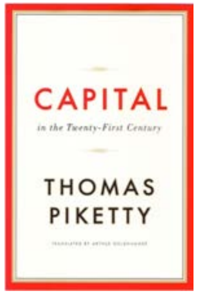
book review



Capital in the Twenty-First Century

Thomas Piketty, translated by Arthur Goldhammer
Published: Belknap Harvard, 2014
ISBN 978-0674430006

Rent in the Twenty-First Century

Thomas Piketty's international publishing sensation is, in significant part, a manifesto for tax justice.

Thomas Piketty's book *Capital in the Twenty First Century* is first and foremost a voluminous and fascinating historical account of how unfettered capitalism tends towards extreme inequalities of income and wealth. Left unaddressed, these inequalities will threaten democratic nation states and their founding social values.

The book is replete with tax justice debate: the entirely avoidable rise of inequality, the case for progressive taxation, enforced transparency, and improved international cooperation. These are long-standing issues for us, which we have (albeit briefly) discussed with him.

Piketty's core argument is that for centuries returns to capital have been higher than rates of economic growth of output and income. The corollary of this argument is that without political interventions the share of national income going to labour declines. The inevitable outcome is that wealth becomes ever more concentrated in the hands of a tiny proportion of the population – the 0.1 per cent – who create rentier dynasties that dominate the political economy. Although tax havens are not a major feature of the book, the wealth management industry that operates from such places merely aggravates this situation by enabling rentiers to dodge attempts to tax wealth, for example through inheritance tax, wealth tax, capital gains tax, and of course, income tax.

Drawing on massive data sets for France, Germany, Sweden, the U.K. and the U.S.A., Piketty shows that brief periods of convergence towards greater equality in the mid-20th century were historical aberrations caused by war, financial crises, trade union power, advances in public education, and the rise of progressive income taxes. The Reagan-Thatcher reaction in the 1980s reversed this momentum, restoring capitalism to its pre-1914 trajectory. The future for Europe and North America, not to mention poorer countries elsewhere as they play catch-up, looks from his perspective like France's 19th Century *Belle Époque*. Barring a revolution, it seems, the American Dream is dead.

The book might have been more accurately titled *Rent in the Twenty-First Century*. It is essentially a study of how unearned incomes such as dividends, interest and property rents accumulate fastest in periods when growth rates stabilise at relatively low rates - 1.0 to 1.5% annually. Faced with ecological constraints and a huge demographic shift from population growth to decline, this may well be the bleak future facing those countries already out there on the technological frontier.

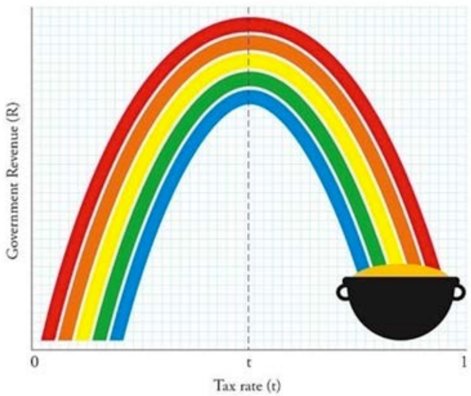
Piketty has a lot to say about tax. He calls progressive taxation "indispensable", argues for massive hikes in marginal income tax rates, and decries the "endless race to the bottom, leading, for example, to cuts in corporate tax rates and to the exemption of interest, dividends, and other financial revenues from the taxes to which labor incomes are subject." Piketty uses the language of "tax competition", or "fiscal competition" - though it's nothing to do with genuine competition: a far better term is "tax wars."

Faced with this and the closely related trend towards an "inegalitarian spiral", Piketty proposes a progressive annual tax on capital, supported by comprehensive and automatic exchange of information between countries. One suggestion certain to provoke the "supermanagerial" class and their acolytes is that the optimal top tax rate in developed countries is "probably above 80 percent." Right wing commentators have reacted predictably to this, claiming that high marginal tax rates reduce work and effort, and reduce productivity growth. To which Piketty responds robustly:

The reduction of top marginal income tax rates and the rise of top incomes do not seem to have stimulated productivity (contrary to the predictions of supply-side theory) or at any rate did not stimulate productivity enough to be detectable at macro level.

