D10 is not only able to squeeze the share of D1–D4 even further, but it can also shrink the share of D5–D9 below 50 per cent of national income. That is, in these countries the arena in which the wasteful 'anti-coordination' distributional game is played out is enlarged to include what in the great majority of countries belongs to D5–D9. Here the administrative classes are not able to protect themselves from D10; the strength provided by their 'coordination' is not enough to defend their half. A good example of the distinction between unequal countries where D5–D9 is able to protect its half and those where

Figure 10. Chile and Zambia: Higher Inequality due to a Larger 'd10+', and the Emergence of 'd10++'



Notes:

When ' $d10^{++}$ ' > 0, I change the notation for ' $d10^+$ ' to ' $d10^{*+}$ ' to reflect that this sector now refers only to the extra share of D10 associated with D1-D4. That is, what would be necessary to transfer from D10 to D1-D4 in order to get a Palma ratio of 1 *after* ' $d10^{++}$ ' has been transferred from D10 to D5-D9 (where it belongs). Therefore, ' $d10^+$ ' = $\{(D10 + [D1-D4])/2 - (D1-D4)\} = \frac{1}{2}(D10 - [D1-D4])$. In turn, ' $d10^{*+}$ ' = $\{[(D10 - d10^{++}) + (D1-D4)]/2 - (D1-D4)\} = \frac{1}{2}[(D10 - d10^{++}) - [D1-D4]]$. Thus, when ' $d10^{++}$ ' = 0, ' $d10^+$ ' and ' $d10^{*+}$ ' are the same (in my methodology both ' $d10^+$ ' and ' $d10^{++}$ ' can only take positive numbers; so, when they become negative, they are assumed to be zero). But when ' $d10^{++}$ ' > 0, they are different (and ' $d10^+$ ' > ' $d10^{*+}$ ').

Sources: see Appendix 1.

it struggles to do so is the contrast between Uruguay (above) and Chile and Zambia (Figure 10).

While in Uruguay, as in most countries, higher inequality is about the size of $d10^+$, in Chile and Zambia the top 10 per cent also succeeds in appropriating a new sector of the pie: ' $d10^{++}$ ' (2 per cent in Chile, 3 per cent in Zambia and as much as 11 per cent in Namibia). Therefore, to make inequality more transparent in extremely unequal countries, one should identify another distorting veil and differentiate what part of the *extra* share of D10 'belongs' to D5-D9, and what to D1-D4. When D5-D9 does not get at least its half (that is, when $d10^{++}$ > 0), I shall call this 'distributional failure 2'. In Chile, the overall 'extra' share of D10 adds up to 13 per cent of income; 2 per cent extracted from D5-D9, and 11 per cent from D1-D4. In Zambia, these figures

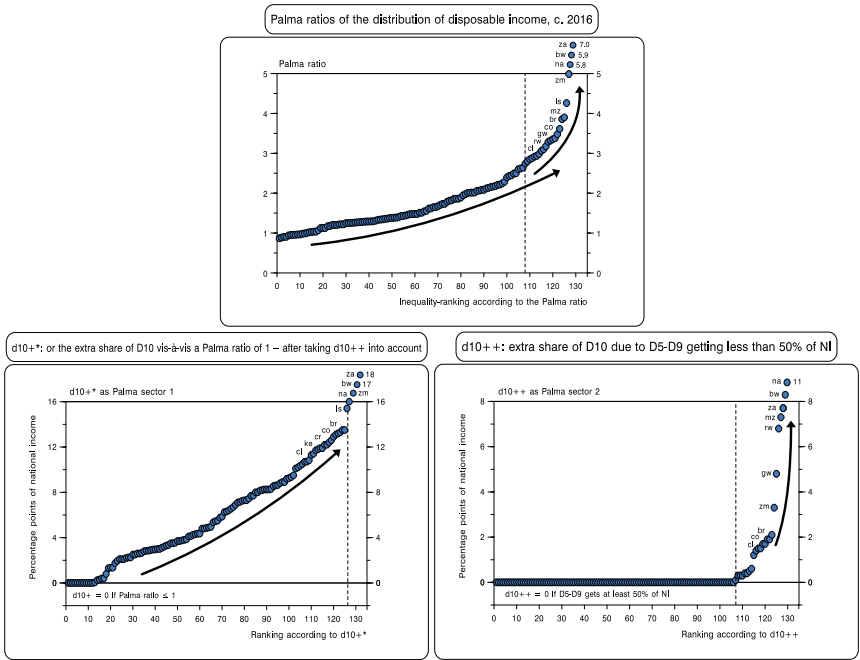
are 3 per cent and 16 per cent, and in South Africa they reach 8 per cent and 18 per cent. In more civilized Uruguay, meanwhile, as $d10++ = 0$, the extra share of D10 is made up only of $d10+$ (7 per cent), reflecting both the greater strength of Uruguay's administrative classes in defending their (at least) half of national income, and of the bottom 40 per cent in restricting $d10+$ to single digits. Finland, meanwhile, meets both yardsticks, and achieves a Palma ratio of 1 as both $d10+$ and $d10++ = 0$. As $d10+^*$ and $d10++$ are areas of the income pie enclosed by two radiuses and an arc, they will be referred to as 'sectors'. And as their logic is derived from the Palma ratio, it has been suggested that they should be called 'Palma sectors' 1 and 2, respectively — but this should be so only when they are calculated in the scenario of what is needed in order to get a Palma ratio of 1, when D5–D9 gets at least its half of the national income.

Note that in my methodology there is room for D5–D9 to get more than 50 per cent as it often does, but by a very small margin — the average for D5–D9 in this sample is 52 per cent, and as we already know, its coefficient of variation is tiny. In such cases, a country can still fulfil both targets, and get a Palma ratio of 1. However, this inevitably opens up the possibility that D5–D9 could get 'too much'. Within this 130-country sample, in only six countries does the share of the administrative classes get to 56 per cent, and four of these are the 'usual suspects' on the shores of the Mediterranean: Greece, Italy, Spain and Croatia (with a fifth, Macedonia, next door). This is a different type of distributional failure, number 3 — 'the rentier-middle and upper-middle' distributional failure. But further analysis of the 'retire-well-at-50-with-Mediterranean-diet' bureaucrat — in which academics can retire early and with 80 per cent or more of their final salary (making us all green with envy) — is beyond the scope of this (already long) article.

The new methodology ($d10+^*$ and $d10++$) helps answer the conundrum of Figure 7 above — the burst of inequality at the tail-end of the Palma ratio ranking. Its geometric increase arises from there now being two sources boosting the share of D10: a greater $d10+^*$, and the emerging $d10++$. The top panel of Figure 11 also replicates the ranking of the Palma ratio for clarity of comparison.

Bringing the share of D5–D9 into play is a crucial component of the outburst of inequality in Latin America (e.g., Brazil, Chile and Colombia), in some sub-Saharan countries (e.g., Zambia and Mozambique), and in Southern Africa's three distributional basket cases. $d10+^*$ (or the 'extra' share of D10 that 'belongs' to D1–D4, after deducting for $d10++$) now grows in a steady, linear form right up to the very last five countries (the usual three, plus Lesotho and Zambia; see bottom left-hand panel). There is virtually no more tail-end burst in this sector of the pie, with the 'explosion' of inequality at the tail-end of the Palma ratio almost entirely due to $d10++$ (see bottom right-hand panel). From this perspective, $d10+^*$ and $d10++$ complement the information provided by the Palma ratio for

Figure 11. ‘d10++’ is the Source of the Surge of Inequality at the Tail End of the Palma Ratio



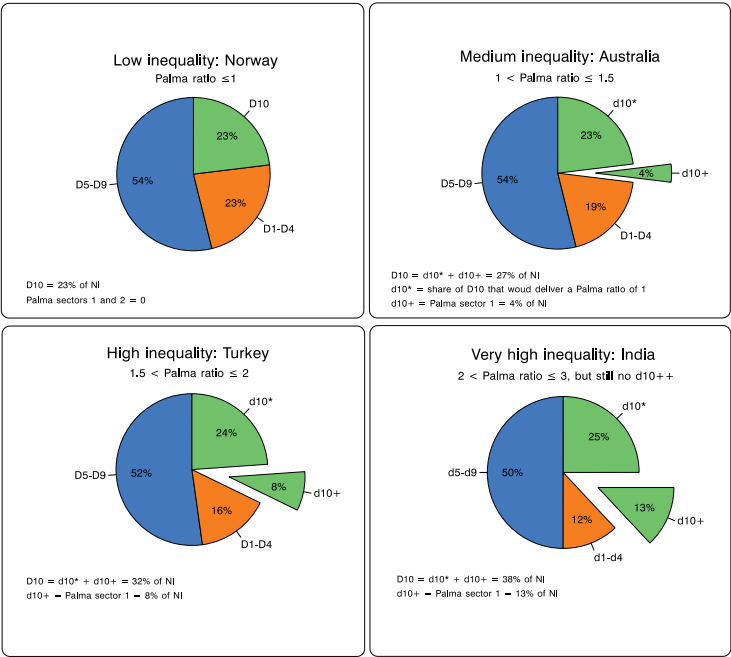
Notes:
co = Colombia; cr = Costa Rica; gw = Guinea-Bissau; ke = Kenya; ls = Lesotho; mz = Mozambique; rw = Rwanda. NI = national income.
Sources: see Appendix 1.

understanding why inequality is so unequal across the world, and why it increases exponentially at the tail-end (issues blurred in the Gini, and also in the Theil).²³ Following Adam Smith (1759), I suggest that the surge of d10++ with a still-growing d10+*, rather than statistics indicating just a burst of inequality, should also be understood as a burst of vanity:

[W]hat is the end of avarice and ambition, of the pursuit of wealth, of power, and pre-eminence? Is it to supply the necessities of nature? The wages of the meanest labourer can supply them [W]hy should [some] . . . regard it as worse than death, to be reduced to live, even without labour, upon the same simple fare with him . . . ? . . . It is the vanity, not the ease, or the pleasure, which interests us. (I.iii.2)

23. As Amartya Sen (1973: 36) emphasizes, the Theil ‘is an arbitrary formula, and the average of the logarithms of the reciprocals of income shares weighted by income shares is not a measure that is exactly overflowing with intuitive sense’.

Figure 12. The First Four Patterns of Inequality



Sources: see Appendix 1.

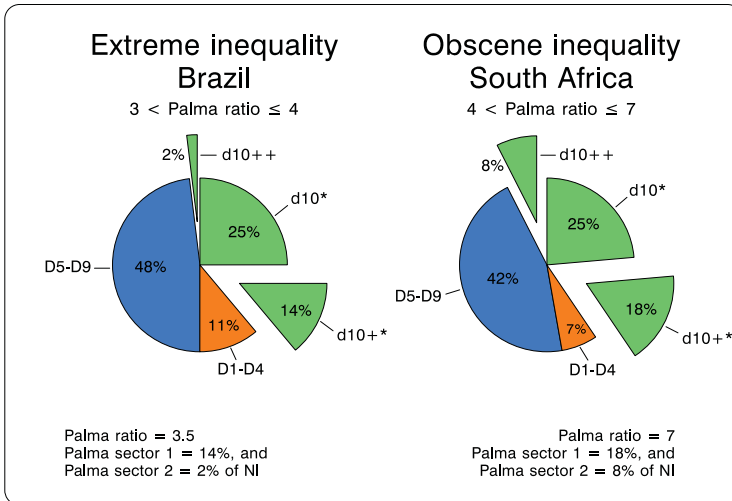
The Seven Patterns of Disposable Income Inequality in Survey Data across the World

The five stylized facts of inequality discussed so far, and the new methodology put forward above, help differentiate seven patterns of disposable income inequality. Leaving aside the case of the very few Mediterranean rentier–bureaucrat countries, in the remaining six almost everything boils down to the share of the rich. That is, how far can D10 squeeze the shares of D1–D4 — and then, in a few countries, also those of D5–D9? Figures 12 and 13 take one example to illustrate each category.

‘Low inequality’ refers to countries with a Palma ratio equal to or lower than 1 — those that do not fall into either of the first two distributional failures above (a total of 17 countries). ‘Medium inequality’ — that is, countries having a mild form of distributional failure 1 — are those in which d10+ emerges, but the Palma ratio does not exceed 1.5 (44 countries). ‘High inequality’ refers to countries with a Palma ratio between 1.5 and 2 (20 countries), and ‘very high’ inequality encompasses those with a Palma ratio between 2 and 3, and no d10++ (23 countries).

Then comes the fifth category, the very few ‘Mediterranean rentier–middle’ countries — the exceptions to the rule that it’s all about the share

Figure 13. Extreme Inequality and Obscene Inequality



Sources: see Appendix 1.

of the rich. In these countries the extra share of the administrative classes tends to come at the expense of the bottom 40 per cent. In Spain, Greece and Italy, for example, the share for D5–D9 is 56 per cent and the Palma ratios are 1.5, 1.5 and 1.4, respectively — and this is associated with a relatively low share for D1–D4 (18 per cent, 18 per cent and 19 per cent, respectively). Exactly the same picture is found in next-door Macedonia (a Palma ratio of 1.4, and an 18 per cent share for D1–D4). In Croatia, however, the extra share of D5–D9 is extracted from both sides of the distribution.²⁴

The sixth category (‘extreme inequality’) largely comprises countries with a Palma ratio between 3 and 4, but also includes six countries with a ratio just below 3, but where $d10++ > 0$ (15 countries). Finally, the seventh category (‘obscene inequality’) refers to those with a Palma ratio above 4: South Africa, Botswana, Namibia, Zambia and Lesotho.

In South Africa, the top decile — now including many who rose through the ‘Black Economic Empowerment’ programme — gets more than half of national income.²⁵ It does this not only by squeezing the share of D1–D4 all the way down to a bizarre 7 per cent (the lowest in the world, and less than a third of its share in the Nordic countries, and in some countries in Eastern Europe and the FSU), but also by shrinking D5–D8 to a quarter of national

24. To avoid double-counting, these countries have not been included in the categories based on the Palma ratio.

25. For the ANC, redistribution of assets and opportunities towards non-whites was needed to make them representative of race demographics.

income (also the lowest in the world — this is a proper ‘disappearing middle’). However, as the share of its civil-service-crowded D9 is also the highest in the world (18 per cent), South Africa’s top quintile appropriates nearly 70 per cent of national income (see also Palma, 2011: Appendix 3) — not surprisingly, the highest in the world and approximately *twice* the equivalent share in Iceland, Norway, Belgium, Finland, Slovakia, the Czech Republic, Slovenia and others. In fact, since the end of apartheid, inequality has increased among *all* the ethnicities recognized in the South African Constitution (Leibbrandt et al., 2010). It is no small analytical challenge to try to understand how one of the outcomes of that most remarkable of liberation struggles is such mind-boggling levels of inequality.

Regarding Brazil, what is most striking about its inequality — like that of the rest of Latin America — is that it is much higher than in many other middle-income countries such as those found in Asia, North Africa, the FSU and Eastern Europe (among others). This is true, even though the latter often have even more market rigidities than Latin America; prices, institutions and social capital that are less ‘right’; property rights over physical assets that are less well-defined and less well-enforced; educational systems that are more segmented, with the poor often getting an even more dismal deal; gender discrimination that is even more acute; greater shortages of skilled labour; democracies that are even more ‘low intensity’, and with more problems of ‘governance’; and an even greater dependence than in Latin America on political connections and corruption to achieve success in business.

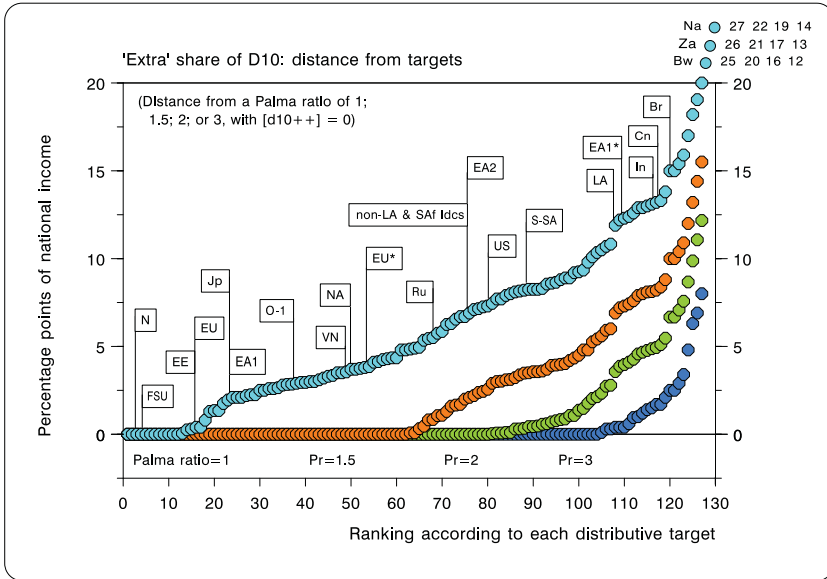
The experience of Latin America thus shows that rather than thinking in terms of the possible *concrete effects* that such factors may have on inequality, it would be more illuminating to try to understand the *concrete expressions* that these factors may find in inequality. Some of the pieces of the distributional puzzle may well be the same, but the way they fit together may differ. The specificity of Latin America’s inequality stems from the particular ways that distributional struggles have manifested there, the different strategies that oligarchies have adopted to face and temporarily overcome these struggles, the further distributional challenges created by this process, and so on. Indeed, the monotonous insistence of many on blaming Latin America’s huge inequality on ‘exogenous’ or crude path-dependency factors is akin to using a pair of scissors to cut an analytical knot that they can’t untie.²⁶

Another Method for Measuring Inequality: Distance from Distributive Targets

The analysis so far also helps in formulating a new method for measuring inequality: distance from ‘distributive targets’. Following the logic of the

26. Some still blame even colonial institutions of half a millennium ago (e.g., *mita* and *encomienda*) for Latin America’s inequality. For Williamson (2009) — quite rightly — this is just a myth.

