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Abstract. We live in an unjust world characterized by economic inequality. No liberal theory of justice is able to justify it. Inequality is not "solved" with equality of opportunity or meritocracy. Nor by the socialist and republican critique. The poor will have to count with them and with democracy to make social progress reality. In their political struggle, they will face one economic constraint: the expected profit rate must remain attractive to business investors. Yet, giving that technological progress in increasingly capital-saving, this economic constraint does not obstruct that wages grow above the productivity rate and inequality is reduced. What really is an obstacle to social justice in the rich countries is, on one hand, the power that capitalist rentiers retain and financists acquired, and, on the other, the competition originated in low wage countries.

Key words: economic equality, social justice, technological progress, capital-saving technology.

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We live in an unjust world. Inequality, both among people within each country and between countries in the world as a whole, is huge. It has existed ever since human societies were able to produce an economic surplus and turned into "civilized" empires. Since then, inequality has been a curse, because it dissolves human solidarity, pitting men against men, women against women, as the strong or the clever start oppressing the weak or the backward to achieve power and appropriate this economic surplus. No theory of justice, whether meritocratic or liberal, will justify such inequality. According to the meritocratic notion of justice, the ablest should be compensated. Nevertheless, the poorer in each society are not less endowed with talents, nor less hard-working. On the other hand, a liberal theory of justice, such as that of John Rawls, justifies inequality provided that it is the price for some improvement in the standard of living of the worst-off members of society. Yet the

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huge differences of income and standard of living among people and among countries cannot be justified with this principle. We cannot say either that the growth rates in rich countries, which are higher than in developing countries (with the exception of some fast-growing Asian countries), are justified because they may benefit the worst-off poor countries, or, within each country, that the high bonuses received by financiers are justified by the modest increase in the income of the poor. This reasoning is embodied in the classical liberal justification of capitalism, but it is a poor one; the lack of clear alternative pathways does not make capitalism less unjust.

Inequality may assume many forms. Human beings are supposed to have equal rights to liberty, to respect, to their own culture, to vote and to be elected, to material well-being, but in reality they do not have such equal rights. To each of these rights there is a corresponding inequality: inequality of liberty – although constitutions proclaim that all citizens are equal under the law, in practical terms they are not; inequality of respect – the poor are usually treated with less respect than the rich; political inequality – each citizen is entitled to one vote in democratic regimes, but their actual power to choose politicians or to influence policy varies widely; multicultural inequality – minority groups are supposed to have their cultures respected, but all societies impose some degree of integration; economic inequality – we know well how huge it is.

In this article I will focus on economic inequality. The fact that I am an economist explains my choice. According to Michael Walzer's (1984) theory of justice, we may admit inequalities within each "sphere of justice", because each sphere will have a different principle of justice that is not necessarily based on straight equality. But there is a rule that should never be disregarded: no one is entitled to cross the borders of the spheres of justice. Yet in capitalism we observe that the rich usually and with no shame cross the borders of the spheres of justice; because they are rich, they believe that are more entitled to power, or to social prestige, or to respect, or to education, or to divine grace, or even to health care – the social goods that define the other spheres of justice. This fact shows how crucial it is to reduce economic inequality. The aim is not to eliminate it, because this will never happen, but to limit its scope.

In discussing economic inequality we will probably consider the numbers of people that suffer from hunger (around 20 percent of the world's population) and the numbers who live on less than one dollar per day (around a billion). According to Branko Milanovic (2007: 108), global inequality measured in 1998 by the Gini coefficient was as high as 64.1. This information is relevant, as are also relevant the normative political theories that discuss injustice, or the sociological theories that tie such inequality to capitalism or the class system, or the economic theories, such as the ones I will present here, that explain inequality in capitalist societies. All this, and particularly the socialist or the critical theories of capitalism, is relevant if we want to reduce inequality. Yet, although I believe that it is essential to criticize inequality and the theories and ideologies that legitimize it, I doubt whether socialist and republican intellectuals, however competent their critiques, will make a great contribution to reducing it. Ideas are important in reducing social injustice, but much more important is the *political organization* and struggle of the poor and the workers. I don't believe that the proletariat has the key to the future – that it embodies the universal value of justice, as Marx and Engels supposed – but I am persuaded that the socialist political parties, the left-wing associations, and the left-wing social movements that were unable to build an alternative economic system to capitalism have nevertheless contributed substantially to a less unequal world. Whereas classical liberalism and the meritocratic or "efficientist" ideology[1] justify the present degree of inequality, two different ideologies were effective in criticizing it: *socialism* and *critical theory* contributed to reducing inequality among people within each country, whereas *developmentalism* – the national development strategy behind convergence or catching up – contributed to the reduction of inequality among countries.

