The Specter that is Haunting Capitalism: Inequality

Richard B. Freeman, Harvard, NBER, and CEP, LSE

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This Talk

1-- The Facts in Brief

2- The Fears – the BM and BMMA models

3- Toward a better future

4- Road maps from here to there

5- Yes, we can

Acknowledgments: Justice Brandeis, Machiavelli, Dwight Eisenhower, James Madison, Thomas Jefferson, John Adams,

I. Inequality Specter Facts

Within countries,

- inequality in income and wealth has risen substantially in past 30 or so years (and is high in Latin American exceptions)
- Informal or irregular work persists
- capital's share of income has increased, shifting distribution toward more unequal form

Across countries,

- income inequality has fallen as low income economies grow more rapidly than advanced economies
- Sci-tech knowledge spreads widely, with China moving to forefront of R&D

Biggest protest in most unequal advanced country divided society between the upper 1% (22.5% of income in 2012) and the 99%

1) But the share of income to **upper 0.1%** increased from 3.1% (1972) to 11.3% (2012) so maybe focus on 0.1%

2) But within the 0.1%, 48% of income goes to **upper 0.01%** and their share of income rose from 1.2% (1972) to 5.5% (2012)

3) But within upper 0.01%, 49% of income goes to **upper 0.001%.**

Within upper 0.001% Top 400 US taxpayers (0.00028% of 143 million returns) earned 1.59% of adjusted growth income, up from 0.52% in 1992: 10% of capital gains, 4% of interest, 4% of dividends. Top 400 is 5,770 times average gross income. (2007, IRS).

In 2014 492 US billionaires (8 of top 10) with net worth of $1.3Trilliion # 2 was China (152); # 3 Russia (111); EU (468) as a whole is #2; Sweden(19) (including # 12), Norway (9), Denmark (5), Finland(4)

Reasons for rising inequality

1—Current story –Skill-biased technological change together with trade with developing countries; (implicit capital-using technical change as well to raise capital's share).

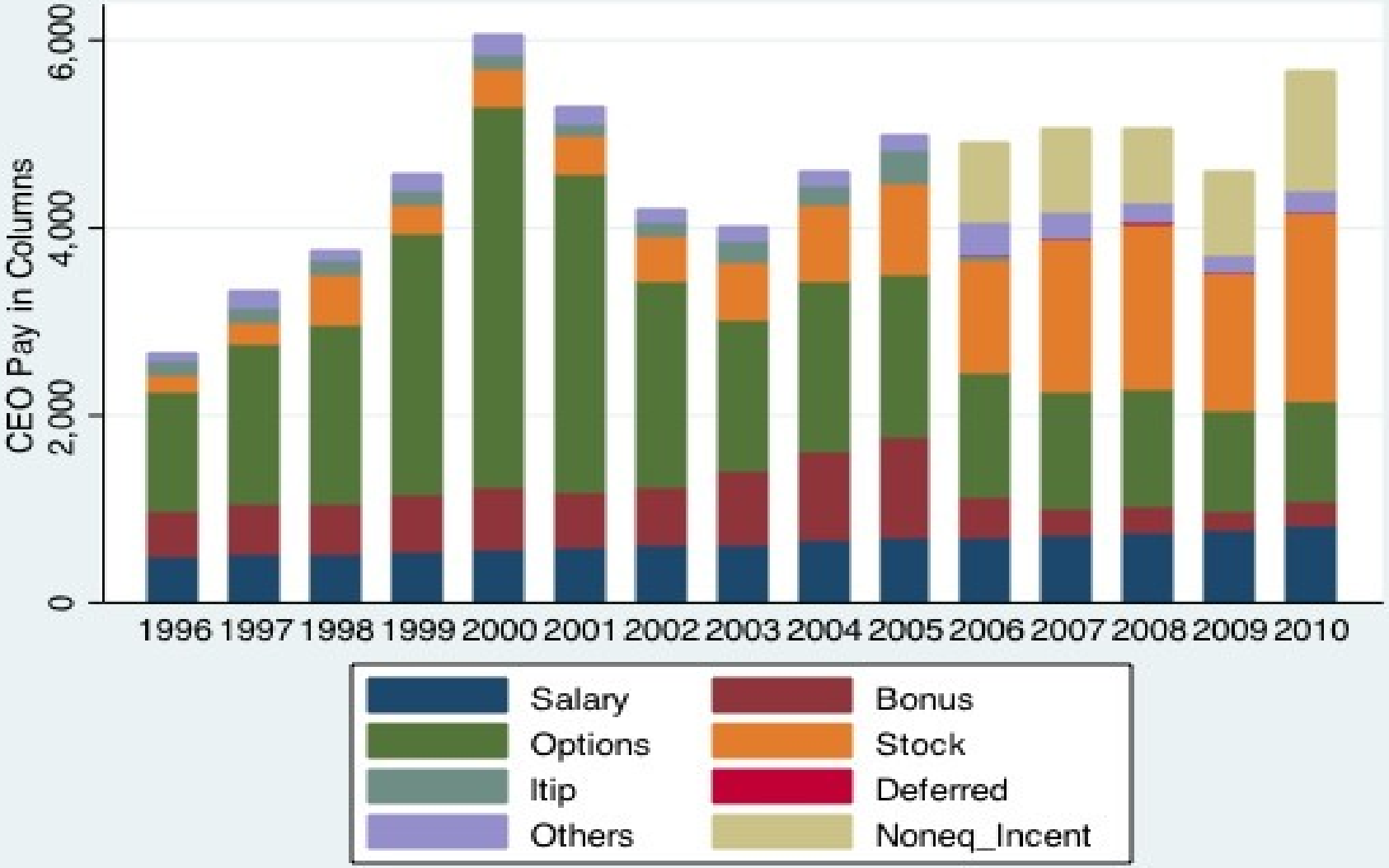
2- My view is that entry of China and India to world market and collapse of Soviet communism essentially doubled global labor force and reduced K/L in global economy

