Self & Society, 2016
Vol. 44, No. 1, 63–69, http://dx.doi.org/10.1080/03060497.2015.1016272

REVIEW ARTICLE

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Capital in the twenty-first century, by Thomas Piketty, Cambridge, MA, Harvard University Press, 2014, 696 pp., £14.98, ISBN 978-0674430006

(*Received 26 January 2015; accepted 3 February 2015*)

The book *Capital in the Twenty-First Century* by Thomas Piketty has been a phenomenon in economics, the social sciences, politics and related disciplines. Piketty examines economic data from several centuries and from several countries, and attempts to draw conclusions about the balance between earned income and capital-driven income, and the resulting outcomes for income distribution and income equality. Piketty illustrates the drastic effects of the Great Depression and two World Wars on capital, and the unexpected positive consequences that have, until recently, led to reductions in income inequality. Piketty then examines the recent slide back towards capital-dominated wealth and its role in increased inequality, and extrapolates how this might lead to future critical inequality and social unrest. Finally, Piketty suggests various possible responses to stave off this crisis, with his preferred option being presented as a progressive system of tax on capital.

Keywords: economics; capital; inequality; wealth; income; social policy

Thomas Piketty points out that economics is far from the perfect forecasting method that it is portrayed to be. He likens it to a form of political science, or a relation to social science. Piketty suggests that we need to challenge conventional wisdoms and look again at the data, which he proceeds to do in a challenging yet interesting volume which draws on tax data, income figures and capital estimates from a number of countries, including France, the UK, the USA and Japan. Piketty builds a picture of the patterns of change, in particular between incomes derived from capital and those derived from employment. He illustrates this with references from literature which are designed to suggest attitudes to those incomes and their comparative status held in the societies of the time. This helps to situate the income levels within a context, so that the reader can relate them to the language of our time, such as the concept of the '99%'. It also dispels any idea that the current growing income inequality is a new phenomenon. Indeed, the opposite is the case, and Piketty essentially concludes that we are regressing to a form of patrimonial capitalism of a type previously seen in pre-Napoleonic France.

The economics are presented using a series of equations and formulae which are conventionally applied to the analysis of capital, income, growth and so on, and

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these are explained and presented layer by layer as the early chapters of the book progress. Piketty makes good use of graphical data to illustrate trends and patterns where the non-economist might long since have been left struggling. The combination of graphical illustration and illustration by example and literature reference makes the economics much easier to follow and, despite its dry nature, surprisingly interesting.

One overall theme is that in pre-Napoleonic times most income was capital driven, mainly in the form of property generating rent for landlords. The 'landed' classes built up their portfolios or estates, and then had a very predictable return in the form of rent. Other classes could never hope to match the income levels derived from such estates, and the income-inequality gap essentially existed between the landowners and those whose earnings derived from employment. With various events in between, not least the French Revolution and the gradual introduction of income tax in various countries, not to mention costly wars mounting up national debts, the general trend remained similar until the twentieth century. Piketty does explain the effects in the meantime of inflation on the capital worth of those who purchased government debt, and the resultant loss of capital wealth for those investors, since this again has great relevance in the present day.

Scroll forward, however, to the triple blow of the Great Depression and the two World Wars and a seismic change hits the capital/employment income balance. Piketty examines the detail, but essentially much capital, including property, industry and other land-based wealth, was physically destroyed, valuables were stolen or appropriated and capital wealth, especially noticeably in mainland Europe, was greatly reduced. After the period of conflict, those who had previously had capital wealth had often lost it all, while skilled workers maintained their skills once jobs emerged out of the chaos. Since it takes far longer for a family to accumulate capital wealth than it does to gain an education and gainful employment, employment-based wealth rebounded far more quickly than capital wealth. Inflation post-war again ate into the capital held in the form of government bonds, as their real value was eroded. The data clearly show the great reduction in income inequality brought about by the conflict period, and this is then added to by the political decisions made by many governments, including that of Britain, to introduce welfare schemes and progressive taxation in the post-war period. The richest then often lost capital fortunes, the poorest were lifted up somewhat by welfare and the middle classes gained education and employment-based wealth. Add to this the 'catch up' growth period reaching nearly to the 1970s in many countries including France, and booming economies with uncharacteristic growth rates added to prospects and overall GDP.

Piketty then essentially asks, if income inequality fell so noticeably – a fact heralded by many politicians of the period – why has it returned so dramatically? He identifies a number of factors. The growth rates in countries post-war have slowed dramatically, now that those economies have 'caught up'. Those countries still showing high growth rates, such as the 'BRIC' nations (Brazil, Russia, India and China), are themselves now 'catching up'. Growth generates income opportunities for both accumulation of assets and employment income. The difference is that accumulated capital wealth remains after growth rates decline. The temporary renaissance for employment-driven wealth has slowed, while those who have accumulated capital are now sitting on that wealth.

