



Transcript of IMF podcast:

Binyamin Appelbaum: Distribution Matters

Binyamin Appelbaum:

We've been conducting this natural experiment in inequality over the last half-century.

Bruce Edwards:

Since the Industrial Revolution began more than 250 years ago, the world has produced enough wealth for every one of its eight billion people to live comfortably. Yet over 40% live in poverty with the wealth being held by an increasingly narrow slice of the population.

Binyamin Appelbaum:

We've been allowing inequality in the developed world to reach the highest levels at least in a century, and we've been able to learn something about the practical consequences of high levels of inequality. And from that data, what has emerged is a correlation, a suggestive correlation that many people regard as sufficient to show some amount of causation, that when you get these high levels of inequality, you get less growth.

Binyamin Appelbaum:

My name is Binyamin Appelbaum, and I'm the lead writer on business and economics for the editorial page of the New York Times.

Bruce Edwards:

And welcome to this podcast produced by the International Monetary Fund. I'm Bruce Edwards. In his recent article in Finance and Development Magazine, Binyamin Appelbaum says, "Rising inequality is weighing on growth and straining the fabric of liberal democracy," and he squarely places the blame on distribution. While there has been a surge of interest, especially among younger economists, to study the inequities of distribution, Appelbaum says many economists still have doubts about the importance of it- for a number of reasons.

Bruce Edwards:

So your article is all about how economists have essentially tended to marginalize the distributional issues and focus on things like the financial markets. What do the financial markets reflect if not the real economy, in your opinion?

Binyamin Appelbaum:

So I think financial markets are an indicator of the real economy, but they're an imperfect indicator. You can see the difference right now. We've seen equity markets marching up, up, and away, even as the real economy is struggling. In part because the large companies that dominate equity markets are outperforming the economy as a whole during this downturn. And so there's a real disjoint between how well, say, Amazon is doing and how well the small businesses that are being replaced by Amazon are doing. So financial markets have a lot of useful information in them, but as with many things, you need to be aware of what the simplification is and of what it leaves out.

Bruce Edwards:

And so economists do have a lot of influence over policy, at least in the more advanced economies, and the distribution of wealth is indeed an economic issue. Why has inequality been allowed to increase to the degree that it has given all these talented economists we have out there?

Binyamin Appelbaum:

So I think it's helpful to think of this in two phases. In the first phase, economists really thought of efficiency and equality as being in opposition, that there was a trade off between maximizing the efficiency of government policy and addressing redistribution concerns and to the extent that a government was seeking to redress inequality, it was likely to slow the pace of economic growth. And so economists really urged governments to focus on maximizing efficiency, maximizing the growth of the size of the pie, and to postpone or defer questions about the size of the slices. And that was true for much of the closing decades of the 20th century and into the 21st century. I think many economists now accept that the relationship between efficiency and equality is more complicated than that, that if you get high levels of inequality, it can actually weigh on efficiency. But even then there are still I think some pretty strong hesitations about dealing with inequality, and I'll just touch on a couple of them.

Binyamin Appelbaum:

One is that inequality almost inherently involves normative judgments, and economists are just more comfortable when they can remain on the ground of quantification and so the hesitation about expressing a normative judgment leads them to exclude it from their analysis. They may tell you that they know it's important, but at the end of the day, the conclusions that they reach, people don't necessarily pay attention to the asterisk. And so I think part of it is just this unwillingness to get into those weeds. A part of it is a continuing hesitation about their ability to grapple with it productively, what we know about it, and what's optimal. And so you get this convergence of reasons that have made it hard for a lot of economists to find a way, or to care to find a way, to fully bring distributional considerations into their work.

Bruce Edwards:

And you talk about how this pursuit of efficiency lies at the very core of a very complicated relationship that economists have with politicians. Why is that?

Binyamin Appelbaum:

So economics pretty much by its nature is about politics. It's an attempt to understand the optimal configuration of public policy. And economists, really, it's not like physics where you're trying to understand the real world, by its nature it's a much more practical science. The old conception of economics is inherently intertwined with politics, I think is right and still true, even though economics has purified its name to call itself just economics rather than political economics. That's still the nature of what the field is doing. And economists and politicians have this very fraught relationship. Economists feel like politicians don't necessarily listen that carefully or implement policies in the way that they might like. They fret that some of their good ideas are left on the table and that others are implemented in imperfect ways. But still, politics remains the medium through which economic insights are translated into useful political realities.