3- Piketty stresses continued rate of return of capital above growth of output.

4- Associated with institutional changes – weakening unions

5- Danger that rich dominate govt --> permanent inequality

Mechanism for huge top incomes in US is that firms link executive pay to capital income (as incentive).



2- The fears

1—Threat to Democracy: US historic view

2- Threat to social stability: Chinese fear

3- Feedbacks on well-being of majority. Inequality → inequality in health, mortality. Monbiot (Guardian, july 7, 2014) attacks centenarian studies for fear that this will produce a race of long-lived billionaires while poor persons die younger than now!

4- Loss of collective ability to respond to global problems – climate change; obesity; pandemic; natural disaster

5- Opportunity cost of failure to exploit massive increase in stock of useful knowledge to benefit society; instead technology to control us

US View: Huge Inequality in Market Earnings → Inequality in Politics → Govt by and for the Super-Wealthy

"We may have democracy, or we may have wealth concentrated in the hands of a few, but we can't have both" – Justice Brandeis
(note this is a multiple equilibrium model)

For the dynamics of the model

"He who has the gold gets to rule
He who rules gets the gold-- Machiavelli
(note this is dynamics for the model)

So we have the B-M Model

Founders of US feared inequality would undermine the American "experiment"

(Madison-Adams Theory → BMMA model)

If all power be suffered to slide into hands not interested in the rights of property which must be the case whenever a majority fall under that description … either they will unite … and become dupes and instruments of ambition, or their poverty and dependence will render them mercenary instruments of wealth**… In either case liberty will be subverted; in the first by a despotism growing out of anarchy, in the second by an oligarchy founded on corruption**.
--James Madison, Observations on the "Draught of the Constitution for Virginia," ca. Oct 15, 1788

