Society for the Study
of Economic Inequality

Working Paper Series

The Return of Inequality

Philip Nel

ECINEQ WP 2006 – 44

ECINEQ 2006-44
June 2006

www.ecineq.org

The Return of Inequality*

Philip Nel†
Department of Political Studies, University of Otago

Review Article

Inequality, Growth, and Poverty in an Era of Liberalization and Globalization
G A Cornia (ed), Oxford: Oxford University Press, 2004

Inequality in Latin America and the Carribbean: Breaking with History?
D de Ferranti, G Perry, F Ferreira, & M Walton, Washington, DC: World Bank Latin American and Caribbean Studies, The World Bank, 2004

Worlds Apart: Measuring International and Global Inequality
B Milanovic, Princeton: Princeton University Press, 2005

Equity and Development: World Development Report 2006
World Bank, New York: The World Bank and Oxford University Press, 2005

University of Texas Inequality Project (UTIP),
Under the leadership of Prof James K Galbraith, http://utip.gov.utexas.edu/

* To be published in *Third World Quarterly*, Vol. 27, No. 4, pp 689 – 706, 2006
† **Contact details:** philip.nel@stonebow.otago.ac.nz. Department of Political Studies, University of Otago, Dunedin 9000, New Zealand

Third World Quarterly, Vol. 27, No. 4, pp 689–706, 2006

Routledge
Taylor & Francis Group

BOOKS

Review Article

The Return of Inequality

PHILIP NEL

Inequality, Growth, and Poverty in an Era of Liberalization and Globalization
G A Cornia (ed)
Oxford: Oxford University Press, 2004

Inequality in Latin America and the Carribbean: Breaking with History?
D de Ferranti, G Perry, F Ferreira, & M Walton
Washington, DC: World Bank Latin American and Caribbean Studies, The World Bank, 2004

Worlds Apart: Measuring International and Global Inequality
B Milanovic
Princeton: Princeton University Press, 2005

Equity and Development: World Development Report 2006
World Bank
New York: The World Bank and Oxford University Press, 2005

University of Texas Inequality Project (UTIP)
Under the leadership of Prof James K Galbraith
http://utip.gov.utexas.edu/

While the study of economic inequality is still much of a Cinderella field in Economics, and takes up only a minuscule part of the attention of sociologists and political scientists, there are signs that this neglect is changing significantly, and rapidly so. Over the past decade there has been a sharp increase in the intensity with which academics and practitioners are engaging with the skewed distribution of income, wealth and economic opportunity in general. New theoretical approaches spearheaded by Amartya Sen and others since the early 1990s, the emergence of more comprehensive sets of data on income distribution in particular, and growing public and specialised concerns about the distributional effect of processes of globalisation, have

Philip Nel is in the Department of Political Studies, University of Otago, Dunedin 9001, New Zealand. Email: philip.nel@stonebow.otago.ac.nz.

ISSN 0143-6597 print/ISSN 1360-2241 online/06/040689–18 © 2006 Third World Quarterly
DOI: 10.1080/01436590600720934

combined to put economic inequality squarely back in the academic and public focus.[1] In the new century inequality studies have become something of an academic growth industry: since the turn of the century there have been major world conferences on the theme, the creation of a specialised journal and a specialised academic association,[2] many papers and journal articles, and a number of major single- and multi-author books, reports and edited collections. In 2004 and 2005 alone four major studies on the subject saw the light of day. These, plus an important web-based source of information on economic inequality form the focus of this review article.

But why is economic inequality a problem? After all, is the rank ordering of people in terms of wealth and status not inescapable in all societies in which there are norms of behaviour to which sanctions are attached, as Ralph Dahrendorf argued in the 1960s?[3] Contrary to the assumption that inequality is an aberration from a presumed original position in which a 'natural' equality exists among all people, Dahrendorf argues that inequality is coterminous with the emergence of a norm-governed, law-based society which discriminates between people to the extent that they conform or do not conform with the reigning normative expectations. Norms, and their codification in positive law, place requirements on people's behaviour, and a rank order of social status and the accompanying differentiation of wealth is bound to emerge. In Dahrendorf's felicitous prose: while people may be *equal* before the law, it belongs to the very logic of society formation that people end up being unequal *after* the law, that is, when their performance in terms of the norms/laws receives positive or negative sanctions. Inequality of status and wealth is thus a 'natural' state of human society, and acts as an important source of incentive for people towards betterment.

In addition, the mere eventuality of inequality of income or wealth cannot in itself be the cause of moral concern. If a billionaire would move into the middle-class street where I live in Dunedin, New Zealand, economic inequality in that street would worsen dramatically, but no one would be disadvantaged nor any other moral sentiment breached. In fact, all property owners in the street would be advantaged as the relative values of their property would increase. Does this not imply that we should not waste our moral and analytical energies on inequality, but rather direct them at 'real' moral challenges, such as the prevalence of absolute deprivation, poverty, which results in millions of people not having their basic needs met? Furthermore, if it turns out that free market entrepreneurship is an effective way of reducing the incidence of poverty, risking the concomitant higher inequality meets the requirements of both economic functionality and of Rawls' influential ethical principles. This implies that inequality is justified only if there is procedural justice in place and if unequal outcomes maximise the utility of the worse-off.

Of course, as the books under review show, hardly any real existing economic inequality can live up to these ethical requirements. In most highly unequal countries economic inequality goes hand in hand with disproportionate access to public power and positions of influence, and procedural rules are often skewed in favour of the economically privileged. In these societies, social inequality does not act as an incentive for individuals to try and improve their social standing, but is often a 'trap' from which generation after generation of the same people cannot escape, disrupting their potential for human development and the economic growth prospects of the society to which they belong. The message that emerges from the books under review is that extreme levels of inequality are indeed problematical: extreme inequality implies that a section of the population is persistently, across generations, denied the opportunities for economic betterment enjoyed by others in that society, despite the existence of sufficient resources on a global scale to provide the basic needs of all. Broadly speaking, economic inequality refers to any state of affairs in which there is a contrast in the economic opportunities that persons or groups of persons face. As Debraj Ray puts it: 'Ultimately, economic inequality is the fundamental disparity that permits one individual certain material choices, while denying another individual those very same choices'.[4] These concerns do not imply that economic *equality* is necessarily preferable or morally more defensible as an alternative to inequality, but they do suggest that a fair distribution of economic resources and opportunities, that is, *economic equity*, is a worthwhile goal to pursue. While Dahrendorf is correct in seeing hierarchy and inequality as inescapable features of society, there clearly are limits to what would be regarded as morally justifiable inequalities. The inequality caused by the relocation of a millionaire to a specific street, as in the example above, becomes a moral concern if there are structural barriers to other inhabitants in the street becoming millionaires as well. Such barriers seem to be common in many low- and middle-income countries, and have recently emerged in many OECD member states as well.

