



UNIVERSITY OF ICELAND

# Thomas Piketty's Capital

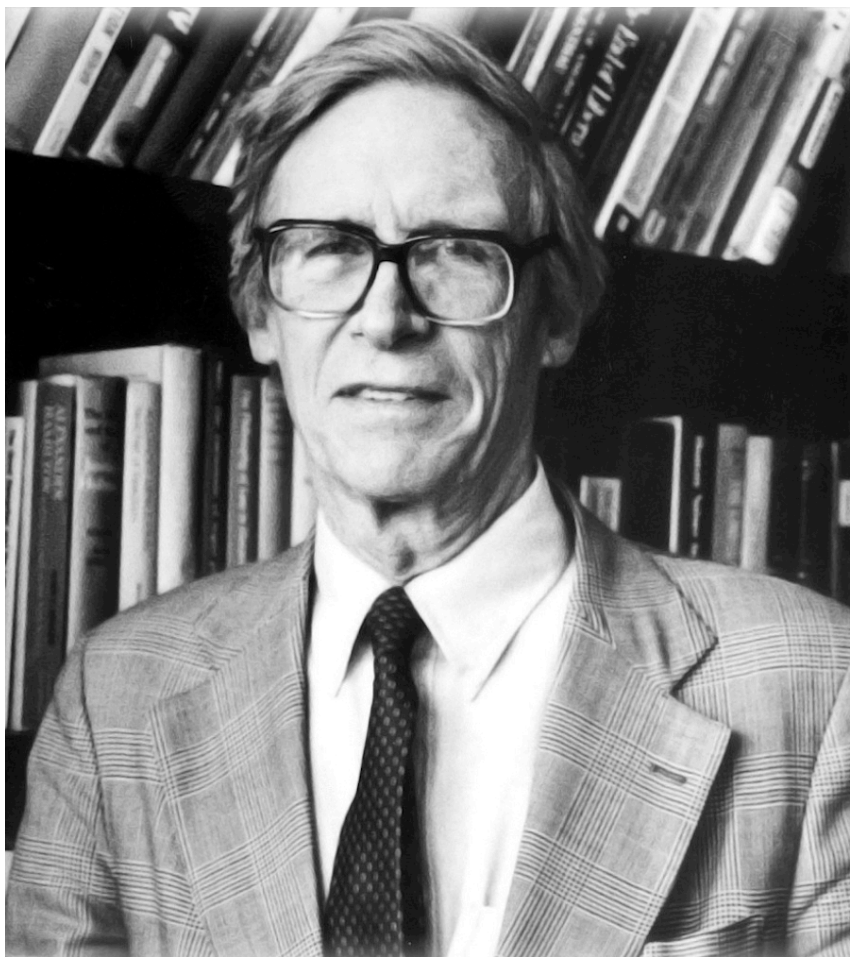
## A Critical Review

Professor Hannes H. Gissurarson

Estudantes pela liberdade, Rio de Janeiro

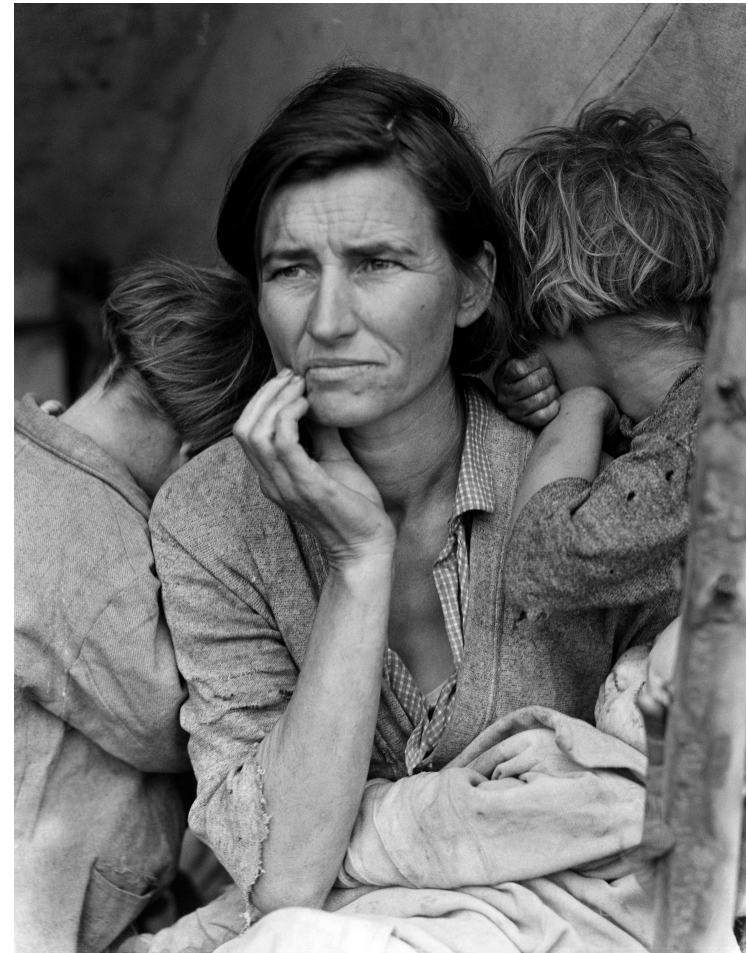
16 April 2016: 15–15.50

# Piketty Replacing Rawls as Prophet

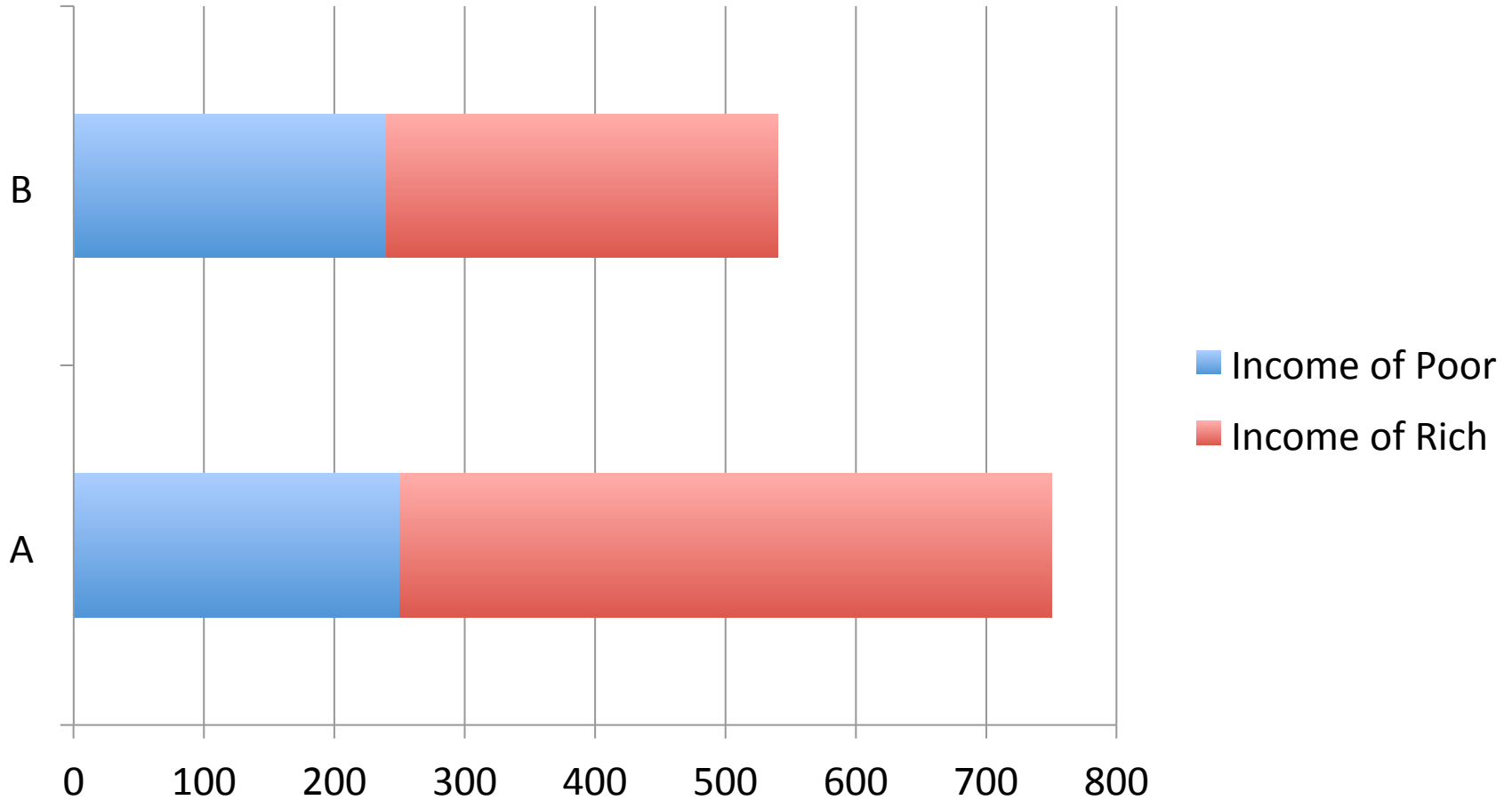


# Rawls, and the Poor

- Main proposition:  
Income distribution just if poor are as well off as they can be: maximum of minimum (maximin)
- Let us look at Index of economic freedom, with data from long time and many places



