



## Commentary

Inequality, sustainability and Piketty's *capital*

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## ABSTRACT

In this article I address the implications of Thomas Piketty's book *Capital in the Twenty-First Century* for our understanding of inequality and sustainability, drawing upon Amartya Sen's capability approach, and the revival of classical political economy it brings. I argue that Piketty's contribution is a significant one which has the potential to lead economic analysis in a more fruitful direction. But its potential becomes much greater if its empirical analysis is combined with the revival of classical political economy undertaken by Sen and other authors, rather than with marginalist theory.

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## 1. Introduction

Thomas Piketty's (2014) book *Capital in the Twenty-First Century* provides a pioneering empirical analysis of inequality, which is a central theme for the contemporary world, and contributed to raise much public awareness of the problem. Piketty's contribution is, however, often interpreted in terms of marginalist theory. Piketty (2014, pp. 213–217) himself also draws upon marginalist theory when discussing the marginal productivity of capital. But marginalist theory poses strong constraints on our ability to discuss inequality, since it assumes that distribution must be determined by laws of marginal productivity. This is actually inconsistent with Piketty's own conclusions, which point towards institutional and political factors as the ultimate cause of inequality.

Moreover, there is also another way in which marginalist theory constrains our analysis, namely because of the presupposition that human beings are permanently trying to maximise their utility, since preferences, represented by a complete preference ordering, are taken to be non-satiated. These assumptions are problematic in face of growing empirical evidence from behavioural science (Martins, 2011a), and lead to the trivialisation of the notion of scarcity (since every good is assumed to be scarce when preferences are insatiable). Scarcity becomes no longer a property of natural resources, as it is the case for the classical political economists, but rather a property of every single commodity. Thus, the particularities and specificities connected to

ecological problems of scarcity become diluted within a theory which simply assumes that everything is scarce without focusing specifically on the scarcity of natural resources.

Furthermore, both themes, namely inequality and sustainability, are connected. In a world with finite resources, justice in distribution is a central theme to address when considering not only long-term economic and social sustainability, but also ecological sustainability. I argue here that Piketty's contribution can provide a fruitful route for discussions concerning distribution and the environment, once the constraints posed by marginalist theory are removed. As a replacement for marginalist theory, I will propose the adoption of Amartya Sen's capability approach, and the revival of classical political economy it brings.

## 2. Economic Theory, Sustainability and the Environment

Marginalist theory is the economic theory taught in every mainstream economics textbook, which typically explains human behaviour in terms of a utility function (and the associated notion of marginal utility), and explains the activity of firms within the economy in terms of a production function (and the associated notion of marginal productivity). It is typically assumed that human beings are never satisfied, and always want to maximise their utility. The use of utility functions leads to the attempt to mathematise human behaviour, and to unrealistic mathematical models that are criticised by Piketty (2014, p. 32).

There are other important implications that follow from the assumption that human beings are permanently trying to maximise their utility. Since it is assumed that human beings are never satisfied, and always want more, all goods are assumed to be scarce, since a finite number of goods are never enough to satisfy infinite preferences. This assumption has important implications for our approach to the environment,

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as I shall argue below. Before doing so, let me just elaborate briefly on the differences between marginalist theory, and the classical theory that was superseded by it in the course of the so called “marginal revolution” of the 1870s. Doing so will prove essential to understanding how the marginal perspective and the classical perspective lead to radically different approaches to distribution and the environment.

According to the classical perspective, as developed more recently by Amartya Sen (1999), human conduct is explained in terms of habit, custom and social norms. Furthermore, human well-being is understood in an Aristotelian multidimensional perspective, where the emphasis is on the attainment of a certain standard of living, defined in terms of basic capabilities that must be achieved by every human being, rather than on the maximisation of utility. The aim, according to the classical perspective, is to enable the reproduction of the economy and society in a way that provides such a standard of living to every human being – see Martins (2011b, 2013a, 2013b) for a discussion.

The classical authors focus on a certain subsistence level that is necessary for the reproduction of the economy and society. But such a subsistence level need not denote bare biological survival. As Sen (1999) explains, Adam Smith and David Ricardo note that the subsistence level takes into account not only the commodities that are essential for biological survival, but also the commodities and amenities that are essential for achieving a certain standard of living set by habit and custom, which depends upon the nature of society.

In the classical theory, wages must enable human beings to achieve the customary standard of living, and are thus set by the institutional, social, moral and political factors that influence the customary standard of living. The standard of living that enables us to achieve a given set of basic capabilities can be obtained with a finite set of essential commodities, purchased with wages set by institutional, social, moral and political factors. Those essential commodities, like the commodities used in order to produce them, constitute the basic commodities, which are essential for the reproduction of an economy that generates a given standard of living in society. The other commodities, which are not necessary for the reproduction of the existing economic system, constitute a surplus, which may be used in luxury consumption, or reinvested in the transformation of the existing economic system. The classical authors centred their analysis on the economic surplus, stressing the need of using the surplus in productive activities that on luxury consumption.