Figure 14. How to Estimate Distributive Challenges: A New Way to Measure Inequality



Notes:

These targets also include, when necessary, that 'd10++' is also transferred to D5–D9 (i.e., that 'd10++' becomes 0). Pr = Palma ratio. Independent rankings (although for most countries rankings are the same in all targets). When a country fulfils the target (or better) it is shown at zero. Acronyms as above.

For clarity, South Africa, Botswana and Namibia are shown at the top right-hand corner.

Sources: see Appendix 1.

Palma ratio — including the fact that there seems to be no objective reason for any country to have a Palma ratio above 1 — Doyle and Stiglitz (2014) proposed including a 'Palma target' in the post-2015 UN framework for global development: a Palma ratio of 1 by the year 2030. Similarly, Engberg-Pedersen (2013) suggested halving the gap between the starting point and a Palma ratio of 1.

However, these targets (neither of which, unsurprisingly, was accepted by UN delegates — they were too difficult to fudge) did not take into account that in a few countries D5–D9 does not get its half of national income. I therefore suggest that a more comprehensive target should also take into account the size of the Palma sector 2 ($d10++$); in that case, we need two yardsticks, one for $d10+$, and one for $d10++$. Figure 14 shows four alternative yardsticks for $d10+$, always including (when necessary) what it takes to make $d10++=0$. The first measures the 'excess' share of D10 — in terms of 'extra' percentage points of national income — from the point of view of reaching the target of a Palma ratio of 1 (that is, how far countries are from getting both $d10+*$, and $d10++$ equal to zero). This would be a scenario in which there would be no distributional failures 1 or 2. The other

three are ‘watered-down’ yardsticks for $d10+$, while keeping the same target of $d10++ = 0$.

In round numbers, when the yardsticks are both Palma sectors = 0, only 17 countries fulfil the targets (as above in the ‘low inequality’ category). When relaxed to a Palma ratio of 1.5, 65 countries meet the targets; when 2, 90. Finally, with a Palma ratio of 3, 110 countries are within these parameters, and only the usual three still have a distributive challenge in double digits. The distance from these targets provides a new way of measuring inequality, at the same time as furthering insights into how inequality increases throughout the world.

Taking Stock: The Story So Far Regarding the Diversity of Distributional Outcomes in Terms of Disposable Income

I am the first to acknowledge that there is more than one way to skin this (inequality) cat — especially from the perspective of different types of data. In terms of disposable income inequality as shown in survey data, my method tries to remove several layers of misunderstanding, that is, some of the veils and distorting mirrors, by breaking down inequality into what I believe are its two main components, $d10+^*$ and $d10++$ (or Palma sectors 1 and 2). In doing this, this contribution not only helps to refocus the study of inequality on the share of the rich, but also reveals how far greater inequality should be understood as a distributional failure: I have identified three such failures in terms of the distribution of disposable income — $d10+^*$ (or Palma sector 1), $d10++$ (or Palma sector 2), and the Mediterranean rentier-middle.

The six categories of inequalities identified above — plus the ‘Mediterranean rentier-middle’ — reinforce the view that there is a significant amount of *choice* and *self-construction* in this respect, particularly at middle- and high-income levels. The remarkable transformations that have taken place in the last four decades may have helped create a wide variety of *opportunities* for increasing inequality, but not everyone has taken them up — although in a large number of countries, rentiers (including those who live from extracting the value created by others, from extortionary finance by capturing policy and avoiding taxes, by tormenting consumers, or by appropriating the rents of natural resources, and so on), have done so very effectively.

Regarding choice, although it may not always be clear what that choice is really about, who can act upon it, and what making that choice may achieve — especially in ‘chicken game’ scenarios, where the brinkmanship of the top can easily push things to the very edge (see Appendix 3) — everything seems to indicate that there are far more degrees of freedom in the distribution of income than is generally acknowledged. However, as famously suggested in ‘The Eighteenth Brumaire of Louis Bonaparte’, people make their own history, but they do not make it as they please; they do not make it under circumstances they themselves have chosen, but under given

and inherited circumstances with which they are directly confronted. We therefore need to understand what leads us to make particular choices when confronted with specific inherited circumstances. What helps in the formation of collective beliefs? How do spontaneous consensus types of hegemony emerge? How can they be changed? And although I am strongly on the side of agency, it is obvious that as far as income distribution is concerned, agency could easily fail if (as indicated above) it does not understand structure.

Nevertheless, there can be little doubt that differences in ‘power structures’, ‘choice’ and ‘agency’ must be playing a key role when, for example, Croatia has a median wage that is twice that of my country (Chile), even though both have the same GDPpc (Duran and Kremerman, 2015). We now know that in the former this is in part due to its Mediterranean rentier-middle preferences. In the latter, meanwhile (despite good intentions), the little effort that has actually been made to improve inequality since the return to democracy in 1990, despite five ‘centre-left’ governments, reminds us that ‘choice’ can also take the form so clearly expressed by one of our presidents at the beginning of the 20th century: ‘in this life there are only two types of problems: those that will get solved by themselves, and those that have no solution’.²⁷

One thing that is surely happening in Latin America (and many other parts of the world), is that improving inequality has lost what for Wittgenstein was the crucial factor for success in public policy: a sense of urgency (Malcolm, 1993).

THE DISTRIBUTION OF ‘MARKET’ INCOME ACROSS THE WORLD: ‘MARKET’ VS ‘SOCIAL’ DISTRIBUTIONAL OUTCOMES

No overall analysis of inequality, of course, can ignore market inequality (that is, inequality before taxes and transferences). In the second part of this article, I analyse its four main stylized facts, and in doing so I identify four more distributional failures.

Stylized Fact 2.1: Significant deteriorations since the 1980s have been confined to the OECD, Eastern Europe and Russia, and China and India

The first stylized fact of market inequality is that significant deteriorations since the 1980s have occurred in just three groups of countries: the OECD; Eastern Europe and Russia; and China and India. As Table 1 indicates, in

27. Quoted on the webpage: www.country-data.com/cgi-bin/query/r-2410.html. If one changes President Ramón Barros Luco’s statement to ‘only two types of problems: those that will get solved by markets, and those that have no solution’, one gets a good sense of what the Washington Consensus is all about, including inequality. And if one changes it to ‘only two types of problems: those that will get solved by markets, and those for which we should be able find a complementary solution’, one gets a good feel of what Keynesianism is all about.

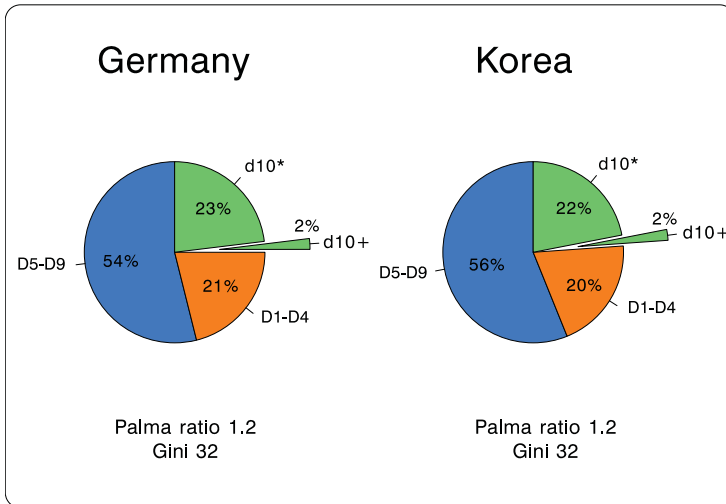
Table 1. *Market and Disposable Income Ginis, 1985 vs 2015*

	Difference between 2016 and 1985		Difference between 2016 and 1985		2016		2016		2016		1985		1985	
	Gini market	Gini disposable income	Gini market	Gini disposable income	Gini market	Gini disposable income	Relative reduction of market inequality	Gini market	Gini disposable income	Relative reduction of market inequality				
OECD* (16)	7	4	49	30	42	26	38%	42	26	37%				
EE & Russia (13)	7	6	46	30	39	24	35%	39	24	38%				
China & India	10	9	48	44	38	35	8%	38	35	8%				
S Af.* (2)	4	3	68	60	64	57	12%	64	57	11%				
LA (16)	-3	-3	47	44	50	47	7%	50	47	6%				
Rest of World (43)	0	0	45	39	45	39	14%	45	39	14%				
World* (92)	2	1	47	38	45	37	19%	45	37	18%				

Notes: OECD* includes 16 countries with increased inequality; S Af.* = Botswana and South Africa.

Sources: see Appendix 1; and Solt (2018). Unfortunately, Solt only provides Ginis, giving no information on income shares by deciles; it is not possible, therefore, to use the methodologies developed above to analyse market inequality.

Figure 15. The Distribution of Disposable Income in Germany and Korea



Sources: see Appendix 1.

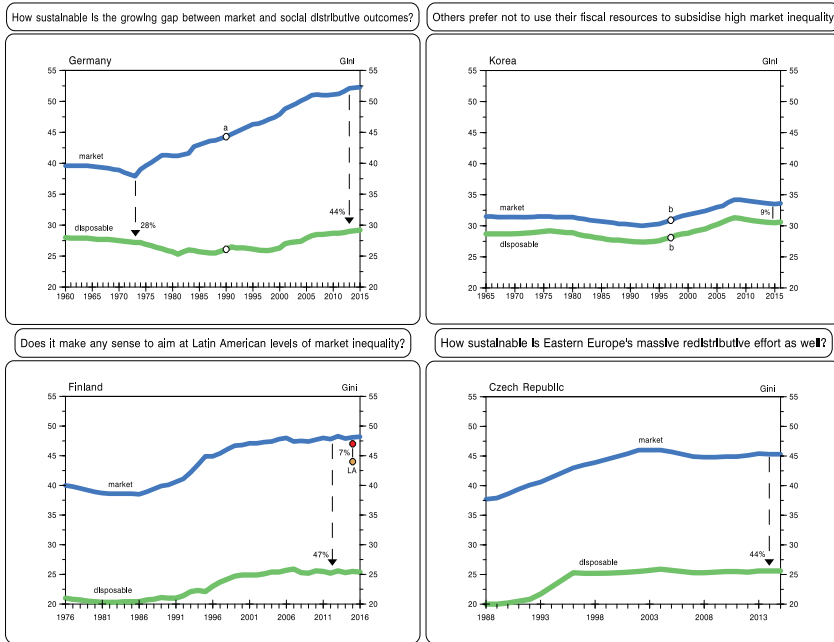
the 92 countries for which Solt (2018) provides information from c.1985, market inequality increased significantly in these three groups of countries. It also continued to increase in Southern Africa. Meanwhile, ‘the rest of the world’, on average, has had no increase in either form of inequality, while Latin America had a relatively minor improvement on both of its huge Ginis. I shall analyse these issues in the following sections.

Stylized Fact 2.2: Most OECD countries attain a low level of disposable income inequality via a tortuous route

When we look at market vs social distributive outcomes, high-income countries now reach low levels of disposable income inequality via two very different routes — one of them being a rather tortuous one. Figures 15 and 16 show the similarities and contrasts between Germany and Korea. In terms of resemblances, their disposable incomes have identical Palma ratios and Ginis (Figure 15). However, this remarkable similarity hides a major difference in how they got there, with Germany’s route being far more convoluted than Korea’s: in order to get to a disposable income Gini of about 30, Germany needs a relative reduction of its market Gini of 44 per cent, while Korea needs a decrease of just 9 per cent (Figure 16).

Germany’s market inequality started its relentless increase around the 1973 oil crisis, the stagflation that followed and the associated radical monetarist experiments. However, as Germany was bent on maintaining its disposable income Gini just below 30, it had to increase its relative fiscal efforts to reduce its market Gini by about two-thirds. Korea, meanwhile, only needed

Figure 16. Market and Disposable Income Ginis, 1960–2016



Notes:

LA = Latin America's average market and disposable income Ginis; **market** = market Gini; **disposable** = disposable income Gini. **a** = German reunification; and **b** = Korea's 1997 financial crisis.

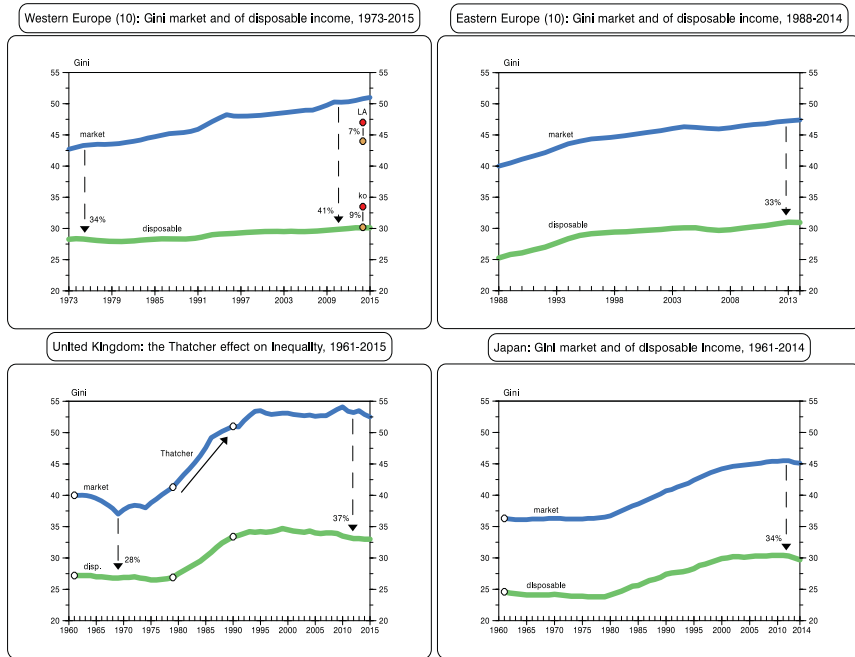
Source: Solt (2018).

a fraction of that effort to achieve the same result; Solt (2018) shows that it comes close to doing so *at source*, with its market Gini at just 33. Surely a first best route!²⁸

Finland — which serves as a role model in so many respects — also joined the OECD's unequalizing rush and even caught up with Latin America's average market inequality (Germany ended up even higher). This is what I call 'reverse catching up', by which I mean it is now the highly unequal middle-income countries that seem to show the advanced countries the shape of things to come. As Figure 17 indicates, most of the OECD also followed the same route of opening up a huge gap between market and social distributive outcomes.

28. The WDI (2018) database indicates a similar disposable income Gini for Korea and Germany as Solt (2018). However, the WID (2018), using tax return information, indicates a rising share of the top 10 per cent. Unfortunately, Solt (2018) does not provide information on shares by deciles. The OECD (2019) shows similar data to Solt (*ibid.*) until 2015. Subsequently it differs slightly due to the use of a new survey following a different methodology. However, for the 28 OECD countries for which new data are provided after 2015, Korea still has the lowest market Gini in the whole OECD.

Figure 17. Market and Disposable Income Ginis, 1960–2016



Note:

Top panels, all available countries for respective periods in each region. For the case of the US, see Section 2.4 below.

Sources: see Appendix 1.

This asymmetry trap can be described in various ways — a ‘reverse catching up’ in market inequality while trying to hold on to past glories in their disposable income inequality (many just by the skin of their teeth); the idealization of greed in one vs that of social solidarity in the other; the tearing apart of the fabric of societies vs the attempt to recreate ‘reciprocal obligations’ (Collier, 2018). Thatcher’s UK led this charge of the unequalizing light brigade, winning the speed record. But for the Iron Lady, ‘there was no alternative’. In fact, I don’t think she would have minded if someone had said ‘that was what it was really all about’.²⁹

What we are witnessing in the OECD is another type of distributional failure (number 4 on my list), which is not about increasing market inequality per se — large though this has been. This failure is about the ever less sustainable *gap* between market and social distributional outcomes, and its inevitable plethora of distortions, transaction costs and public debts. I want to highlight five (for a detailed analysis, see Appendix 5):

29. Although she might have added that she tried to legitimize greed, not hate — as the extreme right does now.

- i. Increased market-inequality has not been ‘Pareto-improving’ even in the ‘Kaldor–Hicks’ sense.
- ii. There are also significant transaction costs in letting market inequality go one way only to try to reverse it later in terms of disposable income. Like the Grand Old Duke of York: ‘He had ten thousand men; He marched them up to the top of the hill; And he marched them down again’.
- iii. But as the OECD’s ‘reverse catching up’ aimed not just at Latin-style market inequality, but also at its regressive taxation, the very rich and large corporations also became *de facto* practically tax-exempt. So, instead of the winners compensating the losers it was those not invited to the party who were left with the bill, and had to be ‘over-taxed’ for this — but over-taxed not because of the growing needs of the poor, but in order to compensate the increasing tax evasion and avoidance of the winners.
- iv. As transfers balloon, governments’ debts are soaring. The EU’s share of ‘social protection’ stands at 40 per cent of public expenditure — and with health and education, this share jumps to two-thirds. But in their new tax status, corporations and the very rich now prefer to *part-pay/part-lend* their taxes, and part-pay/part-lend their wages (Palma, 2009). It’s so much more fun than the old-fashioned way of having to pay for public goods via progressive taxation, and having to put up with positive but challenging wage–productivity dynamics. That is, growing market inequality creates further necessities for public expenditure, while a new generous tax status for those who benefited most denies the necessary public revenues. And as there are limits to taxing those ‘others-than-the-real-winners’ (ask the *gilet jaunes*), governments’ debts are mounting.
- v. Finally, now that OECD markets have finally been unshackled from all those Keynesian ‘rigidities’ and ‘distortions’ brought about by well-intentioned but supposedly economically misguided post-war policies, are Latin America’s levels of market inequality really the new rising sun? Are OECD countries now embarked on a ‘creative destruction’ of those rigidities, or just bent on some (fairly uncreative and highly corrosive) ‘reverse catching up’, including the return of some of their own disagreeable ghosts of the past?