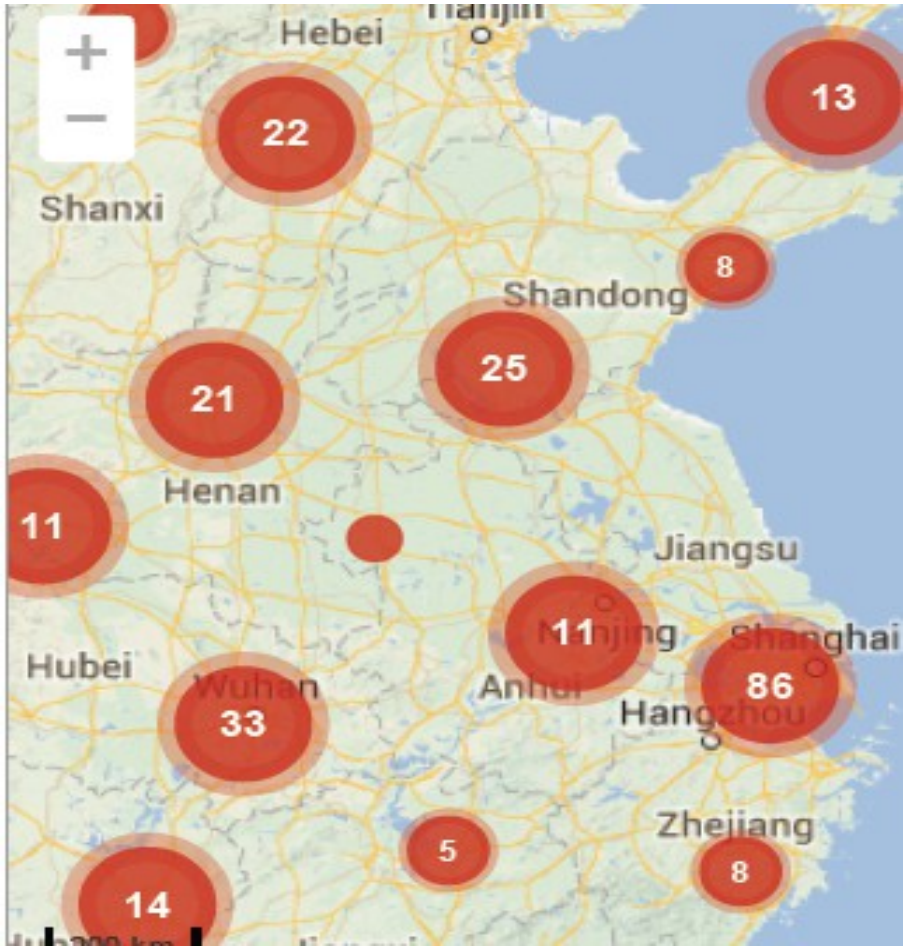
. The only possible Way then of preserving the Balance of Power on the side of equal Liberty and public Virtue, is to make the Acquisition of Land easy to every Member of Society: to make a Division of the Land into Small Quantities, So that the Multitude may be possessed of landed Estates. If the Multitude is possessed of the Ballance of real Estate, the Multitude will have the Ballance of Power, and **in that Case the Multitude will take Care of the Liberty, Virtue, and Interest of the Multitude in all Acts of Governmen**t. – John Adams, Letter to James Sullivan, May 26, 1776[i]

The Eisenhower Military-Industrial Complex speech Jan 26, 1961 updated for today's world

In the councils of government, we must guard against the acquisition of unwarranted influence by Wall Street and the super-wealthy in a highly unequal economy . The potential for the disastrous rise of misplaced power exists and will persist… Only an alert and knowledgeable citizenry can provide **the countervailing power to assure that the country prospers together.**

The prospect of public discourse controlled by an ideological communication media and the funding of research by foundations supported by the wealthy few is gravely to be regarded … public policy could itself become the captive of a wealthy elite who see the preservation of the status quo of inequality as the appropriate goal for the nation.

The China Fears



Strikes everywhere in China every day. Top right is Honda Strike in May 2010. Bottom is strike of IBM China workers for share of profits of sale of server mfg to Lenova in March 2014

Government Response

"if certain social and economic problems are not tackled without delay, the overall stability of the country could be threatened" Jiang Zemin 1998

Contract Labor Law of 2007 guarantees written contracts to migrant labor; Three every-wheres policy: every where a union, collective bargaining, a signed contract

Chinese Officials Rush To Sell Luxury Homes Amid Corruption Crackdown

Aug. 18, 2014, 10:05 a.m.
Real-estate agents say bureaucrats are selling homes at steep discounts.