We know well that unfettered capitalism is an unjust mechanism for determining income distribution. The economic superiority of capitalism over the failed experiments to establish socialism derived originally from the fact that men and women are intrinsically unequal in talents and in cultural and economic heritage, coupled with fact that capitalism *is not troubled* by that inequality. Yet this "original inequality" causing inequality should not be understood in terms of the conservative

[1] Pardon the ugly name, but efficientism is the best word available to identify a fundamental ideology of the twentieth century – the ideology that principally legitimizes the power and income of the professional or techno-bureaucratic class.

tenet that since human nature is intrinsically unequal societies will be always unequal. This argument makes no sense, first, because in the concept of original inequality there are traits that are socially created and conserved; second, because actual inequalities are substantially greater than the inequality that has its origin in individual talents. As for the fact that capitalism goes well with inequality – this is an intrinsic characteristic of this type of society. As Max Weber recalled in discussing the Protestant Reformation and Calvinism, wealth was a signal of divine grace. For sure, a reasonable economic equality is not a condition for the emergence of capitalism, whereas it is for the emergence of socialism. Capitalism defeated real socialism because regulated markets proved to be more efficient than economic planning in coordinating complex national economies, but, besides that, the socialist project faced a major obstacle that was non-existent in capitalism. Both capitalism and socialism were supposed to be efficient, but, in addition, socialism was supposed to confront the original inequalities existing in society and to achieve a substantially less unequal distribution of wealth and income, while capitalism could happily live with rampant inequality. Socialist or statist countries never achieved economic equality, but they were substantially less unequal than capitalist countries with similar levels of income per capita. Yet the price they had to pay for that achievement or for being "above the curve" was authoritarianism and reduced efficiency.

The immediate challenge to a socialist party that wins elections is to reduce inequality while keeping the rate of profit attractive to capitalists – sufficient to motivate them to invest. Socialist political parties soon become social democratic because they have no power to install socialism: their real and difficult challenge has been to manage capitalism more efficiently than the capitalists. They proved successful in so far as their policies of making capitalism less unjust did not reduce expected profits, or, in other words, they did not prevent entrepreneurs and entrepreneurial business corporations from investing and innovating. In the case of successful developing countries – that is, of the underdeveloped countries that were able to industrialize and grow or to realize their own capitalist revolution – not socialist but left-wing developmentalist political parties were in certain cases able to reduce inequality in so far as they were able to supersede the colonial coalition of local merchants, local rentier capitalists and foreign interests. To do so they had to forge a political coalition of public bureaucrats committed to a national development strategy, of organized

labor, and, necessarily, of manufacturing businessmen. This was a condition for growth, but it limited the coalition's capacity to reduce inequality. On the contrary, in most cases, the outcome was growth and increased inequality.

Socialism and progress

Meeting the challenge of creating a more just society depends on values – on the socialist belief that reasonable economic equality is not only a slogan but something to be fought for. But we have to be clear that it also depends on the political capacity to recognize and cope with the economic constraints on reducing inequality. In other words, it depends on politics. In modern societies, after the absolute state gave way to the liberal state, and the rule of law was established, *politics became possible* and a reality. Politics is the practice of governing, it is the act of reforming institutions and defining public policies, it is the art of persuasion and compromise to achieve majorities. It is through political action that the citizens organized as a civil society reform the state and change social life so as to make it less unequal. But politics is limited, on the one side, by the conservative political parties, the pressure groups and the organizations of civil society associated with the rich, today principally the capitalist rentiers; and, on the other side, it is limited by the structural constraints of capitalism.

Capitalism is a form of organized production and distribution determined by the requirements of profit. In order to reduce inequality, wages need to grow faster than the productivity of labor. Yet, given the interest rate and the type of technical progress that is taking place, the fulfillment of the structural condition of economic growth will depend on the expected profit rate. If the rate of profit does not achieve a reasonably and conventionally established satisfactory level, businessmen and business enterprises will not invest. It follows that growth will slow down and wages will eventually fall, instead of increasing faster than productivity, which is the basic condition for the reduction of inequality.

An alternative is to propose a new and more just mode of production and distribution – socialism – where private ownership of the means of production is forbidden. Yet, although such an alternative cannot be completely ruled out, historical experience has shown that this is not realistic even for the richest and or most developed societies,

which in principle are closer to socialism. The Scandinavian societies present the highest standards of equality in the world, but even there it is most improbable that the system of production will cease to be capitalist and become socialist in the near or even in the medium-term future. Socialism will be a viable alternative for a given society only after, on the one hand, democracy empowers the poor and the socialist parties; and, on the other, after certain basic social and economic conditions are fulfilled. First, and *paradoxically*, the level of equality achieved by such a society in the framework of capitalism will have to be high; only at a high level of equality will the democratization of education allow for an increase in the supply of individuals with such entrepreneurial and managerial capacity that it will not be necessary to motivate entrepreneurial initiative with large executive salaries, stock options and bonuses. Second, socialism will become viable when capital is so abundant that the interest rate is very low and the income of rentiers limited. Third, socialism will become viable when social expenditures by the state are so high and provide social services of such quality and efficiency that individual services will lose their present attraction. In other words, the *transition to socialism* depends on a high level of income per capita or of economic growth achieved within the framework of capitalism, on the social critique of capitalism, and on social reforms that make capitalism less unjust and the state, more capable. To the extent that such conditions are fulfilled, the transition to a form of social organization sufficiently egalitarian to merit the name of socialism will become a reality.

