Inequality and the case for UBI funded by sovereign money

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Introduction

The current economic system is generating increasing inter-personal inequality in income and wealth. This is well documented by several observers, including others in this collection of essays, such as James Galbraith, and not least Thomas Piketty in his two books and on-line database (Piketty, 2014; 2020). I therefore don't intend to rehearse the data analysis of inequality in this brief paper, but to take it as a working assumption. My aim rather is to locate causes of inequality, and to consider whether universal basic income (UBI) can claim to alleviate inequality (for background see Crocker, 2020). The main focus for evidence is the UK, but the issues generalise.

Contexts of inequality

For our purposes, income inequality arises:

1. between those employed and unemployed
2. within employment
3. between those unemployed.

Causal variables for income inequality can be proposed, researched, analysed, and potentially mitigated. Wealth inequality is a more random outcome, arising from huge financial success within a lifetime, or resulting from inter-generational inheritance of extremely concentrated wealth holding through aristocratic or meritocratic social classes. Prior to the coronavirus crisis, unemployment was remarkably low in many developed economies, but low wage rates were pervasive, leading to in-work poverty. Employment no longer guarantees income sufficiency. Huge and growing inequality has become endemic between CEOs and other top earners, compared to low wage earners.

Various causes of this rise in inequality have been suggested (see other essays in this collection). The main *political* explanation is that capitalism is essentially exploitative of labour. The power balance has seen a huge shift in favour of capital, and a reduction in labour bargaining power. The specific cause of the power shift is not clear, but a progressive step in the historic stage of capitalism is assumed. According to this diagnostic, the remedy is therefore political, focusing on a return to trade union bargaining power, job guarantees, and high redistributive taxation on top incomes and wealth.

The *technology* explanation (see Crocker, 2012) is that productivity has inevitably reduced the wage share of output. Wage becomes insufficient for personal economic well-being, leading to poverty. Aggregate demand becomes deficient in the macroeconomy, raising household

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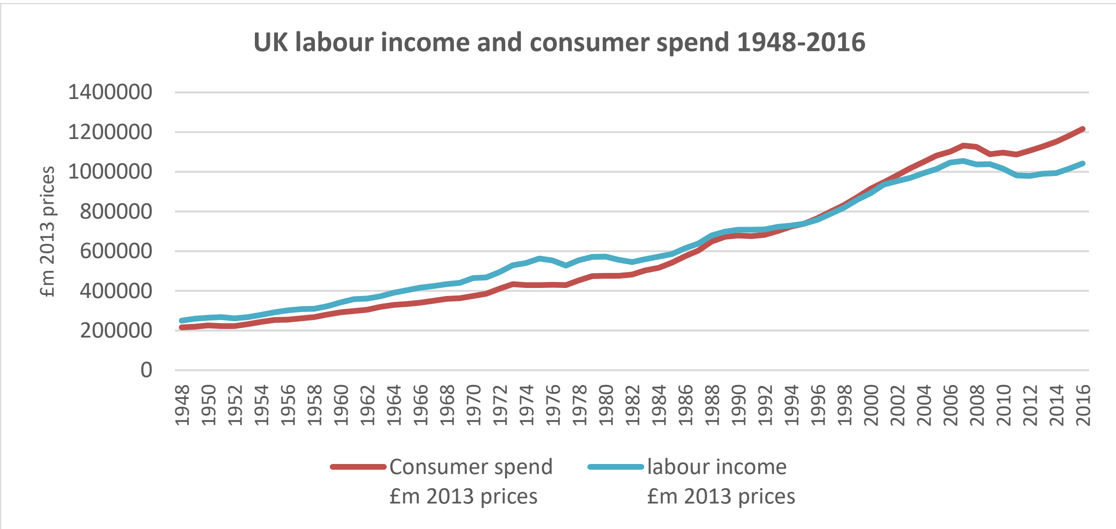
borrowing, thereby leading to crisis. As earned income declines relative to output, so unearned income necessarily rises. This takes four main forms of pensions, dividends, welfare benefits and household debt. The increase in the share of unearned income further drives inequality, since between these sources of unearned income, pensions and dividends are privileged with secure growth, whilst welfare benefits are constrained by austerity, and low-income households bear unsustainable debt, serviced at the punitive interest rates of payday lenders. If the technology explanation for inequality is correct, then apart from resisting technology, which supposes a view on the philosophy of technology that it is subject to human agency, the remedy has to be other than high-wage full employment.

