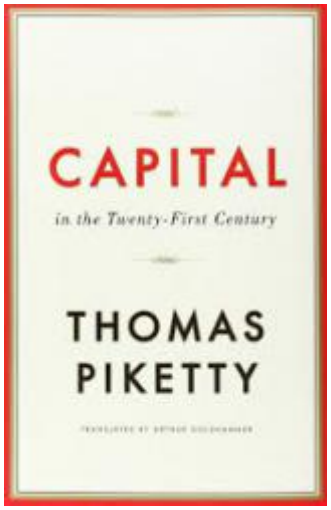
Critique of Piketty on Capital and Inequality

written by Charles Post | October 27, 2014

THE ISSUE OF growing inequalities of income and wealth in the advanced capitalist world over the past four decades has been the subject of both social scientific research and political struggle. On the one hand, there is an extensive literature that amply documents the growth of inequality globally since the mid-1970s. While ideologues of neo-liberalism have attempted to dismiss this evidence or diminish its importance,(1) there is a consensus among social scientists that inequality has been on the rise.(2)

On the other hand, the widening gap between the super-rich and the rest of us fueled the Occupy movement in the fall of 2011. Occupy targeted the "1%" and its growing income, wealth and political influence in the name of the "99%," putting inequality at the center of U.S. politics for a brief period of time.



Fundamentally, it was the political and ideological impact of Occupy that created the conditions for the reception of Thomas Piketty's Capital in the Twenty-First Century. It is quite exceptional for a lengthy, academic study by a trained economist — complete with graphs, data tables and various formulae — to become a major cultural sensation.

Capital in the Twenty-First Century has been the subject of miles of column inches in newspapers and magazines and extensive discussion on the internet, television and radio.(3) As we are writing this review, the book is beginning its fourth month on the New York Times non-fiction best seller list, competing with the latest screeds from various Fox News commentators and Hillary Clinton's self-

congratulatory memoir of her years as U.S. imperialism's chief diplomat.(4)

Leftist commentary on Piketty's book generally makes two points.(5) First, Piketty provides valuable statistical ammunition for activists and organizers in the labor and social movements on the extent of wealth inequality in several major capitalist societies since the late 18th century. Second, Piketty is far from an anti-capitalist radical.

While the son of revolutionary militants in France,(6) he is a member of the (at best) left-center Socialist Party. Piketty rejects Marx's analysis of the capitalist mode of production and believes that changes in taxation on wealth could alleviate inequality while preserving the 'efficiencies of the market economy.'(7)

There is no question that Piketty is not a Marxist. He conceives of capital as a stock of assets used to produce income rather than as a relation between classes; focuses on the distribution of profits, rent and wages rather than social production; and rejects Marx's fundamental insight that the same underlying forces that make capitalism incredibly dynamic inevitably lead to periodic crises.

Still, with few exceptions(8) most left commentary on Piketty has not gone beyond distinguishing his investigation of capital from that of Marx. Put another way, they have not demonstrated how Piketty's non-Marxist conceptual framework cannot explain the patterns of inequality he documents.

The Normality of Inequality

The greatest strength of Piketty's book is, without doubt, his empirical data.

Building upon earlier research that he and a team of French economists have been engaged in for over a decade, Piketty's World Top Income Database (WTID) draws on tax records and other government data to provide detailed documentation of the distribution of wealth and income in France, Great Britain, Germany, Italy, Canada, Japan and the United States (with less thorough data for Argentina, Spain, Portugal, Switzerland, China and India) for the past two and one-half centuries.

While Piketty engages in flights of fancy concerning inequality before the late 18th century, his data clearly demonstrate that growing wealth and income inequality is a normal feature of capitalism. Contrary to the claims of Simon Kuznets and other mainstream economists writing during the height of the Cold War, declining inequality was the exception — the product of the massive destruction of capital during the Great Depression and the two world wars.

Inequalities of income and wealth steadily increased from the late 1700s through the 1930s, declining slightly during the "thirty glorious years" after World War II, and again increasing steadily since the mid-1970s.

Piketty begins with two "fundamental laws of capitalism." The first is expressed in the formula:

$a = r \times \beta$

Here a is the share of national income from capital, r is the rate of return on capital and β is the ratio of capital to total national income. As Piketty recognizes, this is essentially a descriptive, accounting formula — the percentage of national income from capital is equal to the ratio of capital to national income multiplied by the rate of return on capital. His second "fundamental law of capitalism" is equally descriptive:

$\beta = s / g$

Put another way, β — the ratio of capital in national income — is the savings rate s divided by the rate of growth of output per capital g, or wealth "saved" divided by the rate of growth of total production of goods and services.

