The World Is Not Enough

The Rich get Richer.

Even if initial conditions included an even distribution of wealth, different individuals have different capabilities and a meritocracy implies at least some deviation from equality. Once the divergence has occurred is it likely to further diverge or converge?

The rich have access to capital which can be invested for an additional return over and above the returns to labour. This argues for divergence from equality. This divergence is not predicated on any assumptions about the overall growth of the economy. It is entirely possible that the poor get poorer.

Richer households tend to have fewer children.

Many rich households are rich because they have deferred having children and spent more time accumulating wealth. These households are more likely to plan their financial management more thoughtfully. They are likelier to impart this financial acumen to their offspring. Households with fewer children are also likely to devote more resources to better equip their offspring with the necessary skills to prosper. Inheritance faces less dilution in smaller households. Richer households having fewer children exacerbates the concentration of wealth.

Richer households tend to have children later in life. As experience varies positively with age, richer households are likely to have more experienced parents who can transfer such experience to their offspring. However, having more time, resources and stock of wealth may deter risk taking, discourage competitiveness and result in more conservative behavior and a smaller variance of future wealth generating potential among offspring.

Poorer households tend to have more offspring, less time and resources to spend on the offspring and a smaller stock of wealth to distribute among a larger pool in inheritance. However, they may encourage greater competition, greater risk taking and a greater variance of future wealth generating potential among offspring.

Richer households save more and consume less. They have more investment capital. While the current expectations for real return on capital may be substantially negative, this is due to low interest rates and high inflation. The high inflation is likely to be more damaging to lower income households as the source of inflation is coming from higher agricultural prices as well as energy, a larger proportion of what a lower income household consumes.

Another factor of income inequality is globalization and world trade which favors highly skilled workers at the expense of lower skilled workers. Trade liberalization transmits economic inequality across borders depressing lower skilled workers’ wages in developed markets while increasing their wages in emerging markets.

There are many factors which contribute to inequality of income and wealth and these are well known. Above are but a few. While traditional studies of income or wealth inequality focus on directly measurable quantities to estimate the marginal factors of contribution future trends may be less measurable and more oblique instrument variables may be required. Alternatively, a raw statistical study ignoring factors may be more illuminating. It is hard to quantify human ingenuity and motivation. What is clear is that absent a unilateral and oppressive redistributive policy, the variation in human ability and the self reinforcing nature of that variation in ability implies divergent distributions of wealth.

Unconstrained divergence in wealth distribution may be economically viable (although I am not totally convinced about this) but it is certainly neither socially nor politically sustainable.

In a closed system, development sometimes requires the subjugation of an underclass. Income and wealth inequality empowers this. There will be jobs which are not preferred which either command a low compensation or are unsatisfying. It is assumed that the unsatisfying nature of such jobs is priced into the marginal cost of supplying that form of labour. Often in reality it is not.

Countries are not closed systems and in some examples there is an active policy of filling the lower tiers of the labour market with imports. An optimal immigration policy (ignoring social and political aspects) seeks to attract individuals who are accretive to per capital or aggregate GDP growth. Such immigration policy of course includes courting talent for the higher tiers of the labour market seeking individuals who are accretive to per capital GDP growth either directly through their efforts or through osmosis or other transfer of intellectual property. It also includes attracting individuals to fill less attractive functions which indigenous or incumbent residents may be unwilling to supply their labour to. Optimal immigration policy must discourage individuals who are dilutive to the economy whether resident or potential immigrant alike to exit or not seek entry to the country.

This is a wholly unworkable policy. At some stage, the supply of talent for the less attractive functions must be constrained in scarcity. It is not possible to protect resident incumbents from either supplying such labour to the market themselves or from depressing the marginal cost of employing such talents through imports. Ultimately, however, if we expand the boundaries in the example, it seems to imply that at some stage, either some forms of labour will not be supplied at ‘acceptable wages’ whatever that means, or wages in those sectors must rise. In a totally free and unmanaged market, some such sectors must command wages higher than traditionally preferred sectors. In some developed metropolises a plumber may be paid more than a teacher or a skilled healthcare professional. While these are positive examples of the free market in action, many examples exist to the contrary.