Inequality, Growth, and Changing Output: Responding to Piketty

Fred BLOCK[1]

[1] Department of Sociology
University of California, Davis
flblock@ucdavis.edu

ABSTRACT.

While Piktetty recognizes the problematic nature of GDP measurement, his framework continues to rely on growth of GDP as one of the key indicators. This is an unfortunate choice because it tilts the analysis away from the insights of Régulation and Social Structures of Accumulation that focus on the nature of economic production at different points in time. To understand periods of crisis such as the 1930's and the last decade, it is essential to examine how changes in the composition of economic output require broader changes in social organization. Whereas the crisis of the 1930's represented the transition to a Fordist or mass consumption economy, the current crisis can be understood as centering on the shift of consumption towards nonmonetized outputs.

Inequality, Growth, and Changing Output: Responding to Piketty

A. Introduction

From the viewpoint of economic sociology, Thomas Piketty's *Capital in the Twenty-First Century,* is as an extremely valuable contribution to debates in political economy. Piketty is explicit in questioning what Marion Fourcade (2014) and her colleagues have termed "the superiority of economists"—the certainty about their own theoretical program that has led economists to ignore the work done by scholars in other disciplines. Moreover, Piketty's focus on the empirical issue of the actual distribution of income and wealth in developed economies over the last two hundred years is an important corrective to the axiomatic and theory-derived analyses that have dominated economics. Finally, Piketty is explicit in drawing a direct connection between the growing inequality of income and wealth in developed economies and the mounting economic difficulties that Western economies have experienced ever since the onset of the Global Financial Crisis in 2008.

But despite these major strengths, this paper argues that Piketty has not gone far enough in rejecting some of the ways of thinking that are part of the neoclassical economics tradition. In particular, Piketty continues to employ the concept of economic output that has been institutionalized within the current global regime for national income accounting. To be sure, he briefly acknowledges the problematic nature of GDP as a measure, but he nevertheless goes on to define his key growth variable—g—as the annual rate of change in real GDP.

I will argue that in doing this, Piketty diverts attention from the changes in the composition of economic output that have occurred at an accelerating pace over the last four decades. This is where the scholarship in the intellectual traditions of Regulation Theory and Social Structures of Accumulation looms so large.[1] In contrast to neoclassical economics, where the economy at all times is producing widgets or even more classically—wine and cloth—these traditions recognize that changes in what the economy produces, as, for example, the rise of the mass production of consumer durables in the U.S. in the 1920's—makes a huge difference in terms of the social organization of production.

This paper will be organized in three parts. The first will look at changes in what the economy produces and the problems this has created for both national income accounting and the shaping of economic policies. The second part uses the Social Structures of Accumulation framework to suggest what structural changes are needed to create a new period of sustained economic expansion. The final part is a conclusion.

B. Measurement and Changes in Output

In the abstract, everyone recognizes that schemes of measurement and evaluation are rooted in very particular social and economic arrangements. The classic instance is the economics of the Physiocrats who viewed agricultural activity as productive and treated commerce and industry as wasteful or parasitic. Hence, it is unsurprising that the overthrow of the Physiocratic theory by Classical Economists occurred in tandem with the rise of modern industry[Block 1990].

Nevertheless, there has been so far little progress in revising the system of national income accounting that was developed in the 1940's. [2] Back then, a majority of the labor force continued to work on farms and factories producing things that were easy to measure such as tons of steel and bushels of wheat. Today, the percentage of the labor force producing tangible goods—farming, mining, construction, and manufacturing--is only about 20% and a lot of what they make now is not so easily measured. With complex manufactured goods and much of what the construction industry produces, it is a difficult task to disentangle ongoing quality changes from price changes.

Even more seriously, the intangible services produced by the remaining 80% of the labor force are extraordinarily difficult to measure, and in some cases, the national income accountants do not even try. Recently, Christophers [2013] has reviewed the history of measurement of the output of the commercial banking sector, and he has shown a succession of arbitrary and highly problematic techniques used by national income accountants that have greatly exaggerated the output of this sector. Despite very significant growth in public sector employment since the 1940's, the output of government workers continues to be measured as equivalent to their payrolls, so there is no opportunity for productivity advances for this significant share of the labor force.

But the deepest problem with the GDP measure lies in what it leaves out. Precisely because it was conceptualized as measuring the output of market activity, it deliberately excludes some of the key byproducts of economic growth such as improved economic security, a cleaner environment, advanced education, more interesting work, the opportunity to live in neighborhoods with more amenities, and a longer lifespan. This is a problem because as societies develop and improve their capacity to provide people with food, shelter, and other basic goods, they tend to spend more money in providing these nonmonetized outputs.

We can see the problem clearly through the Chinese case and the problem of air pollution in Beijing and other major cities. The air has gotten so bad that more affluent parents are moving their children out of the worst hit places to protect their health. To deal with this problem, China is spending vast sums on clean energy and on moving heavy industries away from major cities. But if they are successful, this will appear as a slowdown in the Chinese economy's ability to produce. But the reality is that cleaner air is what people want and shifting investment from producing more consumer goods to cleaning the air is just a change in output—not a decline as it will appear in the GDP data.