The conclusion that inequality can be iniquitous has become well established among moral philosophers, and the books under review do not add much that is novel on this score. Their distinct contribution and novelty value lies rather in the way in which they show that equity is not only an abstract moral concern, but that its pursuit makes considerable difference to the economic performance and overall human development of societies. While not diminishing the importance of poverty and poverty relief, the hard-nosed economic analyses that underlie most of the work reflected in these books indicate that analysts and policy makers need to take an urgent and hard look at the problems posed by inequality and at ways of dealing with these problems and their root causes. Commentators who have lamented the disappearance of the concept of redistribution from most of the policy debates of the past 20 years will take heart from the fact that an auspicious international financial institution such as the World Bank has, through its flagship development publication, put the theme squarely back into the public debate. Whether this was indeed the intention of George W Bush when he dispatched Paul Wolfowitz to the World Bank in early 2005 is unlikely, but the gestation period of the annual *World Development Report* is quite long, and the ideas behind *Equity and Development* have been percolating up for some time now in World Bank circles. One of the early victims of this percolating process was none other than Branko Milanovic, one of the authors under review here. The fact that he has now been reinstated as a staff member of the World Bank is in itself an indication of the 'return of inequality'.

What exactly is it about inequality within national units that makes it a challenge from the viewpoint of economic efficiency and human development? Three of the books under review, coupled with the data generated by the University of Texas Inequality Project (UTIP), help us to answer this question in the next few pages. A fourth—Milanovic's volume—enables us to place this debate into a necessary broader perspective of global inequality, which is where we start.

The constituents of global inequality

The debate about the relevance of inequality has been much informed, but also confounded, by the question of global inequality. When using this term, analysts usually have in mind the disproportionate distribution of wealth and income *between* the countries of the world, often expressed in terms of per capita national income. But, as we will soon see, it is a misnomer to restrict the meaning of global inequality to this between-country dimension. This misnaming is regrettable in view of the amount of energy spent recently on the stale debate about whether globalisation has reduced or increased global inequality. If only participants to this debate had read Milanovic before they embarked on their narrow pursuit of between-country inequality. As do most recent publications on the bases of data convenience, Milanovic also focuses on *income* inequality exclusively. There is general consensus that wealth all over the world is more unequally distributed than income, but that conclusions pertaining to income distribution would generally apply to wealth inequality as well.

Milanovic carefully distinguishes between three ways in which to think about and measure global or world income inequality. One is the narrow conception referred to above, which sees global inequality as being constituted by the disproportionality in mean national income across the countries of the world. This approach assumes that each country has only one representative citizen, earning the mean income, and then compares the incomes of these 200 plus country representatives. One can imagine a line of 200 individuals, arranged from small to tall, each representing one country, with their relative height being a reflection of their country's mean income. Milanovic suggests that it is more correct to refer to this as *un-weighted international* inequality, as we are comparing countries with one another and we do not take into consideration the size of the population of the relevant countries. Much of the recent difference of opinion about the effects of globalisation on inequality can be traced back to the question of whether it is appropriate to make un-weighted comparisons, thus treating China and Liechtenstein as one unit of comparison each, or whether we should weigh countries for population size.[5] In effect, the latter concept of weighted international inequality would imply that there will now be six billion individuals in our line, with all the citizens of one country having the same height (= mean income of their country).

Milanovic suggests that we distinguish both the concepts of un-weighted and weighted inequality, on the one hand, from a third concept, namely 'global inequality' proper, on the other hand. What we as analysts should be concerned about ideally when we want to make pronouncements on *global* inequality, he argues, is the relative position of each individual in the world line-up, where someone's position (height) is determined by his or her *real* income. In this line-up people from different countries may well be neighbours, as someone's relative position will depend not on her citizenship but on her particular real income alone. Although Milanovic does not use the term, it is obvious that this measure may also be called a cosmopolitan conception of global inequality, as it focuses on how well each individual in the world is doing compared to every other individual, independently of their country of residence or citizenship.

The bad news from such a cosmopolitan perspective is that we do not have information about the real income of each individual in the world, and that we therefore have to fall back on what we do have, namely country means and (often incomplete) data about within-country income distribution. We can then calculate what the likely income distribution among the individuals of the world is, using a generalised overall measure of inequality (such as the Gini coefficient or the Theil statistic[6]) and combining information on the distribution of income within countries with information gleaned from the population-weighted mean incomes of the countries for which we have data. By default, therefore, the notion of global income inequality becomes based on a combination of within-country (national) and between-country (international) income comparisons.

Most of Milanovic's book is spent on working out these conceptual distinctions and what it means when we apply them to measuring trends in global and weighted international inequality. In contrast to some other recent contributions,[7] Milanovic is careful not to take easy sides in the debate about whether globalisation has increased or reduced inequality, showing that much of the conclusion depends on whether one uses weighted or un-weighted country income means, and on how one deals with the problem of comparing the purchasing power of incomes in different countries. His favoured approach is to present the reader with a clear summary of the reasoning behind different measures, and with tables listing the data generated by different approaches, and then letting the reader make up his or her own mind about the trends and their implications. About one thing Milanovic is quite partisan, though, and rightly so: current levels of global inequality are unacceptably high and the fact that we are continuing to witness so much poverty in a world with abundant resources compels us to do something about it. He places his hope on between-country redistribution, arguing against the likes of Rawls that is it not only desirable, but also that it is increasingly becoming possible, if only (and he agrees that it is a dicey 'if') we could overcome the democratic deficit in the institutions of global governance.

