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Should Bill Gates be Allowed to be so Rich?

Function and Justification of Individual Wealth in Economic Paradigms from Classical Economics to Neoliberalism.

Abstract

What is the economic function of individual wealth in economics? How is wealth assessed and justified in economic theory? Is there any necessity or legitimation for the fact that the richest man in the world owns assets worth more than $80bn? There are quite different views in economic theories on this issue. The authors of classical economics used to have a largely ambivalent view of the wealth of individuals. They were critical of wealth if it was used for excessive consumption and not for accumulation purposes. Today economic theorists are searching in vain for a systematic approach to manage wealth. Normative distribution questions are generally not asked in economics. This paper examines several economic theories and shows what changes wealth has been subjected to over the course of time.

Key words

Classical political economy, utopian socialists, marginalism, neoliberalism, moral philosophy.

JEL classifications

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1. Introduction

The issue of the causes and consequences of wealth and poverty has always preoccupied humanity. For the philosophers of ancient Greece, the problem of fair distribution was already of high significance. Several thinkers of the Middle-Ages, the pre-classical economic authors, and above all the authors of classical economics have continued to write about the social question, which was mainly about the origin of wealth for a few, alongside great poverty for many. Although wealth in its various guises is omnipresent in today's world, individual wealth does not de facto play any role as an independent economic category in modern economic theories. In current economic literature, individual wealth is at best a statistical variable in empirical analyses of income or wealth distribution.[1] In fact, economic theorists are searching in vain for a systematic approach to manage wealth. The dominating neoclassical paradigm prefers to leave this subject to sociologists or philosophers. One of the reasons for this is that economics sees itself as a positive science, meaning that normative distribution questions are usually banned from economics as a research topic today. A second reason is that, from a theoretical point of view, the "distribution issue" seems to be solved in neoclassical theory under the assumption of perfect competition. As the present paper shows, this has not been the case in other economic paradigms.

A possible misconception should be avoided at the outset: when economists speak of wealth nowadays, they are often not referring to individual wealth as the term is used in this paper. Instead, they usually have in mind the wealth of a nation as measured by the aggregate income of its inhabitants, for example in the form of gross domestic product (GDP) per capita. This definition of wealth uses a flow in the denominator. Wealth can, however, also refer to the property of large companies, i.e., to a stock of assets. In this paper, the term wealth may refer to affluence in income or to affluence in assets. Al-though there is a large conceptual difference between income and assets, there is a systematic nexus between them. Except for a few specific cases, it can be assumed that individuals with a large amount of assets also have a large income, and vice-versa. Therefore, in the following the difference between affluence in income and affluence in assets will only be made if it is absolutely necessary in the relevant context.

For the analysis of the economic theories to be studied here, the following questions will be addressed: First, what economic function does individual wealth have in each theory? Second, how is wealth assessed in the different economic theories? And finally, should individual wealth be limited or reduced at all, and if yes, in what way and to what extent?

[1] The investigation by Spannagel (2013) shows the difficulties that even empiric investigations are already facing in the operationalisation of the concept of wealth.

In order to answer these questions, the paper is organised as follows: First, two significant Greek philosophers are introduced, as their opinions of capital, interest, and wealth influenced many subsequent generations until the 19th century. The Scottish moral philosopher and economist Adam Smith as well as certain other representatives of classical economics of the 18th and 19th centuries are discussed in more detail, as they offered many, often fruitful thoughts on the function and assessment of wealth. Certain central views of the utopian socialists and Marx are presented. In the fifth part, we shall turn to the marginalist (neoclassical) theories, which have formed the dominant economic paradigm until the present day. Finally, certain rather value-oriented or political-economy-based opinions from economic liberalism or neoliberalism on the subject shall be presented. The paper ends with several concluding remarks.