In the already developed societies of Europe, Asia and North America, the problems with this measurement scheme have now spilled over into the political arena and have helped generate serious barriers to constructive economic policies. The difficulties emerge at several levels. First, the problems with the GDP data create what we can call "output illusion"—the perception that economic growth has come to a halt even though economies are producing more of the nonmonetized utilities that people want to consume. Second, the perception of slow growth has empowered the advocates of austerity who insist that only by reining in public spending can economic growth be accelerated. However, as we have learned from recent experience, periods of austerity often do not establish the foundations for renewed growth; they simply lead to even slower growth and often more concentration of wealth and income at the top.

A third problem centers on the issue of taxation. While citizens receive both a flow of monetized income—wages or salary plus income on saving plus transfer payments—and a flow of nonmonetized income that includes economic security and environmental improvements, they count only the former as actual income. But as the growth of the former has slowed or even declined since the nonmonetized flows represent a growing proportion of total income, people are very sensitive to higher levels of taxation since it is their monetary income that is subject to taxation. Concerns about taxation result in pressures on politicians for tax cuts. The consequence has been that in most of the developed economies, current tax levels are now below levels of ten or twenty years ago.

At the same time, the demands on government budgets have increased dramatically because many of the nonmonetized outputs are dependent upon government expenditures. The consequence is a stalemate where government does not have the resources to provide more of the nonmonetized flows that people want. The result is a deepening sense that governments are ineffective and higher levels of disillusionment with the political system. This, in turn, creates a vicious downward spiral in which the capacity of societies to respond to their problems is further impaired.

C. The Leverage of an SSA Analysis

The Social Structures of Accumulation framework argues that as the outputs of a market economy change over time, crises become more likely.[Kotz, McDonough, and Reich 1994; McDonough, Reich, and Kotz 2010]. The older set of social structures no longer works, but there has not yet been an effort to construct new and more adequate structures. The classic instance was the global economic crisis of the 1930's that was largely made in the U.S. The key precipitant of the crisis had been the rapid advances in industrial productivity that happened in the 1920's as the combination of electrification and the assembly line facilitated the mass production of consumer durable goods such as automobiles and appliances.

In combination with years of advancing agricultural productivity, the result was a mass production economy without the infrastructure to support mass consumption. The defeat of labor unions in the years around World War I meant that wage gains in the twenties lagged behind productivity advances. Moreover, even though the modern advertising industry and mass media came of age in the 1920's, the credit institutions required for a mass consumption economy had not developed. This mismatch between mass production and limited consumer purchasing power ultimately produced the stock market crash and the Great Depression [Block 2015; Prasad 2012].

To be sure, the crash only came after a spectacular boom in which stock prices went through the roof. Moreover, as we know from Piketty's data, the period of impending crisis coincided with a spectacular increase in the share of income going to the top 1% of households. In this respect, that period was quite similar to the period leading up to the Global Financial Crisis in 2008. In both cases, the demand for productive forms of new investment was quite limited because capital goods were becoming more productive while most people's purchasing power was growing slowly. Capital flowed instead into speculative channels that produced dramatic gains in asset prices that redounded to the richest households.

Moreover, in the twenties, the prevailing economic ideas had made it difficult to see the imminent economic crisis. In the spirit of the prevailing marginalist framework in economics, there was little scholarly interest in aggregate or average worker productivity. The invention of our modern measures of industrial productivity had to wait until the 1930's, so it was only retrospectively that anybody could see that wages had lagged behind the growth in industrial productivity.

In the SSA framework, the policies of FDR's New Deal and the reforms of the Truman Administration represented a systematic effort to create the structures required for a mass consumption economy. Domestically, this meant income redistribution through union recognition, social welfare programs, and a more progressive tax regime. It also meant creating a new financial infrastructure for supporting mortgage lending and expanded consumer lending and it included new regulatory structures to control speculative finance. Globally, it involved rebuilding Europe and Japan so they could copy the U.S. mass consumption model.

It was this mass consumption model that created the "Trentes Glorieuses" from 1945 to 1975. However, problems were already apparent in the last of those three decades, although the troubles of the late 1960's and early 1970's did not constitute a full blown crisis like that of 1929-31. It was more an issue of the mass consumption model losing steam or vitality because of changes in consumption patterns, growing environmental problems, and the shrinking of manufacturing employment. But instead of charting a new course, political leaders sought, instead a series of "fixes"—incremental policy changes designed to revitalize the mass consumption model. Even though their fixes were very different, both Reagan and Clinton presided over quite vigorous post-recession economic expansions. It seems likely, however, that the recoveries were not a result of the specific policies but of growth spurts driven by rapid developments in computer and information technologies that boosted investment.

Shortly after George W. Bush came into office in 2001, there was yet another recession. This time resorting to the Reagan fix of tax cuts did not restart the economy; a weak recovery was dependent on a bubble in housing prices and unsustainably high levels of housing starts for single family homes. So it was finally in the 2000's that the mass consumption model that emerged in the 1930's and 1940's reached its crisis stage. As during the 1920's, the shortage of profitable investment opportunities in the productive economy led to a surge of speculative financial activity that again worked to accelerate the shift of income and wealth to the top 1%. [Block 2011].