Milanovic has produced a very useful and timely text, one that will provide intellectual stimulation and rigour to the debate about global inequality for some time to come. However, as a book that purports to be about global inequality, it has to be faulted for under-emphasising one of the two constituents of global inequality. The reader will recall the point made above that by necessity we calculate global income inequality using information about between-country (international) plus within-country (domestic) inequality. Because the hot globalisation debate has dealt exclusively with the former, and Milanovic's main goal is to contribute to this debate about trends in international inequality, he has little to say about within-country inequality. This is unfortunate, given the fact that it can be shown that the contribution which within-country inequality is making to our calculations of global inequality is growing, and that within-country inequality is having a whole series of negative consequences for economic and human development, specifically in low and middle-income countries, and needs therefore to be at the heart of any discussion of global justice. Milanovic is not alone in his neglect of the within-country dimension. In fact, most of the recent moral debates about global distributive justice have focused on the between-country (international) dimension alone, while pretending to deal with *global* inequality.[8] As proponents of moral cosmopolitanism, who set the tone of the debate, have sought to extend the traditional scope of considerations of distributive justice, the emphasis has shifted from the national to the international, and stayed there.[9] As a consequence, within-nation inequality and the determinants and consequences of it have largely been ignored or taken for granted. The other items under review here each in their own way show that this neglect must be reversed.

The within-country share of global inequality is growing

While there is much debate, as we noted, about what has been happening to between-country inequality over the past couple of decades, no one is disputing that within-country inequality has increased for most countries of the world during the most recent phase of globalisation. Using data on 73 countries that are available in the World Income Inequality Dataset (WIID) of the World Institute for Development Economics Research of the United Nations University (UNU/WIDER), Cornia and his co-authors find that domestic inequality has increased in 48 of them during the last three-to-four decades of the 20th century. This may be an understatement of the extent of the recent increase in within-country inequality, given the relatively small coverage of the WIID. Much broader coverage is achieved by the Estimated Household Income Inequality (EHII) dataset compiled by the University of Texas Inequality Project, under the leadership of James K Galbraith. This is the most comprehensive within-country inequality dataset available, covering 154 countries and containing more than 3000 observations over the period 1963 to 1999. What is especially attractive about this dataset is that it is based on a source that remains consistent over time, namely the UNIDO dataset on manufacturing pay or wage inequality. EHII is produced by combining information from the UNIDO dataset with information from another widely used dataset of household income inequality, the so-called Deininger and

Squire dataset based on World Bank household-survey resources,[10] as well as other relevant information such as the ratio of manufacturing employment to total population, the degree to which a country's population has become urbanised, and population growth. This information is then combined in a regression that produces a pooled time-series of estimated household income inequality for 154 countries.[11]

Using the EHII data, Figure 1 traces the average income levels over the eight semi-decades from 1960 to 1999 for three categories of states, namely developing low- and middle-income countries (developing LMICs), ex-socialist transition economies (including China), and high-income countries. Two trends clearly stand out. First, developing LMICs on average have faired much worse than the other two groups in terms of inequality levels. We will shortly return to the significance of this. Second, all three groups of states on average experienced significant increases in their inequality levels starting in the mid to late 1970s in the case of the developing LMICs, and in the 1980s in the case of the other two groups. Although there are specific explanations applicable to the inequality trends of each group, it should be obvious that there was a systemic tendency to higher levels of inequality over the last three decades of the 20th century, something that the Cornia book rightly draws our attention to and explores further in a number of case studies.

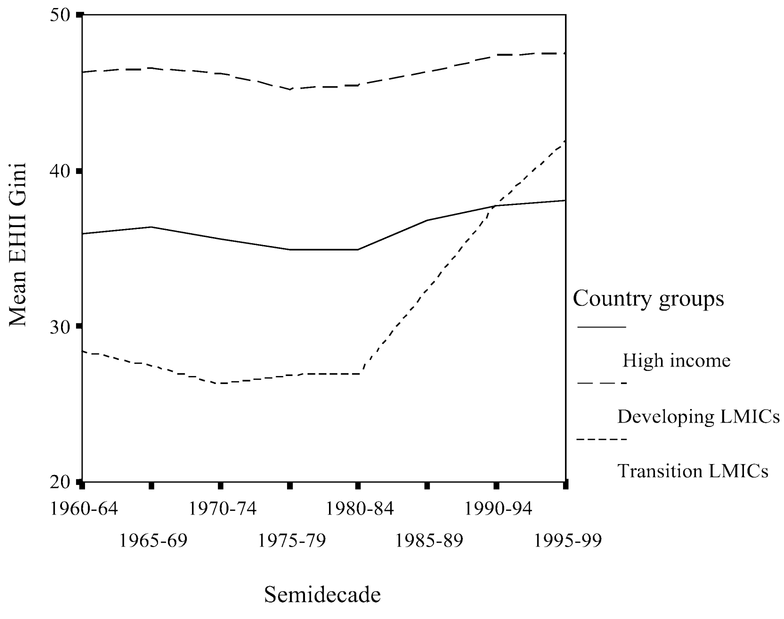

FIGURE 1. Inequality trends for three groups of countries, 1960–99.
Sources: Estimated Household Income Inequality Dataset, University of Texas Inequality Project, available at http://utip.gov.utexas.edu/. For a discussion of this dataset, see J Galbraith, & H Kum, 'Estimating the inequality of household income: a statistical approach to the creation of a dense and consistent data set', *Review of Income and Wealth*, 51 (1), 2005, pp 115–143.

The implication of the above is that the share of within-country inequality in the calculation of global inequality is increasing relative to the share of population-weighted between-country inequality. One way to determine how the ratio of within-country to between-country inequality as a determinant of global inequality is changing is to look at the long-term trends of these two dimensions calculated by Bourguignon and Morrisson in a significant article in the *American Economic Review*[12] and used in the 2006 World Bank's *World Development Report* (of which Bourguignon is the lead author).[13] As Figure 2 shows, Bourguignon and Morrisson manage to compare the within- and the population-weighted between-country constituents of global inequality from the beginning of the industrial era to 1992.

