

“YOU CAN’T HAVE A ROBUST RECOVERY IF ORDINARY CITIZENS DON’T HAVE MONEY TO SPEND.”

DAY 2: CLOSING LUNCH SESSION

CREATING SHARED PROSPERITY

TUESDAY 7 OCTOBER 2014



PROFESSOR JOSEPH E. STIGLITZ

Winner of the Nobel Memorial Prize (2001 Nobel Prize in Economics)
Professor, COLUMBIA UNIVERSITY
and Co-Chair of COLUMBIA UNIVERSITY’S
COMMITTEE ON GLOBAL THOUGHT

In a hard-hitting speech, Joseph Stiglitz highlighted the threat growing inequality of wealth and opportunity poses to the prospects of a robust recovery in Europe and in North America. He also pinpointed European currency union – driven by politicians and poorly implemented, despite concerns raised by many economists – as a source of Europe’s current economic malaise.

“Something isn’t working the way it should,” Professor Stiglitz told EPCA. “It looks like Europe is entering a triple-dip recession. Today, wages are lower than before the economic crisis. The GDP of the eurozone is more than 15% below where it would have been had the 2008 financial crisis not occurred. Unemployment in the eurozone is 11.5%, and youth unemployment is almost 24%. Most European countries have per

capita GDP lower than pre-crisis levels. And the worst performing countries are in depression, with youth unemployment at 50% or above. What’s more, the performance of the best only looks good in comparison with the worst.”

“But how can this be?” Stiglitz asked. Because Europe’s resources – its human, physical, and natural capita – are much the same as they were before the crisis.”

Stiglitz took little comfort in the fact that America is doing marginally better. He noted that GDP is also some 15% below the trend line, and mid-range incomes are lower than a quarter of a century ago. Real wages are stagnating, despite continual increases in productivity. The US labor market remains weak, with high levels of disguised unemployment, and rising inequality has become a major concern, he said.

There are many dimensions to America’s rising inequality, the Nobel Laureate continued. “In America, the top 1% gets almost 25% of income, and has also received 95% of the gains since recession ‘officially’ ended.” He said it was no surprise that America has less equality of opportunity than ‘old Europe’ and less than other developed countries, because countries with high inequality of outcomes end up with limited equality of opportunity.

Stiglitz argued that rising inequality is a serious impediment to achieving a robust economic recovery and took aim at what he described as out-of-date, discredited economic theories. “The old view was that there was a trade-off between economic performance and equality – one could only get more equality by sacrificing economic performance. But the new view is that we pay a high price for inequality, and – when it reaches current extremes – inequality actually undermines economic performance.”

The old theory, which said everyone benefits from the growth of income at the top, was known as ‘trickle down economics.’ But Stiglitz said there never was a proper theory or any evidence to support it. In fact, current evidence is overwhelmingly contradictory. The old theory said most inequality results from differences in societal contributions, which Stiglitz paraphrased as “just deserts of the more able; they make a greater contribution to society.”

The new theory is that much of our inequality arises from “wealth appropriation,” where some individuals and groups simply take a larger slice of the national income pie, rather than making the pie bigger, which is what economists call ‘rent seeking.’ Stiglitz offered several examples of how these market distortions contribute to inequality, including “the natural resources curse,” the fight over who gets the benefits of oil and gas and other resources,



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NADINE DEREZA
Moderator

and monopoly at the top of society, with exploitation/discrimination at the bottom. And in case anyone thinks this 'new theory' argument is the preserve of "liberal leftists," Stiglitz suggested they might check what the International Monetary Fund is saying. "There is almost no pushback to the new theory," he said. He also noted that among Forbes Magazine's listing of the 100 wealthiest individuals there are few real innovators, and none of those whose basic insights had led to the transformation of our economy – those who discovered DNA, the transistor, the laser, etc. He accused US banks of exploitation, market manipulation, and other practices that did not lead to faster economic growth, but did enable the sector to extract outsized returns. "Up to 40% of all corporate profits were going to the financial sector before the crisis," he pointed out.

"So why do more equal societies perform better?" said Stiglitz. It's because there is less scope for rent-seeking, and greater opportunity enables more individuals to realize their potential, he continued. "Less divided societies can pull together, and have more trust. There is wider support for needed public investments, and better macroeconomic performance." Lastly, said Stiglitz: "You can't have a robust recovery if ordinary citizens don't have money to spend."

There are policies that can promote growth and equality, the professor said. Some are obvious, such as more equal access to quality education. But others are not so obvious. For example, current monetary/macro policies are exacerbating inequality, which helps explain why so much of the gains since recovery have gone to the top, Stiglitz observed. He also suggested that better public transportation is a way to improve access to jobs.

The Columbia professor also took aim at the use of inappropriate metrics to gauge wealth, well-being and economic prosperity. GDP was a major target: "GDP can go up, even if most individuals in society are worse off. It's also an inadequate measure because it doesn't reflect other aspects of quality of life, such as improved or poorer health, longevity, increased insecurity or environmental degradation. That's why it's important to use metrics that go beyond GDP," said Stiglitz.

Wading into the failure of euro currency union, the professor said the EU was not an optimal currency area. Those responsible for its implementation had misdiagnosed what was needed to make it work: and it is not an easy matter to make a currency union with such diversity work. Significant problems arise, for instance, when countries borrow in currencies they don't control. He emphasized that the resulting crisis led to widespread fiscal problems, not the other way around. The EU failed to create institutions to enable the euro to work. There are fundamental problems in the structure of the euro – not the structure of the individual countries. Indeed, many of the structural reforms in individual countries are now making lack of demand – the real problem – worse.