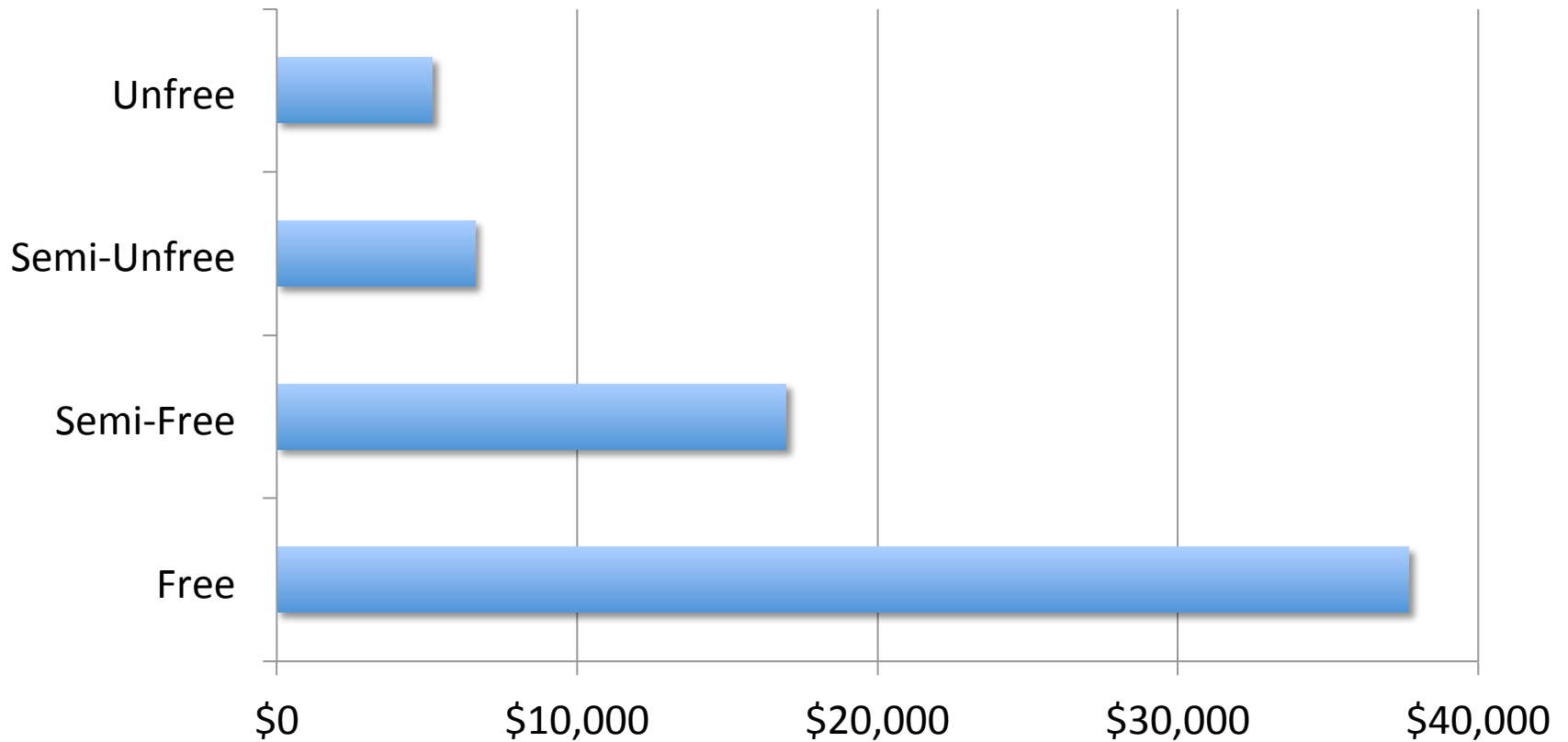
# Which Country Better, A or B?