A very important point to grasp at this stage is that while the central notion of classical political economy is the surplus, the central notion of marginalist theory is scarcity. Thus, economic students learn in their first lessons Lionel Robbins' (1935) definition of economics, according to which economics is the science that studies the allocation of scarce resources. If they had studied at a time when classical political economy was the dominant doctrine, they would learn that economics is the science that studies the distribution of the surplus and its implications for socio-economic reproduction.

Piketty (2014, pp. 5–6) attributes to Ricardo what he calls the “scarcity principle”. But as Piketty (2014, p. 6) notes, Ricardo applied the “scarcity principle” to a specific case, namely land, and to the natural resources it possesses. According to Ricardo, the control of land and its natural resources enables the achievement of returns above normal profits, which generate a rent. An understanding of how those rents are generated and appropriated is an essential ingredient for the explanation of the exhaustion of natural resources. Piketty's (2014, pp. 537–538) discussion on taxation of rents on natural resources such as petroleum can be easily combined with this classical notion of rent, which denotes the part of the surplus above normal profits obtained through the use of scarce resources (which certainly suits the case of petroleum). As Piketty (2014, p. 6) also notes, it is not only oil, but also modern urban real estate that can be explained in terms of the Ricardian principle of scarcity of land.

For the classical political economists, scarcity is a notion used in connection with land, natural resources and rare goods, rather than every single commodity produced as in the marginalist theory. Ricardo

notes that the production of most goods exchanged in a market can be increased as long as we are willing to employ the labour necessary to do so. In marginalist theory, in contrast, all goods are assumed to be scarce. It could appear to be the case that a theory that generalises the notion of scarcity would be more adequate for the study of environmental problems. But in fact, the opposite is the case. The emphasis on scarcity in marginalist theory leads to the trivialisation of the notion of scarcity, instead of focusing on the scarcity of natural resources as the classical authors did. For the classical authors, scarcity is a specific property of some entities such as natural resources, and their approach to the problem enables us to focus our attention on the specificities posed by the scarcity of natural resources.

So the three dimensions of sustainability (economic, social and environmental) can be fruitfully addressed within the classical conception. The classical conception considers not only economic sustainability, by advocating the use of the surplus in productive activities rather than in luxury consumption, but also social sustainability, since the standard of living set by the wage is supposed to enable social sustainability given social habits and custom. Furthermore, the classical conception provides an analytical framework that can also be used to address environmental sustainability, by noting the scarcity of natural resources, instead of trivialising the notion of scarcity.

Clearly, there are radically different implications for our attitude towards the environment depending on the theory we adopt. Sustainable development in a planet with finite resources implies that human beings must consume a finite level of goods. By postulating insatiable preferences rather than assuming the need of adopting a certain standard of living obtained with a finite set of commodities, marginalist theory promotes a way of thinking where environmental problems are always external constraints, rather than taken into account in the internal structure of the theory.

In classical political economy, in contrast, the standard of living which corresponds to a given level of use of natural resources can be adapted to various situations within the internal structure of the theory. This also means that unlike marginalist theory, classical political economy does not assume that the level of wages is mathematically determined through laws of marginal productivity. Rather, the level of wages that leads to a given standard of living depends upon a series of institutional, social, moral and political factors, which can include environmental considerations.

### 3. The Cambridge Controversies in the Theory of Capital

If we assume distribution to be an endogenous aspect which depends upon mathematical laws of marginal productivity, as in marginalist theory, there is no room left to discuss alternative patterns of distribution, regardless of their implications in terms of justice and the environment. There is no room to discuss which distribution is compatible with environmental sustainability, or with a given conception of justice, unless we take distribution to be an exogenous aspect from the point of view of economic theory, subject to ethical and environmental considerations.

The fact that marginalist theory leaves no room to discuss alternative patterns of distribution, or its implications for justice, inequality, sustainability and the environment, is not a criticism of the theory in itself. If marginalist theory were correct, such a fact should only lead us to recognise that there is no room for ethical or ecological considerations concerning alternative patterns of distribution, since the latter are determined by mathematical laws of marginal productivity.

The problem, however, is that marginalist theory is methodologically and theoretically inconsistent. The methodological and theoretical foundations of the utility function have been criticised by Sen (1982), who called the utility maximising agent of mainstream economics a “rational fool”, while noting that it is not possible to reduce all causes for human agency to a complete preference ordering, represented by

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