Jürg Helbling Recommends "Capital in the Twenty-First Century" by Thomas Piketty

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> »*A high inequality of wealth has several consequences, for it will not only slow economic growth but also endanger democracy and threaten social stability.*

Piketty puts economic inequality back on the agenda not only of economic debate but also of public discussion. Whereas mainstream economics considers budget restrictions for households and firms and emphasizes the importance of private property rights, Piketty addresses the unequal distribution of wealth and its consequences for economic growth and social stability. For him, economics is a social science—or political economy—that seeks to contribute to an understanding not only of the current problems but also of the history of industrial-capitalist societies by taking political structures and processes into account as well. Piketty uses a historical and statistical approach to examine the development of the unequal distribution of wealth in Europe and the United States since the late eighteenth century.

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By using an impressive mass and a wide range of statistical data, Piketty demonstrates that the inequality of wealth increased in the long nineteenth century with a peak at the eve of World War I, after which it started to decrease, particularly in the course of the world economic crises in the 1930s and during World War II and, due to progressive taxation of capital and income, remained low until 1975. It was only in the 1970s and 1980s that inequality of wealth distribution started to increase again.

Wealth consists of income and capital (property). Income stems from labor (wages and salaries) and from capital (profits, dividends, interest, rents, and other income from capital ownership). Capital (K), or property, comprises bonds and shares as well as means of production and real estate. The total income (Y) is the value of goods produced and sold during a year (GDP). Total capital is the result of the accumulation of income in previous years. The higher the inequality of income is, the greater the capital formation in the highest decile of the income strata will be. Consumption reduces wealth; saving increases it. Capital can be invested and accumulated. Piketty measures the unequal distribution of wealth as the capital/income rate multiplied by the rate of return on capital ($K/Y * r$). For the share of capital in total income to remain constant, the return on capital (r) must be equal to the rate of economic growth (g). According to Piketty, r tends to grow faster than g in the history of capitalism, with a growing inequality as a consequence. But r may also grow slower than g with the inequality in wealth distribution decreasing, as was the case between World War I and the late 1970s.

As long as the rate of return on capital exceeds the rate of growth, the income and wealth of the rich will grow faster than the typical income from work. A high inequality of wealth has several consequences, for it will not only slow economic growth but also endanger democracy and threaten social stability. The concentration of capital is an endogenous feature of capitalism without state intervention. Only the tax policy of the state can create a counterweight to this. Taxation of inheritance and of high income strata—as well as the skillful use of tax revenues—will thus reduce the unequal distribution of wealth as well as promote economic growth, strengthen democracy, and contribute to social stability.

Literature

Piketty, T. (2013). *Le Capital au XXIe siècle*. Editions du Seuil, Paris. (*Capital in the 21st Century*). Cambridge MA: The Belknap Press of Harvard University Press, 2014.