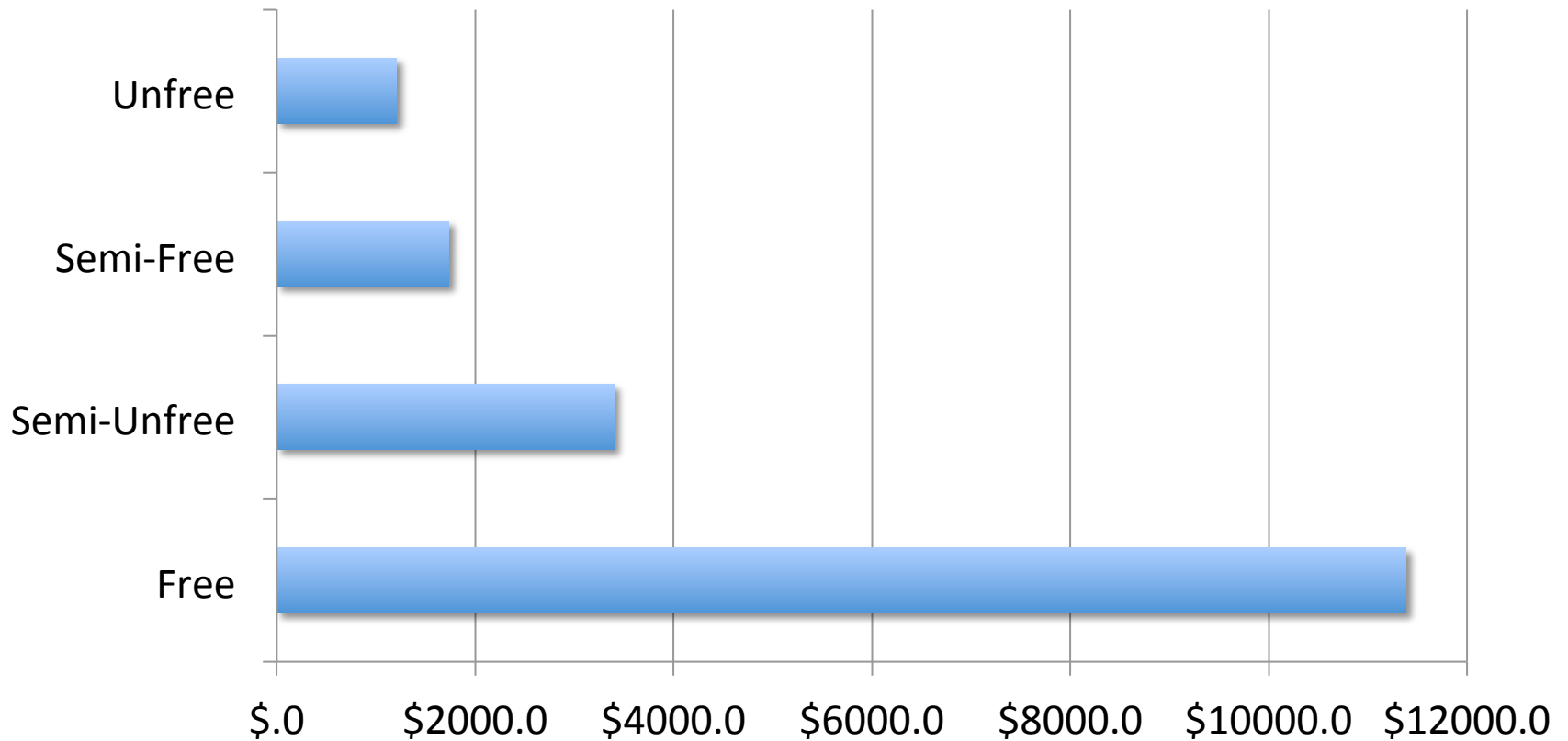
# Four Worlds of Freedom

**Average GDP/capita 2010**



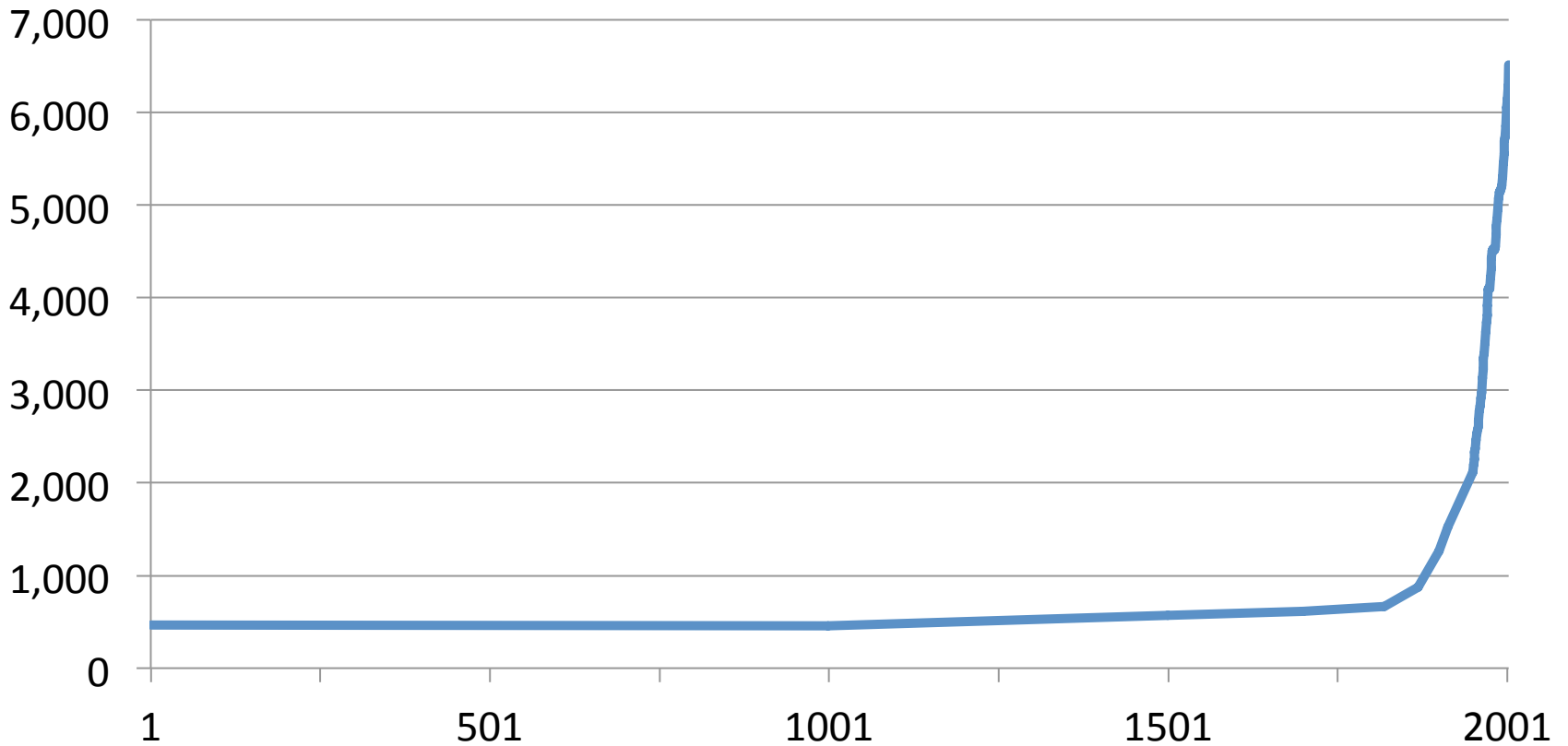
# Lowest Incomes in Four Worlds

**Average Income of Bottom 10% in 2010**



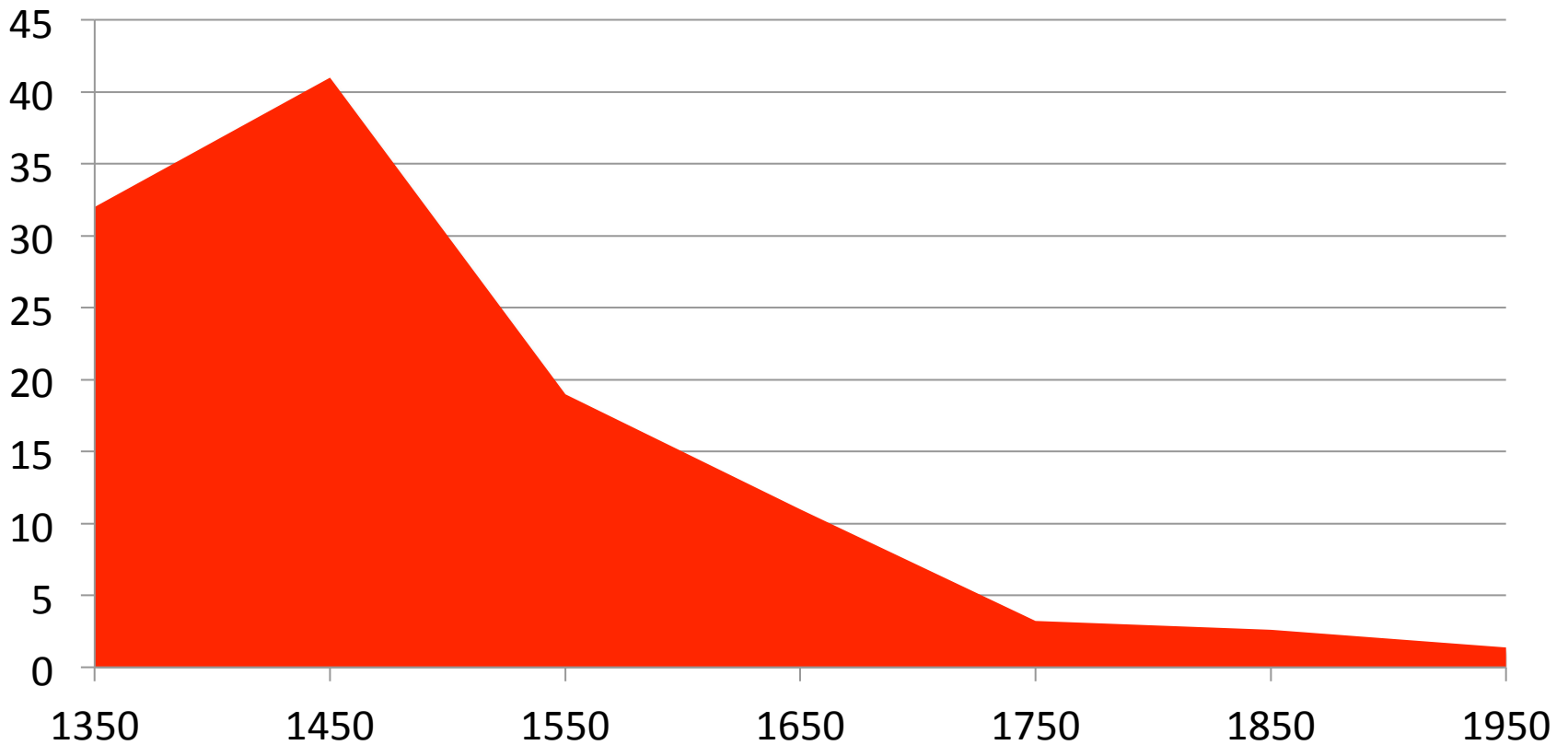
# Productive Power of Capitalism

**World Average GDP per capita 1–2003 