Binyamin Appelbaum:

And so that tension is constant for economists, and some of them take the approach of saying, "Oh, those damn politicians. We're just going to retreat to the ivory tower and figure out what works and they can decide what they want to do with it." And some of them actively engage with politicians and try to educate and convince them. Some of them become politicians and policy makers and try to go into the engine room and actually operate the machinery of government. Whichever road you take, there are going to be frustrations.

Bruce Edwards:

And meanwhile, you have politicians that are looking for one handed economists.

Binyamin Appelbaum:

Absolutely. Yeah, and you get the famous image of a politician as someone who is looking for the answer in the limited circle of light where they think it should be and ignoring anything that falls outside of that area.

Bruce Edwards:

And you also speak of diversity or the lack thereof in the field of economics and the consequences of that.

Binyamin Appelbaum:

I think this is a big issue. Economics historically has been dominated by White European men or European and American men. And I think it's hard to avoid the conclusion that economics might be in a different place if it had been a more diverse field, because some of this tendency to set aside distributional issues to discount their importance or to say, "Okay, it's important, but it's hard and we don't know how to grapple with it, and we're going to leave it for later." It's a lot easier to do those things if you're coming from a place where the distributional issues aren't your issues. And frankly, the victims of distributional issues have tended to be minorities and lower income people who are disproportionately minorities. And that's a group that is not well-represented in the halls of economic academia or in the economics community. And so I think there's a connection between who is doing economics and what conclusions they're reaching or what issues they're prioritizing or just how hard they wrestle with the questions that are harder to answer.

Bruce Edwards:

So going back to this idea that many economists have that efficiency is the key to growth and that addressing those issues that perpetuate inequality would come at the expense of growth. This idea is being challenged now, but there are still many economists out there who would argue it still stands true. How would you respond to that?

Binyamin Appelbaum:

Yeah, I mean, we talked a little bit about this a little earlier. It's clearly the case that used to be conventional wisdom. It used to be the case that pretty much all mainstream economists thought what you just said, that there's a clear trade off, that if you're going to try and address distributional issues, it's going to come at the expense of efficiency and of economic growth. And it's clear as you say that many still do believe that. I think there's a growing body of evidence that the trade off isn't constant, that at higher levels of inequality you start to see inequality weighing on growth. And the mechanisms for that are still being explored and explicated, and they're interesting.

Binyamin Appelbaum:

I don't think we have a complete understanding of the relationship, but it is clear that, for example, if you've got high levels of what you're trying to do is sustain consumption by allowing

example, if you've got high levels, if what you're trying to do is sustain consumption by allowing poor people to borrow from rich people, that something gets lost in the translation, that the model is showing that that's just an equivalent system to having everyone receive an equal amount of income and then spending it are wrong to some meaningful degree and that something is lost in the translation- that consumption suffers, if you're attempting to sustain it on a borrowing basis.

Bruce Edwards:

So this trickle down concept, which essentially is what it is, I mean, if you help growth, which benefits the rich, well, eventually it will end up benefiting the less fortunate. I mean, it's proven not to work. There's a lot of literature out there that proves that it's not an efficient way of doing things in terms of the distribution. Why has it continued for so long given the evidence that it doesn't really work?

Binyamin Appelbaum:

The alternatives are hard. One of the basic truths in policy is that in the absence of a good alternative, a bad system will tend to continue and that's the world we live in. It has been easy to articulate critiques of the status quo and harder to devise compelling alternatives. And there's a couple of reasons. One is that the structure is stacked against the emergence of alternatives. The people who benefit from the current emphasis in policy-making tend also to be the people with the firmest grip on the levers of power. And so our democracies have struggled to implement policies that, frankly, are less beneficial to the rich and powerful, at least in the short term. And here in the United States certainly we have a system that provides an out-sized role for the wealthy to get what they want. So that's one issue.