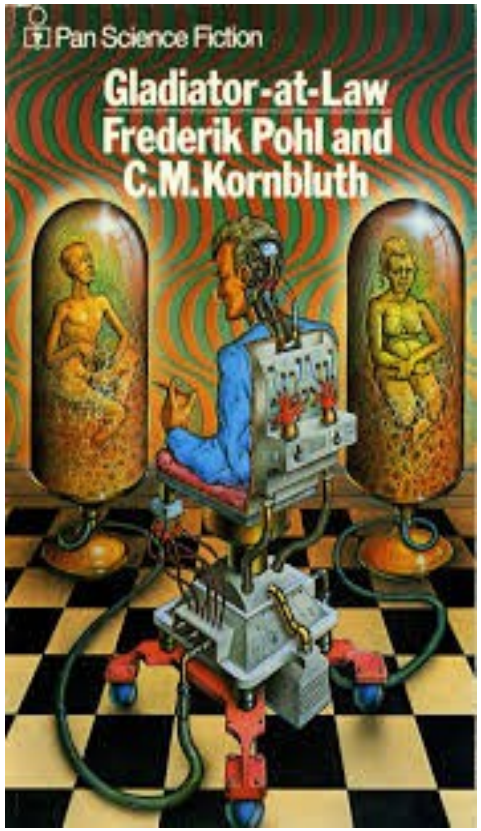
Objection to the BMMA Model

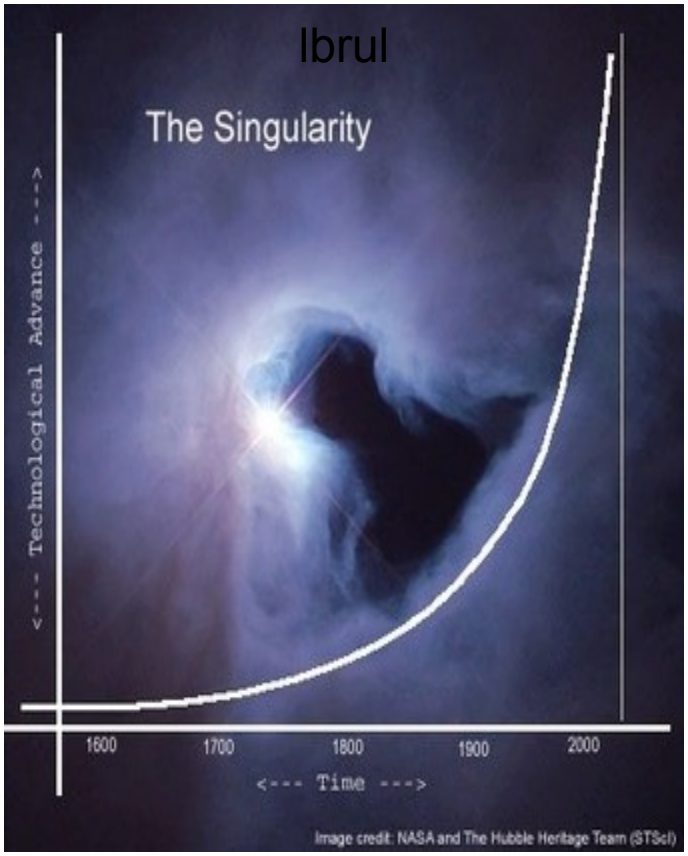
"I've never asked a prime minister for anything... I, in 10 years in his power there, never asked Tony Blair for any favors and never received any,"

Madison-Machiavelli Dynamics

"Every new regulation concerning commerce or revenue, or in any manner affecting the value of the different species of property, presents a new harvest to those who watch the change, and can trace its consequences; a harvest, reared not by themselves, but by the toils and cares of the great body of their fellow citizens. This is a state of things in which it may be said, with some truth, that **laws are made for the few, not for the many**. James Madison *The Federalist Papers*, 62