Put another way, if the cause and result of inequality can be adequately countered by high-wage full employment, then well and good. The worry is that technology has hugely weakened both employment and wage as a tool to ensure inclusive economic well-being. Political and technology explanations for inequality are, however, not necessarily incompatible. If technology does reduce labour demand, then labour bargaining power is thereby weakened. In paradigmatic terms, Marx in his 1847 *Poverty of Philosophy* observed that technology can thus drive the political power structure; writing "the hand-mill gives you society with the feudal lord; the steam-mill society with the industrial capitalist". Data definitively shows a huge secular reduction in working hours throughout the 20th century. If the tide of technological automation is at least partly irresistible, then no amount of labour bargaining power can mitigate its effects on reducing the labour share of output. We, therefore, *have to ask* whether income, rather than employment wage, is the more appropriate corrective to inequality, and whether UBI can fulfil this role. This can be approached in terms of a series of logical steps.

1. A long term steady state reduction in earned income against consumer expenditure

There is an undeniable inexorable long-term trend for labour income to decline as part of consumer expenditure. For example, Exhibit 1:

Exhibit 1 UK Labour Income and Consumer Expenditure 1948-2016



Source: UK ONS (note that ONS define "Labour income"=wages + self-employed income) with thanks to David Matthewson and other staff at ONS for valuable help in defining and interpreting UK income data streams.

In the UK, from 1948 to 1995, labour income was sufficient to meet consumer expenditure, but from 1995 onwards, labour income became insufficient to fund consumer expenditure, which is now increasingly funded by a growing proportion of unearned income.

2. Inference to best explanation prefers the technology hypothesis

Since there is a long term trend of labour income decline as a proportion of consumer expenditure, and this trend persists throughout the period through various regimes of changing trade union power, then a more continuous causal explanation is needed. Whilst there is significant dispute in economics and political economy about the *role* of technology, technology remains the preferred hypothesis as the underlying fundamental influence, i) since it is clear from *a priori* arithmetic that higher productivity will reduce the wage content of output, and ii) because technological innovation has continued unabated throughout the whole period. It is possible however, as a secondary phenomenon, that the rate of reduction in the labour income share was retarded in periods of high labour bargaining power. In the UK case, the argument would specifically be that the labour share reduced at a higher rate from 1980 with the advent of the Thatcher government, which legislated reduced trade union power. Also possible is the hypothesis that “globalisation” (or at least the many factors we associate with this term) has reduced UK labour income per unit of output in the period since 1995. The pattern may vary between countries but the trend remains significant.

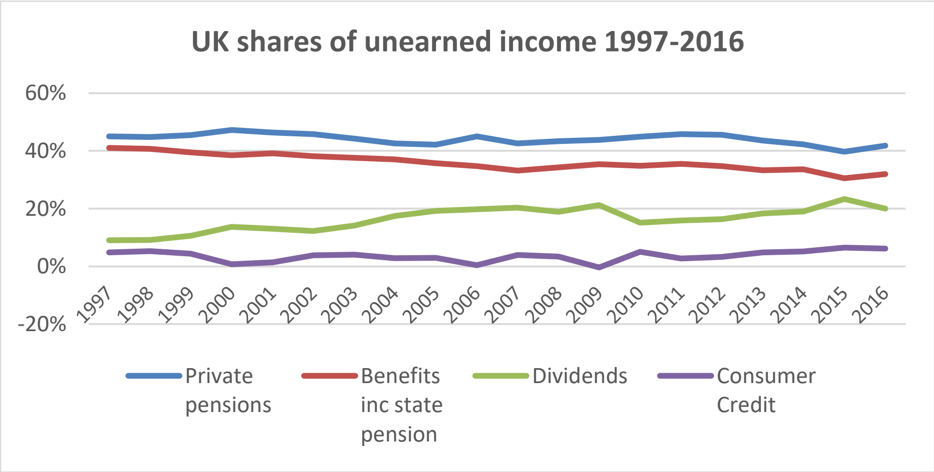
These alternative hypotheses are being tested in a research project *The Economics of Basic Income* at the Institute for Policy Research at the University of Bath UK.[2] As noted earlier, one feature of the labour market is that it is bifurcated between senior executives, highly skilled professionals, and more functional roles, sometimes disparagingly referred to as “bullshit jobs”. It is not that senior executives have greater representative bargaining power, but that they are equipped with skill sets valued in relation to technology. This observation therefore reinforces technology as the preferred explanatory factor of inequality in employment. As much of the material on a “fourth industrial revolution” and “industry 4.0” claims, this is an advantage which may not last long for skilled professionals, as more of their role is threatened by sophisticated automation and the application of artificial intelligence. We therefore see that unearned income is increasing within consumer expenditure, and in analysing the components of unearned income, we now find that there are changes in the component shares of unearned income which are also driving inequality

3. Changes in the component shares of unearned income are further driving inequality

The composition of unearned income has changed significantly over the last 20 years in the UK. Private pensions and consumer credit have accounted for relatively stable shares of unearned income as Exhibit 2 indicates.