We are far from achieving such an ideal, but I disagree completely with the conservative rejection of the idea of *human progress*. I know that the rejection of the idea of progress is also part of critical philosophy, but when a critical philosopher like Adorno expresses his pessimism, this attitude adds to his critical weight, but contradicts the ideas of revolution and emancipation. The denial of progress is consistent with conservative thought – with an ideology that privileges order over justice and is permanently afraid of the new. Since the capitalist revolution, progress or development without adjectives has become a reality. If we take into consideration the more advanced European countries, we have to acknowledge that some steps have been taken in this direction. Critics will certainly argue that I am being too optimistic, that I am not a true socialist, and that it is impossible to make capitalism less unjust. I respect social criticism, because there is no social advance without it. Self-satisfaction

is always a threat to personal advancement as well as to social progress. Yet, since the capitalist revolution made the reinvestment of profits in production a condition of the survival of business enterprises, economic development has become *embedded* in the economic system. And, despite the short-term conflicts between the sustained growth of the economic surplus and the other political objectives shared by modern men and women, there is little doubt that in the medium term they are correlated. Thus, to assert, as I do, that socialism will be possible only at an advanced stage of capitalism does not mean that I don't believe in socialism, or that I see inequality as something intrinsic to human nature or to social life. This would be true only if I didn't believe in progress – but this is not the case.

Thus, to return to reality, the three central *questions* that we must ask in relation to inequality within the capitalist system are: first, which are the structural economic constraints that nations face in reducing domestic inequality? Second, within such constraints, what level of freedom do they allow? Third, what can be done at the international level? This last question calls attention to the fact that inequality may increase or diminish at the national level, among the inhabitants (who are not necessarily all citizens) of a given country, and, at the international level, among the population of the entire world. Within a nation-state there is one major institution – the state – that acts or may act as an instrument of the collective action of civil society or the nation, while at the international level there are already institutions – international treaties, the United Nations – but no state. At the national level, civil society was separated from the state and eventually, in the context of democracy, was able to reduce inequality, although only to a limited degree. At the international level, a global civil society is still being structured and an international political system associated with the United Nations is emerging, but we are still far from a global state.

The structural constraints

I will begin with the structural conditions imposed by capitalism on the profit rate. Usually, when economists discuss the structural constraints involved in income distribution, they base their model on a simple functional distinction between capitalists receiving profits and workers receiving wages. I did essentially that in two

works on the subject (Bresser-Pereira 1986; 2004), where my main concern was to relate distribution to the kinds of technological progress. Only in the last chapter of the 1986 book did I add the professional class and the salaries it receives to the income equation. To focus only on wages and profits makes sense because it makes it possible to clarify the relations between the two key actors in a capitalist society, namely, capitalists and workers; but as this approach either lumps the professional or technobureaucratic class with the workers or ignores it altogether, its realism is limited.

In the model of growth and distribution, I *inverted* the classical theory of distribution adopted by David Ricardo and Karl Marx. Instead of considering wages as given at the subsistence level and profits as the residuum, I considered the profit rate as given and the wage rate as the residuum. Assuming in the model that the *wage rate* was constant, as classical economists did, proved historically wrong, whereas assuming the *profit rate* as given and constant in the long term is reasonable because the existing data confirm that the profit rate is relatively stable in the long run and that the wage rate grows as economic development takes place.[2] The profit rate fluctuates strongly over the business cycle but is constant in the long run because competition limits average profit rates. For that reason no economist argued that the profit rate tended to increase. On the other hand, the basic economic constraint in a capitalist economy is that the profit rate is satisfactory or, to use Herbert Simon's (1957) expression, "satisfying", that is, it is sufficient to stimulate businessmen to invest. Thus, if we assume that economic growth is taking place as a consequence of capital accumulation and technical progress, the profit rate will be allowed to move below or above that satisfactory level in limited way and for only short periods. Competition limiting and institutions protecting the profit rate will make it fluctuate around the satisfactory level. Businessmen may seek to maximize profits, but they are satisfied and ready to invest if the expected profit rate is clearly higher than the market interest rate. Entrepreneurs aim at profits but they also struggle to expand, which increases their power. Their "animal spirits" (Keynes 1936) or their need for achievement

[2] The data on long-term variables are not fully reliable, but according to, for instance, Gérard Duménil and Dominique Lévy (2001: Fig. 1) – probably the most competent researchers of the Marxian variables – the profit rate varied in long cycles between 1869 and 1999, but around a 16% average.