The Two BMMA Model equilibrium





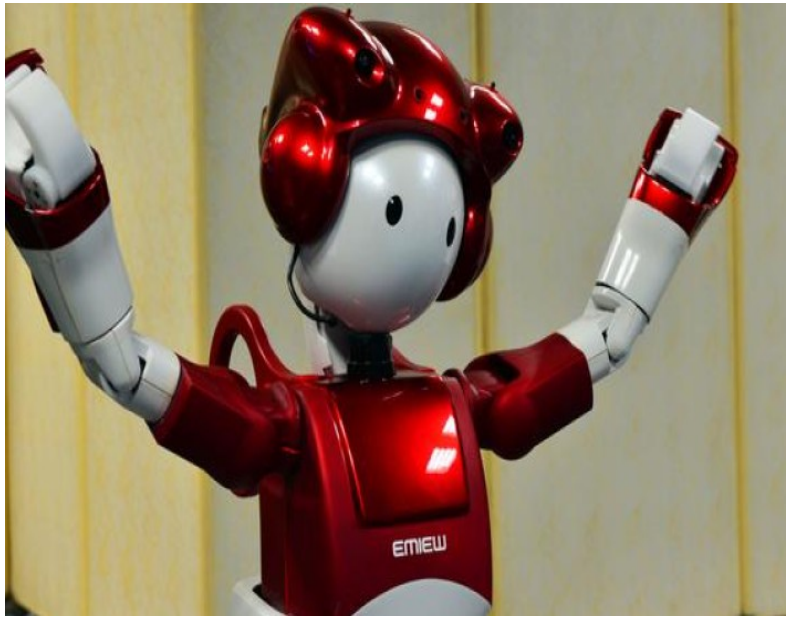
"We Fixed Mr. Lincoln's Wagon, Mr. Charlesworth"
"We did, Mrs. Green. And we will Fix Her Wagon too."

Johnathan Swift's Strulbregs
HG Wells

The Popular Media Version

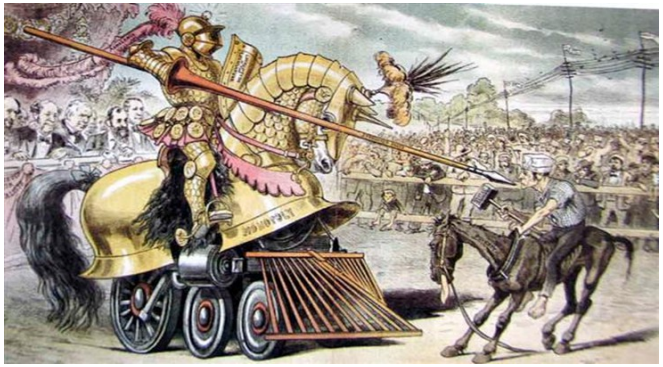
Who owns the robots rules the world

Workers can benefit from technology that substitutes robots or other machines for their work by owning part of the capital that replaces them



3. What Can We Do?

War of labor with capital?
Strong unions? Maybe in
Nordic countries but not elsewhere



Tax capital and govt redistribute tax receipts? Henry George's tax on land as fixed supply but today's capital is mobile.

Government ownership of natural resources; set up fund and pay out to average citizens. Norway and Alaska oil
But biggest stock of capital today is knowledge capital

Instead of trying to tax capital, increase workers' ownership of capital and capital income.

US Founders saw ownership as The Solution

Adams: “the only possible way of preserving…equal liberty…is to make the acquisition of land easy to every member of society”

Jefferson: “legislators cannot invent too many devices for subdividing property”

Hamilton: “the desire of being an independent proprietor in land is founded on such strong principles in the human breast”; “equality and moderation of individual property” would promote growth

Madison: “without violating the rights of property reduce extreme wealth toward…mediocrity

Lots of inclusive capitalism in US (but not yet enough to dent inequality)

% Employees	2002	2006	2010
Profit-sharing	33.50%	38.40%	
Gain-Sharing	23.20%	23.20%	
Own company stock	21.20%	17.50%	17.40%
Options	13.10%	9.30%	8.70%

- Workers ownership/profit-sharing is associated with employee involvement committees, teamwork; high performance work places. Compensation systems have group incentives, company-wide incentives, individual incentives.
- ESOP world: 10,900 firms, 10.3 million workers 40% more workers than private sector unions. 1 trillion market value, 97% in closely-held companies, mostly sales of family businesses to the ESOP.