2. Wealth, Capital, and Interest for Plato and Aristotle

2.1 Plato

The Greek philosopher Plato (427–347 B.C.) offered his view of an ideal state under realistic conditions in his late work, the *Nomoi* (Laws). Ethical norms and the fairness of distribution played a significant role in this vision. Private property and individual wealth were included in his concept of the state, but he disapproved of the striving for riches. Plato warned emphatically against the consequences of individuals having too much wealth, as this would lead to a moral decline in society. Furthermore, individual wealth would be accompanied by a corresponding political power, with unlimited power leading to corruption and eventually tyranny (see Kurz 2016, pp. 7-8). Plato also recognised the social volatility that stems from the simultaneous existence of deep poverty and excessive wealth. He therefore called for a suitable limitation of income and assets:

> “In a state which is desirous of being saved from […] faction and distraction […] there should exist among the citizens neither extreme poverty nor, again, excessive wealth […] Now the legislator should determine what is to be the limit of poverty or of wealth.” (Plato 360 B.C., 5th book).

Plato even gave a concrete limit as of which he considered the wealth of an individual too large and recommended redistribution if this limit was exceeded. For him, a fair society was characterised by the property of the wealthiest not exceeding four times the property of the poorest.

> “But if a person has yet greater riches […] give back the surplus to the state, and to the Gods who are the patrons of the state” (ibid.).

Plato did not just reject wealth in its own right, as of a certain magnitude. He criticised even striving for profit. He equally condemned the demand for interest in loan transactions of any type. Plato saw the existence of interest as usury – an opinion shared after Plato for centuries, especially in early Christian teachings like the so-called Scholastic schools as well as by representatives of various economic schools of thought up to the present day.

2.2 Aristotle

In his *Nicomachean Ethics,* Aristotle (384–322 B.C.) addressed the issue of distribution fairness. For Aristotle, when establishing prices, ethical norms should be applied with the aim of ensuring a fair distribution of wealth and privilege. Furthermore, Aristotle brought attention to the issue that can arise from collective property, with citizens feeling no responsibility for the communal property, and everyone striving to live at the cost of the community (the free-rider problem). Aristotle approved the right to private property due to the natural human disposition, but he rejected the pursuit of profit and individual wealth. He despised chrematistics (from “chrema”, Greek for money) the “unnatural acquisitive art” of wealth acquisition, since it is only the acquisition for acquisition’s sake. In a sense, it is the counterpart to the “natural art of wealth acquisition”, of which the goal is the production and distribution of goods for the citizens, to allow them to live well (see Kurz 2016, pp. 8-10). Chrematistics, on the contrary, was “unnatural” because the accumulation of money for its own sake does not have an end and is therefore incompatible with a good life. In Aristotle’s view, the citizen’s motive for action should not be the acquisition of money, but the striving to satisfy the needs of the members of society as well as possible. Aristotle also considered interest as an expression of usury; interest was supposedly the source of the accumulation of money, which was sterile, however, as money cannot have any progeny.

Both, Plato and Aristotle, strongly influenced Adam Smith’s views on wealth, as we will see now.

3. Wealth, Capital, and Income in Classical Political Economy

The principles of growth and distribution were the main research topic in classical economics, with ethical and moral considerations tightly linked to the discussion of economic issues. This particularly applies to Adam Smith.

3.1 Adam Smith

3.1.1 Function and Assessment of Individual Wealth

Adam Smith (1723–1790) had an ambivalent view of the wealth of individuals. On the one hand, as a moral philosopher he considered individual wealth with scepticism, as it led to waste, greed, vanity, and similar manifestations. On the other hand, for Smith and in general in classical political economy until Marx, wealth had a central economic function for the growth dynamic of an economy, as long as it manifested in the accumulation of productive capital. The wealthy shareholders (not, however, the unproductive landowners!) had the decisive role of the development of the economic dynamic. We shall first observe the functional significance of wealth for Smith and then turn to his more ethically motivated assessments.

Adam Smith frequently showed his worry about how grim the situation of the workers of his time had become. His political economic credo for solving the social problem was: economic growth! The situation of the working population would only gradually improve and extreme poverty could only be solved in the long term through a market economy, a governmental and social order capable of initiating a dynamic economic process.

