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THE IMPACT OF INEQUALITIES ON THE STABILITY OF THE GLOBAL SOCIETY

ABSTRACT

The article analyses the impact of inequalities on the stability of the global society. The author asks questions concerning the reasons for global inequalities. The link between globalization and global inequalities is presented as well as the connections between the free market rules and the growing gap between the North and the South. Some solutions to the problem are also suggested.

Keywords: inequalities, globalisation, free market, capitalism

INTRODUCTION

THE CRITICS AND proponents of globalization wage a fierce debate over the effects of globalization on inequality. Are the world's rich and the world's poor growing closer together or further apart? Can the global international society which contains both extremely rich and extremely poor states be viable over the longer term?A decade ago, there was a general scholarly consensus that global disparities of wealth and income arose between 1970 and 1990. However, more recently the negative impact of globalization on inequality has been questioned, especially by economists suggesting that globalization tends to create a more equal world. The debate is becoming more and more severe.[1]

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[1] B. Milanovic, *Global Income Inequality: What It Is and Why It Matters*, World Bank research paper WPS 3865 (Washington, DC: The World Bank, 2.03.2006), go.worldbank.org/XSKB9QVEE0,

The proponents make claims such as "globalization has brought the world together on a level playing field," while the critics contend that "globalization has created an unequal world." Such general statements, from supporters of globalization and from detractors alike, are too sweeping to be accurate.

It is very clear, however, that current global inequality levels – whether they have been moving up or down – stand very high. The inequality of income, for instance, is as severe in the global society as it is in any particular country in the world. Let us consider the degree of economic disparity in some of the most economically unequal countries in the world, like South Africa, Guatemala, and Brazil. If we envision the whole world as one society – which is precisely what globalization encourages us to do – we would see that the economic inequality among the world population is greater than it is within th countries marked by economic disparity and social fractures.

It is precisely the rising consciousness of an interconnected world – the globalization of our imagination – that calls us to think anew about the social and political implications of global inequality. Global inequalities of particular kinds and of a severe degree are grave matters of political and economic consequence. Therefore, we should care about both poverty and inequality as far as their impact on the future of global international society.[2]

A LINK BETWEEN GLOBALISATION AND GLOBAL INEQUALITY

It is often implicitly assumed that the changes in global inequality can be interpreted as telling us whether globalization leads to widening or shrinking income differences among individuals in the world. However, the causal link between globalization and global inequality is very difficult to make. To see this, let us consider several ways in which globalization affects inequality among individuals in the world. The first channel goes through globalization's effects on within-country distributions. As we would expect from economic theory, the effect varies between rich and poor countries. In the simplest Hecksher-Ohlin world, globaliza-

accessed 19.02.2011; N. Birdsall, *The World is Not Flat: Inequality and Injustice in our Global World*, WIDER Annual Lecture 2005 (Helsinki, Finland: World Institute of Development Economics Research, 2005), www.wider.unu.edu/publications/publications.htm, accessed 19.02.2011.

2 D.A. Hicks, *Global Inequality*, Center For Christian Ethics, Baylore University 2007, www.baylor.edu/christianethics/GlobalWealthArticleHicks.pdf, accessed 19.02.2011.

tion would increase demand for, and the wages of, low-skilled labour in poor countries and the wages of high-skilled workers in the rich world. Consequently, we would expect income distribution in poor countries to become "better" and income distribution in rich countries to get "worse." This is not, however, consistent with what has been observed over the last twenty years when distribution in poor, middle-income and rich countries has grown more unequally.[3] This is an issue which has recently been studied a lot and is still the subject to intense debate: Is openness to blame for increasing wage and income differences in the US? Is openness associated with rising income inequality in poor countries? For example, Milanovic[4] and Ravallion[5] find that openness is associated with increased inequality in poor countries, and lower inequality in rich countries, while Dollar and Kraay[6] argue that there is no systematic effect of openness on inequality.