Piketty uses these two "laws" to illustrate how a rising ratio of capital to total national income before and after the "thirty glorious years" led to a growth of national income from capital and growing inequalities of income and wealth. Conversely, the temporary reduction of the capital/output ratio in the mid-20th century radically reduced the share of national income derived from capital and led to a slight reduction of economic inequality.

The problems come with what Piketty calls the "central contradiction of capitalism."

$r > g$

For Piketty, the rate of return on capital almost always exceeds the rate of growth of per capita output, producing greater inequality. While technological innovation can raise the rate of return on capital and the growth of capital can reduce the rate of return, Piketty claims that the rate of return was generally stable both before and after the post-war era of declining inequality.

By contrast, the rate of growth of output is determined primarily by population growth, except for brief periods when the destruction of existing capital produces growth that exceeds demographic increase. Given slowly growing populations in most of the developed capitalist world in the past two centuries and a relatively stable rate of return on capital, growing inequality was the unavoidable consequence of capitalism.

The exceptional period of 1945-1975, when inequality declined, was the product of the massive destruction of capital and the exceedingly high growth rates of that era.

Piketty's attempt to explain wealth and income inequality, however, is either simply descriptive or theoretically and factually inconsistent.

On the one hand, it is almost axiomatic in both conventional and Marxist economists that the rate of return on capital shapes the rate of growth of output by determining investment. Put another way, the rate of return and rate of growth are not independent of one another — the higher the rate of return, the more likely capital will be invested and total output increased, and vice-versa.

On the other hand, Piketty's claim for a steady rate of return that is consistently higher than the rate of growth is unsupported by any data. For an economist who insists on the need to test all claims against data, this is a rather surprising omission.

Various Marxist economists(9) have argued that Piketty's rate of return does not correspond to Marx's rate of profit — total profits divided by productive capital and total wages — but to the mass of profit, total profits produced annually. There are significant data, in particular by other Marxist economists, that demonstrate that the mass of profit has not been stable, but has fluctuated along with the rate of profit and rate of accumulation/investment.(10)

While Piketty's description of the persistent growth of economic inequality under capitalism is unassailable, his explanation of these patterns is inadequate.

Marx's Account

The inadequacy of Piketty's explanation is rooted in his acceptance of neo-classical economic categories, viewing capital as a mass of wealth rather than a social relation, and wages, rents and

profit as determined by the “marginal productivity” of labor, land and capital, rather than by conditions of production, accumulation and exploitation.

Marx’s account of capitalism provides a much superior account of the growth of economic inequality.(11) The fundamental tendency for inequality to increase under capitalism is built into the exploitative structure of the capital-labor relation.

Effectively separated from means of production and consumption, the mass of wage workers are forced to sell their ability to work (labor-power) to those who own productive capital.

Capitalists consume labor-power by compelling workers to labor in excess of the time needed to reproduce the value of their wages. This unpaid surplus-labor — surplus-value — is the source of profits under capitalism, creating the structural inequality in incomes between capitalists and labor.

As competition among capitalists produces the concentration and centralization of capital, increasing mechanization, and a reserve army of unemployed (and underemployed) workers, the capitalist class becomes numerically smaller while appropriating even larger portions of total social product (Piketty’s capital as share of total output).

The necessary tendencies towards periodic crises of profitability, rooted in increasing capitalization of production, lead to even greater inequalities as capital becomes centralized into even fewer hands through waves of bankruptcies of inefficient firms; and labor’s share of total output is reduced through wage cuts, speedup and the like.

How would Marxist theory explain the exceptional period of declining inequality in the three decades after the Second World War? The slight decline in inequality and the general growth in working-class living standards in this period was the product of two historically specific factors.

As Piketty acknowledges, the depression of 1929-1932 was the deepest and most devastating crisis in the history of capitalism. Across the capitalist world, massive bankruptcies destroyed the least efficient firms and produced a sharp increase in the rate of profit in the 1930s. The destruction of much of the productive capacity of Germany, Japan and Italy during the war sustained this rise of profitability through the late 1940s, producing a period of unprecedented growth through the mid-1960s.