The central topic of Smith's *Wealth of Nations* is the question of the sources and conditions of economic growth. The division of labour and the accumulation of capital are the decisive preconditions for this, according to him. Through the accumulation of capital, a self-reinforcing feedback mechanism can be started: The striving of shareholders for profit leads to the accumulation of capital, which again allows more division of labour. More division of labour leads to an increase in productivity and income per capita – especially capital income, which in turn then leads again to a greater accumulation of capital, etc.

Wealth is viewed positively by Smith and the other representatives of classical political economy, if its owners use it to realise their potential capacity as dynamic driving forces of the economic system. This is the case if wealth is not spent on (unproductive) consumption, but is saved and accumulated. The reason is that for Smith, as for most of his contemporaries, saving was always equal to investment.[2] The central economic function of the shareholder in the classical system was to generate accumulation and growth. Marx (1867-1894, vol. 1, ch. 24, p. 418) expressed this with irony in the well-known quote: “Accumulate, accumulate! This is Moses and the Prophets!”

The situation is completely different, however, if wealth is not used for accumulation purposes, which is especially the case for landowners. In the Middle Ages, wealth consisted almost entirely of land. For the physiocrats, agriculture was the only source of value creation. It justified the wealth of the landlords and legitimised their dominant social position. Smith, on the contrary, was fundamentally critical towards landowners – and these were essentially members of the feudal nobility. According to Smith, the wealth they had accumulated over the course of many centuries and which they had inherited generation after generation was mostly used for unproductive consumption.

Capital owners as well, however, could use their capital for the “wrong” purposes. Starting in the 14th century, in parts of Central Europe considerable amounts of financial assets were being gathered outside of the nobility. These arose out of trade, then later out of slavery and the earliest factories. The possibility of accumulating large assets was lastingly accelerated through the existence of paper money, introduced in France at the beginning of the 18th century. Soon afterwards, the traditional luxury of the nobility was “taken over by the representatives of the republican State and the industry” (Pöll 1981, p. 11)[3]. The spread of wealth went hand in hand with the rapid spread of luxury consumption in the 18th and 19th centuries, when capitalism was developing at an ever-increasing speed (see ibid., p. 12).

Inspired by similar ideas from the physiocrats, Smith introduced the differentiation between productive and unproductive labour into classical economics, an idea that was intensively debated up until Marx. Workers making goods that can be accumulated are productive workers according to Smith. On the contrary, workers are unproductive if they do not contribute to the accumulation dynamic of an economy. Aside from “servants of the state” (officials, soldiers, ministers), this also included servants of the upper class, who – expressed in today’s terminology – provided personal services (see Krämer 2017). The expenses of the rich for their servants were unproductive consumption for Smith, as they thereby “consumed” the capital:

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2 The ex-ante identity of savings and investment has become known as “Say’s law” (Say 1803) and set as precondition for the goods market by most classical economists. Keynes only showed later that this identity is not obligatory in a monetary economy. Malthus and Sismondi had already made similar arguments.

3 Own translation of the original.

> “That portion of his revenue which a rich man annually spends is in most cases consumed by idle guests and menial servants, who leave nothing behind them in return for their consumption.” (Smith 1776, S. 338).

In order for growth to be generated, according to Smith it was on the contrary necessary that the rich not consume too much, but save enough for their income to be put to a productive use. For him, only consumption for productive purposes led to growth:

> “That portion which he annually saves, as for the sake of the profit it is immediately employed as a capital, is consumed in the same manner, and nearly in the same time too, but by a different set of people, by labourers, manufacturers, and artificers, who reproduce with a profit the value of their annual consumption.“ (Smith 1776, ibid.).

Hence, his idea was that the decisive factor was the final purpose of the accumulation of assets and thereby wealth. In Smith’s system, capitalists have an important social function to fulfil. Through the accumulation of (real) capital, they develop the productive basis of the economic system and thereby create material and social progress, leading to a “wealth of nations”. They thereby fulfil, unintentionally and for motives actually disposed otherwise (personal use, striving for profit), a purpose for the good of all. These unintended consequences were emphasised many times by the classical economists since Mandeville’s (1705) *Fable of the Bees*, and directed their findings (see Streissler 1981, Kurz 2012). In the classical system, capital owners and their wealth are seen as unintended vicarious agents for general *social* progress. If it is profit, greed and striving for wealth that contribute to maintaining the growth machine, then in principle Adam Smith has nothing to say against wealth.