Then, and this is the second channel, globalization may differently affect mean income in poor and rich countries: in other words, it might lead to divergence or convergence in country incomes. There is no unanimity on this point either. Most authors agree that openness is positively associated with mean income growth, but some of them[7] find the effect stronger for poor countries, while others[8] argue that the openness premium has been larger for rich than for poor countries during the last twenty years. The first group of authors would expect openness to lead to shrinking differences in national average incomes. Therefore, they have to explain away the observed divergence in country average incomes by the lack of openness among the laggards. According to the second group of authors, the divergence is an indication that the effects of openness might change over time, and that openness, even if positive for all on balance, may exacerbate inter-country inequality. Third, the effects of globalization may vary between populous and small countries.

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[3] G.A. Cornia, S. Kiiski, *Trends in income distribution in the post WWII period: Evidence and Interpretation*, http://www.wider.unu.edu/research/1998–1999–3.1.publications.htm, accessed 20.02. 2011.

[4] B. Milanovic, *Worlds Apart: Global and International Inequality, 1950–2000*, Princeton 2005.

[5] M. Ravallion, *Growth, inequality and poverty: Looking beyond averages*, "World Development" 2011, no. 29, pp. 1803–1815.

[6] D. Dollar, A. Kraay, *Growth is good for the poor*, "Journal of Economic Growth" 2002, no. 7, pp. 195–225.

[7] J. Sachs, D. Warner, *Fundamental sources of long-run growth*, "American Economic Review" 1997, no. 87, pp. 184–188.

[8] B. DeLong, S. Dowrick, *Globalization and convergence*, [in:] *Globalization in Historical Perspective*, M. Bordo, A.M. Taylor, J. Williamson (eds.), Chicago 2003; S. Dowrick, J. Golley, *Trade openness and growth: Who benefits*, "Oxford Review of Economic Policy" 2004, no. 20, pp. 38–56.

This area has not been much explored except in the context of the rather limited (in scope and number) studies of small island economies. Yet, one can imagine that globalization may play out differently in populous countries with large domestic markets, or in small niche economies like Hong Kong, Singapore or Luxembourg, than in middle-size countries.

And finally, and possibly, most importantly, the effect of globalization on global inequality will depend on history, that is on whether populous countries happen to be poor or rich at a given point in time. To see this, let us assume for a moment that globalization has a positive impact on the growth rates of populous and poor countries, and has no effect on internal income distribution. This means, in the current constellation of world income, that India and China will be expected to catch up with the rich world, while their national distributions will not change, and global inequality will tend to decrease. There will be both average-income convergence and reduction of global inequality. But let us decouple the poor and populous countries. Suppose that India and China are rich (and still populous) and let most poor countries be relatively small. Now, average-income convergence will continue, but the effect on global inequality will be ambiguous. China and India will benefit from the pro-big bias of globalization, but since they will rich, globalization will be less beneficial to them than to poor countries. These two effects will pull in opposite directions, and global inequality may go down or up. Moreover, if populous countries are generally poor, the convergence effect is nil, globalization on average favours small countries and leads to the widening of national income distribution, then the overall effect must be to increase global inequality. This illustrates a key point: even if the effects of globalization on internal inequality, average-income convergence, and populous vs. small countries, are unambiguous and do not change over time, globalization's impact on global inequality will vary depending on where countries with different attributes happen to lie with regard the international income distribution at a given point in time. The implication is, of course, that all statements about the relationship between globalization and global inequality are highly time-specific, contingent on the past income history, and not general.[9]

[9] B. Milanovic, *Global Income Inequality: What It Is And Why It Matters?*, "Economic and Social Affairs" August 2006, http://www.un.org/esa/desa/papers/2006/wp26_2006.pdf, accessed 19.02.2011.