As discussed in detail for Europe in Appendix 5 (and in section 2.4 below for the USA), it seems highly unlikely that elites and special interest groups captured policies with the aim of enhancing economic efficiency.³⁰ Here the comparison between Germany and Korea in Figures 16 and 17 is particularly

30. On the power of vested interests in today’s rent-extracting economy, see for example Wolf (2018).

relevant. In the 45-year period since the beginning of the deterioration of Germany's market inequality, its productivity has not even doubled: neither has the productivity of Western Europe or the US. Korea, meanwhile, has increased its productivity sixfold (or eightfold in terms of output per hour worked). Previously, Germany had trebled its productivity level *in half that time* — or nearly quadrupled its output per hour worked (TED, 2018). Now, by contrast, in the latest quarter of 2018 Germany barely escaped recession (Ewing, 2019). Not a lot to show for the 15 percentage points increase in its market Gini.

Of course, many other things were happening at the same time, not least the onset of a new technological revolution, with its likely initial negative impact upon inequality (Pérez, 2016). But it would be hard to argue that productivity growth in Germany (and the OECD, apart from the special case of Ireland) would have been even more dismal had market inequality not been allowed to deteriorate in this bizarre way.³¹ In Germany, for example, the relentless deterioration of market inequality and its underinvestment (both private and public) took place side by side with a reversal of its relationship with emerging Asia. According to one *Financial Times* columnist:

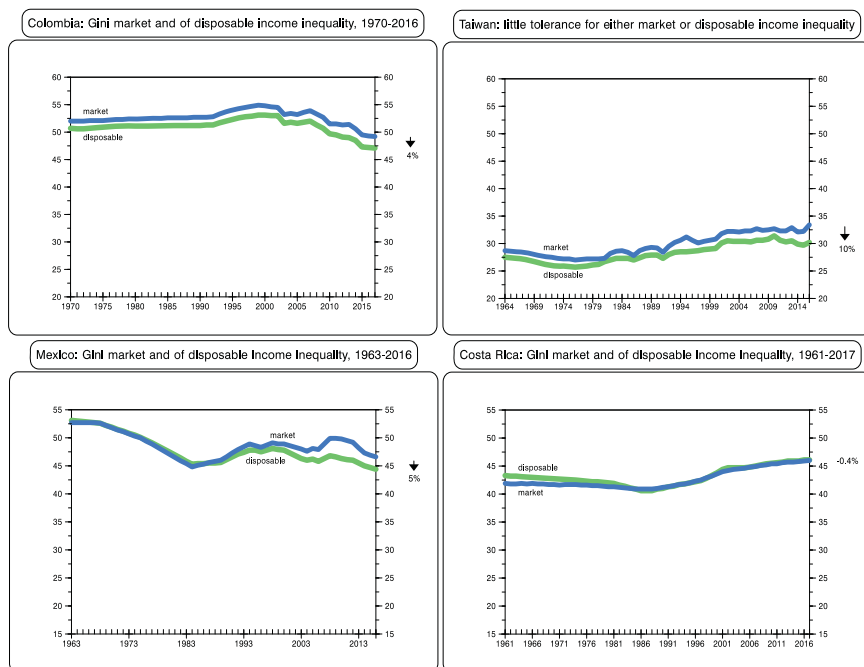
Germany once saw China as an export market for machinery with which China would develop its industrial base. Today, China is becoming the senior partner in the relationship. [Germany's] biggest problem is falling behind in the technological race. . . . [This] is symptomatic of a fundamental European problem. . . . [Now there] are signs that complacency is about to turn into panic. (Münchau, 2018)

In sum, this fourth distributional failure is not about increasing market inequality per se. It is about the ever growing (and less sustainable) *disparity* between market and social distributional outcomes. Inevitably, this 'asymmetry trap' creates problems not just for growth, but also leads to having to make too much fiscal effort *unnecessarily* (as in self-constructed welfare needs). It is even worse if this effort is done off-target in revenues (as in the winners getting away scot-free, and others with less political clout being forced to pick up the social protection bill); if it leads to mounting public sector debts; and if the fiscal effort is put on the wrong track in expenditure (as in making the very rich the biggest welfare recipients of all time). From this perspective, and as discussed in detail in Appendix 5, today's post-modern Robin Hood welfare-state 'robs' the rich to give to the very rich.

Life is not that easy anymore in the OECD, having a family and an oligarchy to support. Should I say 'Welcome to the Third World'?

31. On Ireland, see O'Connor and Staunton (2018).

Figure 18. Market and Disposable Income Ginis, 1960–2016



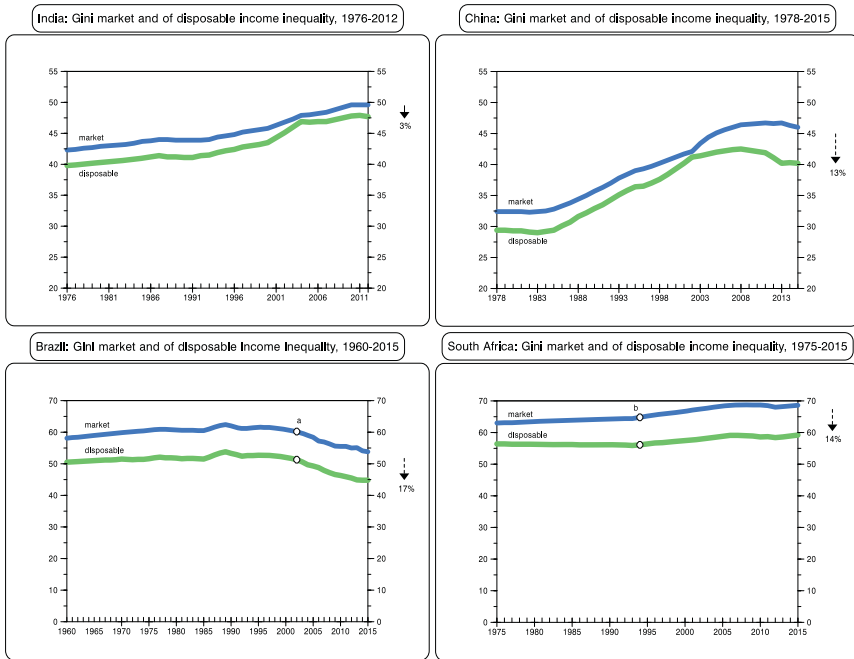
Sources: see Appendix 1.

Stylized Fact 2.3: Emerging markets with extreme inequality in both areas are normally those whose higher tolerance for all types of inequality leads them to make little fiscal effort to correct their high market inequality

Oddly enough, there is one remarkable similarity between unequal Latin American countries and some low market inequality Asian ones: they make little effort to reduce their market inequality via taxes and transferences, as illustrated in Figures 18 and 19. Unlike the first-best route chosen by Taiwan or Korea, *but like the OECD*, Latin American countries let ‘market makers’ do more or less as they please, but as opposed to the OECD they are not prepared to make much effort to close the distributive gap. Here, governments prefer to do more talking than acting in terms of social protection and inequality (Figure 18). Unfortunately, wishful-thinking (let alone progressive ‘hot air’) hasn’t proved to be of much help for inequality.

Figure 19 gives relevant information for four of the five BRICS. In India, the speed of deterioration of both forms of inequality is remarkable, as is the lack of effort it makes to correct this, despite its rapid growth. As a result, there are still more people below the poverty line in India than in the whole of sub-Saharan Africa. There are other dark sides to India’s rapid transformation, such as having become the most polluted

Figure 19. Market and Disposable Income Ginis, 1960–2016



Notes:

a = election of President Lula da Silva; and **b** = election of President Mandela.

Sources: see Appendix 1.

country in the world (Bernard and Kazmin, 2018). And horrific episodes such as the wave of suicides by desperate small farmers (who had been thrown to the wolves), the largest recorded such wave in history, also show the more Dantesque side of India's increasing market inequality and insecurity.

China's deterioration of market inequality has been one of the fastest, but it seems that it has finally begun to stabilize.³² It is unlikely that when Deng Xiaoping said: 'Let some people get rich first', he imagined that the richest 1 per cent of households would end up owning at least a third of China's wealth (the actual figure is bound to be much higher, as there is significant underreporting; Pilling, 2014; Wildau and Mitchell, 2016). But as Figure 20 below indicates, and in contrast to Latin America, the rich at least devote a great deal of their share of income to investment.

32. UTIP (2018) and WID (2018) confirm this; the OECD (2019) reports a smaller Gini reduction (6 per cent). However, studies by Peking University and Southwest University in Chengdu present a more pessimistic picture (Wildau and Mitchell, 2016).

In South Africa, meanwhile, both types of inequality have worsened since the beginning of democracy. Furthermore, even though — like Brazil — its market Gini reduction has reached at least double digits, this is a modest effort since in both countries fiscal revenues are relatively similar to the OECD (Di John, 2006; Lieberman, 2003; OECD, 2019). The difference between these two countries is that South Africa, despite a relatively progressive taxation, fails to achieve more due to an ineffective system of transfers to the poor. Brazil, by contrast, although it has (or should I now say ‘it had’?) a more effective programme of transfers, falls down badly on its highly regressive tax structure. Furthermore, in Brazil transfers to the poor are often a smokescreen to justify transfers to the administrative classes — which are bent on catching up with their Mediterranean counterparts.³³

This also helps put into perspective Latin America’s recent improvements in inequality. Not only do household surveys fail particularly badly to capture the income of the very rich (Meyer et al., 2015), but governments are reluctant to make tax returns available for double-checking these apparent improvements in inequality. (I wonder why.) Indeed, studies based on aggregate fiscal data for Brazil and Chile show that there is no decline of income shares at the top, or in their Ginis.³⁴ The latest study on Brazil (Morgan, 2017) indicates a relatively stable Gini, contradicting its decline in survey data. For Chile, also using aggregate data since access to original data was also denied, one study (Atria et al., 2018) finds that the share of the top 1 per cent has actually increased since 2003, and that of the top 10 per cent keeps hovering around 55 per cent.³⁵ And another study (López et al., 2013), which tries to take into account tax evasion, concludes that in Chile the top 1 per cent appropriates almost a third of national in-

33. While the ‘Bolsa Familia’ for the poor costs just half a percentage point of GDP (Holmes et al., 2011), bureaucrats, for example, retire at 56 (men) and 53 (women), with at least 70 per cent of their final salary — many get up to 100 per cent (OECD, 2017). So, anything up to one-third of public expenditure has been devoted to pensions, while public investment does not reach even 2 per cent of GDP, in a country with a literally crumbling infrastructure (IMF, 2018b). And the proposed pension reform resembles a case of moving out of the frying pan into the fire, as Bolsonaro wants to copy Chile’s private system: one that promised 70 per cent income replacement, but has delivered an average monthly pension that does not even reach the minimum wage (Mander, 2016), and was on its way to a median pension of just 15 per cent of the final salary (Bonnetfof, 2016). So, governments are again having to give massive subsidies to keep this system going, even though stopping subsidies was supposed to be the very reason why pensions were privatized in the first place. In the meantime, exorbitant fees, hidden charges and other tricks generate massive profits for pension providers (CENDA, 2019), who only bother to pay pensions that amount to less than half of what they collect as contributions (Bonnetfof, 2016).

34. For Brazil, see Gobetti and Orair (2016); Medeiros et al. (2014); Morgan (2017); for Chile, see Atria et al. (2018); López et al. (2013).

35. Furthermore, since only 81,000 taxpayers acknowledged in 2018 having an income that would pay the top marginal rate (just 35 per cent), massive levels of tax avoidance and evasion mean that tax returns information underestimates significantly the degree of inequality (Guzmán, 2019).

come (the equivalent figure for Korea is 12 per cent and for Taiwan 11 per cent); the top 0.1 per cent appropriates one-fifth (in Korea this is 4 per cent); and the top 0.01 per cent — about 300 families — gets well over one-tenth of the pie (in Korea that group, which includes some of the most successful entrepreneurs in the world, seems satisfied with a seventh of that: 1.7 per cent).³⁶

In part, this huge inequality is due to the Latin American elite believing it has some divine right to the rents of natural resources, a modern version of the *Droit du seigneur*, as it were; to access fiscal paradises; as well as to free-ride on public goods paid by others. These elites are even reluctant to help eradicate poverty, although this would be remarkably cheap in high middle-income countries (Ravallion, 2010).³⁷

In sum, while Solt's database suggests that Brazil and Chile manage at least a market Gini reduction in double digits (though the OECD only reports 7 per cent for Chile), tax returns indicate a different picture for D10 and for the Gini. It is therefore highly unlikely that the *overall* distribution could have improved much, if at all. Furthermore, as discussed in Palma (2011, 2016a), Chilean evidence also indicates a distributional 'ratchet effect': when inequality improves, this has a temporary effect, and when it deteriorates it leaves a more permanent legacy, as those at the top are better able to sustain their gains. Recent events in Brazil indicate that this asymmetric cycle is about to take a reinvigorated new upswing.

As Walter Benjamin remarked, behind every rise of fascism lies the failure of a major political project: in Latin America (but not only there), it is the failure of the so-called 'Third Way'. In fact, its very dullness — with its preference for improving the administrative efficiency of the intrinsically inefficient unequal markets — seems to have caused such a failure of the collective social imagination that otherwise unthinkable options have become possible.³⁸

36. For Chile's stubborn inequality, see Palma (2011: Appendix 1).

37. ECLAC (2010) calculates that in six countries of Latin America, the cost of a 'one poverty line' monetary transfer to *all* the unemployed, *all* people over 64, and *all* children under 15 of vulnerable households would be equivalent to between 1.8 and 2.7 per cent of GDP — not such an insurmountable task! For why so little is actually done, perhaps Dante's *Inferno* gives a hint — especially in the Fourth Circle (greed), and in the Eighth (fraud). In fact, the *Inferno* has been defined as 'the realm ... of those who have ... perverted their human intellect to fraud or malice against their fellow men' (MacAllister, 1953: 14). For poverty reduction in Latin America, see UNDP (2016); for Chile, Durán and Kremerman (2015); for Brazil, Holmes et al. (2011); and for South Africa, Tregenna (2012).

38. As in many parts of the world, the Left in Latin America divided into two streams after 1980, but both have a crucial element in common: they are still stuck in the past. While the 'old left' (e.g., Chavismo in Venezuela) tried to reconstruct an idealized past by demonizing everything that has happened since, the 'new left' (e.g., Brazil and Chile, as in Britain) attempted instead to construct a future which was almost the exact opposite of the past — and in order to idealize this future, they have demonized every possible aspect of that past.

This fifth distributional failure is about letting oligarchies run amok, while (as mentioned above) governments do more talking than acting in terms of social protection and inequality. While the rich were let off the hook, the middle were over-taxed, got mediocre public services in return, and ended up highly indebted — at some of the highest real interest rates (Wheatley, 2012) and mark-ups (Pearson, 2012) in the world. In turn, although the poor got a little bit of social protection and some crucial rights, they also received a massive dose not only of market insecurity, but also of personal insecurity, with crime spiralling out of control.³⁹

Stylized Fact 2.4: Increased market inequality in the OECD has really been about extracting value created by others

It never ceases to amaze me how little of the deluge of extra income appropriated by those at the top in the OECD — as well as how little of the soaring corporate profits — has been diverted to productive uses, such as investment. The US is again transparent in this distributional failure — my number 6 (Figure 20).