(McClelland 1961), make them invest and innovate. Obviously the profit rate is not constant in the short or the medium term. Capitalist growth is cyclical, and the profit rate will fluctuate with the short and the long cycle. However, it is reasonable to assert in relation to the past (the available data point in this direction) and to predict in relation to the future that the profit rate in the long run will be constant.

To understand the structural constraints on income distribution or the reduction of inequality, it is practical to use the concepts that Karl Marx adopted to formulate his thesis of the tendency of the rate of profit to fall, and to make one key variable, namely, technical progress measured in terms of the productivity of capital, vary historically. There is technical progress whenever labor productivity (which corresponds approximately to income per capita) is increasing. But, in terms of the productivity of capital, current technical progress may be capital-using, neutral, or capital saving, depending on the character of the output–capital relation or the productivity of capital. If the output–capital ratio is decreasing, technical progress will be capital using or the productivity of capital will be falling; if it is constant, technical progress will be neutral; if the output–capital ratio is increasing, technical progress will be capital saving or the productivity of capital will be rising. When technical progress is neutral, wages can rise with productivity and distribution can be constant while the profit rate is constant; when it is capital saving, wages can rise above the productivity rate and distribution improve or inequality diminish while the profit rate remains constant at a satisfactory level.

Under what conditions does the productivity of capital decrease or increase? It usually falls in the first stage of industrialization, when business enterprises substitute machines for labor; it rises in the later stages of industrialization when business enterprises have already substituted machines and software for labor and now primarily substitute new and more efficient machines for old ones; and is neutral when the two kinds of technical progress are balanced, one checking the other.

In equation (1) we see that the rate of profit r = R/K depends on the distribution of income R/K and the productivity of capital, Y/K:

$$r = R/K = R/Y \,/\, K/Y \qquad (1)$$

If we assume that the economy is growing or labor productivity increasing and that the profit rate is constant, what will happen to wages and to income distribution or inequality? Given a constant rate of profit, (1) if technical progress is neutral (or the output–capital ratio is constant), inequality will remain constant, and average wages or the wage rate will increase at the same rate as labor productivity; (2) if technical progress is capital using (or the productivity of capital is falling, as happened in Marx's time), inequality will increase and the wage rate will increase more slowly than productivity or even fall; (3) if technical progress is capital saving (or the productivity of capital is increasing), inequality will diminish and wages will grow faster than the increase in labor productivity.

Phases of capitalist development

Taking Britain as reference (because it was the first country to complete the Industrial Revolution), and given mainly these types of technical progress, we can divide capitalist development after the long primitive accumulation period, in which the basis for economic growth was established, into *five phases*: first, the Industrial Revolution phase, approximately in the 50 years before 1800; second, the post-Industrial Revolution or Marxian phase between 1801 and 1850; third, the "classical" phase between 1851 and 1948; fourth, the "30 golden years of capitalism" between 1949 and 1978; and, finally, the "30 neoliberal years of capitalism", between 1979 and 2008. Naturally, these dates beginning and ending the phases are approximate; transitions from one phase to another are not always clear and are not completed in only one year.

Phases of capitalist development

Phase of capitalist development	Technical progress Y/K	Rate of profit R/K	Wages W/L	Inequality R/Y
Industrial Revolution (1750 – 1800)	Capital using	Constant	Falling	Increasing
Post-Industrial Revolution or Marxian phase (1801-1850)	Capital using	Falling	Constant	Constant
"Classical capitalism" phase (1851-1948)	Neutral	Constant	Increasing	Constant
30 golden years of capitalism (1949-1978)	Capital-saving	Constant	Increasing	Decreasing
30 neoliberal years (1979-	Capital-	Constant	Constant	Increasing

2008)	saving			

In four of the five phases the rate of profit is assumed to be constant. Only in the Marxian phase it is assumed to be falling because technical progress was capital using; thus, to keep the profit rate constant, wages should be falling. Since in the previous phase the proletarianization process had driven the remuneration of workers to subsistence level, the only logical possibility was a falling rate of profit.

In the first period, the primitive accumulation and Industrial Revolution period between 1750 and 1800, inequality increased because wages were probably falling. Technical progress was capital using since industrialization is a process of mechanization or of substitution of machines for labor that takes place approximately according to a rational sequence. First, firms substitute the less costly or the more efficient machines for labor, and after, step by step, they substitute less efficient machines that are still more efficient than direct labor. Given this sequence, whenever a less efficient group of machines replaces labor, the productivity of labor will increase but the output–capital relation will fall; in consequence, the average productivity of the stock of capital will decrease. Since technical progress was capital using and the profit rate was constant at a high level, the wage rate had necessarily to grow more slowly than the productivity rate or to fall, and inequality had to rise. The period of the Industrial Revolution or of mechanization is also the classical period of "proletarianization" – of the transformation of peasants into industrial workers. Strictly speaking, that this was not a period of falling "wages", because peasants were not wage earners, but it surely was a period of falling standards of living.

