"Summary of article by Chris Tilly and Randy Albelda: Not Markets Alone: Enriching the Discussion of Income Distribution" in Frontier Issues in Economic Thought, Volume 5: The Political Economy of Inequality. Island Press: Washington DC, 2000. pp. 166-170

Social Science Library: Frontier Thinking in Sustainable Development and Human Well-being

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The resurgence of inequality in the industrialized world, particularly in the U.S. over the last quarter of the 20th century has revived old debates in economics about the relationship between inequality and growth. The article summarized below argues that the realities of income distribution gets short shrift in this discussion - that growth is prioritized and only market-based factors are given serious consideration. Yet there are good reasons for concern about income distribution in its own right and good reasons to examine income distribution in the context of the political and social institutions which shape and constrain it.

A richer understanding of income distribution can be found in several economic theories outside the mainstream, particularly within the Marxist and Keynesian traditions. But for a comprehensive investigation, economics must seek insight from related disciplines in the social sciences.

Growth and Distribution

Since the 1930s social movements in the developed and developing worlds have struggled for equality on may fronts - for women, for minorities, for nations - with some measure of success. However, in the last two decades the trend has reversed: "Categorical disparities grew by race, educational level, occupation, industry - virtually every criterion except gender. Inequality also rose *within* groups defined by those criteria. Meanwhile, inequality among countries worsened as well." [196] Rather than joining the fight to stem the resurgence of inequality, many economists have rushed to defend it, claiming that inequality resulting from the operation of free markets must be tolerated in the interests of efficiency and growth. But markets are not free, they exist within an institutional framework that is neglected in much economic analysis.

Two theories frame much of the discussion of income distribution. Simon Kuznets proposed in 1955 that during the process of development, the composition of a country's economy changes from an agricultural to an industrial basis. At first incomes are generally low but relatively equal. As some people move into industry their incomes rise introducing inequality between industrial and agricultural sectors. As more and more people move into industry, incomes become more equal, but at a higher level. As long as economic growth proceeds without obstruction, inequality will be transitory.

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In 1975 Arthur Okun proposed that there is a trade-off between growth and equity. Attempts to redistribute income in the direction of more equality constitute disincentives to work and investment. Conversely, inequality introduces efficiencies that foster growth. Okun's own values led him to assert that societies should accept a modicum of economic inefficiency in the interest of equity. Later, neoclassical economists took up Okun's technical argument with a vengeance, but abandoned his humane conclusion. If there is a trade-off between equity and growth, then society must live with inequality in the interest of growth. Furthermore, growth *requires* inequality because needed investments depend on savings which depend on wealth.

Three Challenges to Neoclassical Theory

The subordination of income distribution to growth can be challenged on moral, theoretical and empirical grounds. Quite simply, it is morally right to care about who prospers and who doesn't and about the social instability that results from inequality. Theoretically, there are conflicting theories hidden beneath apparent economic consensus. Even within the three best known schools of economic analysis - neoclassical, Marxian and Keynesian - there are differing views.

Most theorists consider only the relative distribution of income between capital and labor: the average profit rate and wages. For neoclassicals, labor markets are efficient (i.e. there is no involuntary unemployment or shortfall of labor), the rate of growth of the employed work force determines the rate of economic growth and together with savings (investment) determines the profit rate. What's left goes to workers' wages. Any attempt to redistribute income reduces the efficiency of the labor market and therefore reduces growth.

In standard Marxian theory wages are set by customs and class struggle. What's left goes to capitalists as profit. Profits are the source of reinvestment capital for a new round of growth, so wage levels have an inverse relationship with the rate of economic growth: higher wages -> less growth. This resonates with Okun's theory of a trade-off between equity and growth.

Some Marxians are more like some Keynsians, but Keynesians are split. Some uphold neoclassical views that equality is detrimental to long-run growth. Others hold that intended savings and investment are a function of the profit rate and wages are a residual. Stagnation theorists propose that large corporations simply set profits at a fixed markup and consumption drives growth. Institutions like minimum wages or unions that increases the workers' share of income will stimulate growth.