Stiglitz argued that there is currently a global shortage of demand, and that the pursuit of flawed policy – in particular, austerity – had compounded the problem of the euro. Global demand imbalances have also grown worse, and these contribute to weak demand, as countries with deficits cut back faster than those with surpluses are expanding.

Furthermore, the global financial system is not recycling surpluses to where they are needed. Though some have pointed to a savings glut, Stiglitz questioned this. How

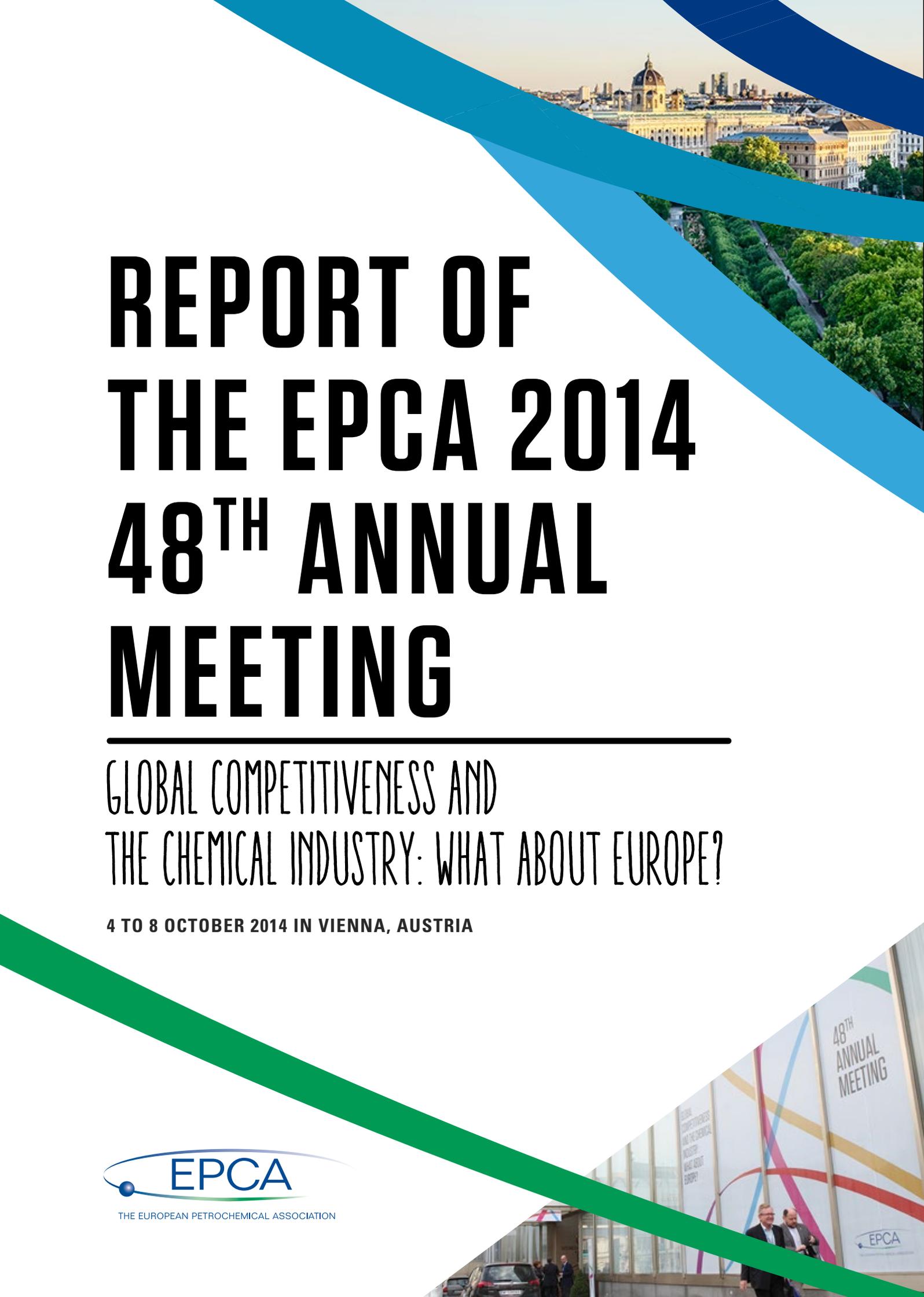
could one say that is a savings surplus, when there is such a huge global need for investment?

Another complicating factor has been the financial crisis: it made us lose focus, Stiglitz believes. "We became fixated on repairing the financial system and dealing with the immediate problem of the euro." But at the same time, long-term problems of inequality, global imbalances and the structural transformation needed to respond to the changing underlying fundamentals of the global economy – including changing global comparative advantage – were not addressed. In fact, some have become worse.

And the financial system is still not fixed. Meanwhile, the focus is on ensuring the financial system doesn't do harm through excessive risk taking and market manipulation, when the fundamental task should be ensuring that it performs the functions vital to a well-functioning economy.

Stiglitz offered a bleak prognosis. He sees the global economy muddling along, and Europe stagnating while the US achieves only weak growth, barely able to create enough jobs for the new entrants into the labor force. He also expects a slight slowdown in China, with knock-on effects in other emerging markets. And as global problems continue to fester, inequality will increase along with global imbalances. While some structural transformations are in progress, they are happening slowly, and loose monetary policies continue to feed asset price bubbles. Stiglitz urged the audience to learn the major lessons of the crisis: Sustained prosperity will be impossible without shared prosperity, but markets won't create shared prosperity on their own.

And even seemingly benign neglect can lead to matters getting worse!



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