Binyamin Appelbaum:

A second issue, again, is that the language of economics, economics has been so successful in dominating public policy debates that it had become the language in which we make these choices to the exclusion of other modes of thinking. And because economics is uncomfortable with some of these normative issues and with things that can't be counted and with some of these broader questions they've tended to be excluded from public debates. So what you get is a phenomenon where economists will say, "Okay, yes," to take the example of the costs and benefits of trade. It may be true that people experience loss as more painful than gain. It may be true that it's really not equivalent to say that this person's going to gain a dollar from this trade deal and that person's going to lose a dollar.

Binyamin Appelbaum:

That may look on paper like it's net neutral, but the reality is that that loss is more painful, and people have loss aversion, and would rather, if you ask a society whether they'd like that deal, the answer is going to be no. Because the people who are losing are going to feel more negative about it than the people who are gaining are going to feel positive about it. That's the type of thing that economics has as a lot of trouble integrating into its model of trade deals. And so the dominance of economics as a language for evaluating trade deals has made it hard for public policy makers to grapple with other modes of assessing policy decisions.

Bruce Edwards:

So we talked earlier about how economists do in fact have quite a bit of influence in governments in the most advanced economies, but you end your article with an interesting fact about how little influence economists have, or at least how economists struggle to have influence in developing countries. Why is that?

Binyamin Appelbaum:

So I think it's a really interesting insight. It's from an economist named Gustav Ranis, and his point was that if you look around the world, economists are constantly frustrated by the degree to which their advice is not accepted. Understandably, if you think you understand how something works, if you think you can make it work better, and people won't listen to you, you're trying to

works, if you think you can make it work better, and people won't listen to you, you're trying to figure out why that is. And in many developing nations, economists have had this frustrating experience of being unable to convince policy makers to do what they regard as obviously necessary to increase economic growth in those countries. And Ranis' point was basically, "Good for whom?" he said. Economists have it backward. They've basically argued that you need to focus on making the pie as big as possible, and then you can worry about the size of the pieces. And then you can worry about the idea that growth would produce democracy. The idea that if you could drive societies toward prosperity, they would naturally become more permissive, more inclusive, more democratic.

Binyamin Appelbaum:

He said, "That's fine as a theory, but you're never going to get people on board with it. People are not going to trust that if they do whatever you tell them to do to drive up growth, for example, accepting wage suppression, accepting limits on unions, accepting limits on cross border financial.... All this stuff. If you require people to do it and you defer the benefits, it's not a winning political argument." People need to agree that the policies are equitable. They need to agree that the policies are conducive to stability. There needs to be benefits at the front and you need to get those things right, and then you can come back to people and say, "Okay, now that we have a democratic society, now that we have a reasonably even distribution of opportunity, now we have a social consensus in favor of these policies."

Binyamin Appelbaum:

And I think it's a really powerful insight, because one of the things that we're experiencing today in the United States and in other developed countries is that basis is deteriorating. And that basis for a sense of we the people, a sense of shared goals, shared challenges is deteriorating as we become increasingly bifurcated and we've got rich people, we've got poor people, and it's harder to agree about anything. And if you're an American economist, you might look at our political challenges and appreciate that a place like Brazil has been dealing with that for a long time and that one of the reasons, I don't mean to pick on Brazil, but a country like Brazil has sometimes struggled to implement policies that economists regard as evidently beneficial, is because if you're Brazilian, you're looking at that landscape and saying, "Yeah, it's evidently beneficial for the 1%, but we don't have an equitable society. We don't have democracy and we're not going to embrace these policies."

Binyamin Appelbaum:

So I think that his point, when he made it, it seemed exotic to ears in the United States or in Europe. Today, I think people might look around and it might make a little more sense to them.

Bruce Edwards:

Binyamin Appelbaum, author and lead writer on business and economics for the editorial board of the New York Times. Thanks so much.

Binyamin Appelbaum:

Thank you.

Bruce Edwards:

Look for Binyamin Appelbaum's recent article titled Distribution Matters in the December 2020 issue of Finance and Development Magazine. Go to imf.org/fnd to read it online or download the Finance and Development app to read it on your mobile device. And look for other IMF podcasts wherever you get your podcasts. Please subscribe, if you like what you're hearing. You can also follow us on Twitter @IMF_podcast. Thanks for listening.

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