There have clearly been significant inequality transitions in the two centuries since 1820 as the ratio between the two dimensions has repeatedly changed. Most notable for our purposes are the recent significant changes in the dynamics of both the between-country and the within-country dimensions of global inequality. The big divergence between countries, which started in the 1800s as certain parts of the world rapidly industrialised while others did not, continues for most of the 20th century, but there is a distinct slowing down of the process in the 1980s and 1990s. This confirms that the latest phase of globalisation has facilitated the mean-income convergence of countries. Remember, however, that we are speaking here about the population-weighted mean incomes, so that rapid economic growth in populous countries (such as China and India) probably accounts for almost all of this convergence. Also, the mean-income divergence between countries remains at very high levels, higher than the within-country inequality level of any state in the world. Significantly, the period of the slowing down of between-country divergence during the second half of the 20th century coincides, first, with the process of decolonisation during the 1950s and 1960s

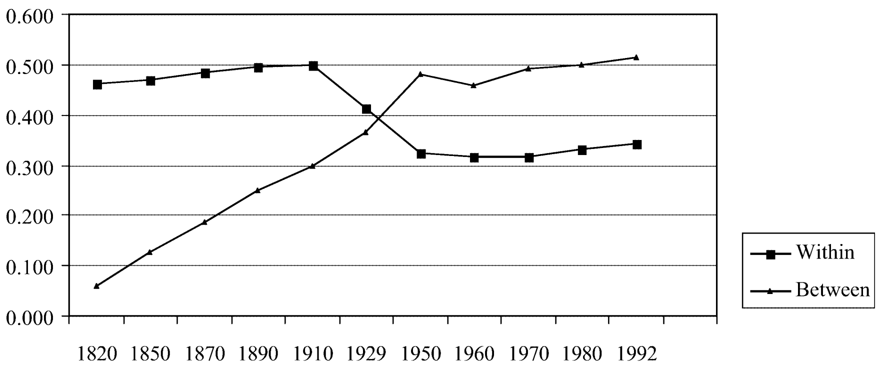

FIGURE 2. Within- and between-country inequality, 1820 – 1992.
Note: Theil statistic is used as inequality measure (Y axis).
Source: Based on data reported in F Bourguignon, & C Morrisson, 'Inequality among world citizens: 1820 – 1992', *American Economic Review*, 92 (4), 2002, pp 727 – 744.

and, second, with the gradual intensification of the process of economic globalisation which took off with the lifting of capital constraints starting in the early 1970s. While between-country inequality was growing at a slower rate, the significant advances made in promoting economically more equal societies during the heyday of the welfare state were gradually being eroded from the 1950s onwards, with a noticeable increase in the average levels of income inequality since the 1970s. The era of decolonisation and globalisation may have had many salutary effects, but keeping a lid on within-country inequality was clearly not one of them. The result of the slowing down of between-country divergence and the worsening of the within-country ratio has been that the ratio of within-country inequality to between-country inequality has grown from 0.64 to 1 in 1970, to 0.67 to 1 in 1992.

The bottom-line of all this is that the relative income of the typical individual is increasingly being determined not only by geography (the country in which she resides), but also by her relative position in the income hierarchy within her country of residence. While the between-country dimension is still more significant in determining her position in the global income line-up, the factor of within-country inequality is slowly but surely catching up on it in importance. This already provides reason enough for those of us who agree with Milanovic that global inequality is a topic 'whose time has come' to spend much more time than we have up to now on trying to understand the causes and consequences of within-country inequality. But that is not the only reason, as the next section will show.

The consequences of within-country inequality

The EHII data represented in Figure 1 above indicate that developing LMICs, on average, are much more unequal than either the low- and middle income transition economies or the high-income countries. On average over the whole period covered by the EHII data developing LMICs scored 10 points higher on the Gini index than high income countries, and in the case of low-income countries the gap was as high as 13 Gini index points. The gap between developing LMICs and the ex-socialist transition economies used to be around 20 Gini points, but thanks to the sharp increase in inequality in the latter group in the 1980s and 1990s, this gap had narrowed to only between six and seven points by 1999. Do these differences in inequality levels matter?

Indeed, they do and for a variety of reasons, some of which are explored in the volume edited by Cornia, in the two World Bank volumes being reviewed here, and in a number of other recent publications. Contrary to an earlier widespread belief that there was a trade-off between inequality and development, and that high inequality was an unavoidable, if only temporary corollary of economic modernisation, recent empirical findings indicate that high levels of initial wealth and income inequality within countries deflate subsequent growth prospects, and inhibit attempts to structure economic growth so as to benefit the poor.[14] Easterly has shown that inequality, independently of other factors, is a large and statistically significant barrier to developing the institutional framework and human capital on which successful development depends.[15] A recent study on inequality within Latin American countries concludes that inequality hinders the implementation of sensible macroeconomic strategies, retards demand, impedes the development of pro-poor trade policies, limits the growth of human capital stocks, raises social discontent, and limits the degree of political participation.[16] The two major World Bank publications reviewed here, as well as the Cornia volume, underwrite these conclusions and make a compelling case that successful development policy demands that we look at the whole spectrum of the income (and wealth) distribution in countries, in contrast to the singular emphasis on the lower end of the spectrum—poverty reduction—that has dominated development thinking for the past decade. The new development consensus is that national economic equity is crucial for economic and human development.

Focusing on the effect of inequality on growth, Cornia and his colleagues find that there is a distinct curvilinear relationship between initial income inequality and economic growth in subsequent periods, as depicted in Figure 3.