[2] See, IPR, University of Bath “The Economics of Basic Income” www.bath.ac.uk/projects/the-economics-of-basic-income/

Exhibit 2 UK component shares of unearned income 1997-2016



Source ONS

The notable changes have been that:

- Welfare benefits including state pension have reduced from 41% of unearned income to 32%.
- Dividend income has increased from 9% to 20% of unearned income.

Wages and benefits have been relatively displaced by dividend income in the UK economy, perhaps partly due to self-employed earnings being redefined as dividend. This has fuelled inequality as higher income shareholders and pensioners benefit at the expense of lower income wage earners and benefit recipients.

The general point is that unearned income is increasingly “necessary” in the macroeconomy, but unearned income itself is driving inequality through shifts in its components. As a form of unearned income, Universal Basic Income (UBI) therefore needs to be defined to achieve greater income equality.

4. Basic income is the preferred form of unearned income

The worrying component of unearned income is annual new household debt. This rose to £166bn in the UK 2004. Its unsustainability against the same low wages which had required it, led to the 2007 economic crisis. Numerous subsequent contributions in political economy argue that household debt feeds inequality, not least because much of it is advanced to low income households at premium interest rates, (e.g. Montgomery 2019).

Since unearned income is demonstrably *necessary* in contemporary high technology economies, then the preferred variant of this unearned income is a basic income paid unconditionally and universally to all citizens (UBI). This is because:

1. UBI avoids the demeaning intrusion of means-tested welfare benefits.
2. UBI, therefore, has the lowest administrative cost of any welfare system.
3. UBI is effective since it has an automatic 100% take up rate, compared to current welfare benefits, especially those targeted to elderly people which have low take up rates.
4. Most importantly, UBI avoids the unemployment and poverty traps of current welfare benefits which are withdrawn when a recipient takes work, whereas a basic income is retained, thus removing any disincentive to work.

Clearly, the question then arises as to *how* a substantial level of UBI can be funded. There are many different funding proposals, but the most attractive is a sovereign money system.

5. The technology hypothesis requires unearned income and sovereign money

Many advocates for UBI (e.g. Torry. 2013) propose schemes which are revenue neutral and therefore funded by increased taxation and/or reduction in other areas of government expenditure, including reducing or eliminating current welfare benefits. Marginal socio-economic change results from such conservative funding schemes, encountering the objection that UBI is either too small to be meaningful, or too high to be affordable. Other proposals to fund UBI from wealth taxes or pollution taxes encounter operational difficulty. For example in taxing the many forms of wealth, or in relying on pollution taxes which are designed to achieve better environmental outcomes and so become self-cancelling. A more radical funding concept is needed to achieve a substantial UBI to reduce inequality.

At present, government expenditure and money creation are funded by the sale of interest-bearing government bonds. This accumulates mountains of national debt, equal to or greater than annual GDP in many economies, and therefore in reality, unrepayable. However, the interest cost of this debt is substantial, amounting to £39bn annually in the UK. This seigniorage is paid from general taxation to privileged bodies in the financial sector and is therefore likely to increase inequality.

A thought experiment shows how basic income is necessary in high technology economies. In a totally automated economy with neither labour nor wage, output would be distributed by annual government vouchers, destroyed and renewed each year. In this paradigm, 100% of GDP becomes basic income, funded 100% by sovereign money. The vouchers represent both basic income and the sovereign money which funds it. Whilst we have not and may not ever reach this extreme of automation, nevertheless there are strong elements of this effect in our contemporary high-tech economies. A nuanced hypothesis is therefore that high-tech economies require some degree of UBI funded by sovereign money. As such, UBI would be necessarily funded by debt-free sovereign money. Since sovereign money is not interest bearing, it removes the inequality in the seigniorage of money creation by the sale of government bonds, which is currently set to rise by a further £645bn in the UK economy to fund response measures to the coronavirus epidemic. There is no reason why this funding cannot be by debt-free sovereign money.