While the long postwar boom provided the possibility for a decline in inequality through rising working-class income, a unique set of political conditions made them necessary. Even more important than the global rivalry between the capitalist and bureaucratic (so-called “communist”) world, the militancy of the working classes in most industrialized countries in the 1930s and 1940s — including near-revolutionary mass strike waves in France and Italy after the war — compelled capitalists and capitalist states to institutionalize collective bargaining with unions, raise real wages, and expand social welfare.

The combination of rising profitability and working-class militancy produced the temporary and exceptional decline in inequality after World War II. The subsequent decline of working-class militancy and self-organization, the result of the defeats of bureaucratic unionism and traditional social-democracy in the 1970s and 1980s, allowed inequality to continue to grow even during the neoliberal boom of 1982-2008.(12)

In sum, the dynamics of capitalist accumulation necessarily produce growing inequality, and only massive disruption — mass strikes and the like — by working people have momentarily tempered these tendencies.

Thanks to Solidarity and *Against the Current* for allowing us to reprint this article.

Notes

1. For the latest attempts to dismiss the overwhelming data on inequality, see Chris Giles, "Piketty Findings Undercut by Errors," Financial Times, May 23, 2014 and Neil Irwin, "Obama's Top Economist Has Problems with Piketty's Book," New York Times Website, May 7, 2014 [http://www.nytimes.com/2014/05/09/upshot/obamas-top-economist-has-some-problems-with-pikettys-book.html?emc=eta1].
   back to text
2. For a synthesis of the research on inequality in the United States, see Dennis Gilbert, The American Class Structure in an Age of Growing Inequality (New York: Sage Publishers, 2014).
   back to text
3. For a sample of the commentary on Piketty, see Jeff Madrick, "Piketty Review Roundup," The Century Foundation Blog, July 1, 2014 [http://tcf.org/blog/detail/piketty-review-roundup-capital-in-the-21st-century].
   back to text
4. The New York Times Book Review, July 6, 2014, 22.
   back to text
5. See, for example, David Harvey, "Afterthoughts on Piketty's Capital," Reading Marx's Capital with David Harvey, May 2014 [http://davidharvey.org/2014/05/afterthoughts-pikettys-capital/]; "Taking on 'Capital' Without Marx: What Thomas Piketty Misses in His Critique of Capitalism," In These Times, May 20, 2014 [http://inthesetimes.com/article/16722/taking_on_capital_without_marx]; and Toni Gilpin, "Them that's Got Are Them That Gets: Piketty's Lessons for Activists," Labor Notes, July 3, 2014. [http://www.labornotes.org/blogs/2014/07/them-thats-got-are-them-gets-pikettys-lessons-activists]
   back to text
6. His parents were members of the Trotskyist Lutte Ouvriere (Workers' Struggle) organization. See "Thomas Piketty," Wikipedia [http://en.wikipedia.org/wiki/Thomas_Piketty]

   back to text

7. See "Dynamics of Inequality: Interview with Thomas Piketty," New Left Review, II/85 (January-February 2014).

1. Three exceptions, from which I have borrowed freely, are Michael Roberts, "David Harvey, Piketty, and the Central Contradiction of Capitalism," Michael Roberts' Blog, May 19, 2014 [http://thenextrecession.wordpress.com/2014/05/19/david-harvey-piketty-and-the-central-contradiction-of-capitalism/]; Barry Finger, "Coasting on Borrowed Time: Making Sense of Piketty's Capital in the 21st Century," New Socialist (Canada) Webzine, June 15, 2014 [http://newsocialist.org/755-coasting-on-borrowed-time-making-sense-of-piketty-s-capital-in-the-21st-century]; and Benjamin Kunkel, "Paupers and Richlings," London Review of Books, 36, 13 (July 3, 2014). [http://www.lrb.co.uk/v36/n13/benjamin-kunkel/paupers-and-richlings]
   back to text
2. See note 8.
   back to text
3. See the work of Anwar Shaikh, in particular (with E. Ahmet Tonak) Measuring the Wealth of Nations: The Political Economy of National Income Accounts (New York: Cambridge University

Press, 1994) and “The First Great Depression of the 21st Century,” Socialist Register 2011: The Crisis This Time (London: Merlin Press, 2010).
back to text

4. This is drawn from Marx, Capital, Volume I (Hammondsworth, England: Penguin Press, 1976) and Volume III (Hammondsworth, England: Penguin Press, 1981).
back to text
5. Kim Moody, “Contextualizing Organized Labour in Expansion and Crisis: The Case of the US,” Historical Materialism 20.1 (2012), 3-30.
back to text

September/October 2014, ATC 172