In the second phase, the post-Industrial Revolution or Marx's phase, mechanization continued or technical progress remained capital using, but inequality ceased to increase and remained constant. Since the wage rate had reached subsistence level and could not be further reduced, the profit rate necessarily had to decrease. This happened in Britain in the 50 years after the Industrial Revolution. Yet capitalist development was not endangered, investments were not paralyzed, because the profit rate fell from an exceptional level that prevailed during the Industrial Revolution to a level that was still attractive to business entrepreneurs. In this period, inequality was reduced not because wages increased (they remained constant), but because the

average rate of profit fell. I like to call this period “Marxian” because it was the period that Marx was living in and directly observing – a period in which the rate of profit was, exceptionally, falling.

Technical progress, however, would not consist of “mechanization” (the substitution of increasingly inefficient machines for labor) forever. Approximately between around 1851 and 1950, in the time of classical capitalism, technical progress changed from capital using to neutral (a constant output–capital relation). Given also that the profit rate remained constant, wages should increase along with productivity, as did happen. Thus inequality remained constant, while real wages were increasing.

Technical progress, however, continued to evolve when countries were already fully mechanized. Thus, in the fourth phase of capitalist development, in the 30 golden or glorious years of capitalism, after World War II (1949–78), technical progress became modestly capital saving. Instead of primarily substituting machines for labor, business firms now were mainly (but not exclusively) substituting less costly or more efficient machines for old machines. The computer industry dramatically illustrates this process. That is the reason why, in that golden age of capitalism, inequality diminished in the rich countries whereas the profit rate remained constant and attractive to businessmen. The constancy of the profit rate was consistent with wages rising faster than the productivity of labor because the productivity of capital was increasing. In fact, in that period the advanced economies experienced high rates of growth and financial stability, while inequality clearly diminished.

Back to increased inequality

After the 1970s, however, *new historical facts* changed the picture. Given just the variables that I have being using so far, and given a constant profit rate and an increasing output–capital ratio, wages should continue to increase faster than productivity and inequality should continue to fall. Instead, wages stalled and inequality increased. How to explain that? Why did the bright golden age of capitalism turned into the somber neoliberal years? The key explanation of this perverse change is political.

In the 1970s, the pressure of organized labor for more wages and, especially the first OPEC oil shock and the general increase in commodity prices squeezed the profit

rate, which fell sharply in the United States together with the growth rate.[3] On the other hand, these same factors caused an increase in inflation despite feeble aggregate demand; in other words, they caused "stagflation" or "inertial inflation". The response, principally of the two more severely affected countries, United States and Britain, was neoliberalism and financialization, a return to and radicalization of economic liberalism and the development of financial innovations that created fictitious wealth, that is, a great increase of the remuneration of capitalist rentiers and of the bright young professionals – the financiers – who invented and managed such speculative and risky financial instruments. Since the Great Depression of the 1930s, economic liberalism had been largely abandoned in favor of the Keynesian or social-democratic ideas that, after World War II, in the 30 golden years of capitalism were effective in building the welfare or social state, mainly in Europe. But in the 1970s, with the reduction in profit rates, liberalism combined with meritocratic professionalism returned in new clothes, transformed into a reactionary ideology: neoliberalism. The change was complete with the coming to power of Prime Minister Margaret Thatcher in Britain and President Ronald Reagan in the United States. In order to deal with the profit squeeze, the new administrations in the United States and Britain were ready to reduce direct and indirect wages and to introduce more "flexible" labor laws, that is, to repeal laws protecting the workers. This radical response overlooked the fact that the 1970s crisis was cyclical, not structural. The idea was to reverse the distributional trend that the increase in the productivity of capital had allowed and organized labor had achieved: to *increase* inequality rather than reduce it, even though structural conditions were supportive of the gradual increase of wages in relation to profits without endangering a reasonable profit rate.

Yet, to understand the neoliberal years and the increasing inequality that then occurred in rich countries, domestic factors alone are not sufficient. We need to take into consideration two international or global factors that made the neoliberal political coalition so aggressive: increasing competition from developing countries and increasing immigration to rich countries. Trade liberalization made possible increased competition from low-paid workers in developing countries and depressed wages in

[3] In reality, according to Duménil and Lévy (2002), the profit rate began to fall in the United States after World War II, but recovered in the late 1950s, only to fall again, sharply, in the 1970s. Only after 1982 would a recovery begin.

rich countries. Since the beginning of the 1970s, with the emergence of the newly industrializing countries (NICs), for the first time the North was confronted with competition from low-wage developing countries. Some NICs, such as Brazil and Mexico in the 1970s and China from the early 1980s, with low wages and a managed and competitive exchange rate, profited from the opportunity offered by globalization and were highly successful in exporting manufactured goods to the rich countries. To this fact we have to add the major increase in immigration to rich countries, which directly depressed their wage levels. This rise in immigration did not result from rich countries opening their borders – on the contrary, they strictly controlled their frontiers – but from the pressure on the poor to emigrate in order to improve their usually miserable standards of living, combined with the reduction in the costs of transport and communication. This, along with the unacknowledged interest of rich countries in employing cheap labor, explains the increase of immigration.

