EC9AA Term 3: Lectures on Economic Inequality

Debraj Ray, University of Warwick, Summer 2023

Supplement to Slides 3: Sovereign Funds



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Social alternatives

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- Fee-free brokerage accounts common in the United States.
- Even in developing countries, you can trade at smaller commissions.
- Trading in fractional shares.
- Financial education is fundamentally important.
- Yes, a distant dream for many, but the processes here are also distant.

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- More generally:
- I'm pessimistic about intelligent, informed equity-holding;
- But society must learn to equitably scale alienable endowments.

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■ We agree:

"universal basic income is a genuine, structural, distributive transfer. Its proper consideration must appear on top of social insurance programs, not as a substitute ... whatever social insurance we do have, such as NREGA, should not be cannibalized for the purpose of making structural transfers such as a universal basic income." Ghosh © Ray 2021

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- 1.4 billon people, 13000 per person = 18.2 lakh crore, or 8% of GDP.
- CGI spending is around 12.5% of GDP, maybe 14% after pandemic.

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- The universal basic share (UBS) Ray (2016) and Moene and Ray (2016)
- Commit fixed fraction of GDP to the provision of UBI.

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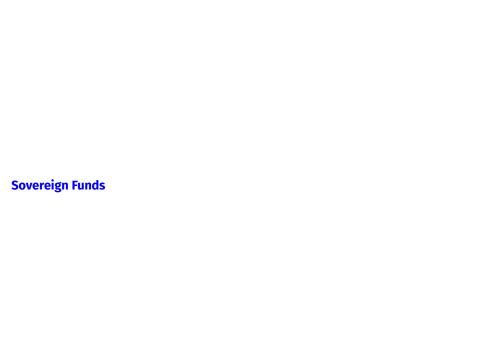
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- E. **Political alignment:** E.g., in treatment of K and L, tax collections, etc.
- F. **Sharing:** Allows everyone to share in the prosperity of a country.



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- Norway fund:
- oil-based, around \$200,000 per Norwegian citizen.
- It could pay out, but as of now, it does not.

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- Natural resources form *only* a variable part of that base.
- The pragmatics come from the logistics of fund building:
- Several proposals in the United States: charity (Stout and Gramico Ricci 2017), financial transactions tax (Baker 2017), higher taxes on capital incomes (Barnes 2014), transfer of existing government assets, e.g., spectrum auction proceeds and various levies on companies (Bruenig 2018).

Based on Ghosh (r) Ray 2021

India — and developed countries — should build a sovereign fund.

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- Portfolio of equity, bonds and other financial assets
- Managed professionally as any fund would be managed (subject to certain constraints)
- A fraction of the return can be paid out as a citizen's dividend.
- But the payout will be slow. Patience is of the essence.

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- Issue x% of existing share base new to the government.
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- II. Ongoing directive to transfer x% of every new share issue
- Whether it is an IPO or expansion of existing share base.

Payment via dilution.

- Conceivably the most compelling point in favor of the plan:
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- All in all, this is an extremely effective form of taxation.

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Political Incentives

- Citizens come into closer political alignment (Moene and Ray 2016)
- Of course, redistribution motive is still present
- But smaller conflict on functional terms: e.g., "capital vs labor."

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- Protectionism and immigration restrictions
- Sector-specific taxation, subsidies, directed credit
- These achieve distributive ends at the cost of reducing the size of the pie.
- The reason behind these conflicts isn't personal inequality but ...
- Discrepancies in relative capital-labor ownership
- These project on to battles about functional restrictions

- Allows for interesting variants:
- A flow tax on wealth:
- Will require ongoing dilution every year.
- A flow tax on unrealized capital gains:
- Require fresh dilution in proportion to the gain in stock prices every year



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- Credibility achievable by device such as a Constitutional Amendment.
- But additional distortions could arise
- Happens with all (non-lump-sum) taxes btw.
- If only publicly traded shares are diluted, might change capital structure,
 e.g., swapping equity for debt or converting publicly traded companies
 into proprietorships.

Portfolio Management:

- Autonomous management a necessity
- Co-optation by business interests (e.g., transacting certain shares)
- Experiences of Norway, China, Saudi Arabia may be instructive.

Constraints on Transactions

- Sovereign funds often hold a diversified global stock portfolio
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Logical limit:

- Must the India Fund rise and fall on the national fortunes of India?
- Then one might even mandate that the Fund hold to the extent possible — the current composition of Indian corporate wealth.
- Worth investigation.

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- We discussed various aspects of this.
- Main Lesson:
- Human endowments need to fundamentally change.
- Individual and social responses
- Building a social fund on the basis of share dilution.