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Income inequality as part of new economic and social conditions of business

Key words: *income inequality, causes, consequences, economic and social business conditions*

Income inequality as a today's phenomenon

The allocation of revenues / income (*Retirement income* is a flow variable expressing the amount of money that an individual or household receives for a certain period of time in the process of initial distribution and redistribution. The term *income* will be used in this paper as a synonym for retirement income due to the fact that this term is used in the statistical documents and other official documents of economic practice. The literature sometimes distinguishes between these terms, where incomes are designated funds flowing from the initial distribution of value-creating processes and as retirement incomes *are referred* resources arising in the process of redistribution. *Distribution* of retirement income is viewed as the initial distribution to the original owners of production factors. *Redistribution* (secondary distribution) is a re-distribution of funds collected from the initial distribution, for example in the state budget) is one of the key factors in the functioning of every socio - economic system from the point of impact on the whole economy (both macroeconomic level and in

terms of microeconomic), but also on the social process. Economic theory analyses income distribution and income inequality especially in the context of economic growth, development and its sustainability, as well as in terms of the impact on quality of people's life [Pauhofová, Hudec, Želinský, 2010].

Inequality is historically part of the existence of any society. Polarization of society in terms of income is a specific type of vertical (Horizontal inequality is between the regions, countries), inequality (between groups and individuals) [Veselková, 2012, s. 127].

The issue of distribution of income and wealth (income inequalities are part of a methodology of comprehensive perspective on income polarization and polarization of wealth in a globalized world), was at first elaborated mainly by sociologists. In the economic literature a greater awareness of the problem begins in the 90th of the 20th century [Želinský, Pauhofová. 2012]. In the opinion of *liberal economists* are income inequalities (income inequality is often equated with the concepts of poverty, injustice of retirement incomes. These are not synonyms. Category of income inequality is purely descriptive in nature, it is the category of positive economics (may differ significantly from the inequality of status, social). Income inequality means that incomes (pensions) of the people are not the same, so they are not equalized) a necessary evil and the price for economic growth. According to them, inequality promotes economic growth via concentration of income at the rich people (rich have a higher marginal propensity for savings than the poor) who are able to save and invest more, and on the other hand, inequality "fear of poverty" motivates individuals to work harder [Kotrasová, Rochovská, 2010]. The opposite view presents a *group of economists around Stiglitz* that the inequality holds for a high price in terms of social, economic and political instability and lower growth. [Fitoussi, Stiglitz 2010. in: Veber, 2010: 11]. According to the Iša [2001] a high degree of economic inequality is not automatically a guarantee of higher growth rates, neither of steady growth, which implies an optimal relationship between investment and consumption. Prob-

lem, even risk of considerable property and income inequality lies in the fact that this mortifies capital and it is not getting into the economic cycle.

Paradoxicality of the current approach by exploring the phenomenon of income inequality lies mainly in the fact that it misses an interest to understand it as the cause of many problems, especially negative issues of the current world, whose solution in the form of equalization of income inequality on the basis of merit and non-discrimination, could be a tool to eliminate them (for several decades significant organizations such as World Bank and IMF are directing their efforts and finances to reduce income inequalities and to achieve various forms of convergence, but the results show the opposite, income inequality is increasing). It is also paradoxical that many times the income inequality is presented as a static and necessarily acceptable phenomenon of the current socio-economic system.

Planar growth of income inequality is a serious negative effect, especially on the aspect of vulnerability to social shocks (It is therefore appropriate a question: Is there a "maneuver" around income inequality substitutionary problem? There is a fundamental question of today: What will be the need for human labor in society in the future? [Želinský, Pauhofová. EÚ SAV, 2012: 117-118].

Milanovic [2006: 13] notes that global inequality has acquired enormous proportions and has a growing trend. Thereby it increases the possibility of growth of its negative consequences and therefore the importance of examining and understanding of this phenomenon.

Decomposition of income inequality, its determinants and consequences.

Income inequality, its determinants and consequences are an important indicator and source of information for the development of the society in the future. It is a multilevel and multifactorial phenomenon and therefore its investigation is carried out not only in economic but also in social, ethical, political, legislative and other spheres of society.

