EC9AA Term 3: Lectures on Economic Inequality

Debraj Ray, University of Warwick, Summer 2023

- **Supplement to Slides 3**: Sovereign Funds

Preparing for the Future

“Meanwhile there will be no harm in making mild preparations for our destiny, in encouraging, and experimenting in, the arts of life as well as the activities of purpose.”

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Individual alternatives

Social alternatives

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- **Dramatic changes in access to equity.**
  - 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.

Individual Alternatives

- **Limitations to Individual Investments**
- Not for **improving** wealth inequality, but **preventing** further decay.
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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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  - But correctly worry about NREGA, health care, nutrition, social insurance
  - Or adequate indexation and protection against inflation.
- **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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F. **Sharing:** Allows everyone to share in the prosperity of a country.

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  - "Alaska's natural resources are owned ... by the Alaskan people themselves." Jay Hammond, 1994.
- 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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- **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).

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Based on Ghosh ⓡ Ray 2021

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- 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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I. One-time directive on existing publicly traded companies:

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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.

Advantages of the Proposal

Payment via dilution.

- Conceivably the most compelling point in favor of the plan:
  - Stock issues by listed firms easy to track;
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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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  - 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

Advantages of the Proposal

- 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.

Limitations and Concerns

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.

Limitations and Concerns

Constraints on Transactions

- **Sovereign funds often hold a diversified global stock portfolio**
  - Unclear whether this can happen immediately for the India Fund.
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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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  - The labor share must decline, even as absolute wages rise.
  - 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**.