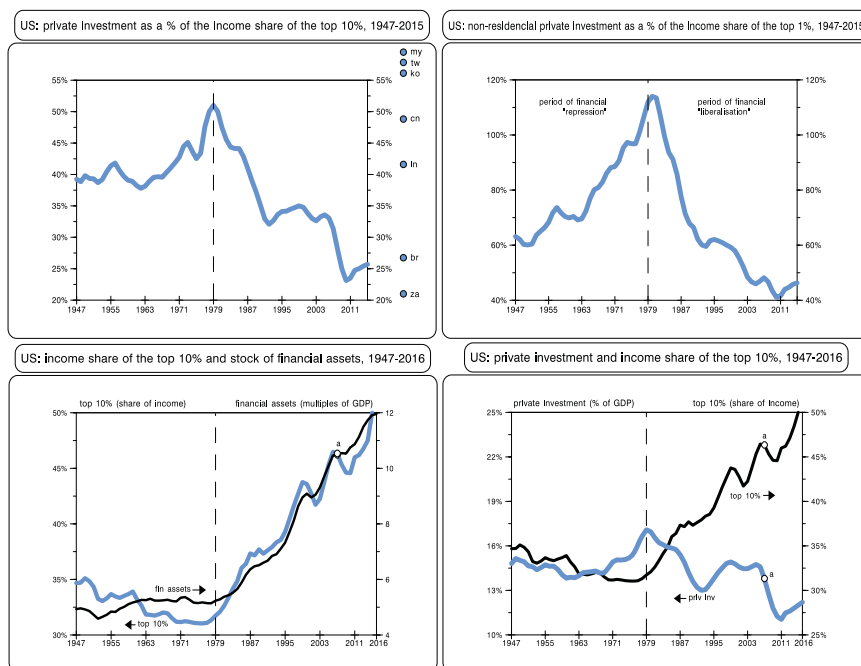
There are at least three fundamental issues that emerge from the four panels of Figure 20. The first relates to the relationship between income distribution and private investment. If the US had the same level of national income, but with the same level of inequality as when Reagan was elected, the top 1 per cent would today be earning about US\$ 2 trillion less than it actually does. In turn, if the US had the same income and inequality as now, but its share of investment to GDP were as it was pre-Reagan, over US\$ 1 trillion more would be invested per year. Linking the two together — i.e., private investment as a percentage of the income share of the top 10 per cent — we find a clear ‘reverse catching up’ in motion with countries at the other side of the Rio Grande (and even South Africa; see Figure 20, top left-hand panel). In turn, *net* private investment all but disappeared (BEA, 2019), and non-residential private investment as a share of the income of the top 1 per cent fell as if in a roller coaster (top right-hand panel).

It is often acknowledged that the only historical legitimacy of capitalism — that is, the legitimacy of a small elite to appropriate such a large proportion of the social product — rests on that elite’s capacity to use it productively, and to develop the productive forces along the way. It can only do this by reinvesting most of that huge share. Keynes (1919: 10), for example, explains the contrast between ‘emerging’ Germany and the US vs

In sum, as neither Left has been able to leave the past behind, when constructing the future (as in *Hotel California*) ‘some dance to remember, some dance to forget’, but ‘we are all just prisoners here, of our own device’.

39. Unequal Latin America has 41 of the 50 most dangerous cities in the world — and all of the top 12 (www.worldatlas.com/articles/most-dangerous-cities-in-the-world.html).

Figure 20. Income and Investment, USA 1947–2016

*Notes:*

fin assets = stock of financial assets; **priv inv** = fixed private investment; **a** = the 2008 financial crisis.

3-year moving averages. Malaysia's current percentage is 77 per cent; Taiwan's 74 per cent; and Korea's 62 per cent.

Sources: Income shares (from tax-returns): WID (2018); Financial assets: FED (2018); Private investment: for the US, BEA (2019; includes equipment and non-residential structures); for the rest, IMF (2018b); WDI (2018).

Britain during the (investment-intensive) 'Third Technological Revolution', or third great surge of industrialization, that of the 'Age of Steel, Electricity and Heavy Engineering': 'The new rich of the nineteenth century . . . preferred the power which investment gave them to the pleasures of immediate consumption. . . . Herein lay, in fact, the main justification of the capitalist system. If the rich had spent their new wealth on their own enjoyments, the world would long ago have found such a régime intolerable'.

There is not much danger of finding these enlightened Schumpeterian characteristics in the current newly rich of the US or Europe (West or East). In contrast to what Keynes says of their counterparts of another epoch, in most of today's newly rich the 'discreet charm' of the Latin American bourgeoisie rules. The reality principle has been slowly but surely hijacked by the pleasure principle — one that is easily satisfied by an endless supply of low-hanging fruit such as effortless asset bubbles, timid state institutions, an obliging macro and public finance, a considerate progressive

intelligentsia, highly profitable market failures, and rents from artificially created oligopolistic concentration, all coming from a growing aversion to competition or any other form of market compulsion. It is not by chance that many lucky rentiers all over the OECD now live a life of milk-and-honey by getting funds from captured Central Banks for free (or at near-zero interest rates), just to relend those funds at high interest rates to the same taxpayers who are subsidizing them in the first place. Even Latin-style oligarchies usually have to try a bit harder than that. In fact, witnessing what is happening today in the OECD helps us to understand why the Latin American élites are what they are: perhaps they have just been able to do, for a much longer period of time, what the OECD's elites can do now! It's all about being able to build a capitalist system without 'compulsions' (see analysis after Figure 22 below). The specificities may be different, but the core problem is the same.⁴⁰

In fact, in this reverse catching up, some of the disagreeable ghosts of the past have also re-emerged; for example, most large corporations are now likely to include forced labour in their supply chains (Foroudi, 2018). Perhaps not surprisingly, with the exception of a few high-tech activities, manufacturing is increasingly becoming an optional extra across the OECD as well.⁴¹

Who needs the sticks of market compulsions and productivity challenges — such as healthy competition and policy driving private investment towards sectors with higher potentials for productivity growth (Wood, 2002) — when political elites are now so good at solving the collective action problem of how to share the carrots, and at making the 'entry' of others as hard and risky as possible. Douglas North was surely right when he developed his 'limited access order' hypothesis, emphasizing how political elites like to divide up the control of rents and block the access of others (North et al., 2007). And this 'limited access order' has worked rather well: if wealth inequality in the US was the same as when Reagan was elected, the top 1 per cent would today own half its current wealth — and the top 0.1 per cent one-third, and the top 0.01 per cent one-fifth (Saez and Zucman, 2016).

The second main issue that emerges from Figure 20 is the relationship between financialization and income distribution. The bottom left-hand panel shows a remarkable co-integration between the surge in the value of the stock of financial assets and the increased share of income of the top 10 per cent (Palma, 2009). However, this so-called 'financial deepening', instead of pulling private investment with it (the revitalizing effects promised by

40. And this helps answer Krugman's second question (see footnote 1).

41. On 'premature de-industrialization', see Palma (2005, 2008); Tregenna (2014); see also Rodrik's much later contribution (2015). For a revealing analysis of how the US economy has been running the dualistic processes Polanyi and Lewis described, but in reverse, see Taylor (2019).

McKinnon and Shaw, one of the founding ideas of the Washington Consensus), had the opposite effect (bottom right-hand panel).

However, this ‘financial deepening’ did at least made a contribution if viewed from Walter Benjamin’s perspective: as fascism expanded the logic of spectacle into the field of politics, financialization, with its pyrotechnics, did the same in the field of economics, as illustrated, for example, by the S&P 500 soaring more than 320 per cent between 2009 and mid-2018, the longest bull market on record, creating more than US\$ 18 trillion of (virtual) wealth on the way. This must have been a spectacle indeed for the rest of the population, whose median household wealth was actually falling (Collins et al., 2018). Furthermore, the rampant financial mania at the top took place side by side with the real economy gasping for air: paradise for the former became a purgatory for the latter (see Figure 22 below).

It has become pretty obvious by now that financialization and increased market inequality in the OECD was about making it easier to get rich by extracting value from those who actually create it, or from cashing-in on assets already created (see especially Mazzucato, 2018). One aspect of this phenomenon is what the chief economist of the Bank of England calls corporate ‘self-cannibalism’: how private investment becomes a collateral damage of the unholy alliance between a new breed of ‘bullying’ shareholders and self-seeking executives that has led to companies being dismantled, or condemned to debt, in order to increase immediate income.⁴²

Easy access to cheap debt has also fuelled a US\$ 40 trillion mergers and acquisitions mania during the last decade⁴³ — the greatest anti-competition drive ever seen — with its fragile leveraged loan structures and bizarre fees and commissions. Some of the bogeymen of the past financial crisis are back in fashion too, like ‘synthetic’ CDOs and credit default swaps (US\$ 8 trillion of them — remember AIG?), although it is patently clear that they are not fit for purpose. Indeed, they have been defined by a *Financial Times* columnist as ‘a gigantic, incomprehensible global joke’. He goes on to ask: ‘Can anyone find a way to bury this absurd pseudo-market?’ (Dizard, 2018b).⁴⁴

42. If shareholders used to get 10 per cent of corporate profits, they now want it all (and more). Where they once kept shares for six years, now it is for less than six months, implying far less concern for the long-term health of the firm. For Keynes, in contrast, the relationship between a shareholder and the firm should be ‘like marriage’ (1936/2018: 140).

43. See the statistics of the Institute of Mergers, Acquisitions and Alliances: <https://imaa-institute.org/mergers-and-acquisitions-statistics/>

44. Credit default swap (CDS) trading firms have even been found to be involved in ‘manufactured defaults’; that is, encouraging companies to deliberately default on their debt in order to trigger CDS payouts (in return for favourable financing). This fraud is technically known by its magical realist name: ‘narrowly tailored credit events’ (Rennison, 2019a). On the return to ‘synthetic’ CDOs and other products blamed for the last financial crisis, an insider complains, ‘it’s almost beyond belief that the very same people that claimed to be

As a finance professor (and buyback proponent) insists, ‘Serving customers, creating innovative new products, employing workers, taking care of the environment . . . are NOT the objectives of firms’; everything is about ‘maximizing shareholders’ value’ (quoted in Brettell et al., 2015a). Yes, but what is the role of competition and policy if not to force a link between both sets of objectives, so that the *only* way that corporations could maximize shareholders’ value would be by focusing on the other set of issues? Unsurprisingly, those seeking to maximize shareholders’ value, irrespective of the way in which it is done, are happy to break those links by letting, for example, a mergers and acquisitions frenzy dilute competition, by allowing buybacks to distort share prices, and by transforming states into emasculated institutions and their policies into a rentier made-to-measure affair. In fact, it now seems that élites would not settle for anything less than governments resembling Stepford wives.

What is really needed to rein in market inequality is to re-engineer the links between both sets of objectives. For example, for most of the 20th century, stock buybacks were deemed illegal because they are just a crude form of stock manipulation. But in 1982 they were legalized by the US Securities and Exchange Commission, becoming one of the most popular tools for inflating share prices, and boosting earnings per share and executive pay. If one adds changes to corporate governance law (e.g., in 1992 Congress changed the tax code to encourage performance-based compensation), and to shareholders’ taxation, stock buybacks become a tax-efficient cash machine allowing shareholders and top executives to extract capital from corporations — what Reuters now calls the ‘cannibalized-company business model’ (Brettell et al., 2015b).

In fact, this ‘buyback derangement syndrome’ has become one of the main fuels powering the stock market, with S&P 500 corporations spending nearly US\$ 5 trillion on them since the first quarter of 2009 (borrowing massively to finance those purchases).⁴⁵ As one insider explains, ‘Basically what you’re seeing in the stock market is a slow-motion leveraged buyout of the entire market’ (quoted in Brettell and Aeppel, 2015). On top of that, an amount equivalent to about two-thirds of this figure has been distributed in dividends (Brettell and Aeppel, 2015; Wigglesworth, 2019). In fact, in 2018 buybacks alone became larger than overall capital expenditure among the S&P 500 corporations (Powell, 2019).⁴⁶

expert risk managers, who almost blew up the world in 2008, are back with the very same products’ (quoted in Rennison, 2019b).

45. Before the latest round of tax cuts, buybacks were pretty much mirrored by higher corporate debt (Yardeni Research Inc., 2019; see also Lazonick, 2014, and Lazonick et al., 2013).

46. Last year, US companies handed their shareholders US\$ 1.3 trillion through dividends and buybacks, lifting the post-crisis bonanza to US\$ 8 trillion (Wigglesworth, 2019). In turn, net non-residential private investment in structures and equipment reached only one-third of this figure.

Trump's tax cuts just fuelled this binge; J.P. Morgan has estimated that about half of all the overseas profits of US corporations repatriated since the tax cuts have been spent on buybacks (Tankersley and Phillips, 2018). In the meantime, 'at least 90 percent of Americans will end up poorer thanks to [Trump's tax] cut' (Krugman, 2019). Apple, for example, immediately announced buybacks and dividends of another US\$ 100 billion on top of the US\$ 210 billion it had already committed since 2012 (see Ram, 2018) — a sum greater than the market value of all but 20 of the US's biggest listed companies (e.g., bigger than Verizon, AT&T, Boeing, Oracle, MasterCard, Coca-Cola, Procter & Gamble, Citi or Disney). The idea of using these huge resources instead to diversify Apple properly into artificial intelligence, robotics, autonomous car electronics, and all those industries of the future seems beyond the pale (that is, beyond the boundary from where emerging Asia begins). Within the pale, instead, it is more fitting to pay exorbitant remuneration to executives, to 'return' a tsunami of funds to intimidating shareholders, to torment customers by (for example) slowing down their older iPhones to force them to keep upgrading to new (and often fairly similar) products, and by the decline of the reliability of products. Perhaps it is about time to start shorting corporations such as Apple.

To state the obvious, sustainable growth comes from enriching the productivity ecosystem as a whole, not the net worth of shareholders and top executives of a handful of firms. Furthermore, the combination of weak corporate investment and rising corporate net saving also drives the growing mismatch in financial markets between abundant liquidity and a shortage of solid financial assets, so that the ease of performing a transaction in a hollow security or instrument has become the trademark of the current process of financialization (Palma, 2009).

No wonder Kindleberger (2005) borrowed from psychoanalysis the concept of 'mania' — an over-excited, grandiose detachment from reality — to refer to what others just call 'bubbles' or 'exuberance'. But the anti-regulatory brigade even uses lessons from 'the prisoner's dilemma' in interactive game theory in their defence: selfish individuals, entirely for their own selfish reasons, have incentives to behave in a pleasant, tolerant and unenvious way. Therefore, if those predestined to win at the market are the *nice guys*, why regulate markets (including finance), or worry about inequality?

The third and final issue emerging from Figure 20 is what's to be done next. In fact, the type of policies tried so far have not just distorted market inequality and crowded out productive spending; they seem to have crowded out neoclassical economics as well, as many of its usually more imaginative followers can now only think about more of the same. These policies — such as Obama's fiscal stimulus, and the FED's bubble-inducing quantitative easing (QE), or what a *Financial Times* columnist now calls the 'cash for trash' scheme (McWilliams, 2019) — may have delivered the longest bull market on record, but only a tiny proportion of its associated

resources were used to create new productive capacities.⁴⁷ And real wages were ‘lower in 2014 than in 2005 for about two-thirds of households in 25 advanced economies — more than 500 million people’ (Tyson and Madgavkar, 2016).

Nevertheless, many insist that the only way forward is for more *unproductive* spending — even if to stimulate that requires an endless succession of bubbles; for example, Summers (2013) argues that ‘Most of what [could] be done under the aegis of preventing a future [financial] crisis would be counterproductive’. Krugman (2013) agrees: ‘[now] even improved financial regulation is not necessarily a good thing . . . it may discourage irresponsible lending and borrowing at a time when more spending of any kind is good for the economy’. So, as a Faustian bargain, their advice is to keep refilling the punch bowl until ‘markets’ are satisfied — as if they ever will be (not much evidence of diminishing returns here).

However, as we already know, credit booms weaken (rather than strengthen) output in the medium run (Borio et al., 2018; Lombardi et al., 2017; Mian et al., 2017), and increased market inequality has a negative impact on growth (see Ostry et al., 2014). Also, as the richest 10 per cent already own about 80 per cent of overall wealth, including six of every seven stocks held by individuals (and the richest 1 per cent own half), more stock market bubbles are unlikely to boost expenditure much (even the unproductive kind) as they will just shift even more wealth to those ‘cash-hoarding’ agents who are already responsible for the ‘savings glut’ (Krueger, 2012; Phillips, 2018).⁴⁸ Furthermore, global debt — and its components — is already bursting at the seams (it has swelled 50 per cent in the decade since the credit crisis), and financial fragility is evident everywhere.⁴⁹ Junk bonds are already knocking on the US\$ 4 trillion mark just in the US, and half of all investment-grade corporate bonds are already at BBB, or just one step from junk status (Rickards, 2019). Therefore, if this goes wrong, it could be ugly: ‘If default rates were to reach only 10% — a conservative assumption — this corporate debt fiasco will be at least six times larger than the subprime losses in 2007–08’ (ibid.).

Furthermore, what secular stagnationists (surprisingly) miss is that given relatively low levels of OECD unemployment, current sluggish growth must be at least as much about the composition of effective demand as its level,

47. Less than 1 per cent of the nearly US\$ 1 trillion of Obama’s fiscal ‘stimulus’ went to highway and environmental projects — in a country that desperately needs both (Palma, 2009).

48. As Krueger (2012: 7) reminds us, ‘the top 1 percent of households saves about half of the increases in their wealth, while the population at large had a general savings rate of about 10%. This implies that if another \$1.1 trillion had been earned by the bottom 99% instead of the top 1%, annual consumption would be about US\$440 billion higher. This would be a 5% boost to aggregate consumption’.

49. For example, in the US ‘half the core business of financing or refinancing houses is under water’ (Dizard, 2019).

that is, increasing inequality driving actual corporate and household spending away from its productive component (see Figure 22 below).⁵⁰

In the meantime, emerging Asia can't believe its luck; all of the above has opened up huge productive opportunities, and many Asian corporations certainly know how to take advantage. Samsung, for example, has just announced a US\$ 160 billion three-year investment in new technologies (including those industries of the future which Apple seems to so reluctant to tackle properly, from artificial intelligence to biopharmaceuticals). According to one *Financial Times* analyst, 'This can be regarded as the world's biggest [corporate] investment. Samsung is injecting the equivalent of their operating profits back into the business' (Harris, 2018b). '[This] investment plan eclipses a pledge made by Apple to divert US\$30bn to expand its US operations' (Harris, 2018a).