AD in \$1990**



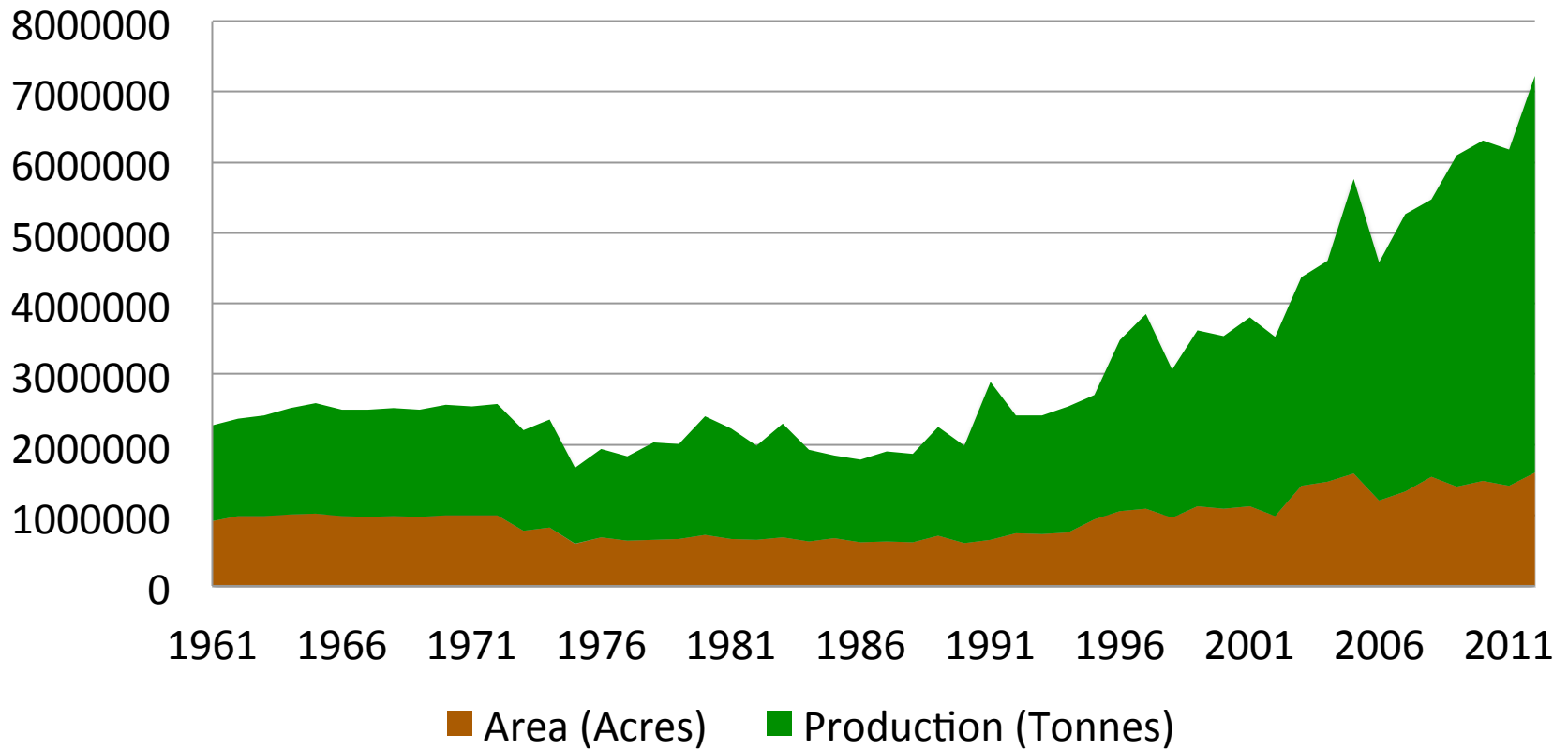
# Much Less Violence than in Past

**Homicide Rate in Europe per 100,000**



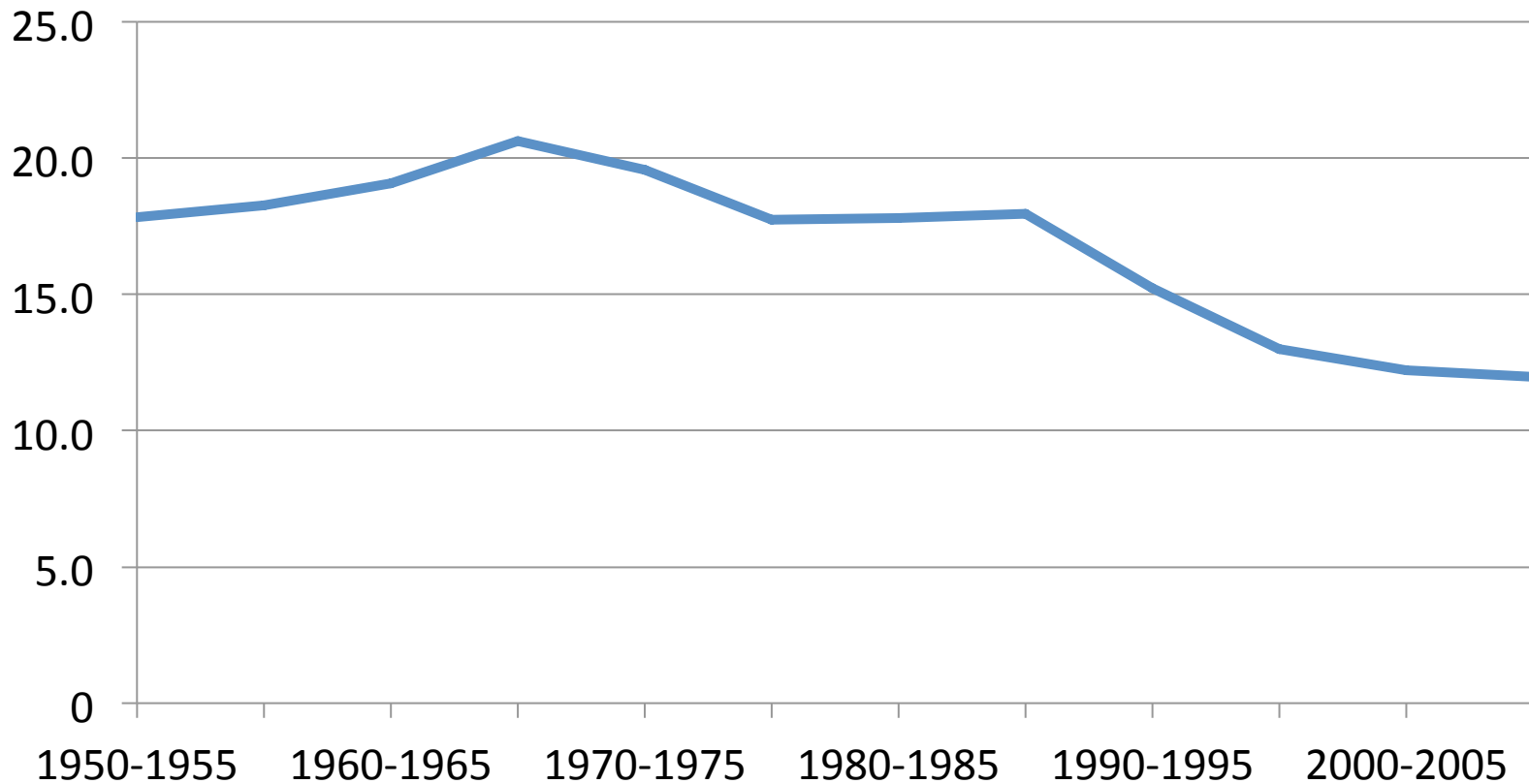
# The Green Revolution

## World Production of Cereals



# Escaping the Malthus Trap

**Rate of Natural Increase of Population per 1,000**



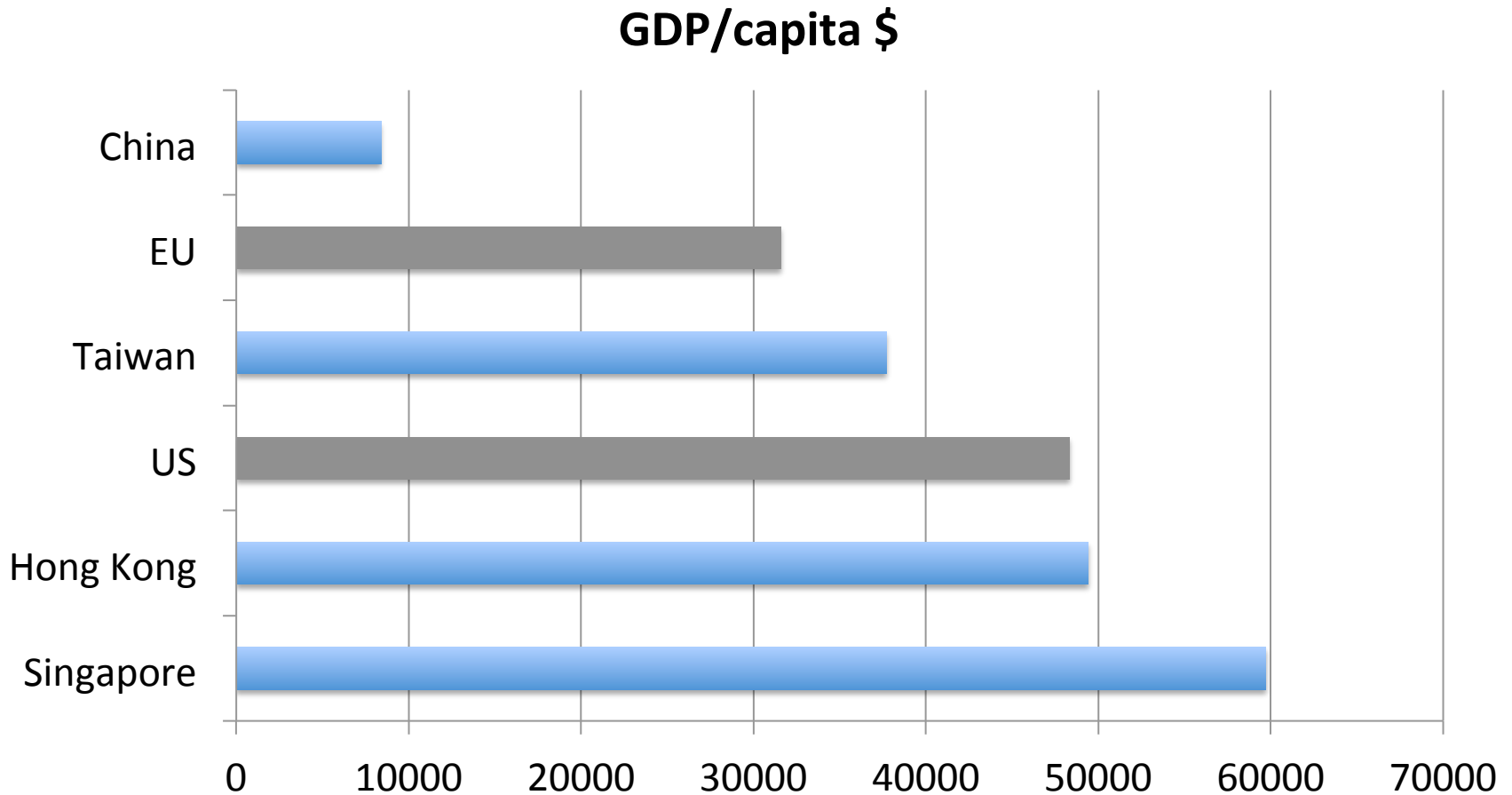