FREE MARKET FOR ALL

It is not easy for citizens deeply influenced by the modern discourse on freedom and individualism to focus on the disparities and corresponding deprivations that economic free markets allow or even exacerbate. Economic arguments about growth, productivity, and efficiency are often taken as a kind of immutable reality that cannot and should not be questioned. The names of Adam Smith and Alfred Marshall, the respective "fathers" of classical and neo-classical economics, are invoked to assert that the economy and its Invisible Hand should be left alone. the fact that Adam Smith himself was a moral philosopher who believed that the economy should operate within a wider framework of justice is less often noted. More specifically to the issue of economic deprivation, Smith insisted that all citizens should have the means "to appear in public without shame," means that are always relative to the society in which one lives.[10] Alfred Marshall added that poverty and its alleviation "are at the heart of economic studies"[11] Smith and Marshall would be deeply troubled by economists and others who believe that inequality and poverty are not the matters of public concern. We must attend to all indicators that give some idea of the effects of the economy on persons' actual well-being. The moral bottom line is the impact of economic policies and conditions on people's lives.

GROWING GAP

According to the UNDP Human Development Report (HDR) 2009 only 9 countries (4% of the world's population) have reduced the wealth gap between rich and poor, whilst 80% of the world's population have recorded an increase in wealth inequality. The report states that "the richest 50 individuals in the world have a combined income greater than that of the poorest 416 million. The 2.5 billion people living on less than $2 a day – 40% of the world's population – receive only 5% of global income, while 54% of global income goes to the richest 10% of the world's population."[12]

[10] A. Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, London 1991, pp. 351–352.

[11] A. Marshall, Introduction to *Principles of Economics*, London 1980.

[12] Human Development Report 2009, http://hdr.undp.org/en/reports/global/hdr2009/, accessed 19.02.2011.

The UN's Report on the World's Social Situation 2010: *Rethinking Poverty*, identifies non-economic aspects of global inequality (such as inequalities in health, education, employment, gender and opportunities for social and political participation), as causing and exacerbating poverty. These institutionalised inequalities result in greater marginalisation within society. The report emphasises the inevitable social disintegration, violence as well as national and international terrorism that this inequality fosters. Ironically, the diversion of social development funds to national/international security and military operations produces further deprivation and marginalization, thus creating a vicious cycle.[13]

In agreement with previous analyses, the above reports identify the forces of globalization, deregulation and liberalization as key contributory factors to global inequality. The HDR 2009 cites the unjust global trade regime as a primary cause in increasing global inequality. The countries of the South would benefit much more in financial terms if they were able to trade equitably with the North rather than receive funds through official development assistance (ODA). However, the North's agricultural subsidies alone cost developing countries' economies nearly as much as they receive in ODA each year. Even the World Bank's World Development Report 2009 'Equity and Development' makes recommendations to end subsidies and tariffs and create an even playing field. Despite widespread recognition of these facts, the South is forced to continue trading on unfair terms, and the consecutive World Trade talks continue to neglect the needs of the majority world. In spite of apparent efforts, it thus becomes more and more common.

INEQUALITIES AS A GLOBAL PROBLEM

Despite a general conviction, this growing inequality is not confined to the global South but is rampant in economically powerful nations. The most striking fact is the growing level of inequality in the USA, a country with the highest GNP and the primary exponent of the "Washington Consensus." Economic inequality has continued to increase in the USA since the late 1970s. This inequality can be seen in numerous aspects of socio-economic life, such as growing income disparities, loss of opportunities – especially for women and minorities, the inequality in health, education and crucially, political participation. One in eight people

[13] Report on the World Social Situation, http://www.un.org/esa/socdev/rwss/index-print.html, accessed 19.02.2011.

in the USA live in poverty and for a 'developed' country it has an unusually low life expectancy level. These factors highlight the extremely distorted benefits of the free market model, even within national borders.

