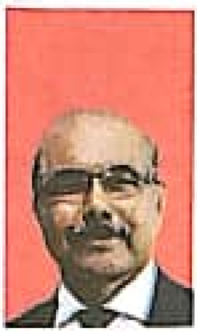
TACKLING WEALTH GAPS

An ecosystem that enables economic, social, political and protective freedoms is necessary to ensure wealth equality



DATUK DR JOHN ANTONY XAVIER

SINCE returning to power, Tun Dr Mahathir Mohamad has been expounding on wealth inequality. As he said recently: "We wish to see everyone equal in all matters that matter, and we would like to see everyone as rich as each other."

According to a 2014 Pew Global Survey, three-quarters of Malaysians consider the gap between the rich and poor worrying. Although it has improved, our Gini coefficient of 0.399 (a measure of income inequality – 1 means all wealth is concentrated on one person; 0 means all wealth is equally distributed) flirts dangerously with the World Bank's 0.4 benchmark, beyond which a country is considered severely unequal in wealth distribution.

Wealth inequality is a strain on economic growth and a source of social instability. The International Monetary Fund estimates that a 1 per cent increase in the income share of the top 20 per cent will drag growth by 0.1 per cent over five years. This is partly because the consequent market-distorting income-redistribution measures of government will adversely affect investments.

Wealth equality is a chimera if we subscribe to the argument of Thomas Piketty, a French economist, in his 2013 magnum opus, *Capital in the Twenty-First Century*. His research on wealth inequality in the US and Europe since the 18th century found that the rate of return on capital — profits, rent, interest, dividends — is 7 per cent. This rate is more than twice that of labour. As such, wealth tends to accumulate quickly causing the rich to grow richer.

However, that does not mean that one should stop from pursuing wealth equality. Many developed countries have pursued economic growth in the hope that the rising tide of wealth will lift all up the income ladder. Even Piketty advocates a wealth tax of 2 per cent and a progressive system of income-tax to prevent social and economic upheaval, reduce inequality and break the wealth monopoly by the rich.

Daron Acemoglu and James A. Robinson in their 2013 book *Why Institutions Fail* proffer evidence from across the rich and poor worlds to show conclusively that social inequality is due more to institutional factors.

Take North and South Korea. Acemoglu and Robinson argue that it is the system of incentives and responsive governance that allow South Koreans to avail to the economic opportunities while the North wallows in stagnation. Therefore, it is inclusive institutions, and not extractive institutions that serve the narrow interests of the elites, which is the most effective in effecting greater wealth equality.

The 1998 Noble laureate in economics, Amartya Sen, argues in a similar vein in his 1999 book, *Development as Freedom*. Rather than solely focusing on wealth and income per capita, development must be viewed as advancement of real freedoms that individuals enjoy.

As Sen says: "Human life depends not only on income but also on social opportunities." In addition to better education and healthcare, Sen advocates political freedom that affords voice in government, economic freedom to pursue prosperity, and protective freedom that affords social safety nets for the poor.

These freedoms are interlinked. For example, social opportunities of education and health complement economic and political freedoms. A healthy and well-educated person is better positioned to make informed economic decisions and be involved in fruitful political discourse to hold the government accountable for its actions.

For Sen, therefore, the larger issue is not rising per capita income. Rather it is about an ecosystem that progressively enables the exercise of these freedoms. Sen's equality of freedoms therefore resonates well with what Tun Mahathir suggests, namely, Malaysians must be equal in all matters that matter — economic, social, political and protective freedoms.

Philosophers too have joined the debate on what is wealth equality. John Rawls, a Harvard political philosopher, advocates an egalitarian view of wealth distribution. In his 1971 book *A Theory of Justice*, Rawls propounds a theory of "justice as fairness" that closely resembles the wealth-distribution policy of our government.

Similar to Sen, Rawls recommends equal basic rights, equality of opportunity, and the promotion of the interests of the least advantaged members of society. He also believes in intergenerational justice where sustainable development leaves resources for the prosperity of posterity. The state therefore must engage in redistributive taxation to ensure a fair distribution of wealth and income across society.

Given the intellectual discourse on wealth equality, the government is on track in attacking wealth inequality on all fronts: income redistribution, institutional reform and in ensuring equality of freedoms.

However, the government should be wary that it does not go overboard, lest it dampens growth. The case of Latin America is in point. There, moderate redistribution has proved beneficial. It has reduced dependence on risky borrowing among poorer households and has spiked savings and investment. Such moderate redistribution may even obviate the need for more aggressive state interventions in the future.

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