# Similar Countries, Different Paths

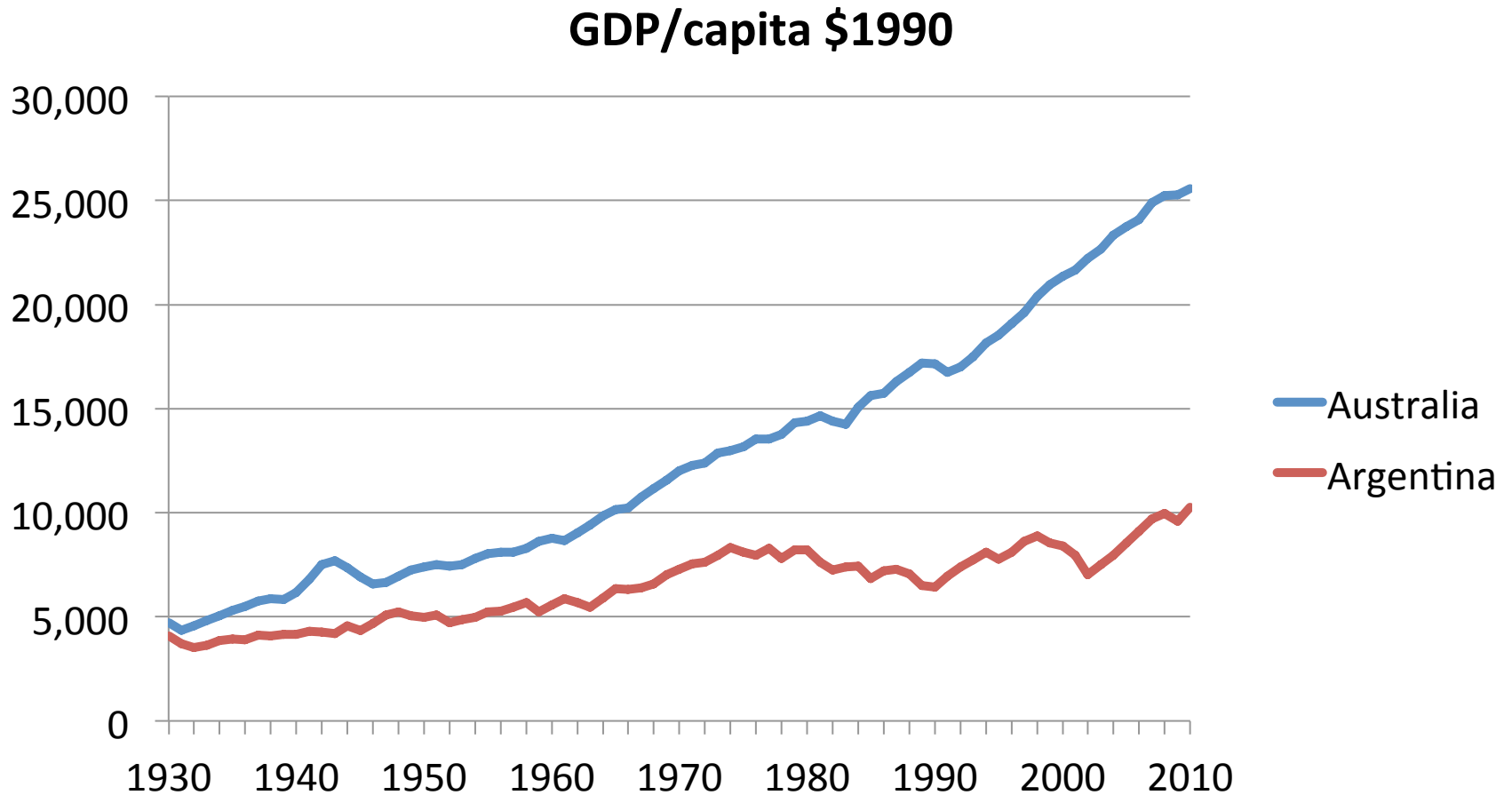
- Four Chinese economies: mainland China, Hong Kong, Taiwan, Singapore
- Australia and Argentina, similar natural resources, European immigrants
- Singapore and Jamaica, small tropical islands under British rule