Some of these models describe real situations, but none captures all capitalist societies at all times and none investigates inequalities *among* workers. Many empirical studies focus on the short-run business cycle trade-offs between inflation and unemployment described by the Phillips Curve. Unemployment hurts the poorest most, but when growth is rapid, inflation may be more of a burden on the wealthy who have fixed rate assets while the poor benefit from rising employment. Tight labor markets also benefit low income workers most because that is where the most slack in the labor market occurs. These arguments worked from the 1950s until the 1980s when economic growth and inequality both increased. Further investigation reveals that historically, the equality-growth confluence depends on the institutional environment.

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The Labor Market in Context

"The dominant, neoclassical theory of labor markets is institutionally naked." [199] The model we are left with depends solely on supply and demand factors: individual preferences, marginal revenue product and prices of goods and of labor (wages). In the long run human capital investment influences worker productivity.

"What does this omit? Among other things: the family, race, ethnicity, gender, community, employer strategy, non-Walrasian power, unions, culture, customary wage patterns, and level of worker effort." [199] Some neoclassical economists derived certain wage-setting institutions, for example efficiency wages, or wages set above market wages in order to induce greater effort and loyalty from employees, from neoclassical principles. But they still neglect factors like power or culture.

Labor market segmentation theories have an historical and institutional bent, finding that "jobs cluster in segments that differ systematically by the skill and training involved, job security and attachment, opportunities for advancement, breadth of job definition, level of worker participation in decisions, and compensation.' [200] Much of our understanding about these issues comes from sociologists and historians. Economists must be humble enough to learn from these related disciplines.

Income in Context

Other forms of income and income distribution are also important to understand as well as the simple reality that humans have physical, emotional and social needs. These needs can be met in three ways: make, share or buy. Under capitalism more and more need fulfillment is commodified, requiring money to buy things. But there are still sectors of the economy outside of market exchange where making and sharing occur, notably households and government transfer programs. Many economists assume that Walrasian power, the power to buy and sell freely, is the only power that matters, but firms may have monopoly power, or there may be more buyers than sellers or vice versa in the market for particular commodities. Concepts of class, the family and the state are key to understanding extra-market mechanisms of income distribution..

Class - Marx defined class in relation to the means of production (capital): one either owned capital or one worked for someone who did. However, rather than generating two polarized classes, "modern capitalism...has led to a proliferation of classes and subclasses" [202] with varying characteristics and economic outcomes. Many economists use class to identify groups with similar size incomes: rich or poor or in between. This shift is partly due to the fact that many people, in the U.S. at least, own some stock in corporations. Neoclassicals focus on endowments (like education) that influence productivity. Participants in the economy receive rewards based on the marginal productivity of their contributions to production.

Family - Families have troublesome for researchers for many reasons. It is necessary to define the relevant unit, and adjust measurements for the number and ages of members. Other reasons go deeper than measurement problems. First, the usual accounts of income distribution neglect

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unpaid labor and the making and sharing of goods and services that occur in the home. Second, family structure affects income distribution within the family. Extended families have different patterns of allocating work and consumption than nuclear families. The number of working adults or whether there are young children to care for profoundly influence a families economic constraints and opportunities. “It is not surprising, therefore, to discover that poverty rates for single mothers are nearly four times as high as for the average family. Third, income opportunities affect family structure as women are drawn more and more into market based work. Fourth, mainstream economic theory consider the family to be a black box, a single unit whose internal decision-making processes are invisible and irrelevant. Feminist economists have broken open the black box, revealing that exploitation may exist within the family and resources are often distributed asymmetrically.

State - The state is the usual agent of redistributive activity. For neoclassical economists, this means that the state should provide incentives for growth, encouraging saving and work rather than consumption and leisure. In the U.S. redistribution has gone to the extreme in recent years of transferring income from the poor to the rich. Even some economists with less-extreme views believe that higher welfare benefits encourage dependency, but this is not born out by empirical research in the U.S. Sweden, with generous welfare benefits also has a 93% labor force participation rate among single mothers. Redistributive transfer policies should take into account the lower wages and greater child care responsibilities that women face, expand opportunities for the poor to control their own lives and include universal benefits to build widespread political support.

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