Given the overwhelming evidence of the inability of the political economy to reduce inequality and deal with non-economic aspects of prosperity, why are free market policies so ardently pursued by economically powerful nations? The answer is, unsurprisingly, profitability. According to the International Forum on Globalization, 52 of the top 100 wealthiest economic entities are corporations as opposed to states. Unlike in the case national countries, however, the key beneficiaries are a limited number of shareholders. It is the economic activities of these corporations that are so vital to the economic power and income of their countries of origin. The share of corporate profit as a portion of national income is at its highest for at least 25 years, and year on year growth in corporate profits is at an all-time high. But, of course, the distribution of these profits is highly distorted. According to *The Economist*, over the past three years American corporate profits have risen by 60%, whereas wage income by only 10%. The neoliberal approach clearly favours corporate interests. Their vast resources and influence on governments and International Financial Institutions through their billion dollar lobbying activities is considerable. This influence, combined with the competitive, economic growth based directives pursued by dominant governments has promoted this model at the expense of the global public – a clear indictment of the democratic process.[14] However, such analysis indicates that the problem of inequalities concernsnot only the field of relations between the South and the North, but also the economies perceived as highly developed, which, consequently, enforces the statement that the phenomenon is global.

PROPOSITIONS OF CHANGES

Having reviewed 41 years of high level reports on poverty and inequality (since the Pearson Report 1969), it becomes clear that any alleviation of inequality is increasingly subdued by the growing levels of economic competition between developed countries, and fueled by profit driven commercial interests. Ultimately, measures to create equality must entail a net transfer of resources from the richest

[14] R. Makwana, *Global Inequality,* http://www.stwr.org/poverty-inequality/global-inequality.html, accessed 19.02.2011.

5% of the population to the majority world – the 40% of the world who currently live on less than $2 a day. Such a transfer requires international cooperation and the redirection of economic and political policy away from the existing competitive, growth driven regime, to a more cooperative, equitable framework. Given the absolute involvement of corporate interests in maintaining existing conditions of global inequality, new regulations capping the power and influence of corporations, and preventing their ability to exacerbate local, national or global inequality, without curbing their ability for innovation must be sought by the global public. Concerted public effort along these lines is crucial if the international political economy is to be rendered democratic and guided by the global public for their own benefit.

The hypothetical sharing of essential global resources to secure basic human needs would entail the removal of corporate control over them, allowing them to be cooperatively owned and managed by the global public, under the guidance of the United Nations. One of the primary results of sharing resources and regulating markets would be drastic reduction in the disparities in wealth and income, access to food, water, energy, healthcare, education, technology and political participation. Marginalisation would be dramatically reduced and the underlying framework of international cooperation necessary to implement a redistributive economic system would inherently foster peaceful relations among nations. Such is the vision proposed by alterglobalists, who seek for solutions at the expense of international corporations and other subjects of economy on the highest level.

THE EVIL CAPITALISM

The cultural ties that bind the super-rich to everyone else are also beginning to weaken. Since World War II, the United States in particular has had an ethos of aspirational capitalism. As George Soros once told, "it is easier to be rich in America than in Europe, because Europeans envy the billionaire, but Americans hope to emulate him." But as the wealth gap has grown wider, and the rich have appeared to benefit disproportionately from government bailouts, that admiration has weakened. There is more and more criticismof the super-elite, expressed even by its representatives. At a *Wall Street Journal* conference in December 2009, Paul Volcker, the legendary former head of the Federal Reserve, argued that Wall Street's claims of wealth creation were without any real basis. "I wish someone," he said, "would give me one shred of neutral evidence that financial innovation has led to economic growth-one shred of evidence." At Google's May Zeitgeist gathering, Desmond Tutu, the opening speaker, took direct aim at executive compensation. "I do have a very real concern about capitalism," he lectured the gathered executives. "The Goldman Sachs thing. I read that one of the directors general-whatever they are called, CEO-took away one year as his salary $64 million. *Sixty-four million dollars.*" He sputtered to a stop, momentarily stunned by this sum (though, by the standards of Wall Street and Silicon Valley compensation, it's not actually that much money). In an op-ed in *The Wall Street Journal* last year, even the economist Klaus Schwab-founder of the World Economic Forum and its iconic Davos meeting-warned that "the entrepreneurial system is being perverted," and businesses that "fall back into old habits and excesses" could "undermine social peace."[15]

THE REASONS FOR A CHANGE

All the arguments cited above concern rather moral questions and a matter of social justice or injustice. Nevertheless, the co-existence of extremely poor and rich states causes a severe problem of financing the former by the latter. In September 2000, the 189 countries of the United Nations unanimously agreed to "spare no effort to free our fellow men, women and children from the abject and dehumanizing conditions of extreme poverty," specifically hunger and the "major diseases that afflict humanity."