The type of wealth has changed from landowning to the ownership of capital in the form of shares and other industrial or economic equity, which, rather than paying rent, pays dividends or other returns. Once accumulated, such wealth continues to grow itself, and Piketty uses the examples of Liliane Bettencourt and Bill Gates, who have seen increases of capital value multiplying tenfold over 20 years.

This tendency for capital to essentially grow itself, let alone the obvious financial ability of those with capital to deliberately seek out more, means that the share of income in the economy coming from capital, and held as capital, is growing, while the share coming from employed income is proportionately falling. The rich are getting richer and the poor are getting poorer. As the first draft of this review article was being written, Oxfam (Seery & Caistor Arendar, 2014) reported that unless action is taken, the proportion of wealth held by the top 1% will next year exceed that held by the remaining 99%. To make matters worse, attempts by governments to reduce national debts following the banking and debt crisis, by applying austerity, further target the vulnerable, reversing the positive effect of the post-war political decision to introduce welfare and progressive taxation. Piketty also compares the top rates of tax in a number of countries, including the Scandinavian countries, France, Germany, the UK and the USA, and notes how the reduction of top rates of taxation in some, supposedly to prevent capital flight and trigger trickle-down economics, have not delivered. There is no noticeable positive catalyst effect on GDP or productivity in the lower-rate tax regimes compared with the higher-rate countries.

Piketty completes the book by presenting a series of strategies. First, he points out that part of the problem in managing wealth held in capital is the lack of comprehensive data. The USA and the European Union already enable the sharing of bank data, whereas tax havens do not. Having a complete picture of wealth would enable the accurate development of policy by future governments, as well as potentially closing down tax loopholes. Piketty suggests a punitive 30% export tariff on offending countries who do not co-operate – not to raise income, but as a deterrent to encourage compliance. Secondly, a global tax on capital would enable the tracing of all capital. Once something is taxed, it ends up being recorded, thus providing further transparency of ownership and enabling better regulation. It would enable a clear picture of who owns what, and would map and expose how wealth is moved and hidden in attempts to avoid other forms of taxation.

Thirdly, a more progressive taxation system, more aggressive in nature, would help to close the income inequality from general income including employment. Piketty suggests an 80% tax rate for those earning over $500,000, and 50–60% for over $200,000. He suggests that this would help to curb overspending on over-generous bonuses for top executives, and gradually encourage redistribution in companies towards the lower wages. It is not completely clear why he thinks other employees would be paid more, rather than big business simply saving the money or redistributing it to shareholders. Fourthly, he suggests a progressive taxation on total wealth, not just income. This would have the obvious effect of taxing people on what they are really worth, not just on what they are officially 'paid'. As Piketty points out, many of the very rich pay into legal tax reduction schemes such as charities or trust funds in order to avoid tax on that part of their income. If the tax were on their overall wealth, they would be charged for their overall capital and income worth, whatever they chose to do with the revenue or income from that capital.

Lastly, Piketty suggests the redistribution of oil wealth. The disparity, for example, between the wealth in Saudi Arabia and Egypt, because of lines drawn on the map by former colonial powers happening to leave oil in one country and not another, should somehow be addressed. Piketty is open in admitting that both the redistributing of oil wealth and the idea of a global capital tax present massive political challenges, but he is optimistic that progress would be worth the effort. Real political and ideological problems would exist with both these and the transparency ideas generally. Many countries would object to rival governments having data about their citizens, types of wealth accumulation and GDP, and for some countries the right to own land and accumulate capital is so ideologically ingrained that one might expect it to be severely challenged by the idea of any capital tax. Since the Americans poured tea in Boston harbour and ended up fighting for their independence over excessive colonial tax, how might they respond to a global capital tax? Moreover, if oil wealth is to be addressed, how about the false value given to the US dollar as a result of the petro-dollar function? Would this be removed with oil traded openly with any currency? What effect might any collapse in the value of the dollar have on the world economy?

Piketty concludes with some ideas on solving the debt crisis. Accepting that the crisis was inevitable as a result of factors including the choice of a 'pay as you go pension' system, which was bound to eventually fail with population growth outstripping economic growth, and a general habit of heavy government deficit and debt, he looks at the three possible solutions. He considers austerity to be the worst possible solution, and comments on the irony that it is the one in use. He considers the traditional method of inflation, used after previous periods of government indebtedness to reduce the value of the debt. He acknowledges that this would work again, but there are a number of side-effects of inflation, some positive and some negative. Debt would be reduced, but so would savings and income value, while owners of capital might be largely isolated from inflation if the value of that capital also rose by the rate of inflation or more. Thus, income inequality might worsen.