As logic and unfettered greed have never been the best bedfellows, perhaps the contrast highlighted above between Korea's market inequality and productivity growth, and those of the OECD will not be too difficult to understand — or indeed the question of why the West is losing its leadership in many of the industries of the future. For example, the US does not even have a telecoms equipment maker left to compete with Huawei. Europe at least still has Ericsson and Nokia (although they are already struggling). In the meantime, its financial sector keeps growing out of control: as a mortgage industry investment banker stated, 'I would say the industry has an overcapacity of about one-third in its current structure (quoted in Dizard, 2019).

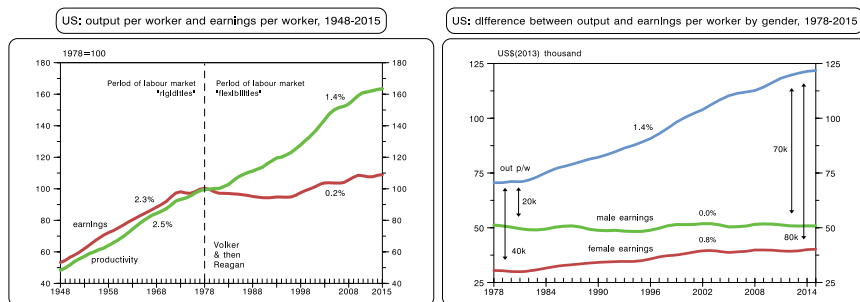
Surely increased market inequality and lethargic growth can be re-engineered. Saint Augustine argued that our free will has been weakened but not destroyed by original sin. Buybacks, for example, can be redefined again for what they are — crude market manipulation — and policy could well help redirect ('discipline') these funds towards investment. Tax cuts for the rich can also be reversed.⁵¹ In fact, since 2001, federal tax changes have reduced revenue by more than US\$ 5 trillion.⁵² US bankruptcy law could also overturn its 1978 change to stop private equity firms using Chapter 11 as a pension-laundering scheme (Whoriskey, 2018); and there is no reason to stick with the 2003 law that prohibited governments from negotiating drug prices for Medicare (which has gifted more than US\$ 50 billion a year to the pharmaceutical industry). By not considering such changes in legislation — which only big money could have had the clout to ram through — we will not

50. 'Secular stagnation' refers to a situation in which there is a slow rate of growth of GDP due to chronically weak demand (relative to potential output). This is blamed on the (unobservable) 'natural' rate of interest for having become negative.

51. One billionaire has saved over a million dollars a day on taxes on his dividends since Bush's 2003 tax cut (Wamhoff and Gardner, 2018).

52. And this figure does not include hundreds of billions of dollars in so-called tax cut 'extenders' for corporations and other businesses that Congress has periodically enacted under each administration (ibid.)

Figure 21. Output and Earnings, USA 1948–2015



Notes:

earnings = real earnings; **productivity** = output per worker.

3-year moving averages.

Sources: Productivity and earnings: EPI (2017); Output: WDI (2018); Employment: TED (2018).

only have to keep paying a high price for current inefficiencies but, as Stiglitz (2018) argues and as events in Eastern Europe, Russia, the Philippines, India, the US, Brazil and several other countries indicate, we are now even risking our democracy. Even the 2018 World Economic Forum in Davos was opened with a speech warning that ‘the ongoing disintegration of our social fabric could ultimately lead to the collapse of democracy’ (Schwab, 2018).

It must have felt equally naïve 130 years ago to believe that it was possible to change antitrust laws to prevent the agglomeration of market power, and Standard Oil and American Tobacco must have seemed as untouchable as today’s FAANGs.⁵³ However, unless one swallows the ‘end of history’ discourse, one has to accept that evolution has always been a challenge to dominant agents. After all, as Chekhov said, the world is no more than our conception of it. Or as Sartre put it, when one has imagined a world, it’s then no big deal to supply the meanings, the interpretations, the significance for things and events (Sartre, 2004). In sum, and in contrast to what the secular stagnationists propose — and the high-end of the art market, private-jet, super-yacht and sports-car industries dream of — the last thing we now need for reactivating the world economy is more of what even the *Financial Times* now calls ‘silly-billy’ (silly-billionaires) (Lee, 2018). Today, many are even deluded into believing they have finally created a ‘perpetual motion’ machine — one which doesn’t require an injection of proper energy (net investment) to keep producing all-time record profits (Figure 21).

In the US, average earnings have been practically stagnant in real terms since the early 1970s, and productivity growth per worker has slowed to just 1.4 per cent p.a. — phenomena which are surely interconnected, as the

53. FAANG is an acronym for the five best-performing tech stocks: Facebook, Apple, Amazon, Netflix and Google.

former is highly likely to become a significant disincentive for the latter. As male earnings have been stagnant, the difference between the value of what an average worker produces and what a male worker is paid rose in real terms from US\$ 20,000 in 1980, to US\$ 70,000 in 2015. That is, the 'gross surplus' per male worker increased 3.5-fold. For female workers, it doubled from US\$ 40,000 to US\$ 80,000.

This changing income distribution within US firms, and the resulting fall in wage shares and weak effective demand and investment rates, has been associated with increasingly hierarchical structures and the systematic redistribution of income to the top of the corporate hierarchy (Fix, 2018). This is reflected in a swelling CEO pay ratio: Disney, while cutting its workers' real pay by 15 per cent, gave its CEO a compensation package equal to the pay of over 9,000 Disneyland workers.⁵⁴ So, here we have the seventh distributional failure (and the last in this list) as this increasingly hierarchical pay structure is unlikely to be an appropriate reflection of the value of marginal productivities. The large bonuses paid to CEOs of banks as they led their firms to ruin and economies to the brink of collapse, for example, are hard to reconcile with the belief that pay has much to do with marginal social contributions these days (Stiglitz, 2016).

This growing distributional failure is intrinsically related to the OECD's 'reverse catching up with high inequality Latin American countries' phenomenon, as the inability of labour to get the value of its marginal productivity has always been one of the key characteristics of countries in which the top 10 per cent gets the lions' share of the half of national income shared by D10 and D1–D4.

Market Inequality vs Market Efficiency and Productivity Growth: How Paradise for the Former Became a Purgatory for the Latter. On 'Inequality Waves', and Some Issues for Future Research

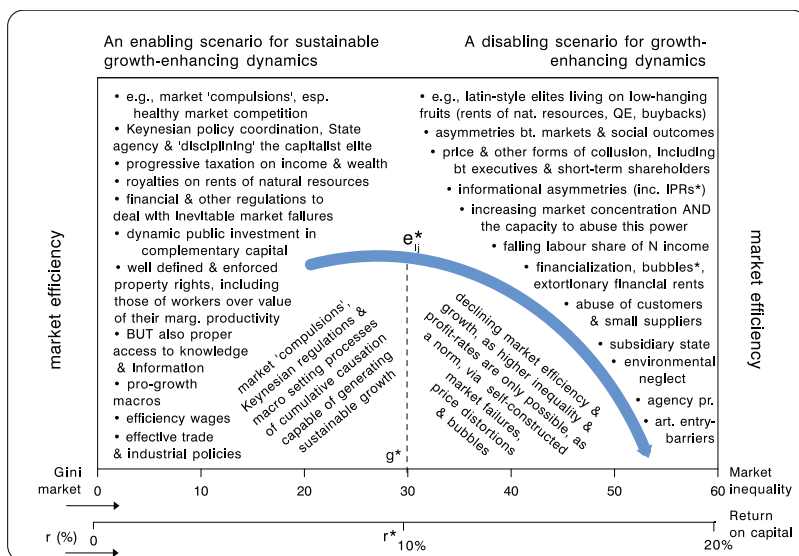
Does an increase in market inequality help enable or disable growth-enhancing dynamics? Figure 22 summarizes in a very simple manner some of the main points made so far regarding the contrasting impacts that different levels of return on capital and market inequality in general can have on efficiency and growth.

The basic hypothesis portrayed in Figure 22 is that after 'e*' (given 'i' and 'j'), the relationship between market efficiency and the return on capital — and market inequality in general — resembles the second half of an inverted-U. That is, inevitably, there comes a point at which further increases in the return on capital and in market inequality can *only* come (as a norm) at the expense of a rapidly declining market efficiency and growth.⁵⁵

54. For other examples, see Ahmed (2018); Del Valle (2018); Neale (2018); Pearlstein (2019).

55. The nature of several factors on both sides of Figure 22 is far more complex than that of those typical of the standard paradigm of well-functioning markets solving Adam Smith-

Figure 22. *Market Efficiency and productivity growth vs the Rate of Return on Capital and Market Inequality*



Notes:

e^*_{ij} = point at which higher returns on capital and increased market inequality can only come, as a norm, at the cost of market efficiency; The subscript 'i' indicates that the level of ' e^* ' may vary across sectors. In turn, the subscript 'j' indicates that the level of ' e^* ' can also vary along the technological cycle (Pérez, 2002, 2016). g^* and r^* = levels of market inequality and return on capital associated with e^* . Also, esp. = especially; bt = between; inc. = including; IPRs = intellectual property rights (see footnote 56); N = national; on bubbles, see also footnote 55; and pr. = problems.

Within this general hypothesis, the specific point I want to put forward is that what most clearly characterizes the current twin scenarios in the non-Asian emerging world — high corporate profits and market inequality, with sluggish growth — is that most non-emerging-Asia economies (and certainly those in the OECD) are already well into a generalized 'post- e^* ' state of affairs, one that is very familiar to Latin Americans. As we know so well

type problems via the invisible hand. For example, IPRs (despite the likely protestation of lobbyists of industries such as pharmaceuticals) are located at the right-hand side of the Figure because they may actually slow down (rather than speed up) the pace of innovation. As these rights relate to knowledge (and information), they may well be counterproductive, as knowledge is a (global) public good (that is, there are no marginal costs associated with its use). Therefore, restricting its use via the enforcement of traditional property rights (e.g., TRIPS) would *necessarily* cause market inefficiency, especially because knowledge is the main input for the creation of further knowledge. The need to provide incentives to innovate is one thing; artificially restricting access to knowledge is quite another (Stiglitz, 2007). In turn, although bubbles surely belong to the right-hand side of the Figure, those that help the build-up of the necessary infrastructure for new technological paradigms (e.g., the dotcom one) could, at least in part, qualify for the other side of the Figure (Pérez, 2002).

by now, if capitalism is just ‘unleashed’, markets can easily be manipulated by those at the top, becoming not just inefficient but self-destructive (as in the ‘cannibalized-company business model’ discussed above). That is, the current institutional scenario has allowed capital to achieve levels of profits which are only possible when some (if not all) of the factors mentioned on the right-hand side of Figure 22 come into play — at the cost of low levels of investment and productivity growth.⁵⁶

Although this scenario may well be capable of generating an excess supply of ‘silly-billys’, it can only do so at an increasing cost in terms of sluggish growth and market inefficiency in general. It is not by chance that the number of billionaires has more than doubled since the 2008 financial crisis, and is set to double again in a much shorter period of time; and last year their wealth increased by record amounts (PwC and UBS, 2018). But this paradise for ‘silly-billys’ becomes a purgatory for the real economy — and for the rest of us. Indeed, in 2017 the US economy managed the greatest gap ever recorded between ‘efforts and accomplishments’: while corporate profits reached an all-time high, investment (relative to GDP, or the income share of the top 10 per cent) came close to an all-time low. It is as if in economics the law of gravity has taken a sabbatical; but when it returns — as it inevitably will — it may come back with a vengeance (Palma, 2009).

Moreover, these ‘silly-billys’ — by succeeding in constructing a ‘post-e*’ paradise on earth — have also constructed economies that can only go forward if pulled by ever more ‘extraordinary’ fiscal and monetary policies. As Summers explains, ‘If budget deficits had ... not [grown] relative to the economy ... [and if] an extra \$10tn in wealth had not been created by abnormal stock market returns, it is hard to believe that the US economy would be growing much at all’ (Summers, 2018). The problem now is what to do next, and secular stagnationists can only think of more of the same. For Krugman (2013) the core problem is clear: ‘If the market wants a strongly negative real interest rate, we’ll have persistent problems until we find a way to deliver such a rate’. So, let’s keep refilling the punch bowl for the few, let’s keep making transfers to those that are (unnecessarily) left behind, and let’s keep over-borrowing and over-taxing the new ‘silent majority’ to finance both — and let’s keep hoping that they continue to be silent.⁵⁷ For Keynesians, the bottom line is very different: how to reconstruct a type of scenario characterized by the left-hand side of Figure 22. Basically, it is about time that governments start exercising different forms of state agency aiming at ‘disciplining’ the capitalist elite into spending productively (that

56. Some aspects of this phenomenon have been well researched; among the growing literature, see Ostry et al. (2014), and Card and Krueger (1995). The 2018 IMF report on the US economy also expresses serious concerns about the current negative interactions between higher market concentration and lower levels of investment (IMF, 2018c).

57. As Einstein emphasized, insanity is doing the same thing over and over again and expecting different results.

is, aimed at creating ‘compulsions’ for increased productive spending by corporations and those at the top). And it is about time that governments start ‘disciplining’ themselves into doing the same via increased public investment financed by progressive taxation. Current proposals for a ‘Green New Deal’, for example — one that would transform green issues from problems into solutions — are not just essential for environmental protection, but they are desperately needed for all of the above. The same is true about recreating the growth-enhancing link between wages and productivity. It is not often that reason, ethics and economic logic coincide in such a remarkable way! I can’t remember the last time that mind, soul and smart pockets were being pulled in the same direction — the only missing ingredient now is the muscle, including the ideological one (as discussed above, and as Gramsci rightly said, battles of this kind are usually won or lost on the field of ideology).

In sum, the left-hand side of Figure 22 illustrates the ‘enabling’ scenario for sustainable growth-enhancing dynamics. Rational and intelligent agents interacting in *competitive* and properly regulated markets, with all the required conditions, government agencies and policies indicated in the Figure (and more), may well be able to set in motion processes of cumulative causation, characterized by their positive feedback loops into the system, and capable of generating a momentum of change which may become self-perpetuating (e.g., in the Veblen/Myrdal or the Smith/Young/Kaldor manner). It will still be capitalism, warts and all, but at least it will be a capitalism capable of developing the productive forces of society in a sustainable way. However, as the post-war scenario illustrates, even the best policies can become inflexible and get outdated if they are unresponsive to change. But as Hirschman (1982) argued, people often stick with policies after they have become counterproductive. This leads to such frustration and disappointment with existing policies and institutions that it is not uncommon to experience a ‘rebound effect’ — as the one that started at the end of the 1970s. This also helps to explain the messianic attitude of the neoliberal tsunami, as well as its poor outcome. And as now neoliberalism has long passed its sell-by date, a new ‘rebound effect’ is long overdue — and the longer it is delayed, the stronger (and perhaps also the more mechanistic) it may become.

Recent events, however, have shown that one of the peculiarities of the scenario built since the 1980s (on the right-hand side of the Figure) is that, once established, it seems to have very few, if any, *endogenous* pressures for an ‘upgrade’. Once achieved, it takes on the characteristics of a Hotel California: ‘We are [only] programmed to receive. You can check out any time you like, but you can never leave’.⁵⁸ And the (not so) invisible hand of the (not so) unfettered market forces is unlikely to come to the

58. That is the main aim, for example, of the new (so-called) ‘trade’ agreements, such as the TTP-11, which are basically intended to be policy straightjackets to prevent emerging markets from rethinking their development strategies (Palma, 2018a).

rescue. In other words, neoliberalism, as an ideology, has proved to be such an effective technology of power that it has so far paralysed most of its opposition. That is, borrowing from Kafka's 'The Silence of the Sirens' (1917/1995), the (unequalizing) sirens have, up to now, had a still more fatal weapon than their song, namely the ideological silence of their 'progressive' opposition.

It is this cyclical switching between the two sides of Figure 22 which has generated, at least in part, the 'distributional waves' of the last century. And when on the right-hand side of Figure 22 (where we currently are — let's call it 'scenario 2') Piketty's ' $r > g$ ' becomes a self-fulfilling prophecy, because a self-constructed increase in ' r ' is what this scenario is all about — and a struggling ' g ' is the inevitable collateral damage (in this scenario, increased market inequality is as much a twin of inefficiency as the apple is of the law of gravity). At the same time, the waves I have in mind differ from Milanovic's (2016) 'Kuznets waves' as mine are more about Gramsci than Kuznets, Hirschman than Solow, Mazzucato, Amsden or Pérez than his understanding of the relationship between technology and inequality. My waves are about self-construction rather than fundamental forces of the universe. What matters most in them are issues such as what it is that helps in the formation of collective beliefs. How do spontaneous consensus types of hegemony emerge? How can they be changed? That is, they are more about ideology than technology, agency than structure, choice than historical 'accidents', discursive articulation than economic determinism, fighting distributional failures in a Keynesian sense rather than surrendering to them (à la 'new left'). Another perspective from which to look at my type of waves is that of Foucault's relationship between power and knowledge, in particular the role of the economic 'discipline' in democracy (as a form of 'disciplinary power' via the production of particular kinds of knowledge). From this standpoint, what we really need to fight inequality — i.e., to help set in motion the next 'wave' — is to have a more critical perspective within economics of the range of our options for participation.