It would be expensive to accomplish this great objective, and the price was later estimated at about $195 billion a year. It would be very difficult for this amount of money to be raised by private charities or individuals. It would require the combined efforts of governments throughout the world to do it. In the March 2002 Monterrey Conference, 22 of the world's wealthiest countries agreed to make "concrete efforts" towards the goal of each giving 0.7 per cent of their national income as aid to the poorest countries. This conference was attended by British Prime Minister Tony Blair, U.S. President George Bush, French President Jacques Chirac, and many other world leaders. In the September 2002 Johannesburg Summit, these same 22 counties re-affirmed their commitment to reach the 0.7% goal. This would provide enough money to raise the amount of $195 billion per year.

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[15] C. Freeland, *The Rise of The New Global Elite*, "The Atlantic," January/February 2011, http://www.theatlantic.com/magazine/print/2011/01/the-rise-of-the-new-global-elite/8343/, accessed 19.02.2011.

The countries made this agreement because they realised that it was hard for each of them to give a consistent, minimum level of aid each year on their own. Despite good intentions, a country would find that the aid it wanted to give was eaten away by competing political interests, concern about budget deficits, "problems at home," "problems abroad," etc. So they agreed to a minimal, flat rate that each country could afford each year regardless of its current political or economic state.[16]

The increase awareness of the problems of developing countries is not a sole reason for taking steps against global inequalities. To fight them effectively, it is essential to maintain economic stability in richer states. Maintaining economic stability is partly a matter of avoiding economic and financial crisis. Economic stability also means avoiding large swings in economic activity, high inflation, and excessive volatility in exchange rates and financial markets. Such instability can increase uncertainty and discourage investment, impede economic growth, and hurt living standards. The dynamic market economy must involve some degree of instability, as well as gradual structural change. The challenge for policymakers is to minimize this instability without reducing the ability of the economic system to raise living standards through the increasing productivity, efficiency, and employment that it generates.[17]

Economic and financial stability is both a national and a multilateral concern. As recent experience in the world financial markets has shown, countries are becoming ever more interconnected. Problems in one apparently isolated sector, within any one country, can result in problems in other sectors and spread across borders. Global economic and financial conditions have a significant impact on the developments in most national economies. Taking into consideration the fact that the most developed national economies allocate part of their funds in less developed systems, it becomes essential to guarantee a certain level of stability for the richer ones – if, as a result of instability, more developed economies cease their help towards poorer states, the risk of the global economic crisis, deeper than the one we experience nowadays, becomes real.

[16] 2009 International Aid, http://www.poverty.com/internationalaid.html, accessed 19.02.2011.

[17] *How the IMF Promotes Global Economic Stability*, http://www.imf.org/external/np/exr/facts/globstab.htm, accessed 19.02.2011.

DO GLOBAL INEQUALITIES REALLY MATTER?

As one may expect, there are two views concerning this question. A certain group of people claims that the notion of "global inequalities" is irrelevant, as there is no global government or global civil society. According to this opinion, what really matters, are the national inequalities, because they are the content of public discourse and they organise the interest groups. Another reason for the irrelevance of global inequalities is the fact that only changes in absolute income matter to the poor and the rich alike.[18] In the words of Anne Krueger, "poor people are desperate to improve their material conditions rather than to march up the income distribution ladder." Thus, even if the absolute income gap between an average American and an average African increases, these authors are unconcerned. After all, they argue, the average African would be a bit less poor. This, of course, assumes that our income relative to the incomes of others does not matter. Yet, this conclusion is at odds with psychological studies that invariably show that people do not care only about their absolute income, but also about where they stand in the social pyramid, and also whether they think this position to be fair.[19]