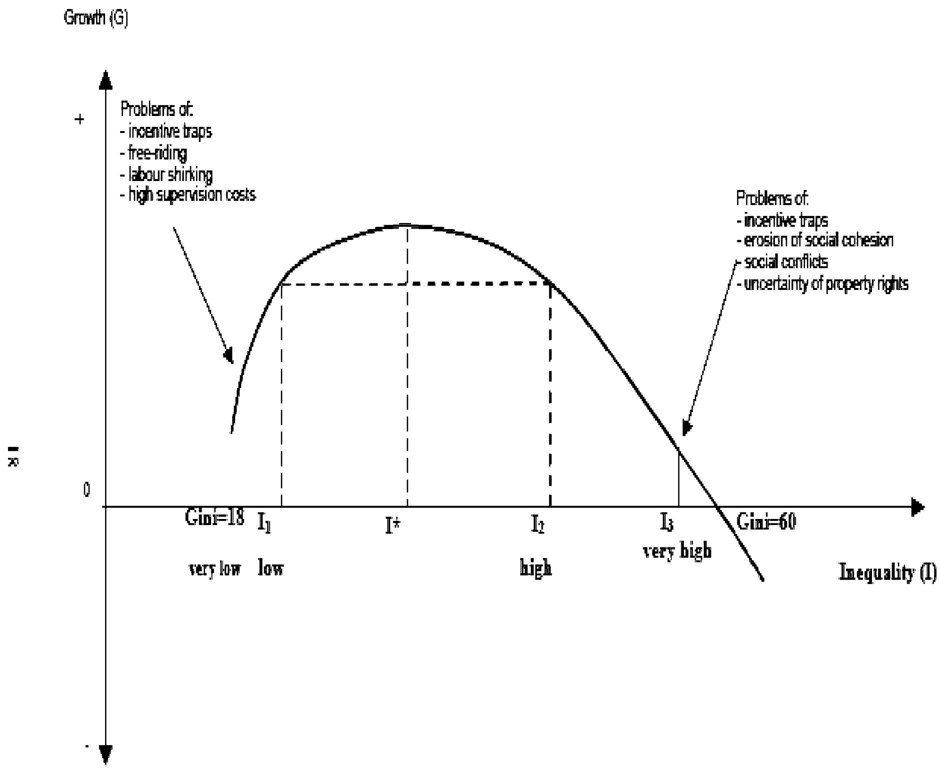

FIGURE 3. The curvilinear relationship between inequality and growth.
Source: G Cornia, T Addison & S Kiiski, 'Income distribution changes and their impact in the post-Second World War period', in G Cornia (ed), *Inequality, Growth, and Poverty in an Era of Liberalization and Globalization*, Oxford: Oxford University Press, 2004, p 45.

It shows that too low inequality may be bad for growth, but also that too high levels of inequality (at 40 and higher on the 100-point Gini index) can have negative consequences. If we assume that economic agents adjust their efforts to comply with their perceptions of whether their relative position in the distribution ranks corresponds to previous effort, low inequality induces free riding and can be conducive to labour shirking, which inhibits growth. The curve section preceding point I^1 in Figure 3 represents such a situation, where low inequality retards growth. As we move along the curve towards higher levels of inequality, growth potential increases as levels of incentives go up, leading to higher incomes for certain groups and potentially more savings, which stimulates investment. However, there comes a point (I*) where inequality is no longer positively associated with growth, and beyond which the relationship sharply turns negative: $I^2 - I^3$. In their econometric tests Cornia and his colleagues determine 40 on the Gini index as the turning point, I*, beyond which inequality becomes dysfunctional.

The dataset used for Figure 1 is not the same as the dataset used by Cornia *et al* and one should therefore be careful not to extrapolate findings from the one to the other without adjustments. It is likely that the turning point I* beyond which inequality becomes dysfunctional lies somewhat higher than 40 in the EHII dataset used in Figure 1. Nevertheless, we have good reason to believe that the majority of developing LMICs in particular have inequality levels that put them in the danger zone, I* to I^3.

Why do high levels of inequality depress growth prospects? There is an extensive literature on this question,[17] but some of the causal mechanisms suggested by the literature under review are the following:

- High levels of inequality coincide with highly skewed access of groups to power and influence. High inequality encourages more intense rent-seeking activities by advantaged and powerful elites, which the poor and disadvantaged cannot challenge because of their relative powerlessness, and the result is that property rights and investment incentives are undermined by the resulting widespread graft.
- High levels of inequality imply that a relatively large section of the population has little or no assets with which to acquire credit. This failure of credit markets leads to lower levels of investment in human capital, and higher fertility rates among those at the lower end of the distribution, thus depressing the growth potential of an economy.
- Concentration of wealth and income on one end of the spectrum leads to distortions of the consumer market, creating smaller domestic markets for non-luxury goods, and inhibits the development of balanced domestic demand.
- Inequality increases social tension, or at least the expectation among potential investors that tension may erupt, which places a lid on domestic and foreign direct investment.
- In an era in which democratisation of polities is widespread the rich in highly unequal countries fear that democratisation will lead to widespread redistribution, and hence shift their wealth offshore. While this enhances

the prospects for democratisation (the shifting of resources removes the potential opposition of the rich elite against democracy), the effect is to starve the local economy of savings and investment. In countries where much of the wealth of the rich is immovable, such as land, opposition by the elite against democratisation is much more pronounced and the prospects of civil conflict and right-wing coups d'etat much greater, with disastrous consequences for growth and human development. Latin America provides good examples of how the concentration of land ownership favours the emergence of reactionary politics.

- High levels of income inequality is associated with a large divergence between the rich and the rest of the society in terms of access to political power and influence. This undermines attempts at democratising these societies, as the poor and the middle class lose confidence in the political institutions to improve their relative situation. Populist coups or other forms of extra-constitutional political action then become attractive.
- However, the negative relationship between inequality and political stability is not linear. High levels of income inequality reflect large disproportionalities in political power and collective action-resources in a society. In these societies, inequality is associated with more, not less stability, as the have nots find it difficult to stage any effective political challenge against the haves.

As the World Bank's 2006 *World Development Report* (WDR) makes abundantly clear, economic growth and political stability are not all that we should be concerned about when considering the effects of inequality. Human development includes economic modernisation, increases in prosperity, and democracy. But it also involves improvements in the overall capabilities of people to lead healthy and rewarding lives, which in turn is dependent on the ability of countries to develop stable economic, political and social institutions that would generate and support the policies that are necessary to achieve better overall human development. High levels of inequality prevent the emergence of those institutions, such as political accountability, property-rights protection, a transparent legal order, and general access to educational opportunities and health care that can guarantee human development.[18] In addition, the 2006 WDR argues:

> Equity in the acquisition of human capacities—through early childhood development, formal education, health services, and social protection—is at the core of a strategy to equalise the opportunities for people to lead productive, fulfilling lives. Broad provisioning of these services is also good for development and poverty reduction through impacts on innovation, productivity, and social cohesion.[19]

So, although within-country inequality is only one of two constituents of global inequality, the publications under review supply abundant evidence that this share is growing and that the high levels of inequality common to developing LMICs, and the rising levels of inequality in transition and high-income countries, pose serious obstacles to the human development prospects of all their residents. This implies that we have to emphasise domestic redistribution and restitution to a much greater degree than used to be common during what Cornia and his colleagues call 'the era of liberalization and globalization', also known as the era of the neoliberal Washington Consensus. Fortunately, we seem to have taken leave of that era now.