As a moral philosopher and part of the Scottish school of enlightenment, Adam Smith, however, had a critical view of the striving for wealth in its own right. In this respect, he was (still) in the tradition of the ancient Greek philosophy of the Stoa and of Christianity. According to his view, it was also inappropriate to equate wealth with happiness (see Kurz 2012, p. 50). Greater wealth often does not lead to an increase in well-being. This especially applies to the satisfaction of basic needs. “The desire of food is limited in every man by the narrow capacity of the human stomach;” (Smith 1776, p. 181). On the other hand, Smith recognised that the wealthy have a tendency towards self-indulgence in certain areas:

> “[…] but the desire of the conveniencies and ornaments of building, dress, equipage, and houshold furniture, seems to have no limit or certain boundary […]What is over and above satisfying the limited desire, is given for the amusement of those desires which cannot be satisfied, but seem to be altogether endless.” (Smith 1776, ibid.).

A characteristic of luxury consumption is that it does not fulfil any of these real needs, instead it only serves to brag and flaunt and to exhibit social status.[4] For many, wealth is above all a matter of representation and only has its purpose in a "parade of riches": "With the greater part of rich people, the chief enjoyment of riches consists in the parade of riches" (Smith 1776, p. 190).

Smith criticised the parade of riches for two reasons. The first was that he perceived it as the expression of an erroneous way of life favoured by the wealthy. The lifelong striving for wealth supposedly prevented people from being happy and spoiled their morals (see Conlin 2016, pp. 24–28). In his *Theory of Moral Sentiments,* Smith showed this through the well-known parable of "The Poor Man's Son" (Smith 1759, IV.I.8, pp. 200-2). Smith tried to show that it is virtue, rather than the striving for materialism, that prepares the path to happiness: an ambitious man, with poor parents, despises poverty and longs for the luxury and servants such the wealthy enjoy. "He thinks if he had attained all these, he would sit still contentedly, and be quiet, enjoying himself in the thought of the happiness and tranquillity of his situation" (ibid.). To achieve this goal, he submits to "more fatigue of body and more uneasiness of mind than he could have suffered through the whole of his life from the want of them" (ibid.). Furthermore, "he serves those whom he hates, and is obsequious to those whom he despises" (ibid.). As he is industrious and talented, he does indeed become rich, but he does not find rest. It is only in his very old age that the man recognises he chased after the wrong things:

> "It is then, in the last dregs of life, his body wasted with toil and diseases, his mind galled and ruffled by the memory of a thousand injuries and disappointments [...], that he begins at last to find that wealth and greatness are mere trinkets of frivolous utility, no more adapted for procuring ease of body or tranquillity of mind than the tweezer-cases of the lover of toys; and like them too, more troublesome to the person who carries them about with him than all the advantages they can afford him are commodious." (Smith 1759, IV.I.8, p. 201).[5]

The second reason for Smith's critical view of parading riches is that it leads the whole of society to direct its glance to the glitter of wealth, and to develop stronger sympathy for the rich than for the poor, although the latter need the attention and support (see Hanley 2009, pp. 45–51). For Smith, the true meas-

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4 Smith thereby anticipates what Veblen (1899) calls "conspicuous consumption" in his "Theory of the Leisure Class", over one hundred years later.

5 Smith's parable presents similarities with F. Scott Fitzgerald's 1925 novel *The Great Gatsby*. Jay Gatsby also comes from a poor family that he leaves early with the intent of becoming rich. With conspicuous consumption, he displays the wealth he gained through dishonest dealings. His dream remains however unfulfilled, and his life ends in tragedy. He does not however live long enough to recognize the emptiness of his way of life characterized by vulgar materialism.

ure of the wealth of a people was not the size of the royal treasury or the property of the few wealthy people of a country, but the wages of the "labouring poor" (Smith 1776, WN I.viii.; see Rasmussen 2016, p. 343ff.)