The neoliberal and meritocratic domestic response to these challenges was market-oriented institutional reform: privatization, deregulation, a flattening of the existing progressive income tax system, flexibilization of laws protecting labor, and economic incentives for workers and professionals. Between 1978 and 2008 the world experienced the “neoliberal years”. In the rich countries increased competition and policies repressing wages were effective in keeping wages stagnant, whereas productivity and economic output continued to increase, although at lower rates than in the golden age.

Does this mean that the profit rate increased? Although the data on this matter are imprecise, I believe that it did not; the profit rate was kept at a satisfactory level. To whom, then, was transferred the increased economic surplus resulting from wages growing more slowly than productivity or even becoming stagnant, whereas capital-saving technical progress allowed for increased wages? First, some of the supposedly greater economic surplus did not materialize; instead, the gains accrued largely to fast-growing middle-income countries, particularly China, which exported manufactured goods and experienced higher rates of growth. Second, neoliberal ideology and the consequent deregulation of financial markets allowed the *political coalition* behind *capitalist rentiers* and *financiers* to capture a major part of the surplus, in the form not of profits but of dividends, increases in financial wealth, and bonuses. Modern rentiers or inactive capitalist living on interest, rent and dividends

were unhappy with the low rates that prevailed in the golden age – most probably, as John Kenneth Galbraith remarked in his 1967 classic book, *The Industrial State*, because capital had become abundant in the world. In consequence, the real rates accruing to rentiers were around 2 or 3 percent a year – a little above the interest rate on US Treasury bonds. It was eventually to "solve" this problem that a coalition of financial operators or financiers and capitalist rentiers was formed; and, based on this coalition, financialization – an increase of fictitious capital at a rate three or four times that of the increase of production – materialized. This was possible not only because the more risky financial innovations were more profitable, but also because classic speculation in asset markets (principally in stock, real estate and oil) created bubbles – stock exchange bubbles, commodity bubbles, real estate bubbles – a daily phenomenon in the neoliberal years.

Financiers did not offer this gain to rentiers for free. Since the golden age, the professional class and particularly the high executives of all corporations were able to substantially increase their pay – in the form not only of direct salaries but also in bonuses and stock options – in the name of meritocratic values. This was predictable because organizations had replaced family units as the basic productive unit, because in organizations professionals or executives play a strategic role, because high executives replaced stockholders as controllers of the organizations and determined their own remuneration, because, in sum, the strategic factor of production was ceasing to be capital and becoming knowledge. In such conditions, the professional or techno-bureaucratic class, that is, the controllers of administrative, technical, and communicative knowledge, benefited. In principle, benefits should have accrued to the workers as the productivity of labor as well as of capital increased. In fact, they accrued mainly to high executives and financiers. Since the 1950s, high professional executives, and since the 1980s also financiers – both part of the professional or techno-bureaucratic class – gained sufficient political power to be able to capture a substantial part of the economic surplus that was being produced by the economic system.

The professional or technobureaucratic class had already grown large and powerful and its efficientist and meritocratic ideology had become widespread by the 1950s. This became still more evident in the 1980s, when salaries and bonuses increased enormously, making the simple profit–wage functional distribution that I have been

using to measure inequality unrepresentative. It would be necessary to take into consideration salaries and bonuses to gauge the relation between salaries and wages, or, since this measure is normally not available, to take into consideration the distribution based on deciles of income, despite the shortcomings that these statistics suffer from because they underestimate the income accruing to capital. In the neoliberal years, for instance, wages remained practically stagnant in the United States whereas salaries – mainly high salaries – and bonuses skyrocketed.

This distortion in favor of the professional class will not be corrected soon. So long as education does not allow for an increase in the supply of professionals sufficient to reduce their market value, high executives and financiers will continue to capture a sizable share of the economic surplus. Even after that, they will probably continue to have large remuneration, for two additional reasons: because high executives control the management boards of the great corporations, and because, in a world where the value of the business enterprise is measured by discounting its cash flow, competent executives have a strategic weight in such value: a competent management can increase the value of a business enterprise, and an incompetent one can reduce it sharply, in a relatively short time span. Thus, unless democracy is deepened, and the state is able to reduce income inequality through progressive taxation and through the orientation of social expenditure toward the poor, inequality deriving from the relative shortage of highly qualified professionals and from the widespread meritocratic ideology that legitimizes large differences in incomes will probably continue to be very great, despite the adoption of increasingly capital-saving technologies that allow for the reduction of inequality without risking making the profit rate not satisfactory for business entrepreneurship. On the other hand, even when constraints related to satisfactory profit rates and to supply and demand of knowledge people are relatively neutralized, ideologies legitimizing inequality will continue to limit the scope of the political fight against inequality.