Redistribution for the sake of equity

There has rightly been much emphasis placed recently on the challenge of global distributive justice, and two of the publications under review are quite explicit in advocating it. We saw above how Milanovic emphasises the democratisation of the institutions of global governance as a means towards greater global distributive justice. Refreshingly, the 2006 WDR also places the challenges posed by inequality into a broader, global perspective. The final chapter of this report is devoted to an analysis of what must be done by the global community to promote the conditions under which greater political, social and economic equity would become permanent features of developing and developed states alike. This chapter contains a spirited plea for making global market forces work more equitably by opening domestic markets of the North to imports from the South, for setting trade rules that are fairer to developing countries, for lifting the draconian constraints imposed by developed countries on international labour flows, for improving development assistance by increasing and better targeting aid flows, and for linking aid more directly to the relieving not only of poverty, but also of income and wealth inequalities in developing countries (through the joint financing of land redistribution schemes, for instance). While these suggestions are not new and have been circulating among critics of the Washington Consensus for some time, the wholehearted endorsement of them by an official World Bank publication does provide additional evidence that this Consensus is no longer as cohesive as it used to be during the 1990s.

However, there is also a danger of over-emphasising the global dimension of distributive justice, and here the focus of my critique is more directed at cosmopolitans such as Milanovic than at the World Bank. One of the perverse but unintended consequences of cosmopolitanism's emphasis on the importance of international (between-nation) redistribution has been to shift moral blame and responsibility away from the governing elites of developing countries. Now, there can be little doubt about the effect of negative externalities on the way the international economy is conducted for producers and consumers in vulnerable developing economies. Also, Thomas Pogge is perfectly correct when he points out the major responsibilities that the old states of the world carry for the deprivation that still characterises so much of the younger states of the world.[20] Indeed, the norms, rules and practices of the international state-centred regimes have been prejudicially in favour of stabilising and legitimising rent-seeking activities by the often-corrupt ruling elites of the new states, and against the interests of the poor and marginalised within those states. However, that does not imply that these ruling elites carry no responsibility for the high levels of deprivation that characterise so many new states in Latin America, sub-Saharan Africa and South Asia. Unfortunately, so far cosmopolitanism has had little to say about and to these ruling elites and about how they have failed to address the challenge of redistribution within their countries. These rulers may want to hide behind the excuse that globalisation and the macroeconomic policies that major aid donors have imposed on them have restricted their room for manoeuvre with respect to redistribution. We have seen that the coincidence of globalisation and the global hegemony of supply-side macroeconomic thinking has indeed worsened inequality in many developing countries, and one should not assume that the choices of Third World leaders are totally unconstrained. However, choices there always are and the well documented exploitative strategies of ruling elites are as much, if not more, to blame for the low performance of so many new states on indexes of human progress, such as the Human Development Index. Moral cosmopolitanism is incomplete, and misleading, for not addressing within-country inequality and the failure of rulers to deal with it comprehensively and systematically.

There is a sense in which John Rawls' refusal to extend the principles of domestic distributive justice to the global arena is perfectly justified, despite the widespread criticism that has been directed at his *The Law of Peoples* (including criticism by Milanovic in his *Worlds Apart* book). A number of authors has recently argued that Rawls was quite correct in stipulating that principles of distributive justice can only apply to a collection of individuals who have institutionalised among themselves the legitimate means of coercion.[21] Affecting the distribution of valued goods that are in short supply relative to demand entails at least potentially the infringement of the autonomy of persons. This equals coercion, which would be in need of justification to those who are affected by it and who are interested in safeguarding their autonomy. Put differently, only *legitimate* institutions can be instruments in the promotion of distributive justice, given the implied coercion in distributive and redistributive decisions. Such legitimate institutions, for the time being at least, exist only at the level of the state, or in the case of the European Union on the supranational level of an emerging confederation of states. No one would want to argue that such legitimate distributive institutions exist for the world as a whole and, as Nagel argues, it is unlikely that such institutions will emerge before the creation of a single world political community. Legitimacy is created by political institutions, not the other way around.[22] This is not to deny that the practices of international regimes with near global scope, such as the World Trade Organization (WTO) or the IMF, for instance, do have distributive consequences. But these institutions were created as co-operative schemes and receive their legitimacy as such, not as redistributive institutions.

The point of the above is that the state is, for the time being, the only legitimate context within which relative deprivation can be addressed through redistributive policies and practices. In terms of the discussion in the early part of this essay, this implies that the morally appropriate place to do something about global income inequality is first and foremost in the dimension of within-country inequality, that is, at the level of the state. This does not mean that between-country inequality can or should be ignored. However, in terms of the full understanding of what redistribution entails, it is a misnomer to speak of 'global distributive justice', except if we mean by that the sum-total of distributive justice achieved by individual states. For it is at the level of states only that the principles of *distributive justice* can and may apply, as it is on this level alone that we have the institutional means to legitimately take from the rich and give to the poor. To this we can add a point that Robert Goodin makes, namely that the state is the *functional* unit through which distributive justice can most efficiently be achieved, and that the state should therefore be at the heart of any scheme to secure global justice.[23] Thus, even if one rejects the restrictions that I impose on the applicability of the principles of distributive justice, prudence would determine that we place much more emphasis on within-country inequality and what to do about it than current debates about global inequality imply. It is in this regard that the 2006 WDR *Equity and Development* is especially to be welcomed as a sign that 'official' development thinking has turned an important corner as far as domestic redistribution is concerned. Whether this report will also lead to sustained international and domestic action to address inequality within countries systematically is another question. However, what should happen if we want to maintain the momentum is that the norm of inequality reduction should become as enshrined as that of poverty relief in the macroeconomic 'suggestions' that multilateral and bilateral donors of official development assistance make to recipients. There are good reasons to believe that reducing inequalities through the redistribution of assets and income could be an important policy tool for inducing poverty-reducing growth (to be distinguished from growth *per se*). As the 2000/2001 WDR comments: 'while economic growth is systematically associated with poverty reduction, the rate at which growth translates into lower poverty depends on the initial level of inequality in the distribution of income and how that distribution changes over time'.[24] An International Labour Office study by Dagdeviren *et al* confirms this conclusion. The authors find that for almost all of the countries in their sample a strategy of marginal redistribution of wealth from the rich to the poor, or a strategy of equal distribution of growth benefits, is more effective in reducing poverty than increases in economic growth that are distributionally neutral.[25]