> "No society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable. It is but equity, besides, that they who feed, cloath and lodge the whole body of the people, should have such a share of the produce of their own labour as to be themselves tolerably well fed, cloathed and lodged." (Smith 1776, p. 96).

Smith's critical moral opinions on wealth stand in contrast to the positive economic function that wealth can potentially have in driving the accumulation of capital. This ambivalence in the assessment of wealth in the works of Adam Smith is interpreted in different ways. For Hill (2017), Adam Smith contradicted himself in this and he openly recognises a sort of "Adam-Smith-Problem"[6]. On the contrary, Rasmussen (2016) does not see any contradiction between Smith's two different views of inequality and wealth. According to him, Smith on the one hand considered inequality as desirable to a certain extent, as a driver of economic development, but on the other hand he regarded "extreme inequality" as detrimental. This leads us back to the question of what level of inequality or what extent of individual wealth is possible before the useful properties turn into the harmful ones.

3.1.2 Possibilities for Limiting Individual Wealth According to Adam Smith and David Ricardo

Economic laws play an important role in Smith's system. Smith's main scientific merit is the recognition and analysis of the regulative structures of an early capitalist market system. According to his fundamental insights, production and distribution follow certain set laws.

According to Smith, the distributive laws will ensure that the income of the three social classes (landowners, capitalists, workers) will develop in completely different ways in the long run. Although the economic dynamic is essentially driven by the motive of profit making and capital accumulation by the capitalists, they have to accept a reduction of the profit rate in the long term ("tendency of the rate of profits to fall"). While workers' wages may rise with an increase of productivity and increased labour demand, strong population growth eventually keeps wages in check. As wages are also determined on "cultural and historical" grounds, however, the growth of labour productivity will supposedly lead to a slow and moderate increase of wages above the bare subsistence level. Only the landowners could expect a long-term growth of

[6] On this, Hill (2017, p. 10) writes: "[…] tensions in this aspect of [Smith'] thought are a product of his competing roles as a man of wisdom and virtue on the one hand, and his role as a social scientist on the other".

their income and wealth. Ironically, it is precisely the class that "reap where they never sowed" (Smith 1776, p. 67) that can enjoy a constant growth of their proportion of the total income!

For Adam Smith, labour is the source of all wealth; each forms of unearned income (profits, interest, rent) are a "deduction from the produce of labour" (Smith 1776, p. 83). Profit should therefore be a residual, meaning that the outcome of the dispute over wages determines the amount of profits. In other words: between capital and labour, there is a constant battle over income distribution.

Smith presented the factors of influence that would reinforce or weaken both social classes in their dispute over wages (see Smith 1776, pp. 83-84). These include the combat and bargaining strength of each social class and the possibility of collective associations. Capitalists, he claimed, would have the principle advantage here. Fewer in numbers as compared to the workers, they were in a much better position to cooperate and to organise themselves. Smith saw a second factor of influence in the legal and political framework that would influence the balance of power of each class. And finally, wealth also had an important role to play: in times of strikes and unrest, the wealthy had more endurance in case of conflict. It can thus be concluded that – within narrow limits – Adam Smith was aware of the possibility of influencing the primary income distribution, limiting the striving for profit and wealth growth.

Concerning the possibilities of changing the secondary income distribution, many of Smith's statements on taxation can be adduced. Here it should suffice to say that Adam Smith, in his proposals for the development of a taxation system, argued in favour of taxation corresponding to both the principle of equivalence and the capacity of the taxpayer. For Smith, greater wealth should also make a correspondingly large contribution to the financing of state functions.[7] On the other hand, there is little evidence that Smith was in favour of drastic state intervention to reduce, let alone abolish, economic inequality through income redistribution. For Smith, a certain amount of inequality was necessary for economic development.