6. How UBI reduces inequality

In a simple sense, one might think UBI *must* gradually increase equality in a society of unequal incomes, since it is a payment of the same amount made to all individuals. However, this depends on how great the UBI payment is, and how it is funded. If it is funded to be revenue neutral by increasing top level taxation, then it will reduce inequality, though less so than the same funding applied as a targeted welfare benefit transfer payment. If on the other hand it is funded exclusively by reducing welfare benefits, then inequality will almost certainly increase. Indeed, some versions of a UBI scheme have been shown to increase child poverty, so that very careful UBI scheme design is needed to ensure the preferred balance of winners and losers compared to current income outcomes. If UBI is funded by debt-free sovereign money, then income inequality will reduce, although probably only marginally.

What debt-free sovereign money would enable is the reversal of austerity cuts to the value of full potential output GDP, the latter constraint ensuring a non-inflationary outcome. This would more definitely reduce inequality by the restoration of welfare spending cuts, whether these are re-instated as means-tested benefits, or preferably, as UBI. Clearly, this requires a huge paradigm shift away from current financial orthodoxy, which insists that government budgets should balance, that government expenditure must be accounted as revenue or debt, that money is real and cannot be created or destroyed, and that government financial balances determine economic affordability. Modern Monetary Theory (MMT) is one way to think differently about the potential (see Fullbrook and Morgan, 2020). MMT insists that sovereign states can create money (e.g. Ehnts, 2017). Exact propositions differ between:

1. MMT advocates who invoke sovereign money to fund Job Guarantee, Green New Deal, and US Medicare for All proposals (e.g. Kelton 2020). In this interpretation, sovereign money remains balanced in double-entry accounting as interest-bearing debt. The proposal is that the debt is manageable because it is itself balanced by surpluses in the other two financial sectors of the economy according to the “Godley identity” (see Godley and Lavoie, 2012, however see Teixeira, 2012).
2. Sovereign money advocates, who propose shifting *all* money creation from commercial banks to the state central bank, to avoid excessive lending creating economic crisis, and to return seigniorage to the state (e.g. Huber, 2017)
3. UBI advocates who argue for sovereign money to fund UBI and a reversal of austerity cuts (Crocker, 2020). In this definition, sovereign money is simply issued without any associated sale of government bonds, assumption of debt, or payment of interest.

Recall that in our previous thought experiment, a totally automated economy operating with 100% GDP as basic income, has the option to implement total equality by allocating all individuals the same annual income. This is where the prefix “basic” has meaning and force. The practical question then remains as to how to design a basic income scheme such that everyone has a reasonable standard of living enabled by natural resources, the deployed technology, and the inherited infrastructure, whilst leaving scope for extra personal initiative and skill to generate more individual income.

UBI has been piloted, though never thoroughly implemented at macroeconomic level as a truly universal unconditional scheme. Various pilot projects in Brazil, Iran, Namibia, India and Finland have been extensively reviewed (Torry, 2019). The Finnish pilot project found little effect in the labour market, but reported a general increase in well-being associated with the guarantee of a secure income. The problem with microeconomic pilot schemes is that they tend to report a positive response to secure income, which is hardly unexpected. Community response depends on what alternative welfare benefit schemes are already in place in any specific country. Hence Nordic communities with high current welfare provision are less interested in UBI than Eastern European communities where current welfare provision may be negligible. Since pilot projects can only test temporary basic income with limited coverage, they can never report on the macroeconomic effects on aggregate demand which are a main driver of the case for UBI. Pilots take several years and delay the macroeconomic UBI which is more urgently needed - the current pandemic only serves to underscore this.

Conclusion

UBI is proposed as a human right, a fundamental *equality*. As Guy Standing (2010) has argued, we all have certain "birthrights", including to the benefits of commonly inherited infrastructure and technology. Current levels of inequality in income and wealth fail to recognise and respect fundamental human worth and dignity. Today's economic system is delivering inequality, poverty, even in-work poverty, low pay, pervasive debt, austerity, ecological damage, and crisis. This is in the *richest* countries in the world in a system that likewise harms even as it "develops" the rest of the world (see for example Wade's essay in this collection). The system needs a radical re-think and re-engineering. UBI and sovereign money are key to this re-definition.

Detailed UBI scheme design must then ensure that inequality is reduced by its implementation, since this is not necessarily so. Sovereign money makes a meaningful level of UBI affordable, and also enables the restoration of austerity cuts, the latter possibly proving more effective than UBI alone in reducing inequality. Sovereign money and UBI in combination are mutually reinforcing and more than additive in their effect, invoking Aristotle writing in his "Metaphysics" that "the whole is greater than the sum of the parts".

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