The renewed emphasis on domestic redistribution as a proper and prudent policy tool also implies that there rests a negative duty on the shoulders of the rule makers in global regimes to weed out those norms and practices that inadvertently restrain or deliberately discourage redistributive macroeconomic policies in developing countries. Although this point can sometimes be overdone, there is no doubt that open economies lose some control over the setting of prices, that it becomes infeasible to depress the expected after-tax rate of return on mobile capital, and that those in favour of redistribution, such as trade unions, may have their bargaining power undermined in the process.[26] However, it is an illusion to think that globalisation has totally depleted the redistributive arsenal of the welfare state. Much can still be done to promote equity in wealth and income in poorer countries, also by countries acting on their own. This would include land redistribution on a willing-seller, willing-buyer basis and the taxing of absentee landholding; improving imperfections in the credit market so that the poor can gain access to credit and start to build-up human and fixed capital; and the use of progressive taxation to fund general education and primary health care.[27]

This is not incompatible with an endorsement of transnational attempts to do something on a grand scale to reduce poverty incidence, such as the plea that the 23 members of the OECD Development Assistance Committee should double overseas development assistance (ODA) to developing countries over the next decade. What is crucial to understand, however, is that there is no guarantee that increased aid that is earmarked to flow through the state apparatus of developing countries will reach its intended targets, namely the poor, if such states do not have functional redistributive strategies in place. Thus, domestic redistribution in this sense is a prerequisite for effective global transfers, not the other way around. Generous and targeted foreign aid to improve access to education, or to set up a credit facility for the poor, for instance, can do much to promote the prospects for economic growth in the medium and longer term, which will promote convergence in income levels across nations. Within- and between-country inequality is thus intimately related, but it is important that we conceptualise this link and its implications correctly.

Therefore, it is important to remember that there is a crucial difference between ODA transfers, no matter how large, and within-country redistribution. As we said above, only the latter can legitimately fall under the purview of redistributive justice, and entails longer term attempts to improve equity within a political community. As the experience of welfare states in northern Europe shows, such redistribution continues even after absolute poverty has been eradicated, because it is driven by considerations of distributive justice. In contrast, foreign aid is and can only be driven by considerations of humanitarian beneficence, at least until such time that a single world political community is created that can legitimate redistributive transfers that also go beyond the goal of poverty relief. The humanitarian impulse behind foreign aid is limited in time and in purpose. Once the incidence of absolute deprivation has been reduced to zero, and this becomes self-sustaining, the general humanitarian rationale for ODA disappears. Domestic redistributive justice, on the other hand, is a continuous attempt to address the issue of relative deprivation, irrespective of the incidence of absolute deprivation.

Conclusion

The recent publications and UTIP website under review suggest that there are two sets of reasons to pay more attention to domestic inequality than is common in the current ethical or policy-oriented literature. The one relates to the fact that political–economic studies have over the past decade shown that earlier beliefs about a trade-off between economic development and income inequality cannot be sustained. A stream of evidence is emerging to show that inequality at the high levels commonly seen in developing countries inhibits growth and development through a variety of political and economic mechanisms. Crucially, having a high level of inequality makes it difficult for a country to translate economic growth into pro-poor growth.

The second reason has to do with the important normative distinction between circumstances under which principles of distributive justice can apply, and where they cannot. According to the approach to distributive justice developed by John Rawls, and endorsed here, the use of coercion to effect the redistribution of resources/income/wealth can only be justified to those who are affected by it, if they share a set of political institutions with the defender in terms of which coercion can be legitimated. This context is provided by the state, and redistribution as an act of distributive justice must be restricted to it. Cosmopolitans do their own cause a disfavour when they ignore the within-country dimension of income inequality, which can be shown to be the 'natural focus' of distributive justice.

None of the above implies that the terrible international levels of income inequality should be left out of consideration, however. But we have to appreciate that the transfer of resources between societies can not and should not have the purpose of effecting international distributive justice. The purpose is and should be the humanitarian goal of reducing the incidence of absolute deprivation and to promote development prospects. This goal is worthwhile in its own right, and considerable transfers will be necessary to achieve even the limited Millennium Development Goals. However, it is not appropriate to categorise these transfers as part of distributive justice.

Once we have sorted out these conceptual and normative distinctions, the task of all who are concerned about the high levels of global inequality is to promote equity through redistribution as a primary national policy goal, and to make sure that governments are woken up to this challenge, but also empowered to take it on through global co-operative schemes.

Notes

1 A Sen, 'From income inequality to economic inequality', *Southern Economic Journal*, 64 (2), 1997, pp 384–401; Sen, *Inequality Re-examined*, Oxford: Oxford University Press, 1992; and T Persson & G Tabellini, 'Is inequality harmful for growth?', *American Economic Review*, 84 (3), 1994, pp 600–621.

2 Both the International Studies Association (2001) and the American Political Science Association (2003) have devoted annual conventions to the theme of inequality. The *Journal of Economic Inequality* was launched by Springer in 2003. In 2005 a new international Society for the Study of Economic Inequality was founded at a conference in Mallorca, Spain.

3 R Dahrendorf, 'On the origin of social inequality', in P Laslett & WG Runciman (eds), *Philosophy, Politics and Society*, Oxford: Blackwell, 1969, pp 88–109.