Income inequalities (the concept of income inequality is sometimes wrongly equated with the concept of poverty, but they are two different

concepts. In terms of quantification of poverty and inequality based on analysis of income, inequality of income can be seen as a broader concept than the concept of poverty. Construction of rates of income poverty is in fact based on analysis of income only of that part of the population whose incomes fall below the level (the poverty line), while the construction of rates of income inequality is generally based on the analysis of the income of all members of society. Available at: <http://portal.statistics.sk/showdoc.do?docid=28598#obsah>) *reflect the processes that led to them*. They indicate a much more complex phenomena and connections of the current polarization, which are not related only with income [Pauhoufová, 2010]. Šikula a kol. [2010] indicate at present an unacceptable and unsustainable disproportion between growing wealth creation and *deepening inequality of its distribution* as a major contradiction between the economy and the man, what became based on authors critical dimensions not only in the session of economically developed and developing countries, but also within many economically developed countries

Among the most empirically validated *sources of inequality* in market incomes is disparity in wages, household composition, labour market status and disparity in investment and capital incomes [Kenworthy, 2008]. If talking about inequality in available incomes, they are mainly the result of *redistribution mechanisms* (set of socio-political mechanisms and tax system). *The structural shifts* in the economy, trade and population are therefore not the only holders of disparity [Veselková, 2012: 127].

Many experts consider the increasing income inequality *as a major factor in the current crisis*. Fitoussi's and Stiglitz's analysis of the global crisis and its deeper causalities has shown that it is an unprecedented phenomenon, which was created by the synergy effects of *extreme polarization of income and wealth, reduction of space for the recovery of surplus capital unable to generate sufficient effective demand in the real economy, due to unsustainable exploitation of natural resources and environmental devastation, more deformed structure of production and consumption, unprecedented expansion of the financial sector and its increasingly destructive impacts*

on the real economy [Keynes, 1973], what has an *disintegration effect on morale and value orientations in human behaviour and in the functioning of the society*. *Lack of demand and valorisation space in the real economy* is increasingly being replaced by *virtual demand generated by expanding financial sector* based on cumulated indebtedness [Šikula a kol. 2010. *Stratégia rozvoja slovenskej spoločnosti*. Bratislava: EÚ SAV. s. III. <http://archiv.vlada.gov.sk/old.uv/data/files/5613.pdf>] [In: Veber, 2010: 119].

Even Pauhoufová [2012] as a major factor in the on-going crisis indicates the increasing income polarization (polarization of wealth), which is a *product of current civilization and economic model*. According to her, income polarization arises as a combination of various factors, where the main ones are:

1. *method and form of distribution and redistribution in the society.*

Redistribution has a significant effect on the polarization of incomes, on the so-called "delayed reward", where wages and bonuses of top management of various companies are very different from ordinary wage of workers.

The average German made his fortune seven times higher in the second half of the 20th century. This seven times enrichment was created so that the GDP for this period was divided by the number of Germans. 9% of Germans are active in employment and those got rich 2-3 times on average. The richest income groups and big companies got richer twenty times in this period. The average of twelve times enrichment of the rich and two-to three times enrichment of 90 percent of Germans gives the number 7. In Germany, employees paid in 1950 a quarter of all taxes, in 2000 already four-fifths of taxes. It means that by stagnant incomes of employees (roughly stagnates since the early eighties), they subsidize these four fifths of the tax burden, while the proportion of those whose incomes expanded, has dropped on the payment of taxes from three-quarters to one-fifth. <http://strana-lavica.sk/keller.php>

Rising income inequality of the population is then reflected in the problems of poverty, high unemployment, low national or global consumption linked with low domestic demand, but at the same time with the risks of social tensions formation.

2. *uneven and progressing level of concentration of capital and assets in the hands of individual sections of society.*

Nemoga [2010] notes that for the polarization of wealth has always contributed also *development of information technologies* (IT), because access to information is one of the basic prerequisites of success in many areas of society and the economy.

Highly polarized inequality by Kenworthy [2008] raises *social exclusion* associated with many negative consequences (leading to a weakening of social cohesion, the rise in unemployment, a rise in the number of persons in material need, the loss of social prestige, the reduction of birth rates, the growth of excessive indebtedness of states and households, the increase in the deficit of public finance, the increase in income inequality of successive generations, the growth of virtual wealth into negative stratification of society, the worries about the future, or even to weakening of economic growth and its long-term sustainability [Veselková, 2012: 127].

The main cause of the debt crisis in the EU is considered to be *excessively costly social model*. Analytical results of many authors document deepening of income inequalities in the EU. This means that the realized social model does not suppress income polarization. The tip on scales is increasingly huge dimension of *corruption*, which increases spending on social model by 20-30 [Želinský, Pauhoufová, 2012: 117].