When housing prices started downward, in 2007, the whole structure of speculative finance began to implode. Since the U.S. had sold mortgage bonds based on rapidly defaulting subprime loans to financial institutions around the world, the crisis quickly became global leading to the sharpest fall in international trade since the 1930's.

The parallel between these two crisis periods raises an obvious question. If the root of the crisis of the 1930's was the failure to make the transition to a mass consumption economy, what is the root cause of the crisis that continues down to the present? My answer is the failure to make a transition to an economy centered on qualitative growth [Block 1990]. A qualitative growth economy is one that increases the flows of nonmonetized services such as economic security, a healthier environment, clean energy, residential neighborhoods with more amenities, and more effective systems for producing quality education and health care.

The obstacles to a successful transition are considerable. First, the public and the politicians would have to understand that the goal of economic policy should no longer be maximizing GDP growth since that has ceased to be a useful indicator. Second, there needs to be an overhaul of taxation and financial flows to facilitate the investments needed to expand the output of nonmonetized services. With current arrangements, underinvestment in these services will remain the rule. Third, there has to be changes in the global financial architecture since a nation that pursued the qualitative growth agenda would be likely to suffer crippling outflows of capital.

But the continued failure to overcome these obstacles is likely to doom the global economy to a prolonged period of secular stagnation since overall investment levels in the developed nations can be expected to remain well below what is required to move economies towards full employment. And we know from history and from the present that secular stagnation poses a grave danger to international peace and stability because it produces increases in political extremism, intensified international conflicts over resources, and beggar-thy-neighbor policies.

The key point is that redistribution of income alone will not solve the problem. Even if we imagined a global agreement to implement the kind of wealth tax that Piketty proposes, redistributing income to the bottom 50% of households is unlikely to generate enough increased demand to generate the surge in productive investment that is needed to move the global economy to a sustainable expansion. Existing factories could raise their output of most consumer goods without needing additional productive capacity. And even if there were stronger demand for services such as education and health care, political changes would be needed to translate that demand into an expanded supply of quality services.

D. Conclusion

One of the great lessons of the New Deal period was that reformers gained powerful leverage by linking the issue of unjust income distribution to a very concrete idea of how a reformed economy would work. They argued that income should be redistributed to workers and farmers, so they could partake of the fruits of a mass production economy. To be sure, the more radical vision of this project which emphasized collective consumption was marginalized and defeated. Nevertheless, the fact that right-wing campaigners are still trying to undo the New Deal is a continuing reminder of how deep and important were the reforms of that era.

It follows that contemporary reformers must work to link redistributing income with a concrete vision of how a reformed economy would work. To date, some elements of this vision of an economy focusing on qualitative growth have been effectively elaborated, especially when it comes to clean energy and environmental sustainability. But there is still considerable work to be done to elaborate a concrete vison of how we can direct investment flows to support revitalized cities, improved education and health services, greater economic security, and an ever expanding capacity for productive innovation. That vision of where we are headed is indispensable in order to win the reforms at the national, supranational, and global level that would open the path to a more egalitarian economy organized around qualitative growth.

E. References Cited

Block, Fred. 1990. Postindustrial Possibilities. Berkeley: University of California Press.

-----------------2011. "Crisis and Renewal: The Outlines of a Twenty-first Century New Deal." *Socio-Economic Review.* 9 (1): 31-57.

---------------- 2015. "A Neo-Polanyian Theory of Economic Crises." *American Journal of Economics and Sociology*, 74:2 (March): 361-378.

Christophers, Brett. 2013. *Banking Across Boundaries*. Chichester: Wiley Blackwell.

Fleurbaey, Marc and Didier Blanchet. 2013. *Beyond GDP*. New York: Oxford.

Fourcade, Marion, Ettiene Ollion, and Yann Algan, "The Superiority of Economists." Maxpo Discussion Paper 14/3. http://www.maxpo.eu/pub/maxpo_dp/maxpodp14-3.pdf

Kotz, David, Terrence McDonough and Michael Reich. 1994. *Social Structures of Accumulation.* Cambridge: Cambridge University Press.

McDonough, Terrence, Michael Reich, and David Kotz. 2010. *Contemporary Capitalism and its Crises.* Cambridge: Cambridge University Press.

Piketty, Thomas. 2014. *Capital in the Twenty-First Century*. Cambridge: Harvard University Press.

Prasad, Monica. 2012. *The Land of Too Much*. Cambridge, Mass.: Harvard University Press.

Stiglitz, Joseph, Amartya Sen and Jean-Paul Fitoussi. 2010. *Mismeasuring Our Lives.* New York: New Press.

---

[1] There is considerable overlap between SSA Theory and Regulation Theory, so when I refer to SSA, I am referencing f both of these traditions.

[2] There has been increased discussion among economists of problems with the existing national income accounting framework. See especially Stiglitz, Sen, and Fitoussi 2010 and Fleurbaey and Blanchet 2013.