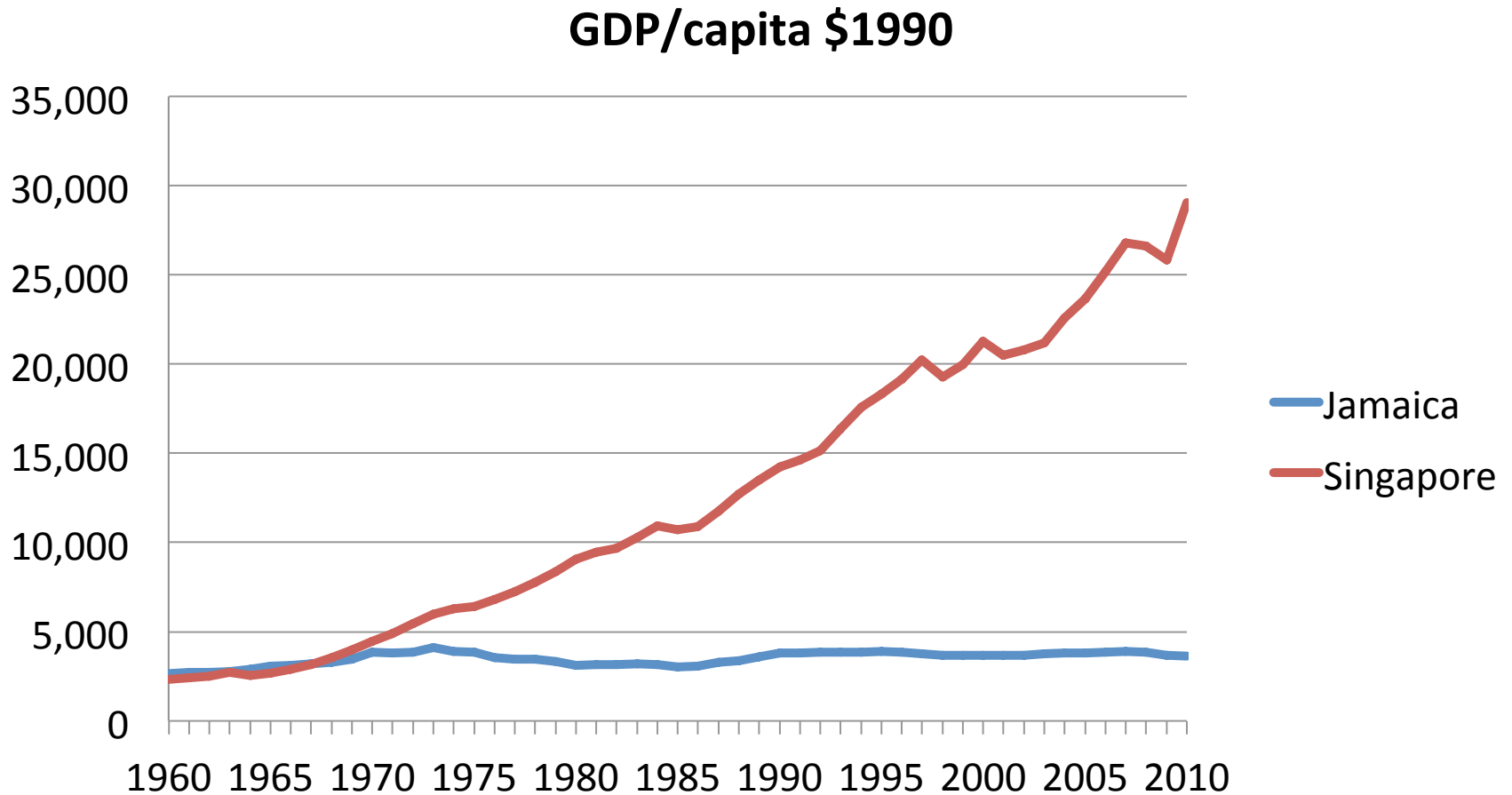
# Four Chinese Economies 2011



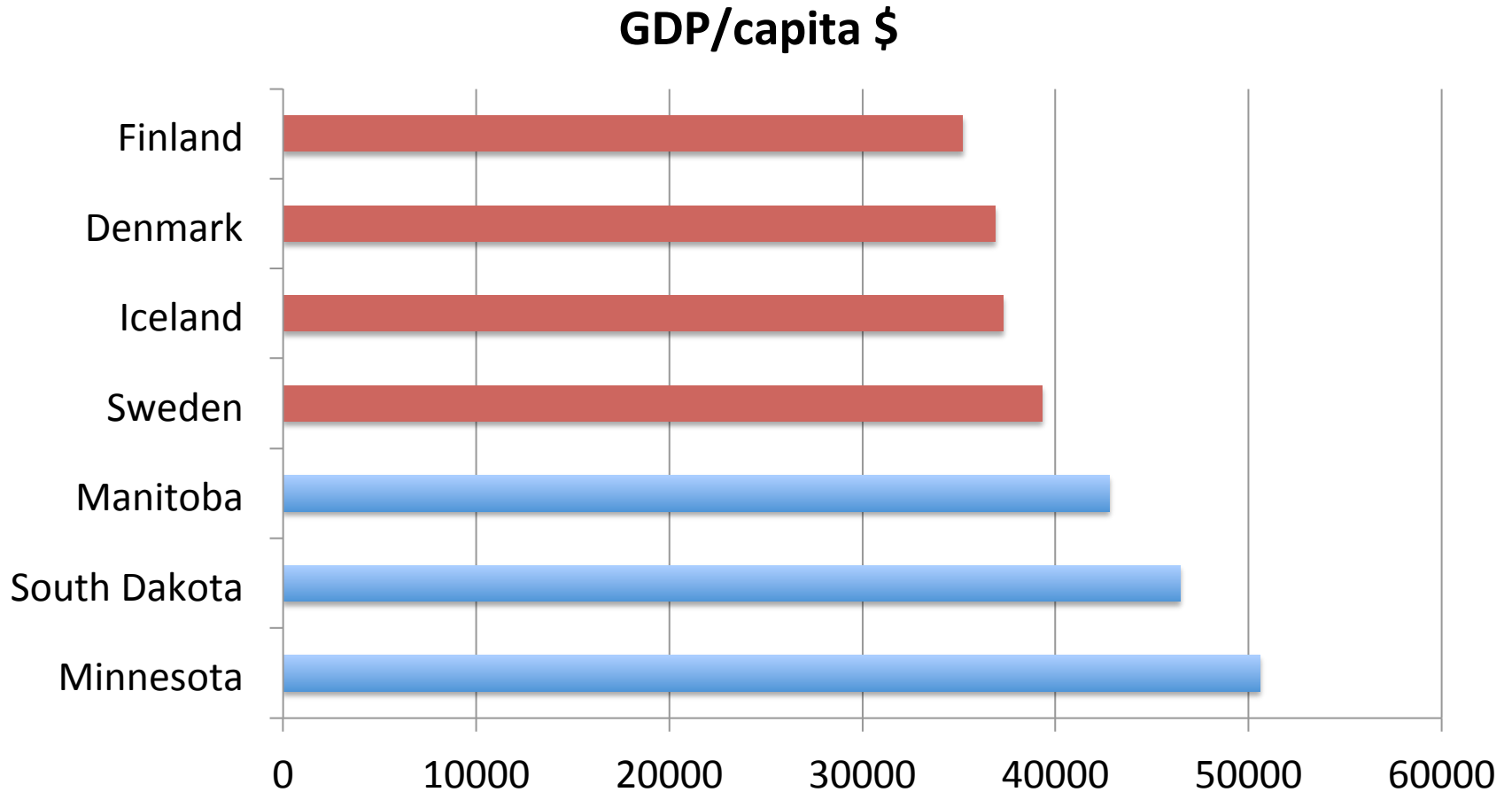
# Parting Ways: Australia and Argentina



# Parting Ways: Jamaica and Singapore

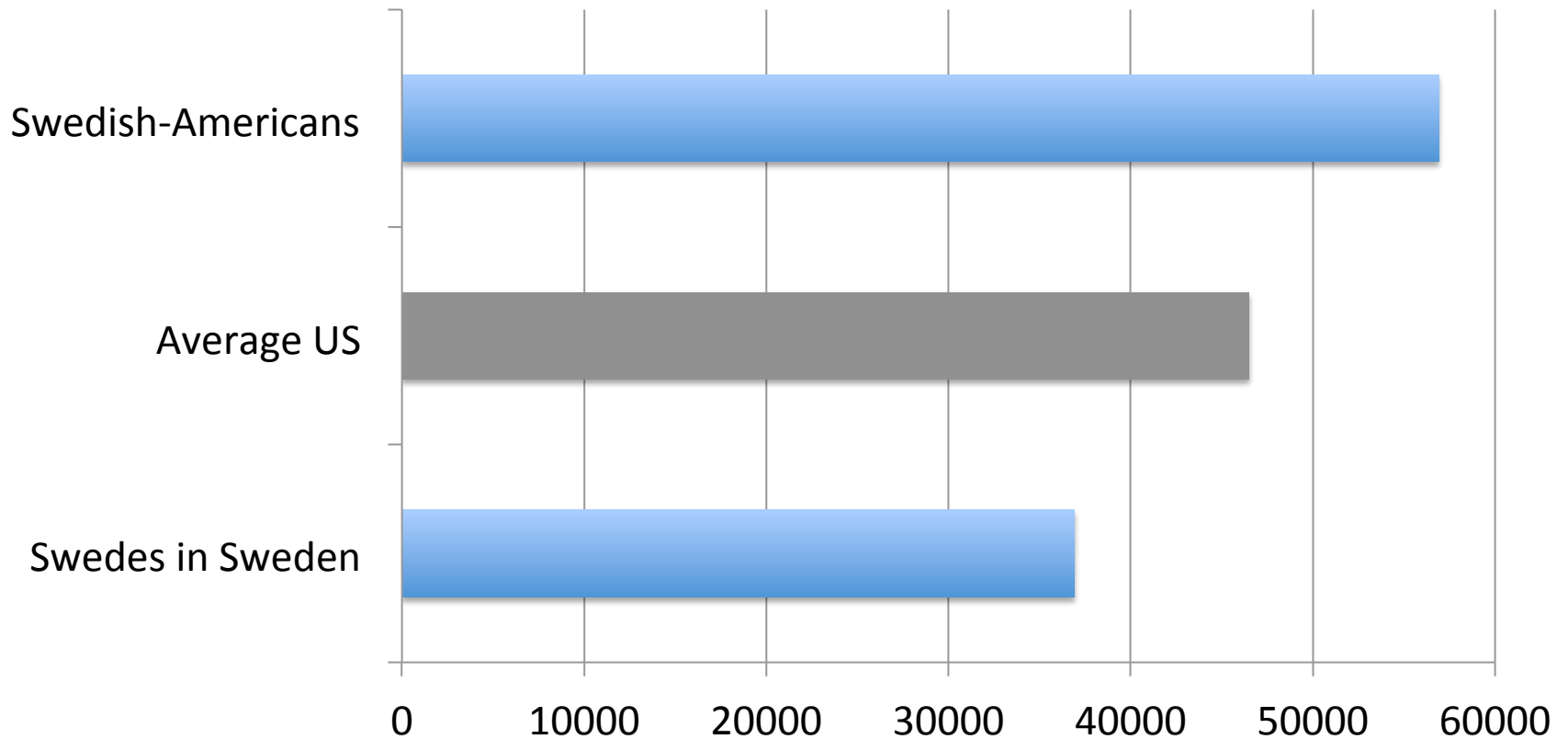


# Seven Nordic economies 2010



# Swedes in Different Economies

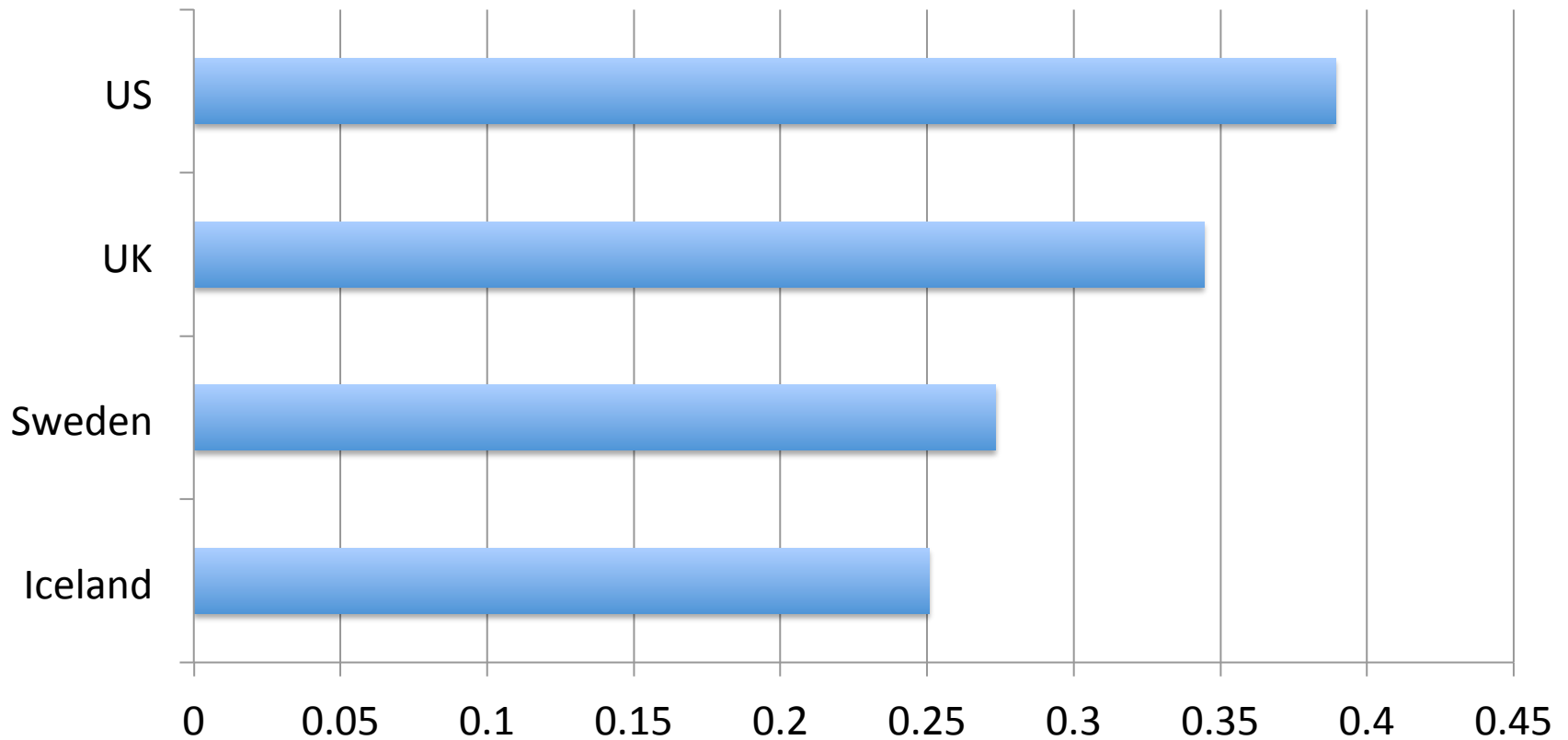
**GDP/capita 2008 \$**





# Income Distribution in Four Countries

**Gini Coefficient 2011 Disposable Income**



# Country of Immigrants

- US subject to waves of immigrants, first from Europe and Asia, now from Mexico and Central America
- Brings down US averages, even if only temporarily
- Creates a statistical illusion

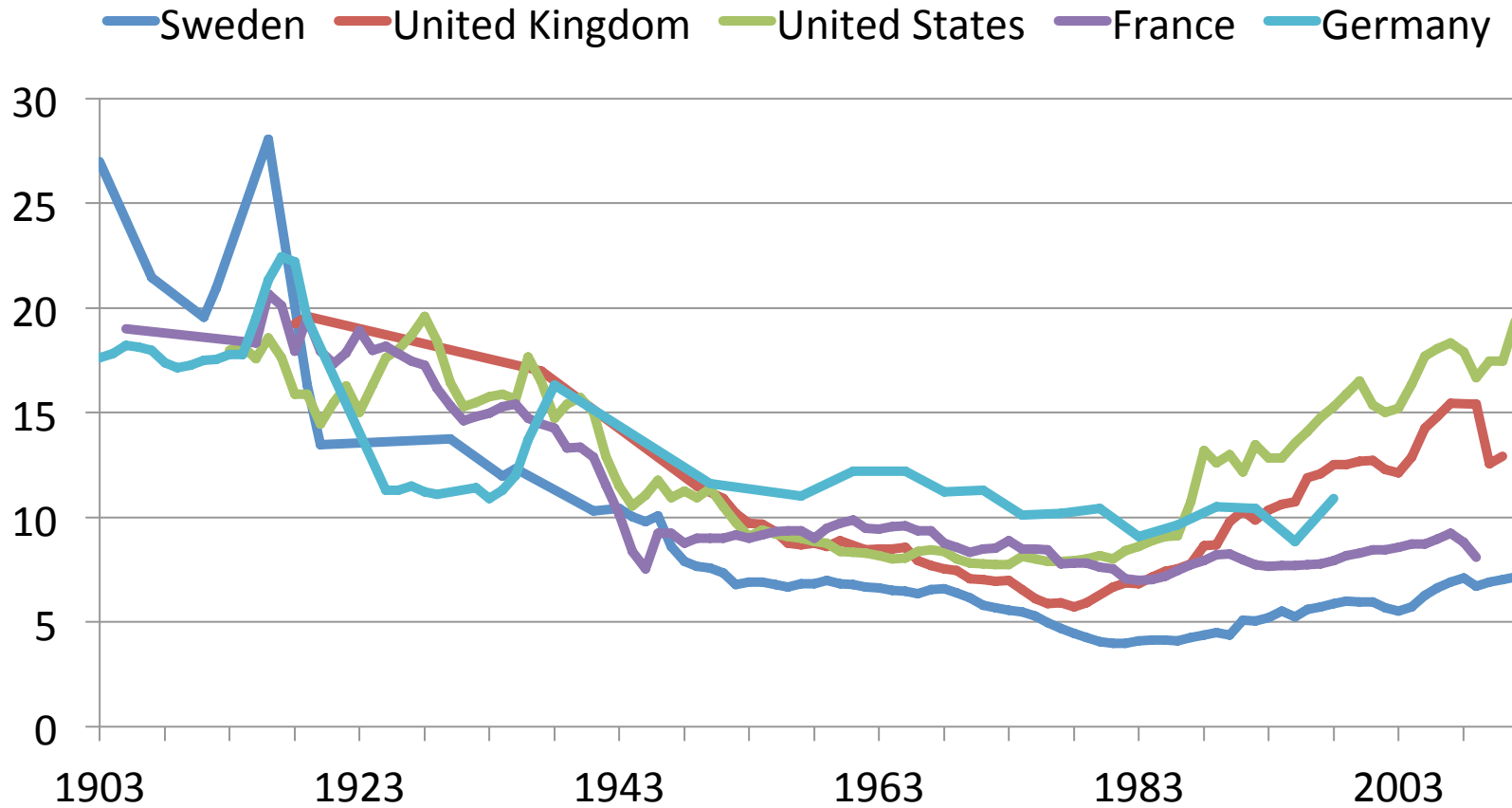


# Piketty, and the Rich

- Main proposition: poor do not gain from capitalism
- Capital accumulated by rich, because  $r > g$
