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ECONOMIC INEQUALITY AND THE MAIN FACTORS THAT CAUSE IT

Abstract: This article discusses economic inequality and the main factors that cause it.

Key words: economy, inequality, distribution of resources, economic factor, risk, market relations

Economic inequality is the difference in economic well-being between individuals in a group, between population groups, or between countries. The problem of economic inequality is related to the concepts of equity, equality of outcome and equality of opportunity.

The unequal distribution of income and wealth was not considered wrong for a long time. One of the first to think about the question of income inequality was the 15th-century humanist Matteo Palmieri. In the dialogue “On Civic Life” he points out that the rich have more money because they are more talented and hardworking. The idea that talent and hard work are rewarded with money is a popular misconception, despite many examples to the contrary.

Karl Marx was the first to develop an economic theory that questions the fair distribution of income. Analyzing the formation and movement of capital, Karl Marx formulated the idea of exploitation of employees. One of the results of his work was a mathematical formula that estimated the degree of exploitation as the ratio of the size of surplus value to the cost of labor. In other words, the ratio of the time a worker creates value for others to the time he works for himself (creating the equivalent of his wages).

Karl Marx believed that the process of increasing economic differentiation in the capitalist world is going on continuously - the rich are getting richer, and the poor are getting poorer, the middle class is disappearing. As economist Thomas Piketty notes.

At the end of the 19th century, Vilfredo Pareto identified a specific structure of income distribution among Italian households, which was characterized by the concentration of 80% of income in 20% of families. He believed that the degree of economic inequality, the proportion of rich people in the population, is a constant thing.

Pitirim Sorokin argued that the degree of economic inequality over long periods should fluctuate around a known constant. Assuming that an excessive increase in the degree of inequality or equality is equally fraught with a national catastrophe and upheavals, Sorokin believed that an increase in inequality would lead to the fact that a narrow group of plutocrats would be easily overthrown or destroyed. Indeed, some of the oligarchic regimes in South America subsequently proved unstable. According to Sorokin, the limitation of the difference in incomes by the ratio of 175:100, carried out during the years of war communism by decree of 1918, contributed to devastation and famine.

When Simon Kuznets wrote about changes in inequality in rich countries (and a couple of poor ones) in 1955, the US and UK were experiencing the largest decline in income inequality ever recorded in history, coupled with rapid growth. It therefore seemed quite reasonable to look at the factors behind the decline in inequality, and Kuznets found them in the expansion of education, in the lower intersectoral disparity in labor productivity (thus the rent component in wages was equalized), in the lower return on capital, and in the political pressure to increase social benefits. Then he looked at (or rather imagined) the evolution of inequality over the past century and thought that inequality had been growing and peaked in rich countries at the turn of the 20th century due to the movement of labor from agriculture to industry. This is how the famous Kuznets curve (reverse U curve) appeared.

The Kuznets curve has been the main tool used by inequality economists in analyzing the relationship between development/growth and inequality over the past half century. But the Kuznets curve gradually fell out of favor as it predicted low levels of inequality in very wealthy societies, while there was a steady increase in income inequality that began in the late 1970s in virtually all developed countries.

Currently, the Kuznets curve is trying to revive the economist Branko Milanovic.

The distinction between "circumstance" and "effort" as determinants of income was crystallized in the work of John Reumer and has its roots in the work of John Rawls and Ronald Dworkin. On the basis of differences in the determinants of income, economists divide total inequality into two components: inequality of opportunity—defined as inequality due to external circumstances that an individual cannot control, such as parental education, race, and country of origin—and residual inequality, which is supposed to arise due to the difference in effort and luck. The influence of external circumstances on income, such as discrimination in society based on gender and race, is considered wrong, and therefore the resulting inequality as a result of these circumstances is unfair.

As Hufe, Kanbur, and Peychil point out, the intuitive power of separation between circumstance and effort in distinguishing between fair and unfair change in income is very clear, but it is not the only moral feeling when it comes to the distribution of income. Society cannot refuse someone in need of help, even if the person in need had a “good start” in life and “destroyed it” as a result of his own choice. Khufe, Kanbur and Peychil call this the demand for "freedom from poverty". Thus, a normal distribution of income should reflect both fundamental moral principles. On the one hand, individuals must be held accountable for decisions under their control. On the other hand, there must be a lower bound on the critical consequences of the choice. Thus, the overall measure of unacceptable income distribution, which could be called unfair inequality, should combine "equality of opportunity" and "freedom from poverty". Of course, forced redistribution has a negative effect on incentives. However, it is possible to establish a framework within which the ideal of egalitarianism can be reconciled with incentive constraints, according to Nobel laureate James Mirrlees.

Hufe, Kanbur and Peychil estimated the components of inequality for 31 European countries. On average, 17.6% of total inequality, as measured by the mean log deviation (MLD), is unfair—that is, attributable to violations of equality of opportunity and freedom from poverty. Unfair inequality is most common in Lithuania, Italy and Romania - 27.9%, 31.6% and 29% of total inequality, respectively. Incomes are most fairly distributed in the Netherlands, Finland and Norway - unfair inequality is 7%, 9.3% and 12.5% of the total, respectively. Outcomes are determined by equality of opportunity and freedom from poverty in roughly equal proportions.

Low social mobility. Country-by-country analysis shows that as economic inequality increases, so does social mobility—the Great Gatsby curve. Economist Raj Chetty found the same effect of inequality on intergenerational social mobility when analyzing the impact of environment on children within the United States. In his report "The Lost Einsteins", Raj Chetty points out that the decline in social mobility is a negative factor for economic growth and innovation.

Negative impact on the development of children. According to a number of studies by neurologists, poverty and high economic inequality negatively affect the development of the brain of a child.

Crime. Statistics show a positive relationship between economic inequality and crime rates. Morgan Kelly, analyzing data from the US, found that inequality had no effect on property crimes, but there was a clear association with violent crimes.

Lower life expectancy. Statistics show a decline in life expectancy with increasing economic inequality. This relationship is observed both between countries and within countries.

Contributes to financial instability. Rising inequality leads to overconsumption. The widening income gap is pushing the underachievers into exorbitant debt. Robert Frank of Cornell University argues that rising elite incomes lead to a so-called consumption cascade that ends in a rise in debt: “The rich spent more simply because they had more money to spare. This cascade makes it much more difficult for middle-class families to achieve their financial goals.” The same findings are found in the work of Elizabeth Warren and Amelia Tiagi. Their book The Double Income Trap traces the rising tide of individual bankruptcies that began long before the general financial crisis. The authors showed that a significant factor in these bankruptcies was the growing inequality of public education, which in turn reflected income inequality: middle-class families tried to buy houses in areas where there were good schools, for which they had to take out loans that made them vulnerable in case of illness or job loss.

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