Šikula [2010, s. 30 - 33] analyses the causes and consequences of extreme growing inequalities of income and wealth distribution. According to him *real basic cause* lies in the *nature of capital accumulation*, which does not provide enough opportunities for recovery and is accompanied by accumulation of debts which have become a powerful leverage to promote growth.

Sustaining of the growth is thus increasingly dependent on the indebtedness (about the tendency of expansion of the financial sector and growing indebtedness related to GDP as a medicine against the tendency to stagnation of the economy has pointed political-economic analysis since the 60th years of the 20 century (e.g. the U.S. GDP in the period 1970-2007 increased 13.8 times but the total debt was increased about 32 times. Cumulative increase in the debt burden in relation to GDP, has risen from 151% in 1959 to 373% in 2007. The structure of debt was also changed: in 1970 the largest borrowers were businesses and households, but in 2007 it was the financial institutions). This nature of increasingly unacceptable indebtedness as a major factor of fictitious growth can not continue indefinitely [Šikula, M. 2010a]) and became to have huge dimensions, which was allowed by the combination of deregulation, liberalization, IKT technologies and innovative diversification of financial products. Disproportionate polarization leads to a significant restriction of consumer demand for low-income populations. This causes the accumulation of excess production capacities (in the most industries is the volume of production capacity higher by 20 to 40 percent, than the actual need. This applies to the pharmaceutical, automotive, electronics and other industries. If we are to make real production and production capacities, we should lay off excess. Prognosis of the International Labour Organization says about the end of 35 to 60 millions jobs in developed countries. So far, however, it is on hold. We all hope that when Americans will consume less, it will be replaced with China. This, however, will replace about 20 percent of global consumption of the United States. Stanek, P.: Just pour money is not enough. Available at: <http://www.pluska.sk/slovensko/rozhovory/ekonomicky-analytik-peter-stanek-naliat-peniaze-nestaci.html>) and this way the capacity creation investments began to move into the financial sector, creating the impression of more lucrative opportunities (out of 100 dollars, which during the second change the ownership, is 98 dollars not covered by production activity).

Especially big economies (for large economies, such as Germany, France, the United Kingdom is realistic to expect that into the survey did not get sample units for income of the most disposed groups, which could significantly distort input data), record a significant *growth of internal regional disparities* that cause the transition of employees for job-sharing, or to so called "Kurzarbeit". In countries characterized by a rise in income inequality, it is possible to register a significant increase in unemployment. High risk in terms of future is differentiation within the European Union.

Inequalities in various areas of economic and social life in crisis deepen, in many regions of the Union is the society clearly polarized and poverty acquires undesirable forms. These are not only associated with an increase in unemployment, but also with slowing of wage development. Those are significantly more prevalent among new EU member states. Within the stratification of the population's income is significantly strengthening the position of low-income households and also of very small group of wealthy. Available at: http://www3.ekf.tuke.sk/NaRE2012/subory/workshop/Herlany_Zbornik_web.pdf

It is not just about high levels of income inequality of new member states but also old ones [Želinský, Pauhofová, 2012: 117-118].

For a clearer grip of the issue of income inequality is now important to touch the issues related to the solution of the debt crisis in Europe. As the political elite do not want to deal with this, logical outcome is not the solution of the debt crisis, but *shifting costs of the state to citizens*. If they do not have a sufficient amount of incomes, the outcome will be *deepening of social polarization*. The risk of income inequalities increases if there is an increase in the whole area.

The status of middle class has currently and in the future will have a key role in terms of social and political stability of the society. Middle class are nowadays in a difficult position. The perssure is growing to moderate their wage demands. It also often serve as the latest sponsor of the welfare state. If a scenario of forced changes applies, then society as a whole will get poorer. Middle classes, which are the fruit of a functioning society, in this

scenario decline in incomes and socially and they are mixed with other regraded layers.

Since the mid-90th of the 20th century the European area is in *permanent income freezing of the majority of the population*, while there is an *extreme increase in corruption*. Income freeze is closely involved with an *outsourcing*. If one adds to this the rapid growth in the number of *companies evasion of payment obligations* (social, tax), so there is a mix, resulting in a current style of *debt crisis*. *From the side of political elites for the last 10 years there is a conscious influence in the direction of inequalities deepening* (the fall in the average wealth (median) for the last three years by nearly 40% marked the decline of American wealth that was accumulated in last 20 years (FED, 2012)) [Želinský, Pauhoufová, 2012].