“Preponderance of Evidence” says it is economical

Meta-analysis finds “two thirds of 129 studies [including performance and attitude studies] found favourable effects while one tenth found negative effects”. “Research on ESOPs and employee ownership is overwhelmingly positive and largely credible.”

2007 UK Treasury Oxera study to examine impact of tax breaks for *individual* employee stock ownership estimated production functions for 16,844 corporations with confidential financial information and found ownership increased value added per worker by ~ 2.5% in the long run.

Privately-held ESOPs are half as likely to go bankrupt or close as controls; are four times more likely to have defined benefit plan. Pension assets/employee significantly higher in ESOPs than in non-ESOPs

ESOP default on company stock acquisition loans of 1-2% annually lower than defaults of LBOs and private equity portfolios; BLS study of rates of return from 1991-2011 show ESOPs outperform 401k plans in most years, were less volatile, and mean performance is > all plans

Kruse, Freeman, Blasi NBER study of 41,000 worker reports in 14 firms found that worker co-monitoring helps overcome free riding because workers with a greater stake in performance monitor others more closely and intervene more to reduce shirking behavior. Workers perform better the greater the depth of the system. Increased employee attachment, lower turnover, more employee suggestions for improvements; works best with other "high performance" labor practices and policies.

Blasi, Kruse, Freeman, 2012 Great Places to Work study finds that of the 100 Top 17% have ESOPs, 10% majority employee owned,16% give options to most employees; those with more inclusive capitalism --> high performance work practices and worker; higher market to book value of assets 'Tobin's Q'. Sample captures 10% of total sales and total employment and 20% of market value of all publicly traded corporations in 2007.

Creme de la crème of Worker Ownership

CHARLIE MAYFIELD

Friday 4 July 2014

Employee ownership day 2014: Why this business model is good for the economy

The Chairman of John Lewis Partnership explains why businesses should be owned by their employees

A tale of two companies

Shared capitalism works at Wegmans and Cisco

Grocers at Wegmans and techies at Cisco profit from inclusive compensation systems and the higher profits these programs deliver. Wegmans Food Markets, Inc. is a family-owned, U.S. regional supermarket chain with about 37,000 employees in 75 stores in New York, Pennsylvania, New Jersey, Virginia, and Maryland. In 2009 Consumer Reports ranked it the nation's best large grocery chain. It was ranked 3rd on Fortune's "100 Best Companies to Work For" in 2010. Wegmans has profit-sharing for full-time employees and a host of benefits for part-timers as well as full-timers.[10] According to Fortune Magazine:

All that means Wegmans' labor costs run between 15 percent and 17 percent of sales, [industry guru Bill] Bishop estimates, compared with 12 percent for most supermarkets (the company declines to comment). But its annual turnover rate for full-time employees is just 6 percent, a fraction of the 19 percent figure for grocery chains with a similar number of stores, according to the Food Marketing Institute. Almost 6,000 Wegmans employees—about 20 percent—have ten or more years of service, and 806 have a quarter-century under their belts. The supermarket industry's annual turnover costs can exceed its entire profits by more than 40 percent, according to a study conducted by the Coca-Cola Retailing Research Council. When you understand that, you begin to see the truth in Robert Wegman's words: "I have never given away more than I got back."[11]