In the type of distributional waves I have in mind — and to differentiate them from 'Milanovic's waves', let's call them 'Palma waves' (in which Hirschman's 'rebound effect' can play an important role) — what matters most is to take responsibility for our distributional choices (e.g., aiming at 'scenario 1' or '2' in Figure 22, remembering that these are policy 'package', and you mostly can't pick and choose). Above all, there is no room for claims that we are just somehow innocent bystanders of irrepressible distributional forces. No-one has forced the OECD to 'bananize' their market inequality by moving ever further into 'scenario 2'. This choice is as much a self-defining act as any can be.

CONCLUSIONS

As this essay has already emphasized, in order to understand current distributive dynamics one needs to study the share of the rich — and, in terms of growth, what leads them to choose what to do with their income and wealth, and in which of the two scenarios of Figure 22 they have to perform. Schumpeter (1918: 7) stated that ‘The fiscal history of a people is above all an essential part of its general history’. I would add that its (closely related) distributional history is just as essential.

However, given the many limitations of *all* types of distributional data, one should try to look at the distribution of income from all possible angles, including surveys, tax returns and payrolls.⁵⁹ This article has offered an analysis from the point of view of surveys — a perspective in which inequality, with all its veils and market failures, becomes a subject so complex that following Leonard Cohen’s advice (‘Show me slowly what I only know the limits of’), I have tried to discuss in as much detail as necessary.

Although the 2018 World Economic Forum had identified the ever-growing gap between rich and poor as ‘the problem’, the 2019 meeting (helped no doubt by the absence of Trump) focused on nationalistic threats to trade, globalization and democracy (see Schwab, 2018). It seems that anxieties about inequality per se have somehow evaporated with the realization that a new layer of distorting mirrors — such as those provided by Trump, Brexit and the re-emergence of the extreme right — can help project resentment away from inequality and onto bad economics, xenophobia, homophobia and other forms of hatred and intolerance.⁶⁰ And while many in the global elite feel very uncomfortable with these events, due to their lack of ideological sophistication and the fact that they are nourished by a cruder cult of violence, they have nonetheless adapted to these changes rather well — like an aristocratic family in a Jane Austen novel forced to welcome some newly discovered lower-class relatives (Byatt and Sodr , 1995; Sodr , 2015).

In this article, I have identified nine stylized facts concerning the diversity of inequality and seven distributional failures, with few countries able to escape them altogether. The five stylized facts of the distribution of disposable income are: i) inequality is highly unequal across countries; ii) inequality is particularly disparate among middle-income countries, with

59. On survey data, see Appendix 1; on tax returns, see WID (2018) and Alvaredo et al. (2018); and on payroll data, see UTIP (2018). Regarding WID (2018), it would be more useful if its compilers would not mix in their database the bottom 40 per cent with some of the middle. It would be great if they could provide separate information for D1–D4, and D5–D9. Solt (2018), too, could help a great deal by providing information on market inequality by deciles.

60. All of which reminds us of Chekhov’s statement: ‘There is nothing more awful, insulting, and depressing than banality’ (Chekhov, 2006: 238).

some increasing diversity also found among high-income countries; iii) diversity changes into homogeneity when each country's population is divided into halves: the middle and upper-middle, and the top and bottom; iv) although both halves tend to get a similar income share (about half), they divide it among their own constituents very differently; v) in a few countries inequality becomes extreme because D10 can also bring the share of D5–D9 into play. In turn, the four stylized facts of market inequality are: i) significant deteriorations since the 1980s have been confined to the OECD, Eastern Europe and Russia, and China and India; ii) most OECD countries attain a low level of disposable income inequality via a tortuous and highly inefficient route; iii) emerging markets with extreme inequality in both areas are normally those whose higher tolerance for inequality leads them to let market inequality get out of control, and to make little fiscal effort to correct this; and iv) increased market inequality in the OECD has really been about extracting value created by others, or of cashing-in on assets already in existence.

Regarding distributional failures, the three relating to disposable income are: i) 'd10+' (or Palma sector 1); ii) 'd10++' (or Palma sector 2); and iii) the Mediterranean rentier-middle. In turn, those of market inequality are: i) the OECD's ever less sustainable disparity between market and social distributional outcomes; ii) unequal middle-income countries letting oligarchies run amok, while doing more talking than acting in terms of social protection; iii) the very small proportion of the deluge of extra income appropriated by those at the top in the OECD — and of soaring corporate profits — that has been diverted to productive uses, such as investment; and iv) increasingly hierarchical pay structures that are unlikely to be an appropriate reflection of the value of marginal social contributions.

As to disposable income, these stylized facts help us differentiate six patterns of inequality (plus the 'anti-utopian' rentier-bureaucrat one). And almost everything boils down to the share of the rich. Regarding market inequality, it is remarkable how the election of Reagan and Thatcher, and the fall of that infamous wall, triggered among the OECD some *reverse* catching up, including the 'bananization' of their market inequality. As Warren Buffet suggests, 'When you combine leverage with ignorance, you get some pretty interesting results'.⁶¹

We are all indeed converging in this neoliberal era, but the route map points towards features characteristic of some highly unequal middle-income countries: huge inequalities due to mobile elites claiming property rights over the rewards of economic growth in a winner-takes-all scenario. Last year they nearly got there: 82 per cent of the new wealth created was appropriated by the richest 1 per cent, while the poorest half of humanity got nothing (Oxfam,

61. Quoted on the home page of Berkshire Hathaway Inc.'s website: <http://berkshirehathaway340.weebly.com/about-us.html>

2018; see also Hope, 2018) — and the surreal politics underpinning this. It is even tempting to say, ‘Welcome to the Third World’.⁶²

This has also happened with regard to the economic role of the state, which has switched from being the heart of innovation and change, to being the epitome of inaction — reminding us of those Conrad novels where, as in so many sea stories, the main enemy of creativity is stasis. It is, in fact, the deadliest thing of all (Segal, 1997).⁶³ It seems that these states also misunderstood what it means to have a new ‘subsidiary’ role, and took it to mean that they should keep subsidizing the rent-seeking practices of free-riding capital.

As the epigraphs at the start of this article suggest, inequality is about *choice*. Sartre would argue that one must always reject mechanical determinisms (characteristic of most orthodox explanations of inequality) and insist on our ultimate freedom and responsibility. ‘I am my freedom’, says a character in one of his plays. Every act is a self-defining one, and no act can really be blamed on ‘external’ factors (Sartre, 2004). Therefore, nothing could reveal who we truly are more transparently than the inequality our society collectively chooses to construct. As the title of my 2016 paper indicates, each country actually deserves the inequality it has (Palma, 2016a). It is just not credible any longer to keep claiming that we are innocent bystanders of exogenous fundamentals.⁶⁴

Perhaps it is finally becoming ‘common sense’ (in Gramsci’s definition) that the ever-increasing market inequality that has characterized the global landscape since Reagan and Thatcher has been a self-constructed and highly distorting distributional failure. Buffett explains this clearly and succinctly: ‘There’s class warfare, all right, but it’s my class, the rich class, that’s making war, and we’re winning’ (see Stein, 2006). Fundamentals? What fundamentals?

If Smith’s ‘invisible hand’ existed, and were what guides behaviour, this relentless increase in market inequality could not have taken place, as market ‘compulsions’ would have easily put a stop to it — and to its artificially ‘tailor-made’ foundations. In fact, it now feels almost ridiculous even having to say this — like the person at a circus pointing out that when the magician saws a woman in half, it’s only a trick!

In the words of Krugman (2009), the last financial crisis exposed it all: ‘America is looking like the Bernie Madoff of economies: for many years it

62. Trump is like a composite of Latin America’s ‘Magnificent Seven’, those visionary leaders who selflessly introduced neoliberal reforms to the region: his business practices resemble those of Salinas; his aesthetic sense, Menem; his attachment to democracy, Fujimori; his human rights, Pinochet; his ideological sophistication, Collor; his fiscal earnestness, Pérez; and his mental health, Bucaram.

63. On the state’s role in innovation, see Freeman (2008); Mazzucato (2013, 2018).

64. The all-time classic quotation on this matter is provided by Shakespeare, in a speech in *King Lear*: Edmund, Act 1, Scene 2 (132): ‘This is the excellent foppery of the world . . .’. See: www.online-literature.com/shakespeare/kinglear/3/

was held in respect, even awe, but it turns out to have been a fraud all along'. For Stiglitz (2012), as far as financial markets are concerned, globalization 'opened up opportunities to find new people to exploit their ignorance. And we found them'. And at home (Stiglitz, 2018): 'The American economy is rigged'; 'The rules of the economic game have been rewritten, both globally and nationally, in ways that advantage the rich and disadvantage the rest'.

Moreover, as Tony Atkinson reminds us, increased market inequality leads to more of the same due to its cumulative causation, because, 'inequality of outcome ... directly affects equality of opportunity for the next generation' (Atkinson, 2015: 11). In fact, an average wealthy family in the US now spends US\$ 1.7 million per child from nursery to high school to help them get into the Ivy League (Jackson, 2017) — moving the US even higher in the 'Great Gatsby curve', and ever closer to Latin American countries.⁶⁵

Even some of the founding fathers of neoliberalism might have been shocked, as it turned into an artificial environment (of the type of 'scenario 2' in Figure 22) in which (paraphrasing Oscar Wilde) anyone trying to make money by doing something socially useful simply lacked imagination.⁶⁶ I wonder if Karl Popper, for example, would have now added the new breed of all-powerful rentiers to his list of enemies of his 'open society'.⁶⁷ Or (using his own concepts), if he would have called current economic structures a new form of 'totalitarianism' (with their questionable means and arbitrary power). Surely he would also have declared that hegemonic neoliberal ideas (especially economic ones) have become immune from being 'falsified' by criticism; and that neoliberal idealization of unregulated markets has become a new form of 'primitive myth'.

A century ago, the Spanish philosopher José Ortega y Gasset (1918) stated that 'many [in Latin America] have a narcissistic tendency to use reality as a mirror for self-contemplation'. He found the existence of so many 'self-satisfied individuals' striking — a phenomenon that for him was a major obstacle for progress. Perhaps there is no better way of summarizing what is wrong with so many current political settlements and distributive outcomes than Ortega's observations, as these Latin American features have been globalized with a vengeance. As a wealth manager has summarized it, plainly and concisely, 'In the wealth management industry, now you have to kiss a lot of frogs' (quoted in Ross, 2019).

65. According to this relationship, the more unequal the country, the more likely it is that those who are born affluent will keep their status. And if those amazing sums spent per child are not enough, fraud becomes a convenient 'Plan B' for getting them into the Ivy League (The FT View, 2019; Vandevelde and Chaffin, 2019).

66. For an analysis of the original ideas of neoliberalism, see Foucault (2004); see also Frangie (2008); Palma (2009).

67. For Popper's 'Open Society and its Enemies', see: https://archive.org/stream/TheOpenSocietyAndItsEnemiesPopperKarlSir/The+Open+Society+and+Its+Enemies+-+Popper%2C+Karl+Sir_djvu.txt

Current wishful thinking regarding the long-term sustainability of such a ('post-e*') environment — including the sustainability of the growing asymmetry between market and social distributive outcomes in the OECD — has truly become delusional. As argued above, the only low-inequality that is sustainable is the one that is anchored in the production structure, so, unless we re-engineer our development strategy and get a grip on market inequality, we will not only have to keep paying a high price for its inefficiency, but will even be putting our democracy (and our collective sanity) at risk.

The fundamental problem with the current neoliberal development strategy is that there are not many ways to reshape the structure of a 'system' with so little entropy (as it were): there are few ways in which one can redesign its fundamental structure (so that it can move 'forward' in time), if one can't change the fundamentals of its status quo — that those at the top continue to appropriate such an absurd share of national income, and for doing the (low hanging fruit) type of activities they do now. The main problem with such a 'system' is that so much energy is wasted in trying to 'stop time', that there is little energy left to move the system forward. And if anything has to be sacrificed, recent events indicate that it is likely to be democracy.⁶⁸ Indeed, it is quite remarkable how this neoliberal model has proved so effective thus far at reproducing and maintaining itself, as if a sort of autopoiesian system when considered *as a whole*. So far attempts to change it structurally have failed as its networks have tended to remain unchanged, maintaining their identity and proving surprisingly effective at regulating its composition and conserving its boundaries.

This has become evident in the current re-emergence of neofascism, as one of its common characteristics is the tendency to mix extreme-right politics and 'dark ages' morality, with exactly the same primordial neoliberal economics and acute inequality (despite some populist discursive indulgences à la Trump).⁶⁹

Since extreme inequality has been shown to be intrinsically corrosive on so many fronts, I see no valid positive or normative reasons to justify why we cannot live in a world with a much narrower spectrum of inequality — all

68. As President Bolsonaro proudly boosts, 'Democracy and liberty only exist when your armed forces want them to' (Viga Gaier, 2019). Perhaps a less crude way to express this worldview would be 'democracy and liberty only exist if "markets" can afford them'.

69. Bolsonaro, for example, can say in the same sentence that Brazil's military regime should have killed people rather than just tortured them, and that he would prefer his son to be dead rather than gay; but when it comes to economics, he then becomes 'modern' and wants to privatize pensions and anything that moves in the public sector (including the strategic sector that the military used to be concerned with, and what would be left of social protection); he is also happy to let manufacturing become an optional extra, cut even further the meagre taxes paid by the rich and big corporations, stop safeguards protecting the Amazon and other aspects of the environment, and eradicate all vestiges of redistributive 'socialism' (Palma, 2018b).

the way up to a Palma ratio of around 1 in terms of disposable income, with the middle and upper-middle getting at least their half. In terms of market inequality, I also see no objective reason for such uncreative destruction of all of those remarkable post-war achievements. My main unease is that the mounting challenges that we face are happening at the worst possible time, as our social imagination has seldom been so barren.

APPENDIX 1: DATA SOURCES

In this article, the source for the survey-based data on disposable income inequality is WDI (2018) — the last year for which this source reports information (but only if after 2005). Countries with a population of less than 1 million were excluded. However, for China and India, I use OECD (2019), as the data seem far more credible, and also similar to Solt (2018) and LIS (2018). For four countries for which the WDI does not provide information, I used the following: Hong Kong (2018), New Zealand (2018), Singapore (2018), and Taiwan (2018). Finally, in the section on market inequality, I use Solt (2018) for both market and disposable income inequality. For country acronyms in the Figures, I use abbreviations that are used for internet domains (see especially Figures 1 and 2).

APPENDIX 2: PIKETTY'S EXPLANATION FOR INCREASED INEQUALITY

It is unfortunate that Piketty, in his otherwise remarkable book (2014), by unnecessarily relying on the neoclassical theory of factor shares, leads the debate over increased inequality in most OECD countries since Reagan and Thatcher, and the fall of that dishonest wall, in the wrong analytical direction — like the head of a hunt that leads the pack on the wrong path.

Basically — and unlike Kuznets's original proposition, or of Milanovic's 'Waves' — Piketty believes that there is no natural tendency for inequality to decline when a country reaches economic maturity. Rather, increasing inequality is intrinsic to a capitalist economy irrespective of its level of development. For him, it took 'accidents' such as two world wars and a massive depression to disrupt this pattern. Remarkable stuff, but why did he have to trap himself inside a neoclassical modelling straightjacket to explain this? This neoclassical approach is based in the 1950s' Solow–Swan model (whose 'best before date' is long gone), which not only assumed properly competitive markets, but also that the growth rates of inputs such as labour and knowledge, and the GDP share of saving and investment, are constant and *exogenous*. In other words, this is a world where prices are always 'right', where there are no market failures, everybody gets the value of marginal productivities, and there are constant returns to scale and diminishing returns, in finance as well as in manufacturing. Furthermore, an autonomous

and permanent increase in investment rates is supposed to produce only a *temporary* increase in the growth rate of productivity (people in emerging Asia must think that this is a Western joke). In turn, this theory assumes that the only role for financial markets is to fuel the real economy, and that the rate of depreciation is constant, that is, not subject to shocks such as new technological paradigms. Moreover, in this approach there is no government, no increasing returns on manufacturing, no unemployment or spare capacities, no diversity of goods, no natural resources or institutions, and no Latin American-style oligarchies.

Furthermore, the world of the 1950s that this ‘factor shares’ theory (rightly or wrongly) tried to disentangle was rather different; profits were made almost entirely in the real economy, and financial markets only had the levels of liquidity they were able to handle without accumulating more risks than was privately, let alone socially, efficient. There were effective financial regulations, tough capital controls, progressive taxation and pro-growth macros. There was also a close symmetry between total corporate capitalization and the replacement cost of tangible assets: the Tobin’s ‘Q’ hovered around 1, as opposed to the pre-2008 financial crisis level which was well above 2 (Bichler and Nitzan, 2009; Palma, 2009). This growth theory was intended for economies in the ‘maturity’ stage of a specific industrialization paradigm — related to automobiles, oil and mass production for mass consumption — and not economies struggling to adapt to a new technological revolution and a rapidly changing international and financial order.