Or – quite opposite – global inequality may matter. On this side of the issue, there are also different approaches. For Thomas Pogge and Sanjay Reddy, as well as Peter Singer, global poverty and global inequality are ethical issues. Hence, the rich world cannot disown all interest in global poverty and inequality: to some extent, the fate of every individual in the world affects us. Distributional justice within a nation, and in the world as a whole, is – from the ethical perspective – the same thing.[20]

There are also more pragmatic reasons why global inequality may matter. Kuznets produced the following statement half a century ago: "Since it is only

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[18] A.O. Krueger, *Supporting globalization*, remarks at the Eisenhower National Security Conference on 'National Security for the 21st Century: Anticipating Challenges, Seizing Opportunities, Building Capabilities', 26 September 2002, http://www.imf.org/external/np/speeches/2002/092602a.htm, accessed 19.02.2011; M. Feldstein, *Reducing poverty not inequality*, "Public Interest" Fall 1999, pp. 33–43.

[19] C. Graham, A. Felton, *Does inequality matter to individual welfare? An exploration based on household surveys in Latin America*, Center on Economic and Social Dynamics Working Paper No. 38, Washington 2005; R.H. Frank, *Positional externalities cause large and preventable welfare losses*, "American Economic Review" 2005, no. 95 (2), pp. 137–151.

[20] T.W. Pogge, S. Reddy, *Unknown: The extent, distribution, and trend of global income poverty*, http://www.columbia.edu/~sr793/povpop.pdf, accessed 19.02.2011; P. Singer, *One World: The Ethics of Globalization*, New Haven 2002.

through contact that recognition and tension are created, one could argue that the reduction of physical misery associated with low income and consumption levels permit an increase rather than a diminution of political tensions because the political misery of the poor, the tension created by the observation of the much greater wealth of other communities may have only increased."[21] When people observe each other and interact, it is no longer simply a national yardstick that they have in mind when they compare their income with the income of others, but an international or global one. What globalization does is to increase awareness of other people's income, and therefore, the perception (knowledge) of inequalities among both the poor and the rich. If it does so among the poor, then their aspirations change: they may no longer be satisfied with small increases in their own real income, if they know that other people are gaining much more. Therefore, the process of globalization by itself changes the perception of one's position, and even if globalization may raise everybody's real income, it could exacerbate, rather than moderate, feelings of despondency and deprivation among the poor.

Globalization, in that sense, is no different from the process which led to the creation of modern nation states out of isolated, and often mutually estranged, hamlets. National income distribution was similarly an abstraction for the people who did not interact with each other, and almost ignored each other's existence and way of life. However, once nation-states came into existence, national inequality became an issue – simply because people were able to compare their own standards of living and to make judgments as to whether these income differences were deserved or not. If one believes that the process of globalization would slowly lead to the formation of a global polity, then global inequality will indeed become a relevant issue. For it is difficult to envisage that a fully free exchange of goods, technology and information, transfer of capital, and some freedom in the movement of people can go on for a long time without creating a global polity of sorts and requiring decision-making processes at the global level.

If so, then we need to develop some rules for global redistribution. The first rule is that funds should flow from richer to poorer countries. This requirement is easily satisfied. Even today, bilateral aid is given by rich to poor countries (not the other way round). But in a globalized world, this is not enough. Redistribution needs to be globally progressive – that is, to satisfy the same criteria that we require from it within a nation-state. This means that the tax-payer ought to be richer than the beneficiary of the transfer. But both rules may be satisfied while the beneficiary

[21] S. Kuznets, *Economic Growth and Structure: Selected Essays*, New Delhi 2002, pp. 173–174.

is a relatively rich individual in a poor country and the tax payer is a relatively poor individual in a rich country. And it is precisely the perception that many transfers end up in the pockets of the rich elite in poor countries which is fuelling the current discontent with multilateral and bilateral aid. Thus, the third requirement ought to be that transfers be such that inequality decreases in both donor and recipient countries. Only in such conditions can the global society stay viable over the long term.[22]

[22] B. Milanovic, *Global Income Inequality: What It Is And Why It Matters?…*