Cisco Systems, Inc, is one of the world's leading consumer electronics, networking, and communications technology and service firms, with over 65,000 employees. It is an archetype Silicon Valley high-tech multinational corporation, which at the height of the dot com boom had the highest market capitalization of any corporation in the world. It has been awarded "for the exemplary quality of their relationships with employees and communities," and appears regularly on the Fortune "100 Best Companies to Work For" list, ranking 16th in 2010. Its CEO, John Chambers, has spoken publicly about the importance of Cisco's broad-based incentive systems:

…On employee ownership…there's not been a single successful company in the history of high tech in the last two decades that has done that without broad-based stock option plans. When I originally heard about that in school, I would have called it socialism, when in fact it is the ultimate form of capitalism. It is a very effective way to align interests.[12] *I find it ironic that the United States invented the sharing of the success of the company with its employees very broadly, and now we have other countries around the world that beat us not only in education and infrastructure, but also in terms of employee ownership.*[13]

4. Roadmap from here to there

Has to be gradual, consistent with national attitudes and traditions, open to variety and experimentation; supported by firms and workers, encouraged rather than forced down anyone's throat. Tax breaks due diligence to potential for Gordon Geckos to exploit loopholes and use influence to preserve as much of the status quo as

Reforms for US

Add firms with broad-based employee ownership/profit sharing to those with preferred treatment in government procurement programs

Seed regional/state centers to provide information and training and to develop state-based policy ideas to facilitate private sector development of share plan

Reform governance of pension funds and pension fund ownership of shares

Expand tax incentives for spreading capital ownership --Lower estate tax for a retiring owner who sells to the workers (UK has just done this); require approved share plans for corporate tax incentives. Progressive capital gains tax, with lower rates for lower income citizens

Reform Internal Revenue Code 162(m) which subsidizes employee stock ownership and profit/gain sharing plans for top five executives by making deductions conditional on plans for all employees.

Sweden's *löntagarfonder:* wage-earner funds

First proposed in 1975 by Meidner to strengthen wage solidarity; enacted by Social Democratics in 1983 after employers reject it in bargaining. But "funds achieved little in terms of furthering economic democracy" (Pontusson and Kuruvilla 1992)

Why did it fail?

Anti-incentive: based on 20% profits tax from firms into union-controlled wage earner funds; designed to break the link between workers and their firms profits.

Plan highly politicized change

Weird local influence (50% of voting rights in firm delegated to employees/trade unions in company. Contrast to Drucker's pension fund socialism.

Firm-Based Swedish Capital Ownership

Leaf through Skanska's 200 page Annual Report 2013. By chance, stop at page 167-168 and you will find discussion of the firm's employee ownership program, and the changes made in the program

The ownership program is a share purchase scheme that covers employees, key employees and executives, where the company matches shares that individual purchase with one or more matched shares depending on group performance, with greater matches for key employees and top executives. In 2012 the Global Equity Organization gave Skanska the "Best Plan Effectiveness" award for companies with more than 30,000 employees.

Like most share purchase plans, the plan attracts some employees but not all who can benefit from it. Looking at it from the old LO goal of worker ownership, unions could bargain for a more progressive share ownership scheme that would attract more lower wage workers; and press other firms to develop plans that suit their economic situation.

V. Yes, We Can:

Summer 2014 Market Basket Protest, New England,

Who is Market Basket? family-owned New England Grocery (Rated #6 of 55 in US) using business model based on profit-sharing and good wages and low prices (rated lowest by one industry organization) in low/middle income n-hoods. Promoted management within. 25,000 employees, $4B in revenues

Battle for Control

Owned by Greek-American family with two warring sides. One ripped off the other years ago; court restored its 1/2. Arthur T runs firm with tiny majority. Epitomizes the company. But one family member shifts so cousin Arthur S. has control of board; gets huge income payment to shareholders. Then fires Arthur T. so family could maximize income and squeeze workers and customers. Senior managers refuse to work for new management, so they get fired. Truckers refuse to deliver products.