In this neoclassical theory, what mattered most for distribution of income was the link between the capital intensity of production and the share of profits in national income; and the nature of this link depended on the elasticity of substitution between capital and labour. In this framework, this elasticity needs to be greater than unity if an increase in the capital–output ratio is to lead to an increase in the share of profits in national income — and higher inequality.

As Piketty’s neoclassical model does not ‘fit the facts’, the only way left for him to square the circle was by linking the actual increased share of profits in national income since 1980 with a virtual rise in the capital/income ratio and (a non-existent) high level of substitution between capital and labour. In other words — and against considerable evidence to the contrary — he was forced to assume that we are living in a world in which increasing inequality is due to *too much* real investment and *too much* production flexibility (Harcourt, 2015; Palma, 2016a, Rowthorn, 2014; Taylor, 2014, 2019). That is, in this neoclassical logic if one has too much of a good thing (in fact, in this case two good things), one unfortunately ends up with higher inequality. It would be very difficult to put a better spin than this on increasing inequality.

Furthermore, this type of neoclassical logic relies on a methodology and social ontology that assumes that particularly complex and over-determined

processes, such as the distribution of income, are just the simple sum of their parts; therefore, their account can be reduced to the description of individual constituents and the algebraic representation of the supposedly simple causality interconnecting them (e.g., $r > g$). Thus, this approach can ignore the complex interactions between political settlements and market failures that define contemporary patterns of inequality.

Piketty also overemphasized the role of wealth destruction during World War II in falling inequality; the US saw a similar decline in inequality to that experienced in Europe, despite the fact that the only wartime destruction on the US mainland was an air attack by Japanese planes on Oregon in 1942.

However, after the publication of his book, Piketty recants: ‘I do not view $r > g$ as the only or even the primary tool for considering changes in income and wealth Institutional changes and political shocks — which to a large extent can be viewed as endogenous to the inequality and development process itself — played a major role in the past, and it will probably be the same in the future’ (Piketty, 2015: 48).

The other spheres that he mentions (institutional changes and political shocks), which he rightly views as *endogenous* to the inequality and development processes themselves, could have helped him address questions such as: can rents make up an ever-increasing share of profits, and growth still be sustainable? What are the effects of a greater bargaining power of rentier capital on negative productivity shocks and other collateral damages? Can the gap between the return on financial and physical capital, or that between productivity growth and wages, continue to increase forever? Can the resulting gap between the average ‘ r ’ and the marginal ‘ r ’ also continue to grow and grow? And in particular, can the gap between the ‘ r ’ for the rich — who can invest more in information, who have better access to financial markets, to political patronage and rents, and who can better mitigate the agency costs of their investment — and the ‘ r ’ for the rest (mostly lifecycle savers for retirement) grow for ever?

As mentioned above, despite his unfortunate choice of modelling, Piketty’s (2014) analysis of inequality makes at least three invaluable contributions: it shifts the focus to capital, it helps us learn from history, and it provides invaluable new data.

APPENDIX 3: ONE NARRATIVE OF THE DISTRIBUTIONAL CONTRAST BETWEEN THE TWO HALVES OF THE POPULATION; ‘COORDINATION’ VS ‘ANTI-COORDINATION’ GAMES

Simple game theory language can help explain the contrast shown in Figure 4 (above) between the distributional dynamics found within the middle and upper-middle, and within the top and bottom deciles. While the distributional homogeneity among the constituents of the administrative classes resembles outcomes of ‘coordination games’, what emerges from the heterogeneity in the other half is a scenario of ‘anti-coordination’ games.

An example of the outcome of a coordination game is when players agree which side of the road to drive on. An illustration of an anti-coordination game would be players engaged in ‘playing chicken’ (i.e., which player yields first) as in the film *Rebel without a Cause*: stolen cars are raced towards an abyss, and whoever jumps out first will be deemed a ‘chicken’. This is an ‘anti-coordination’ game because the shared resource is understood as *rivalrous* — that is, sharing comes at a cost (subject to negative externalities).

The homogeneity found in the left-hand panel of Figure 4, and the heterogeneity of the other panel, may well reflect these asymmetries, as ‘chicken’ games are by nature more unstable and their outcomes more diverse, while in coordination games players tend to choose similar or corresponding strategies, leading to positive externalities. For example, the administrative classes, by prioritizing the defence of their overall half, do not contest much among themselves on how to distribute that half between the middle and the upper-middle. That is, the strength given by their unity enhances their capacity to build effective political coalitions to defend their half.⁷⁰ In the other half, by contrast, the perennial rivalry between D10 and D1–D4 could easily lead to negative externalities. From a Marshallian/Keynesian perspective, of course, this does not have to be the case at all, as (for example) increasing wages can be a great incentive for productivity growth, given low elasticities of substitution and positive feedback loops with effective demand. But how to explain that to Latin-style oligarchies, more concerned with defending privileges than with the construction of challenging processes of positive cumulative causations between growth and distribution?

One effective tactic in ‘chicken’ games is to signal one’s intentions convincingly enough, so that the game becomes one of brinkmanship — a strategic move designed to avert opponents switching to aggressive behaviour. Since credible threats — no matter how irrational — can be very effective, the set of institutions and rules within which a distributional struggle is played out, which promote the credibility of one or another party, becomes very important. In fact, one way of understanding post-1980 neoliberal transformations is in terms of the creation of an institutional scenario where the brinkmanship of the top — irrational though it may be — should be taken very seriously by workers and the state.

By now it seems clear that these neoliberal transformations had little to do with increased efficiency, and a lot to do with helping capital to regain the upper hand which it had lost in the depths of the 1930s to the determination of FDR, the horror of war, and the genius of Keynes. The new reforms were intended to have a debilitating effect on workers and the state by creating an institutional environment in which life for them

70. In Latin America, mostly by allying with the rich, and in India by allying with the poor: see Di John (2006); Khan (2004); Lieberman (2003). For Chile and South Africa, see below, and Palma (2011).

would be permanently unstable and highly insecure. In this scenario, a mobile and malleable agent (financial capital) could achieve an unrivalled dominance. In the jungle, capital is king! In this context, any progressive nationalist development agenda, or the exercise of Keynesian forms of state agency capable of (productivity-enhancing) ‘disciplining’ of the capitalist elite, carried the risk of becoming collective suicide pacts.

This brings to mind Foucault’s (2004) proposition that neoliberalism is not really a set of economic policies but a new, more effective technology of power (see also Frangie, 2008; Palma, 2009, 2014b). For Walter Benjamin (1966), all class society is in a permanent state of emergency because rulers are always under threat; neoliberalism could therefore also be understood as an ideology and praxis that attempts to create a class society in which rulers escape from this threat by their ability to debilitate the rest of society enough by imposing on them a continuously insecure life.⁷¹ So workers are now back to old-fashioned precarious jobs, permanently threatened with transfers of those jobs to low-wage countries; safety nets are increasingly porous; easy access to persecutory debt leads to what Krugman (2005) calls ‘the return to a debt-peonage society’;⁷² governments have little or no space for policy options; and so on. And the uncertainties of a new technological paradigm have not helped either, giving massive opportunities to financial capital and a few particular skills, while bringing further uncertainties to the majority of workers and the state (Pérez, 2002).

The bottom line for neoliberalism is how to reconstruct an economic and institutional scenario in which everybody knows that capital can pull the plug whenever it wants to. Under these circumstances, ideological acceptance of the ‘pure’ (game) strategy of the rich could be considered ‘smart’, rather than ‘chicken’, making such an unfavourable position more bearable. Shared pain can even feel reassuring. As Benjamin also reminds us, before all philosophy comes the struggle for material existence (Thompson, 2013). In developing countries, the challenge for capital to develop more effective forms of legitimacy, and more sophisticated technologies of dispossession, has been even greater. In the new complexities of a post-Cold War scenario, just having a Pinochet or two is no longer enough.

The neoliberal discourse may have burst onto the world stage during the thirst for new ideas in the 1970s, promoting ‘order’, market efficiency, individual initiative, non-paternalism, sound macroeconomics and a new concept of the state. However, what was ultimately on offer for workers and the state was a permanent life on the edge, and a high-risk and unstable ‘order’ in which only mobile capital can thrive, with the state mostly reduced to a ‘fire-fighting’ role.

71. On ‘states of emergency’, see Arantes (2007).

72. What Thatcher had in mind was probably not a property-owning democracy, but rather a ‘mortgage-owning’ one.

In a way, Keynes was about fighting these types of inefficient and old-fashioned ‘anti-coordination’ games, searching for more efficient and stable cooperative outcomes. The mass production for mass consumption technological paradigm also helped, especially as it was in its mature stage (Mazzucato, 2013, 2018; Pérez, 2002). However, if ‘chicken’ games turned out to be inevitable, it was imperative to prevent a player prone to ‘irrational’ behaviour — e.g., financial capital — from getting the upper hand. Oscar Wilde warned us about people who knew the price of everything but the value of nothing.

So, perhaps unsurprisingly, what we find in Figure 4 (above) is distributional homogeneity within the administrative classes, and heterogeneity in the struggle between the top and bottom — and the latter is what leads to the diversity of overall inequality across the world shown by the Gini in Figures 1 and 2. The sequence of distorting mirrors and veils that characterize inequality tend to blur this fundamental fact.

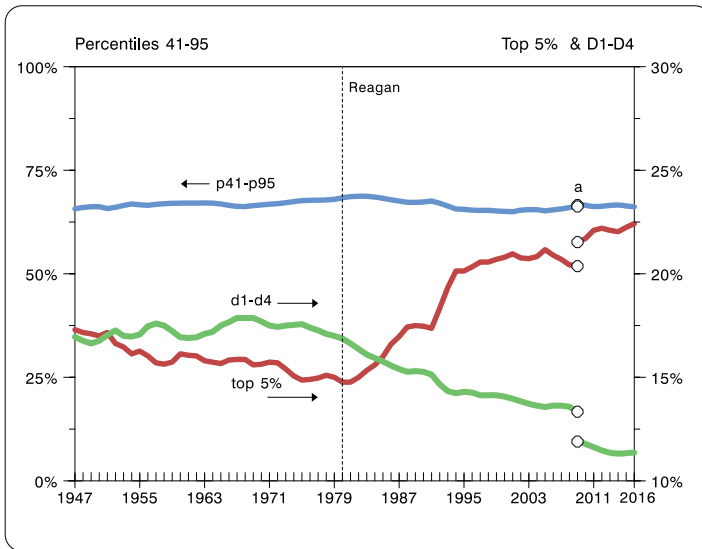
APPENDIX 4: HAS THE HOMOGENEITY OF THE MIDDLE AND UPPER-MIDDLE BEEN STABLE OVER TIME?

As mentioned above, the limited historical data available indicate that, at least for high-income OECD countries and some middle-income ones, the income share of D5–D9 has been fairly stable over time. In the case of the US, for example, the stability in the middle vs the instability at the tails tends to have some clear past-dependency roots (Figure A4.1).

Since, surprisingly, the US Census Bureau only reports quintiles and the top 5 per cent, I have no choice in Figure A4.1 but to divide the population in a slightly different way than I would have preferred (top 5 per cent, and enlarged middle and upper-middle which now contains percentiles 91–95, and bottom 40 per cent).⁷³ This reveals the changing fortunes of the top 5 per cent and bottom 40 per cent: starting in 1947, when both had the same income share of about 17 per cent, the bottom 40 per cent initially improved their lot at the expense of the top 5 per cent — a degree of civilization that would be unimaginable today! Later, and especially after the stagflation that followed the 1973 oil shock, the top 5 per cent began ‘the revenge of the rentier’. This gathered pace in 1979 with the Federal Reserve’s radical monetarism and Reagan, and by 2016 it had over 11 percentage points more than the bottom 40 per cent. However, the 55 per cent making up the ‘enlarged middle’ (percentiles 41–95) appropriated a stable share throughout — not affected by all the many political and economic shocks in between, or even by the change in methodology.

73. When doing the same in a previous paper (because of the same data restrictions), it led to an absurd confusion among some critics, who asked whether the homogeneous middle and upper-middle was D5–D9 or some other larger group.

Figure A4.1. US: Income Shares of Top 5 per cent, Percentiles 41–95, and D1–D4, 1947–2016



Notes:

Unfortunately, these data sets do not provide information for D10.

a = change of methodology. **p** = percentile.

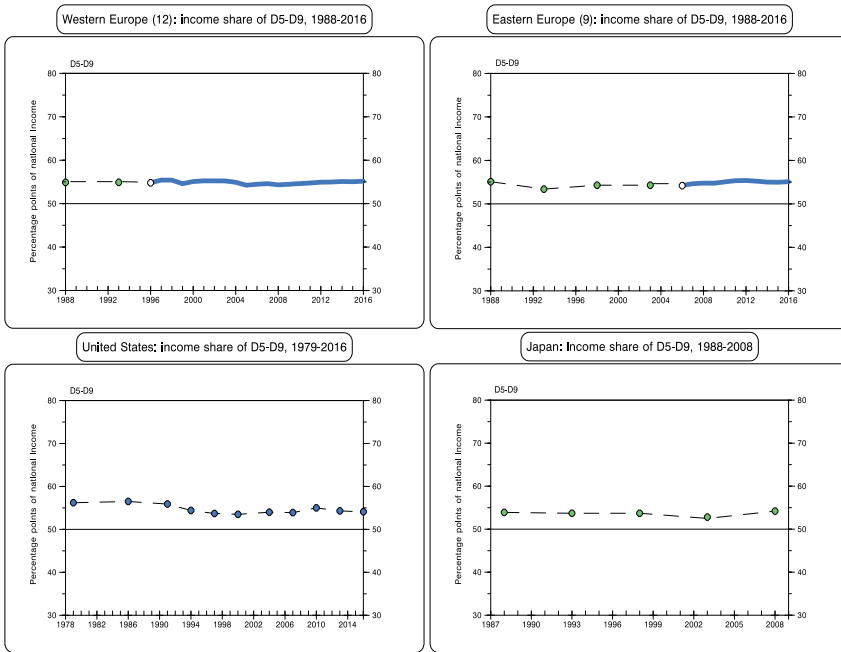
3-year moving averages.

Sources: from 1947 to 2009, US Census Bureau (2010); and from 2005 to 2016, US Census Bureau (2018), with a changed methodology.

Thus, in the US, the last 40 years seem to have been associated with two distributional dynamics: a (better-known) ‘centrifugal’ force in terms of the income shares of the top and bottom deciles, and a (lesser-known) stability of the income share of this slightly enlarged middle and upper-middle. Again (as above), there is not much evidence of the so-called ‘disappearing middle’; rather, we find a middle and upper-middle with a remarkable capacity to hold its own. Other data sets indicate a similar stability in the share of the middle and upper-middle in OECD countries and Eastern Europe (see Figure A4.2).

Furthermore, the little information we have indicates that in many developing countries the relative stability of D5–D9 around 50 per cent also holds; and where it does not, in some countries there is a centripetal movement towards the ‘50–50 rule’ (50 per cent of the population in the middle and upper-middle getting at least 50 per cent of national income). The former applies to some Latin American countries that had already reached the ‘50–50’ level in the 1980s (Figure A4.3, top left-hand panel) — and again, this stability has taken place despite massive upheavals — while the latter is found in unequal countries such as Brazil and Mexico, as well as

Figure A4.2. *Income Shares of the Middle and Upper-middle (Selected OECD Countries)*

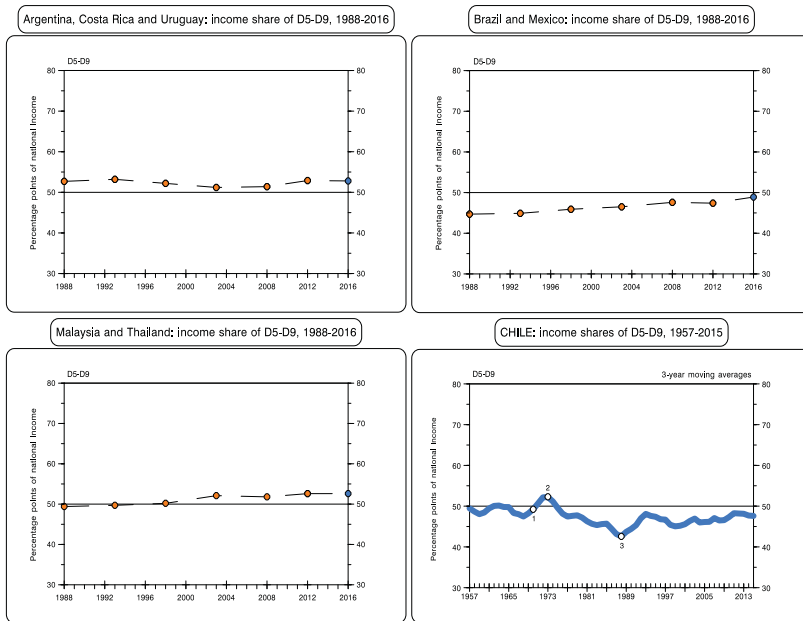


Sources: for the US, all years for which WDI (2018) provides information (note that the source for the US is different in this figure than in Figure A4.1); for Europe, Eurostat (2019); for Japan (and for the period before which Eurostat provides information), WPID (2013; 5-year interval data).

Colombia, Ecuador, Guatemala, Honduras, Paraguay and Peru (Figure A4.3, top right-hand panel).