- Need for Confiscatory international taxes on wealth and top income



# Piketty's Income Share of 1% Top



# Problems with Piketty's Numbers

- *Financial Times*: Errors in calculations of wealth distribution in the UK
- French economists: inflated real estate prices cause overestimate of wealth
- Neither criticism very relevant to Piketty's income distribution
- However: no correlation between the redistributive welfare state and income inequality

# Problems with Piketty's Method

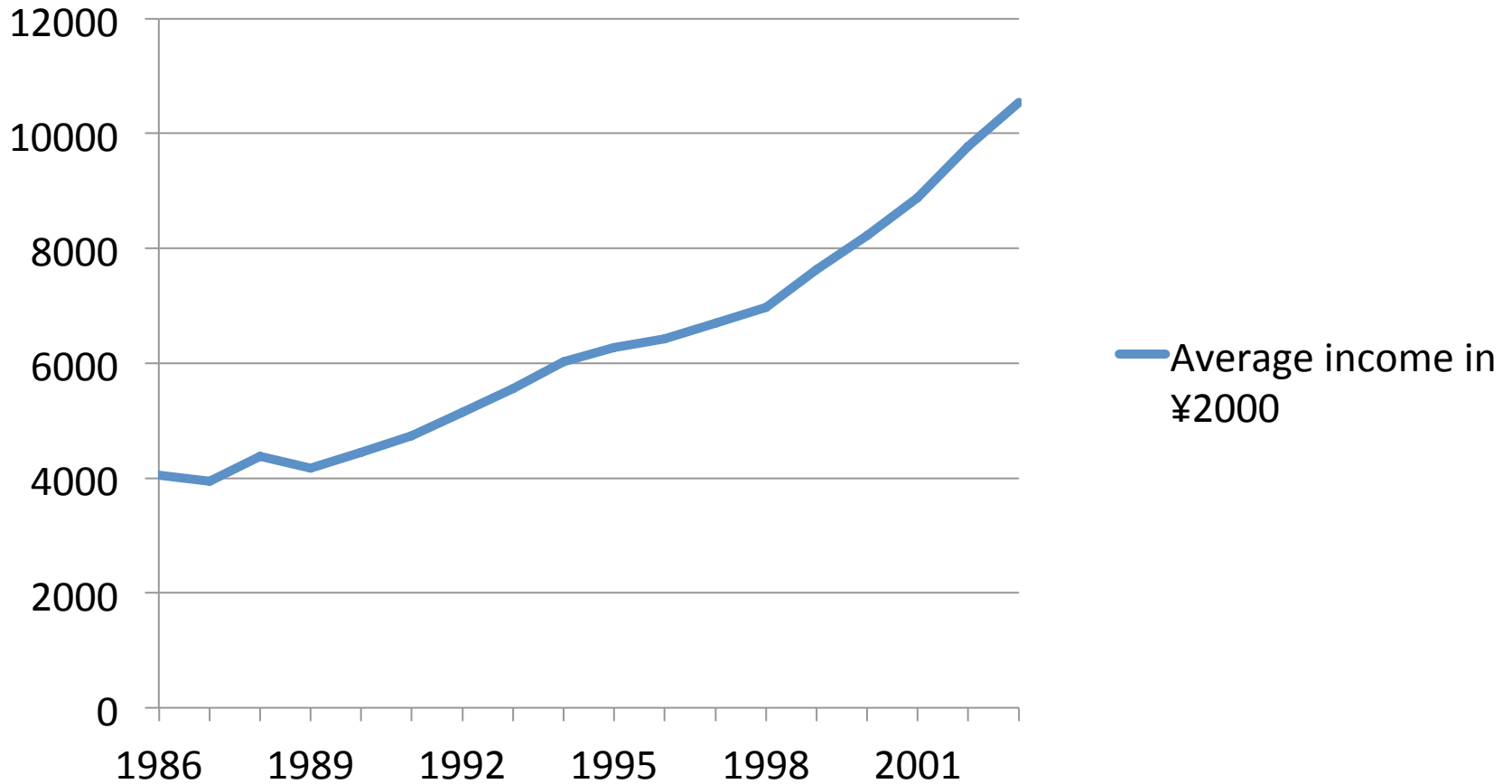
- Underestimates bottom income: uses income before transfers
- Overestimates top income: ignores changes brought about by changed taxation, top income becoming more visible
- Method suffers from same problems as Gini coefficient: relative share of top increases if more people study longer or live longer