Workers/associates in warehouse refuse to move products to "scab" trucks. Customers announce boycott. Social media filled with support for Artie T. New management threatens more firings. Lays off part-timers. Holds job fair with promise of promotions. Virtually no one comes. Suppliers say bills are wrong (too high!). Major fish supplier refuses to sell. Governor asks workers to go back and let the owners settle dispute. Boycott/work

A sign sits atop mostly empty meat shelves at Market Basket in Haverhill, Mass. *The Associated Press*

Power to the workers: How grocery chain employees saved beloved CEO

Arthur S. agrees to sell for $1.6B Artie T borrows funds from finance sector and buys, returning amid jubilation. Workers start restocking and customers return. Everyone celebrates as if Red Sox/ Patriots/ Bruins/ Celtics win championship. "Biggest day in New England history since we defeated the Red Coats in the Revolutionary War"

Google market basket and see the mass of stories.

Market Basket employees at the Chelsea store clasp their hands as they watch a televised speech by restored Market Basket CEO Arthur T. Demoulas.

Lessons, if any for reducing inequality?

Proof that in right circumstances stakeholders have power to shape a firm without collective bargaining, support of unions, government. But need for share capital as ally.

If Market Basket workers and management succeeded in controlling direction of "their company", can others do same?

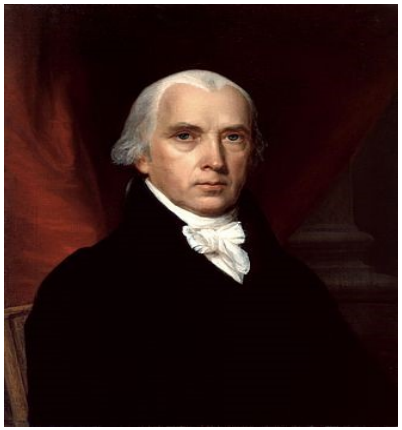
Will this spark employee/manager activism elsewhere? Spur more B-corporations, code of conduct ethics people in business to be more active?

If governments and international economic agencies truly view inequality as danger to economic well-being, they can start moving policy in a more inclusive capitalist direction.

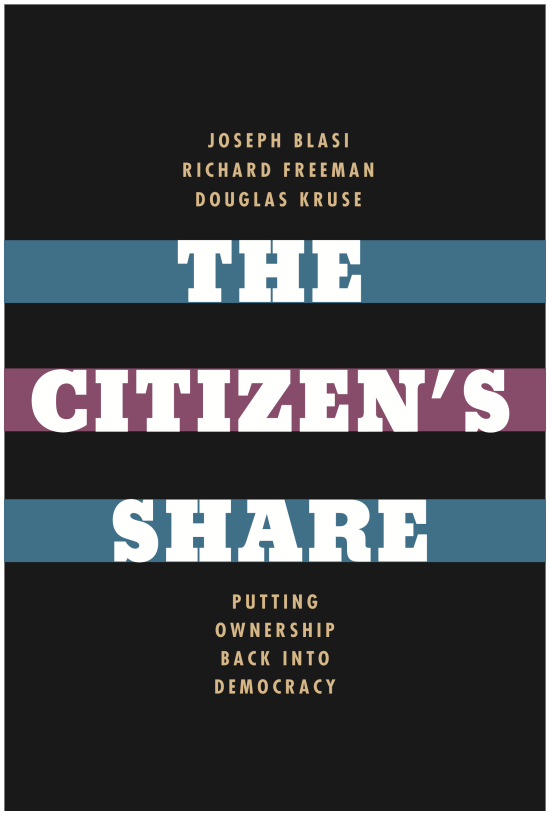
CONCLUSION

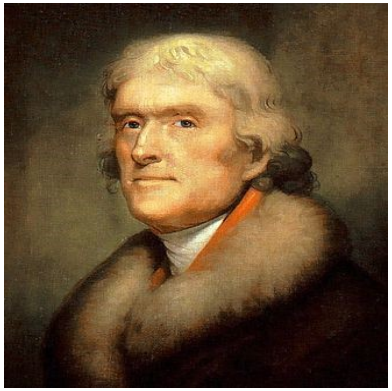
The dual meaning of equity: fairness and ownership.

To defeat the specter society must find way to combine the two meanings in society broadly and in places of work.



Oh yeah!





Go for it!