The solution he favours, therefore, is a one-off exceptional tax on private wealth, overall wealth including capital, not just income. This was tried successfully in post-World War II France, and a 15% levy might clear public debt. Piketty suggests that, first, a discussion should be had to decide what an acceptable level of public debt is, and then the rate of tax should be levied to reduce debt to that level, with no need necessarily to clear it altogether. The tax rate could be applied progressively so that low incomes and capital were exempt and the wealthier in society paid a progressively larger share. This would effectively press a reset button on the debt problem. One obvious potential problem with this, however, which Piketty does not address, is that much of the so-called 'assets' held by financial institutions are actually hypothecated debts that may never be repaid, therefore if a bank claimed to have, say, £10 billion in assets and actually half of that was in poor-grade debt, it is hard to see the bank being able to pay a percentage of the overall 'capital' without experiencing severe cash flow problems. Private debt might be transferred to public debt via bailout, increasing the problem. Another problem, which Piketty does acknowledge, is that the tax would have to be applied globally, otherwise capital would flow abroad unless frozen in advance – a problem seen in Cyprus when a capital levy was considered and then abandoned.

The reader might be forgiven for first thinking that Piketty had written a purely economic text, but this could not be further from the truth. Along the way he discusses the effects of global politics and the ideology of wealth distribution, and he spends a considerable part of the book discussing the value of spending and investment in education in challenging wealth inequality.

Atkinson (2014) writes that although Piketty addresses at length the vertical nature of current and historic inequality, in other words typically between the 1% and the 99% to use current parlance, he fails to address other forms of inequality that exist horizontally. In particular, issues of gender gap are not addressed. One example of this can be seen in the change in employment comparing women and men in the UK between 1971 and 2013 (Office for National Statistics, 2014). Because of largely political and ideological changes, the percentage of male versus female employment changes from 92.1% and just over 50% in 1971 to just under 80% and 67.7%, respectively, by 2013. Although the income divide between families may not show this in vertical analysis, clearly the earning power and potential individual income of women has changed dramatically over this period, and this is not reflected in Piketty's work.

Piketty responded to this criticism in his 2014 reply to the *British Journal of Sociology* symposium, acknowledging that further analysis was needed in this area. It is perhaps churlish to expect any one book, even such a substantial one, to contain both vertical and horizontal analysis. However, this omission was not stated in the original text, to encourage the reader to explore this area themselves. As with gender inequality, other horizontal inequalities relating to education, regions within countries, disabled persons, ethnicities and so on would certainly bear further analysis. Perrons (2014) also takes up the gender argument, suggesting that a feminist analysis of the patterns behind inequality might reveal how themes of identity held by those in the position to decide remuneration and wealth distribution cause behaviours and outcomes in that distribution. Whereas Piketty attempts to work out what the data say about trends in inequality, and from that to work out potential explanations, Perrons touches on the underpinning human nature and behaviours. This could in turn be expanded into the realms of a Goffman-like analysis of whether certain groups have become institutionalized in elitist privileged behaviours, or a Foucauldian analysis of whether these groups are a product of subjectification.

Bear (2014) also makes reference to the more qualitative nature of potential study, including areas such as informal labour, social reproduction and changing institutional forms of public debt. Just one of those points – informal labour – with its ramifications for credit unions, barter systems and community groups, and how these relate to quantitative changes in financial inequality, would provide a fascinating expansion of the identified trends in Piketty's book. Hopkin (2014) points out that while the book brings the subject area into mainstream debate, the central question of capital is 'almost meaningless without proper consideration of its political foundations'. Although an interesting point, one might counter-argue that one of the advantages of the book is that it does not over-burden the reader with political explanations; rather, it looks at the patterns and then tries to comment on the situation that the data are illustrating. There is perhaps a trap of engaging too strongly in political theory, since it can lead to the bending of data to match the desired ideological hypothesis. Piketty clearly does lay a trail of breadcrumbs leading to the conclusion that we need a capital tax to reduce inequality, which may seem an ideological desire in its own right; however, that is rather different from, for example, seeking to use the data to evidence that capital is being accumulated by the ruling classes with wealth gradually being trickled away from the workers by using them simply as a means of production. Both of course may be true, but Piketty's book is rather refreshing because it does not overburden the reader with blatant politics.

In a short article such as this it is not possible to do credit to the other leading contributors to the feedback the book has received, nor to Piketty's interesting feedback to them. To summarize, however, Piketty (2014) has generally acknowledged that the book has limitations, gaps and imperfections, and has shown the same humility in his feedback that is evident in his writing. In all, *Capital* is a fascinating book, which should not be considered the consummate explanation of all things economic in regard to trends of wealth inequality but, rather, a catalyst for debate, further study and further writing for many years to come.

Disclaimer

No potential conflict of interest was reported by the author.

Notes on contributor

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