The ultimate consequence of the existence of income inequality is the *destruction of the quality of life of the individual*. That means some increase in aggression in society, which increases its susceptibility to social shocks. It significantly extends the control system of society, when the possibility for feedback is dismissing. The risk of income inequality increases if there is an increase within the whole area. [Želinský, Pauhoufová, 2012].

Question of the global distribution of wealth is becoming more urgent than the question of optimal production and consumption in the richest. [Quiggin, 2012].

Conclusions

Although it is very difficult to separate the causes and consequences of income inequality (as they intersect with each other, influence and support), as well as to clearly define (*ceteris paribus*), I assume, based on the analysis of presented opinions, for the *main cause of income inequality* the **current civilization and economic model**, which translates into determinants / factors / processes:

A. **economic** in three areas:

1. *distribution* (the ratio of labour and capital, the ratio of wages and salaries of managers, respectively owners; permanent income freezing of

most of the population; disparity in capital and labour income) and *redistribution* (the tax and contribution system, government and public expenditure).

2. *nature of capital accumulation* (uneven, acting, economically unjustified concentration of capital and assets in the hands of individual sections of society; accumulation of assets, which enables and makes further accumulation, economic globalization; TNK),

3. *structural movements in the economy* (more deformed structure of production and consumption; deepening economic differentiation of human resources, an unprecedented expansion of the financial sector; innovative diversification of financial products; deepening conflict between the real and the financial economy, the development of IKT)

B. non-economic (socio-political mechanisms; social model; political system; integration processes, corruption, unethicity, passivity and acceptance of social injustice; legislative support of income polarization, non-functioning legal system; etc.).

As the main *consequences of income polarization* may be given:

A. economic: non-use of economic resources: labour, land, capital, growth in the number of people in poverty, insufficient effective demand in the real economy, narrowing the space for the recovery of surplus capital; virtual demand growth, unsustainable way of exploitation of natural resources and environmental devastation; growth of excessive indebtedness of states and households, increasing income inequality of successive generations; growth of virtual wealth, excessive production capacities, non-payment of tax and social obligations, passing on the costs to the citizens from the state (health, education,...), weakening of economic growth and its long-term sustainability, etc.

B. non-economic: unemployment, weakening of social cohesion, loss of social prestige; impossibility of self-fulfilment; reduction of birth rates, aging of population, negative stratification of society; worries about the future; devastation of morality and value orientation in people's behaviour and in the functioning of society, social exclusion, social discrimination,

destruction of quality of life, social tensions, increase of aggression in the society, susceptibility to social shocks, etc.).

Generalized *causes and consequences of income inequality* present many negative (and growing) problems of the contemporary world, whose solution in the form of equalization of income inequality on the basis of merit and non-discrimination could be a tool to eliminate them. But also represents new economic and social conditions for business.

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Summary

The allocation of revenues / incomes is a key factor in the functioning of every socio economic system. Problem, even considerable risk of significant property and the income inequality lies in the fact that this would mortify capital and does not get into the economic cycle. Dangerous is that income inequality is understood (forces to be accepted) as a static and necessarily acceptable phenomenon of the current socio-economic system. The deepening income inequality is the cause of many negative issues of the contemporary world.

World inequality (growing disparity in capital and labour income) obtains enormous proportions and has a growing trend, thereby it increases the volume and strength of its negative consequences, such as: economically unjustified concentration of capital and assets in the hands of individual layers of society, economically unjustifiable and unsustainable disparity between wealth growth and deepening inequality of its distribution, disregard for the principles of merit and non-discrimination within the manner and form of distribution and redistribution in society, narrowing the space for the recovery of capital surplus, increasingly deformed structure of production and consumption, unprecedented expansion of the financial sector; virtual demand generated by the expanding financial sector , excessive production

capacities, increase of regional disparities, increasing economic and political power of TNK, increase of deficit of public finance; shifting of state costs to the citizens (health, education, social care, etc.), permanent income freezing of the majority of the population, growth in the number of people in poverty, escape of firms from paying social and fiscal payables, insufficient effective demand at real economy, corruption, excessive growth of government and household indebtedness, unemployment, inadequate position of people at the labour market, devastation of the environment, the decline of moral and value orientation in people's behaviour and in the functioning of society, decline of the birth rate, aging of population, social, economic and political instability, susceptibility of the society to social and economic shocks, etc. These facts also represent new economic and social conditions for business.

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