4 D Ray, *Development Economics*, Princeton, NJ: Princeton University Press, 1998, p 70.

5 See G Firebaugh, *The New Geography of Global Income Inequality*, Cambridge, MA: Harvard University Press, 2003; and G Firebaugh & B Goesling, 'Accounting for the recent decline in global income inequality', *American Journal of Sociology*, 110 (2), 2004, pp 283–312 for spirited defences of why population-weighted between-country comparisons are more appropriate than un-weighted ones.

6 These summary measures of inequality are well explained by 'tutorials' on the University of Texas Inequality Project website, at http://utip.gov.utexas.edu/.

7 See Firebaugh, *The New Geography of Income Inequality*, for example.

8 See, for example, B Barry, 'International society from a cosmopolitan perspective', in D Mapel & T Nardin (eds), *International Society: Diverse Ethical Perspectives*, Princeton, NJ: Princeton University Press, 1998, pp 144–163; C Jones, *Global Justice: Defending Cosmopolitanism*, Oxford: Oxford University Press, 1999; and L Wenar, 'The legitimacy of peoples', in P de Greiff & C Cronin (eds),

Global Justice and Transnational Politics: Essays on the Moral and Political Challenges of Globalization, Cambridge, MA: MIT Press, 2002, pp 53–76.

9 A partial exception is Kok-Chor Tan, *Justice without Borders: Cosmopolitanism, Nationalism and Patriotism*, Cambridge: Cambridge University Press, 2004.

10 K Deininger & L Squire, 'Measuring income inequality: a new data base', *World Bank Economic Review*, 10 (3), 1996, pp 565–591; K Deininger & L Squire, 'New ways of looking at old issues: inequality and growth', *Journal of Development Economics*, 57, 1998, pp 259–287.

11 J Galbraith & H Kum, 'Estimating the inequality of household income: a statistical approach to the creation of a dense and consistent data set', *Review of Income and Wealth*, 51 (1), 2005, pp 115–143.

12 F Bourguignon & C Morrisson, 'Inequality among world citizens: 1820–1992', *American Economic Review*, 92 (4), 2002, pp 727–744.

13 The study by Bourguignon and Morrisson is based on time series data on within- and between-country inequality for a group of 33 country groups. The groupings are based on criteria of homogeneity and historical consistency, while significant countries in terms of population size and economic output (USA, China, India, etc) are considered individually. There are six regional blocs of country groups. Coverage of the developing world is quite good: sub-Saharan Africa, for instance, is represented by four groups, and there are groups for Asia, Eastern Europe and Latin America (Middle East and North Africa is not included).

14 See, for example, S Chen & M Ravallion, 'How did the world's poorest fare in the 1990s?', World Bank Policy Research Working Paper No 2409, August 2000, at http://www.worldbank.org/research/povmonitor/method.htm; M Gugerty & C Timmer, 'Growth, inequality, and poverty alleviation: implications for development assistance', Consulting Assistance on Economic Reform II Discussion Paper No 50, 1999, Harvard Institute for International Development, December, at http://www.cid.harvard.edu/caer2/htm/content/papers/confpubs/paper50/paper50.pdf; N Birdsall, 'Why inequality matters: some economic issues', *Ethics and International Affairs*, 15 (2), 2001, pp 3–28; R Kanbur, 'Income distribution and development', in A Atkinson & F Bourguignon (eds), *Handbook on Income Distribution*, Amsterdam: North-Holland, 2000, pp 791–841; P Nel, 'Income inequality, economic growth, and political instability in sub-Saharan Africa', *Journal of Modern African Studies*, 41 (4), 2003, pp 611–639; and Nel, 'Democratisation and the dynamics of income distribution in low and middle-income countries', *Politikon*, 32 (1), 2005, pp 17–43.

15 W Easterly, 'Inequality *does* cause underdevelopment: new evidence', Center for Global Development Working Paper No 1, June 2002, at http://www.cgdev.org/wp/cgd_wp001_rev.pdf.

16 P Justino, J Litchfield & L Whitehead, 'The impact of inequality in Latin America', Poverty Research Unit at Sussex Working Paper No 21, 2003, pp 64–65, at http://www.sussex.ac.uk/Users/PRU.

17 Parts of this literature is well summarised by E Thorbecke & C Charumilind, 'Economic inequality and its socioeconomic impact', *World Development*, 30 (9), 2002, pp 1477–1495.

18 See also Easterly, 'Inequality *does* cause underdevelopment'.

19 World Bank, *World Development Report*, Washington, DC: World Bank, 2006, p 155.

20 T Pogge, 'Priorities of global justice', *Metaphilosophy*, 32 (1&2), 2001, pp 6–24.

21 See, among others, Wenar, 'The legitimacy of peoples'; M Blake, 'Distributive justice, state coercion, and autonomy', *Philosophy and Public Affairs*, 30 (3), 2001, pp 257–296; and T Nagel, 'The problem of global justice', *Philosophy and Public Affairs*, 33 (2), 2005, pp 113–147.

22 T Nagel, 'The problem of global justice'.

23 R Goodin, 'Globalizing justice', in D Held *et al*, *Taming Globalization*, Cambridge: Polity Press, 2000, pp 68–92.

24 World Bank, *Attacking Poverty—World Development Report 2000–2001*, Washington, DC: World Bank, 2001, p 35. See also T Addison & G Cornia, 'Income distribution policies for faster poverty reduction', UNU-WIDER Discussion Paper No 2001/93, 2001.

25 H Dagdeviren, R van der Hoeven & J Weeks, 'Redistribution matters: growth for poverty reduction', ILO Employment Paper 2001/10, Geneva: International Labour Office, 2001.

26 N Rudra, 'Globalization and the decline of the welfare state in less-developed countries', *International Organization*, 56 (2), 2002, pp 411–445. See also S Bowles, 'Globalization and redistribution: feasible egalitarianism in a competitive world', Working Paper No 34, Political Economy Research Institute, University of Massachusetts at Amherst, 2000, at http://www.umass.edu/peri/pdfs/WP34.pdf.

27 Bowles, 'Globalisation and redistribution'. See also F Bourguignon, 'Can redistribution accelerate growth and development?', unpublished paper prepared for the Annual World Bank Conference on Development Economics/Europe, Paris 26–28 June 2000, at http://www.worldbank.org/research/abcde/eu_2000/papers_eu2.html.