# Impact of Globalisation

- Piketty possibly right that bottom income stagnant or even slightly decreasing
- Competition from China and India: Massive migration into middle class
- Global income distribution become more equal, while income distribution in West less equal
- West only 1 of 7 billion people on earth

# Income Share of 90% Bottom, China



# Do Data Reflect Reality?

- Data on bottom or average income in West show stagnation in equalised \$
- But living conditions of bottom group (and all groups) much better than before
- Takes fewer hours to work for most goods, not only lightbulbs, vacuum cleaners and food, but also books

# Cheaper Goods, Easier Life



# Better Goods, Require Less Work

Appliances	Hours of work 1959	Hours of work 2013
Washing machine	100.5	23.3
Clothes dryer	81.3	23.3
Dishwasher	90.9	20.7
Refrigerator	167.5	22.4
Freezer	153.1	17.1
Stove	90.9	28.5
Coffee Pot	11	3.6

# Why the Super-Rich?

- People with special, non-replicable skills (i.e. earning rent from abilities), innovators, entrepreneurs, entertainers, athletes, film stars
- By definition, supply (almost) fixed, while demand flexible
- Suddenly find demand, the market for their services, going from 300 million people to perhaps 3–4 billion, impact of globalisation

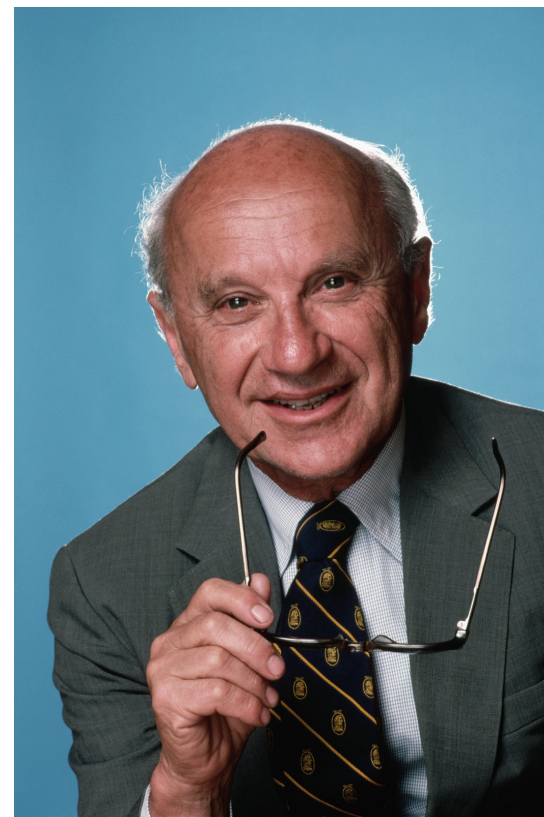


# Larger Market for Special Talents



# What's Wrong With Inequality?

- Country with income distribution  $D_1$
- Milton Friedman gives lecture
- 1,000 attend, each paying \$50
- Friedman \$50,000 richer, 1,000 people each \$50 poorer
- Less equal distribution  $D_2$
- No problem: everybody happy
- Distribution by choice: from each as she chooses, to each as she is chosen



# More Problems with Piketty's Ideas

- Rate of return of capital not always higher than economic growth
- Capital not immobile and unbreakable
- Capital not in hands of rentiers, landowners and bondholders, also innovators, entrepreneurs, investors, funds, third sector organisations
- Dispersed by children, divorces, risks, uncertainties

# Challenge to Retain Wealth

**Barbara Hutton**



**Charles Koch**





# Reading Balzac



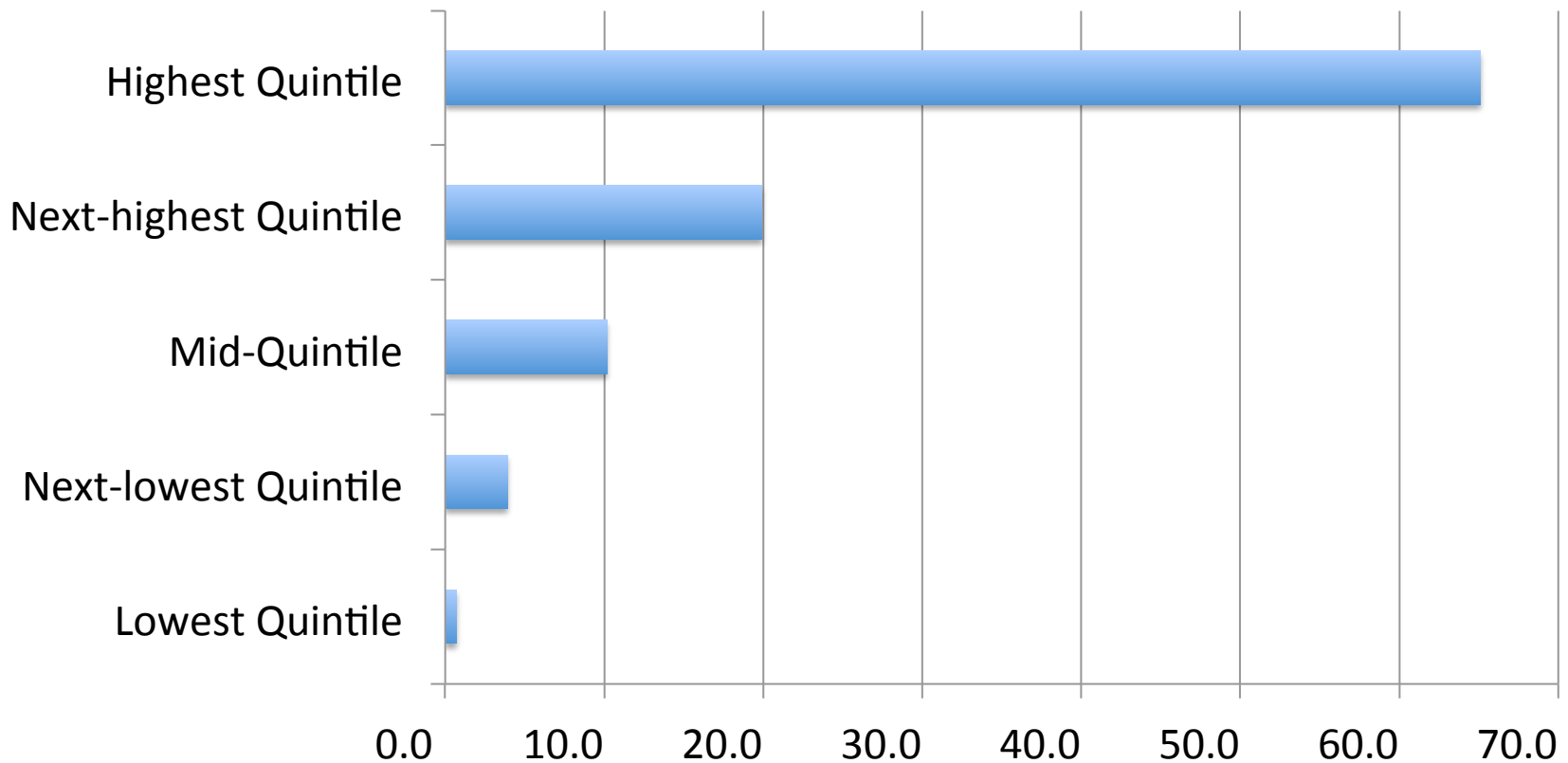
- Piketty quotes Balzac, *Old Goriot*
- Story of fragile wealth
- Goriot penniless
- Anastasie's lover with gambling debts
- Delphine's husband failed speculations

# Economic Growth

- Piketty's confiscatory taxes would become a self-fulfilling prophecy
- Immense creative powers of capitalism
- Almost unlimited possibilities of economic growth
- Capitalism needs innovators, entrepreneurs and investors
- Welfare state needs taxpayers

# Sustaining the Welfare State

**Proportion of US Total Tax Payments in 2000**



# Rand's Thought Experiment

- The rich contribute most of tax revenue
- What happens if they emigrate (as they sometimes do, cf. Cuba and France)?
- What happens if they choose to disappear?  
Theme of Rand's *Atlas Shrugged*





# Further Benefits of the Rich

- Pay for experimental process to turn luxuries into necessities
- Provide risk capital; 1,000 experiments instead of 10
- Have means to fight bureaucratic aggression and government oppression



# The Challenge of the Red Queen

**Proportion of Gross International Product**