To sum up, always having Britain as paradigm because it was the first country to complete its Industrial Revolution:

first, after the long phase of primitive accumulation, in the Industrial Revolution, approximately between 1750 and 1800, inequality increased, because technical progress was capital using, but investment materialized because the profit rate was

maintained at a high level while the wage rate or the standards of living of workers deteriorated to the subsistence level;

second, immediately after the Industrial Revolution, in the Marxian phase (approximately 1801–50), inequality remained constant while the wage rate remained at the subsistence level, in so far as technical progress remained capital using, but the profit rate fell;

third, in the classical phase, between 1850 and 1950, inequality remained constant as technical progress became neutral, and it was possible to increase the wage rate in line with the increase in productivity while the profit rate remained attractive to capitalist entrepreneurs;

fourth, in the golden age of capitalism, approximately between 1950 and 1980, inequality was reduced as technical progress became moderately capital saving, which allowed wages and salaries to increase while the profit rate remained constant;

fifth, since 1980, in the neoliberal years, inequality increased even though technical progress continued to be capital saving, in principle allowing the profit rate to remain constant while wages and salaries increased faster than productivity; instead, wages increased more slowly than productivity or became stagnant because they were depressed not only by neoliberal policies but also by the competition from immigrants and from fast-growing middle-income countries exporting manufactured goods, while the profit rate remained constant and the salaries and bonuses of the professional class – particularly of the richest 2 per cent – increased greatly.

In the near future, after the 2008 financial crisis, it is possible that inequality will remain constant because technical progress will continue to be capital saving, and this may compensate for the negative effects on wages stemming from competition from developing countries exporting manufactured goods, and from immigration. As for neoliberal and meritocratic policies aiming to increase inequality, they will probably be neutralized because the political coalition promoting them was severely hit by the 2008 global financial crisis. Yet we should not be optimistic: the neoliberal coalition was hit but it did not collapse: it only lost relative power.

Developing countries

All the above relates to distribution within rich countries. What to say of developing countries? What to say about the distribution *within* developing countries and *between* them and rich countries? First, we have to distinguish poor from middle-income countries; second, among the latter we must distinguish the fast-growing from the slow-growing countries. But before that, it is necessary to remember an old, insightful, but not fully consistent theory: the Kuznets curve. According to Simon Kuznets (1955), economic development is characterized by an inverted U curve. In the beginning of the process, income is concentrated; after some time inequality ceases to increase; and eventually inequality diminishes. Why? One explanation is the tendency of technical progress to change from capital using to capital saving. But Kuznets did not use it. Instead, using simple supply and demand reasoning, he argued that in the early stages of growth investment in physical capital is the main mechanism of economic development; thus, the rich, who supposedly save and invest more, will be compensated by high profits and by an increasing share of national income. After some time, however, this tendency is exhausted as knowledge or human capital becomes increasingly strategic and wages and salaries grow faster than profits.

I believe that the two theoretical frameworks outlined above are valid explanations of the inverted U shape of the distribution. Yet there is historical way of looking at the problem that takes into consideration either, in terms of Marx, the transition from pre-capitalist to capitalist societies or, in terms of modernization theory, the transition from traditional to modern societies. According to these two views, this transition, especially its main episode, the Industrial Revolution, is highly income-concentrating in so far as it causes the proletarianization of the peasants. Yet in Latin America and particularly in Brazil, where a mercantilist colonization combined with slavery prevailed, an egalitarian peasant society such as the one that existed in the north of United States never emerged. Inequality was inherent in the mercantilist colonization, the plantation system and slavery. Thus, when industrialization begins, there is an unlimited supply of labor to manufacturing industry at very low wages. This fact, combined with the existence of an industry that exports some commodity using local natural resources, creates the conditions, in a first moment, for primitive accumulation, and, in the second, for industrialization. In both moments, income is

very highly concentrated. The capital accumulated in this export industry creates an opportunity for industrialization still within the framework of a highly unequal society. Industrialization will be initially oriented to the domestic market, and will keep inequality high, because Arthur Lewis's (1954) "unlimited supply of labor" prevents wages from growing with the increase in labor productivity.

To consider only the economic variables, inequality in a developing country will continue to increase so long as an "unlimited" supply of labor or a reserve army of unemployed or underemployed workers does not become exhausted. The economic surplus produced in manufacturing will benefit not only the capitalist class but also the professional middle class. These two groups plus a layer of highly skilled workers form the modern or capitalist sector of the dual or underdeveloped economy, whereas the other workers remain in the "marginal" sector, which is no longer an untouched pre-capitalist or traditional sector but sector complementary and functional to the process of capital accumulation and growth.