Due to this ‘centripetal’ movement in Latin America, its average D5–D9 has now finally reached the 50–50 mark. The same has happened in some countries of other regions, such as in Malaysia and Thailand. Finally, Chile indicates that the share of D5–D9 can also be fragile to major political turmoil. First, until the election of Allende in 1970 this share hovered around 50 per cent. Then, during his short presidency, it increased to 53 per cent, only to collapse to 43 per cent at the end of the long dictatorship. Finally, with the return to democracy, this share recovered but settled just below 50 per cent. Unfortunately, lack of data makes it difficult to look at other developing countries for a similar period of time, but Chile indicates that the income share of D5–D9 is not immune to major political and economic shocks. In sum, there is strong evidence from some countries of a stable D5–D9, and of some catching up to the ‘50–50’ rule as well — but not assured immunity against brutal shocks.

Figure A4.3. Income Shares of the Middle and Upper-middle (Selected non-OECD Countries)



Notes:

1 = election of Allende; 2 = 1973 coup d'état; 3 = Pinochet loses his plebiscite to remain in power. Data on Chile in 3-year moving averages.

Sources: for Latin America (except Chile) and East Asia c. 2016, WDI (2018); WPID (2013) before that. In the case of Chile, calculations done by Pamela Jarvis using FACEA (2012); includes 'Greater Santiago', or about 40 per cent of overall population; see Palma (2016a).

APPENDIX 5: FIVE PROBLEMS ASSOCIATED WITH THE OECD'S GROWING DISPARITY BETWEEN MARKET AND SOCIAL DISTRIBUTIVE OUTCOMES

As mentioned in stylized fact 2.2 above, what we are witnessing in the OECD is another type of distributional failure (number 4 on my list), which is about the ever less sustainable *disparity* between market and social distributional outcomes, and its inevitable plethora of distortions, transaction costs and public debts. Here I want to expand on five of them.

First, the OECD's relentless increase in market inequality has obviously not been 'Pareto-improving', as there have been so many losers. However, a Pareto-efficiency type scrutiny is too weak a criterion for normative analysis; making it more operational requires a distributional metric, such as something resembling a social welfare function. And as the steady trajectory of Germany's disposable income Gini indicates (Figure 16, above), it seems

patently clear that this was the *non-negotiable anchor*. That is, no matter what happened in the market (or why, or how), this was unalterable. More specifically, the absolute anchor was a totally stable share for D5–D9 (see Appendix 4, above). So, given this constraint, surely it would have made more sense (and been far more efficient) for Germany to have taken stock of this — as Korea did — and to limit how much the capitalist elite was allowed to change resource allocation for the purposes of self-enrichment, even in the unlikely scenario that they might have chosen to do it efficiently.

Second, inevitably, there are significant transaction costs: what would be the point of such market distributional deterioration just for the winners to compensate those left behind (via taxes and transferes)? It is surely a government failure not to minimize the inevitable waste of resources inherent in first letting things go one way, only to reverse them later — as in the already mentioned nursery rhyme, in which the Grand Old Duke of York marched his ten thousand men to the top of the hill, only to march them down again.

However, third — and crucially — this distributional failure is even more problematic: while the winners got away scot-free, those with less political and economic clout had to finance compensations. That is, instead of making the real winners compensate the losers, in our new modernity it is ‘not-the-real-winners’ who have been forced by the governments to do this. In the USA, for example, not only does Warren Buffett’s secretary pay more taxes than he does, but also billionaire residents in Manhattan’s finest luxury towers only pay about half the federal income tax paid by their concierges, security guards and cleaners.⁷⁴ And the poorest 20 per cent pay an effective state and local tax rate that is half as much again as the top 1 per cent (ITEP, 2018). Basically, as that infamous New York socialite and billionaire boasted, ‘we don’t pay taxes; little people do’ (Rampell, 2009). On top of that, tax cuts under Trump have reduced Federal tax receipts from corporate income by half.⁷⁵

Europe’s ‘reverse catching up’ with this Latin-style regressive taxation became almost as thorough.⁷⁶ As late as the early 1990s, 12 OECD countries still had taxes on net wealth (Sandbu, 2019a). Things are very different

74. See Gilson (2011). The IRS tabulates tax returns by ZIP codes, but some buildings in New York are so large that they have their own ZIP.

75. For Federal Reserve economic data, see: <https://fred.stlouisfed.org/>. And all this in a country in which the combined rate of tax on the income of high earners could rise to 73 per cent without proving counter-productive (Diamond and Saez, 2011). As Summers (2017) argues, in Trump’s tax cuts the sums do not add up. And Krugman (2017) rightly asks, where are those prominent ‘deficit-hawk’ Republican economists hiding?

76. In the UK, ‘New Labour’ Chancellor of the Exchequer Gordon Brown created a tax break for partners of private equity firms, by which they only had to pay a 10 per cent capital gains tax on the sales of shares, instead of the usual 40 per cent. He did this while abolishing the 10 per cent tax band for low incomes, making all earnings above the personal allowance taxable at 20 per cent. As one private equity partner admitted, thanks to ‘socialist’ New Labour he now pays a lower rate than his cleaner (Prynn, 2007).

now — even though, if just one-third of net wealth (e.g., the least productive) was taxed at 2 per cent, that would generate about 5 per cent of GDP of extra fiscal resources (Sandbu, 2019b).⁷⁷

The Danske Bank's € 200 billion money-laundering scandal, the world's biggest, also exposed the extent of Europe's tax evasion and avoidance.⁷⁸ As a law professor states, 'There's no reason anymore to fear prosecution for committing serious corporate crimes' (quoted in Protess et al., 2018).⁷⁹ Why fear prosecution indeed, when — if convicted for tax fraud — instead of prison one may be just sent back to university! In Chile, a judge recently sent corporate executives convicted of a major tax fraud on a course in corporate ethics (with the condition that they had to get a passing grade!), and two prosecutors lost their jobs for investigating corrupt corporate money in politics. At the same time, large corporations such as the FAANGs hardly pay any taxes on profits due to imaginative tax schemes.⁸⁰ The Tax Justice Network estimates tax losses of half a trillion dollars due to global shifting of profits (Cobham and Janský, 2017).⁸¹ In fact, the *Financial Times* now asks if money laundering has become the favourite crime of the elite (Dizard, 2018a).⁸² Who said that crime doesn't pay?

All of this means that in this third aspect of this distributional failure others must be 'over-taxed' to keep the disposable income Gini somehow under control. In the UK, for example, Thatcher, while dropping the top rate of income tax from over 80 per cent to 40 per cent (Reagan did so from 70 per cent to 28 per cent), increased the regressive VAT from 8 per cent

77. For Sandbu (2019b), a columnist in the *Financial Times*, '[a] net wealth tax ... may be the least harmful way to tax capital, even to the point of boosting productivity growth. ... [It could] penalise low-return investments and reward high-return ones'.

78. UK partnerships (largely limited-liability partnerships) comprised the second largest non-resident client group at the offending branch of Danske Estonian (Binham and Parker, 2018). In fact, Danske's board gave its CEO a full year's salary as severance payment (US\$ 1.8 m), and then closed down the branch to cover up. And an executive declared '[Danske Bank] has no obligation to report false client accounts to the authorities' (quoted in Milne and Binham, 2018). Even García Márquez would have smiled.

79. In this 'too-big-to-jail' world, when HSBC became the bank of choice of Mexican drug cartels, or Standard Chartered of those on the official terrorist list, they just got a fine and no one went to prison.

80. Such as the 'double Irish with a Dutch sandwich'; the 'Irish inversion'; exemption of foreign affiliate income from additional home country tax; transfer pricing; inter-firm royalty payments; intra-corporate loans; the geographical allocation of parent overheads and costs; tax havens; and 'round-tripping' (Contractor, 2016; Houlder, 2014; Houlder et al., 2014).

81. It is amazing how some corporations manage to get huge market capitalization despite consistently reporting losses. For a proposal for a new corporate taxation system, see Wolf (2019). On the relationship between international tax competition and inequality, see FitzGerald and Dayle Siu (2019).

82. And the FED seems happy to oblige; while the EU took out of circulation its largest denomination bill to combat money laundering, the FED, instead, has doubled the number of hundred-dollar bills in circulation (to US\$ 1.3 trillion) since 2008, making it the most widely used dollar-note; in a supposed 'digital era', now there are 13 billion hundred-dollar bills stuffed into wallets, safes and suitcases globally helping hide transactions (Tett, 2019).

to 20 per cent as transfers rocketed — largely due to the transformation of the proletariat into the poor-letariat.⁸³ In fact, Thatcher's government never fulfilled its repeated promises to reduce the GDP share of the public finances: it simply shifted taxes around. These increased transfers surely fail 'the compensation test' — of the Kaldor–Hicks variety — as the real winners got away with their gains, and those not invited to the party were left with the bill. Incidentally, but relatedly, the winners would have had plenty with which to compensate others, to make increased inequality into a 'Kaldor–Hicks improvement' process — but we would need another FDR to sort this out.⁸⁴

This misguided targeting to finance social protection is what traditional critics of the welfare state get so wrong. When a German philosopher called it 'fiscal kleptocracy' (Sloterdijk, 2010), he ignored the fact that the 'new' welfare state is as much a subsidy to the rich as a help to the poor, since one way to solve the 'Hobbesian Dilemma' of how to keep the peace in societies with such contradictory distributional aims is for governments to 'rob' someone other than the real winners to compensate those who have become redundant in the new forms of capitalist accumulation. The generous trillion-dollar bank rescue packages of 2008–09, and the over US\$ 15 trillion QE liquidity-pumping machine (which exchanged old bad financial assets for good new money, and drove asset prices skywards on the way) have made the very rich the biggest welfare recipients of all time. So, as mentioned above, our German philosopher should know better: today's post-modern Robin Hood welfare state robs the rich to give to the very rich!

The urgent need to avoid a total financial collapse after 2008 was one thing, but it was quite another to rescue financial institutions without demanding in return a proportional ownership of them — one that could then be sold when markets picked up again to recover those subsidies. This was the Swedish route to dealing with its 1990s financial crisis: to extract a pound of flesh from bank shareholders before writing cheques.⁸⁵ As the *Financial Times* reports, 'All told, the primary effect of monetary policy since 2008 has been to transfer wealth to those who already hold long-term assets — both real and financial — from those who never will' (Kay, 2016).

83. Unemployment immediately jumped by 2 million (1 million in manufacturing) (Marcel and Palma, 1988; Palma, 2005, 2008).

84. For example, in 1982 a person needed only US\$ 75 million to qualify for the Forbes 400 (at today's prices it would be about double that); today it is not far off US\$ 3 billion (Thomhave, 2018). And in the US, the top three billionaires now have as much wealth as the bottom half of the population combined. In turn, the retirement assets of just 100 CEOs are now equivalent to the entire retirement savings of 116 million fellow citizens (Collins, 2018; Collins and Hoxie, 2018; see also Anderson and Klinger, 2015; Palma, 2016b).

85. Sweden did not just bail out its financial institutions by having the government take over the bad debts. 'It . . . held banks responsible and turned the government into an owner. When distressed assets were sold, the profits flowed to taxpayers, and the government was able to recoup more money later by selling its shares in the companies as well' (Dougherty, 2008; see also Palma, 2009).

Basically, higher wealth inequality and shifting taxes down the income scale were not the unintended consequences of this policy, but its very objective — and it did so by driving a growing wedge between those who depend on wages for their (over-taxed and fairly stagnant) income, and those who depend on (under-taxed and rocketing) rents of all kinds, dividends and capital gains. Even Paul Volker now calls the US a ‘plutocracy’⁸⁶ — one in which the share of labour in national income fell by 8 percentage points. Meanwhile, in China it has grown by more than 14 percentage points since 2007 (to over 60 per cent), with the minimum wage growing up to 20 per cent p.a. in parts of China. A similar pattern has unfolded elsewhere in Asia since the global financial crisis, with the labour share of income jumping by about 10 percentage points in Vietnam, the Philippines and Indonesia, and by more modest amounts in India, Malaysia and Pakistan (Johnson, 2019).

In the UK, instead, real wages since the 2008 crisis have had their worst performance since the Napoleonic Wars. In Cambridge, for example, average real academic salaries have declined; yet with the deluge of QE liquidity distorting asset prices, my house — instead of falling in price proportionally to the scale of such a crisis — has actually doubled in price from the already bizarre level it had reached *before* 2008.⁸⁷ And those capital gains are nicely tax free. As a *Financial Times* columnist about to retire rightly laments, ‘But who cares if pension savers . . . may find to our horror that we are the (QE) schmucks?’ — as QE has passed the buck to pension funds long on zero real-yields bonds (Authers, 2018). But those short on ideas but long on cash have done rather well, as the FTSE 100 has shot to an all-time record. Austerity, what austerity?

When words are detached from their meanings (e.g., austerity, welfare state, quantitative easing), we lose our ideological moorings. How else can one understand that, parallel to the asset-price hype and the tsunami of subsidies to the very rich, social protection took the entire ‘austerity’ hit, and now 3.5 million children live in poverty in Britain — more than half in some areas (End Child Poverty, 2018) — while deaths of homeless people in 2018 were up 24 per cent in one year (Strauss, 2018).⁸⁸ Accounts of poverty and destitution in the US make similarly harrowing reading: for example,

86. ‘[One with] people that have convinced themselves that they are rich because they are smart . . . and they don’t like to pay taxes’ (quoted in Collins and Hoxie, 2018).

87. Not that long ago, borough council employees where I used to live in London paid eight times their average annual salary for a property; now it is more than 20 times (and for a smaller house) (ONS, 2017) — in a city that at least for some is beginning to resemble Fritz Lang’s Metropolis. I can’t remember the last time I saw a financial price reflect a fundamental. But do any of the Washington Consensus ‘get-the-prices-right’ zealots care anymore? Central bankers certainly don’t. Something similar happened in parts of the US, where in the last decade median real hourly earning has remained stagnant, while house prices in cities such as San Francisco have doubled (BLS, 2018).

88. All this led a British judge to call the current welfare system ‘cumbersome, overrun and creaking’ (ITV, 2019).

within a 3-mile radius in Massachusetts (from Cambridge to Roxbury), life expectancy drops by 30 years.⁸⁹ Perhaps the only thing I agree with that German philosopher about is that, despite progress, ‘civilisation’s potential for barbarism has also been growing’ (Sloterdijk, 1999).

The fourth distortion created by the *disparity* between market and social distributional outcomes that I want to highlight is that public debts are soaring. As the European Union’s transfers have ballooned, the share of ‘social protection’ now stands at 40 per cent of public expenditure. If we add in public health and education, this share jumps to two-thirds (Eurostat, 2019; Lindert, 2010; OECD, 2019). However, since there are limits to taxing those ‘not-the-real-winners’, governments’ debts are skyrocketing. In the EU they averaged two-thirds of GDP before the 2008 crisis; now they are close to 90 per cent. As the International Monetary Fund (IMF) indicates, the OECD’s public sector finances are in a sorry state (IMF, 2018a).⁹⁰

As discussed above, the new tax status of corporations and top incomes is based on the idea that now they have the right to part-pay/part-lend their taxes (as well as part-pay/part-lend their wages) (Palma, 2009). No need any more for old-fashioned tax structures where they had to pay for public goods via progressive taxation; nor for old-fashioned production structures based on positive but challenging wage–productivity dynamics (see Figure 21, above).

As for governments, while it is so easy and cheap to turn a blind eye to the rising costs of all those *self-constructed* welfare needs — e.g., in real terms, the US minimum wage is now more than a quarter below where it was half a century ago, so a parent earning the minimum wage today does not even get above the federal poverty line — why not just kick the inevitable ever-increasing debts into the long grass and, for the time being, forget all about the highly inefficient nature of all this? Speculators with more liquidity than imagination help by actually paying for the privilege of lending money to governments. But for how long?

It is difficult to imagine how much longer the current delusion of *sustainability* of this growing asymmetry trap between market and social outcomes can continue: that one can go on living with some semblance of civilization, while market inequality and debts are being propelled into outer space by an all-powerful inertia. It is as if a ‘compulsive daydreaming’ type attitude takes over, with its growing detachment from external reality and mounting passivity. On the one hand it is like the Chilean president quoted above (‘in

89. Statement by Rep. Ayanna Pressley (D-Mass), quoted in McKiernan (2019). See also Abramsky (2013); Alston (2017).

90. In an otherwise excellent report, the IMF, however, fails to emphasize that the bottom line of this is a new combination of growing market inequality with a new tax status for those who benefit most from it. As mentioned above, the former creates new necessities for public expenditure, while the latter denies the necessary finance as it lets those at the top free-ride on public goods paid for by others — including the social peace facilitated by others paying the cost of keeping the disposable income-Gini relatively under control.

this life there are only two types of problems: those that will get solved by themselves, and those that have no solution’); and on the other, there is the persistent wishful thinking that this problem will be of the first kind. In the meantime, mobile elites can keep creaming off the rewards of economic growth, and enjoying social peace too.

Fifth and finally: now that OECD markets have finally been unshackled from all those Keynesian ‘rigidities’ and ‘distortions’ brought about by well-intentioned but supposedly economically misguided post-war policies, are Latin America’s levels of market inequality the new nirvana? And is the explosion of the stock of financial assets the best guide for resource allocation? Have OECD countries really embarked on a ‘creative destruction’ of those rigidities? In fact, Moody’s has calculated that, of the resources generated by QE, often *less than 1 per cent* was used to create new productive capacity (BBC, 2018).

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