He demolishes American economist Arthur Laffer and his magical mystery curve, which claims – without empirical evidence - that tax cuts lead to higher tax revenues, through curbing avoidance and boosting economic growth. The fear that higher marginal tax rates on incomes above €500,000 would lead to a

book review (contd)



The Laffer Curve. Laffer's theory is that above a certain rate, higher taxes lead to lower revenues. Piketty estimates this rate is around 80 percent. (With thanks to www.and-smith.com.)

flight of top executives to Switzerland or Canada, says Piketty, is "*not only contradicted by historical experience and by all the firm-level data at our disposal; it is also devoid of common sense*." Indeed.

Despite the grandiose title, this is no rehash of Marx' *Das Kapital*. Marx argued there was an inexorable tendency for profits to decline, forcing the process of technological change and deeper exploitation of labour, and ultimately driving the system to its end. Capital was more than physical or financial assets; its essence lies in the power relations between owners of capital, land owners, the state, the managerial class and labour. Piketty, by contrast, looks at society through the lens of wealth and income, with power disproportionately held not by the top 1 percent targeted by the Occupy movement, but by the mostly rent-seeking multi-millionaires and billionaires in the top 0.1 percent.

Like John Maynard Keynes, Piketty wants to save capitalism from itself. Growing inequality is structurally embedded in capitalism, and the solution lies with democratising markets. "If we are to regain control of capitalism" he says, "we must bet everything on democracy." Indeed, again.

Piketty concludes that a tax on capital is the over-riding priority for tackling inequality. High marginal income taxes might partially redistribute the extraordinary incomes of the bonus-grabbers but will do little to redistribute inherited wealth. He suggests confiscatory annual capital taxes at 10 percent or higher on billionaires. Phew!

A tax on capital, he adds, might promote a necessary overhaul of accounting standards, leading us to transform how we define and value various types of assets, liabilities and net wealth. Current flaws in the system, he notes, "have contributed to the many financial scandals the world has seen since 2000." I can picture Prem Sikka and Richard Murphy nodding their vigorous agreement.

Piketty's data sets do not include developing countries in any meaningful way, though he does note that people in developing countries may be the biggest losers of the sweeping historical transformations that boost inequality. To help staunch the outflows of capital from Africa and other parts of the developing world – which outpace aid by a wide margin - he urges fiscal co-operation and data sharing to help poorer countries "root out the systematic pillage" that has emptied their treasuries. Foreign companies, their stockholders, and their enablers are, he says, "at least as guilty as African élites." I couldn't have said it better myself.

He also admits that the true wealth and inequality picture "is actually even larger than we estimated on the basis of official accounts" - because so much wealth is hidden behind offshore trusts and companies in tax havens. He cites our landmark study *The Price of Offshore, Revisited,* with its estimate of $21-32 trillion offshore, but settles on a substantially lower figure produced in a study by Gabriel Zucman, while admitting that could be merely a "lower bound". I'd argue strongly that ours is a far more robust estimate: we've not seen any serious effort to take down our numbers, though many would like to. In any case, despite the importance and sheer magnitude of this issue, this is in one sense a distraction from Piketty's astonishing accomplishment with its vast historical and empirical sweep. The strength of his book lies elsewhere.

This book is a very, very rich pudding. I have read all of its 577 pages and it's clear that many of the reviews out there were written on the basis of a quick skim (at best) and a dusting-down of old ideological prejudices. Piketty calls his tax on capital proposal "utopian" and he's probably right, but he's on our side, folks, in wanting to open up a discussion about economic injustice and what can be done to tackle it.

There are many, many bag-carriers of the wealthy elites who will want to close down this debate. They will do whatever it takes to rubbish Piketty and his book. We should resist them. Read the book and draw from its strengths.

Review by John Christensen