Before this marginal sector is exhausted, what can put a stop to income concentration is democratic transition. Usually, the victorious political coalition that achieved democracy relied on the participation of the working class and, more broadly, of the poor. Thus, after coming to power, it is constrained to adopt income policies benefiting the poor. This is what happened in Brazil in the 1985 democratic transition. The democratic political coalition assumed political commitments to the poor that were relatively honored after the transition. Since 1985, successive administrations have adopted a variety of policies aiming to reduce inequality, by making health care and basic education universal services, by increasing the minimum wage, or by adopting relatively focused minimum-income policies. In consequence, inequality in Brazil between 2001 and 2008, measured in terms of the Gini index, although still high, fell from 0.594 to 0.544, while, between 1999 and 2008, the minimum wage increased by 61 percent in real terms...[4]

[4] Source: Hoffman (2009). Although the minimum wage played a role in the systematic reduction in inequality in Brazil, in a personal conversation with Rodolfo Hoffman he remarked that this reduction began before the minimum wage increases – in 1995.

Conclusion and distribution among countries

To summarize, rich countries have already reached the stage of capital-saving technology where a reduction of inequality is consistent with a constant and satisfactory profit rate, but, in contrast with what occurred in the 30 golden years of capitalism, their societies have been unable to use this opportunity in the succeeding neoliberal and meritocratic years. Concurrent with this negative outcome, which occurred for political or ideological reasons associated with neoliberalism and meritocracy, competition from middle-income countries began in the 1970s, when they started to export manufactured goods to rich countries and sections of their populations started to migrate to rich countries. These last two factors depressed wages in rich countries. In other words, the domestic constraints were reduced, but the international constraints and the hegemony of two reactionary ideologies (neoliberalism and meritocracy) worked against equality.

Developing countries, on the other hand, are probably either in the phase of mechanization, when the productivity of capital is falling, or in the classic phase of capitalist development, where it is constant. The countries that are in this latter condition could grow without increasing inequality, but they face a major obstacle: the unlimited supply of labor. Democracy, however, may force elites and politicians to adopt effective redistributive policies.

So far I have discussed distribution within countries, both rich and developing. This is what specialists working in the area of measuring inequality normally do. Yet we must also consider distribution among countries. On that matter, one thing is clear. Fast economic growth and catching up in developing countries are effective in reducing world inequality, even though many of these developing countries are in the phase of increasing domestic inequality. This seems a contradiction or a paradox, but it is not. To take, for example, the limiting case of China: after it abandoned communism and adopted state-led capitalism in the 1970s, growth was enormous, and concentration of income equally great. Yet, since 1980, and notwithstanding the domestic increase in inequality, more than 400 million people have left the condition of poverty; and almost all the 1.4 billion Chinese have reduced the difference between their average income and that of rich countries. Obviously, this fact has contributed to some reduction in world inequality. The Gini coefficient for the “weighted

international inequality" (which should not be confused with the "global inequality" previously referred to) fell down 55.7 in 1965 to 50.5 in 2000 (Milanovic 2007: 85). This happened because several developing countries, particularly some Asian countries, grew faster than rich countries. The improvement in domestic distribution in some of these countries may have played a role, but most probably a small one.

We know that in the short run economic growth causes income concentration, while in the long run it causes a reduction of inequalities not only because of the character of technical progress, but also because richer countries tend to be democratic, and in democracies economic policies tend to reduce inequality. In this case, however, we observe that in the short run economic growth in poor and middle-income countries causes a reduction in international inequality independently of democracy.

In this article I have argued that policymakers in democratic states, usually representing left-wing or social-democratic political parties, are able to achieve a reduction of inequality. In other words, there is some discretion for politics in this matter. The social or welfare states built in western and northern Europe after World War II are proof of this possibility. Some favorable results in developing countries are another. Two basic means are used. On one side, the adoption of progressive taxes; on the other, an increase in the tax burden to finance increased social services in the areas of education, health care, social security and social assistance. In this last area, minimum income or basic income programs may effectively reduce inequality. The adoption and gradual increase of the minimum wage is also a major redistributive policy.

Given our economic structural constraints – basically the rate of profit – who is supposed to pay for these redistributive policies? We may always say that there is some room for reducing profits, but this is a poor response. Those who must see their incomes reduced in democratic societies are capitalist rentiers and the top level of the professional class – both groups whose incomes bear no relation to their contribution to society. In successful experiences of income redistribution within the capitalist system, entrepreneurs or entrepreneurial business enterprises continued to make satisfactory profits, whereas inactive or rentier capitalists living on interest, rents and dividends lost income. Keynes, in the *General Theory* (1936), referred to the "euthanasia of the rentiers". In modern, *social* capitalism, in the welfare state,

democratic politics is supposed to follow this path, to combat the curse of inequality. As for a reduction in the outlandish pay of high executives and financiers – this is a battle that is just beginning, which reached the public agenda in the 2008 global financial crisis. An increased tax burden on the remuneration of capitalist rentiers and high professionals will not make capitalism just, but it will reduce its intrinsic injustice.

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