David Ricardo (1776–1823), who developed Smith's theory further, had similar views. Together with Smith, Ricardo was one of the most influential economists of his era. Already at the beginning of his main work, the *Principles of Political Economy and Taxation*, Ricardo (1817) clarified that for him, the determination of the laws according to which income is distributed between the three classes is the central task of political economy. Ricardo especially developed the theory of ground rent further by introducing the concept of differ-

7 In his *Lectures on Jurisprudence,* Smith represents the view that a taxation amounting to 30 or 50 percent of the income would represent a misuse of the governmental authority (see Robertson 2016, p. 351).

ential rent. According to his analysis, the "niggardliness of nature" and population growth always raises the price of land, leading to a constant increase of the share of rent in national income. Ricardo thus concluded that it is possible and necessary to increase the tax on rent.

Furthermore, Ricardo carefully showed that the real wage and the profit rate for a given level of productivity develop in opposite directions. Capital and labour therefore have an antagonistic relationship. The workers find themselves in a fundamentally worse position: According to the Malthusian Law of Population, the number of workers grows too fast in relation to the food production; wages are therefore always pushed back to the subsistence level. The implementation of machines can also rapidly replace workers in the production and thereby lead to more redundancies ("technological unemployment"). After the end of the Napoleonic wars, David Ricardo also expressed his view of the particular responsibility the wealthy have for the community. He argued in favour of a general wealth tax to quickly reduce the United Kingdom's debt that had sharply risen during the war.

3.2 John Stuart Mill and Utilitarianism

John Stuart Mill (1806–1873) attempted to summarise the central doctrines of his predecessors in a consistent way and solve existing errors and problems. Nowadays he is viewed as a theorist of transition, as he blended concepts from classical economics with marginalist principles, which again led to a number of other inconsistencies (see Spahn 2001, Kurz 2001). For the subject of wealth discussed here, it is important to highlight that for Mill – as opposed to Adam Smith and David Ricardo – strict economic laws only ruled in production. In the preliminary remarks of his *Principles of Political Economy,* he observed that there are no equivalent laws for the distribution of income and wealth:

> "Unlike the laws of Production, those of Distribution are partly of human institution: since the manner in which wealth is distributed in any given society, depends on the statutes or usages therein obtaining;" (Mill 1848, PR. 31).

According to Mill, distribution can be influenced by social institutions and norms. This allows existing social tensions to be pacified through distribution policies. However, the influence of policies on distribution has certain limits. Mill continued:

> "[…] But though governments or nations have the power of deciding what institutions shall exist, they cannot arbitrarily determine how those institutions shall work. The conditions on which the power they possess over the distribution of wealth is dependent, and the manner in which the distribution is effected by the various modes of conduct which society may think fit to adopt, are as much a subject for scientific enquiry as any of the physical laws of nature." (Mill 1848, ibid.).

According to Mill, the distribution of income and assets is determined by political influence and the strength of the groups participating in this struggle. This is a decisive innovation in the classical economic approach, as Mill "politicises" the income and wealth distribution analysis. Influential representatives of marginalism later opposed this approach. They were eager to erase this view back out of economic theory.[8] The fundamental idea represented by the entirety of political economy, according to which there is a measure of freedom in distribution, leaves the classical system open to power-related approaches of distribution.[9]

John Stuart Mill, along with Jeremy Bentham, was one of the most important representatives of the doctrine of utilitarianism. The goal of a utilitarian social order was to ensure the "greatest happiness for the greatest number". To attain this goal, a reduction of economic equality is supposedly necessary, as from a utilitarian point of view, rising income is linked to decreasing marginal utility. Each additional unit of money by which the income of an individual is raised brings an even smaller increase in utility than the previous unit of money. This means that income and wealth redistributed from a rich person to a poor person raises total utility in the society. For Mill, one of the classical authors of economic and political libertarianism, wealth is therefore not sacrosanct, as opposed to the views of his later liberal successors. On the contrary: John Stuart Mill insistently argued for a substantial wealth and inheritance tax. According to the views of John Stuart Mill, one of the major founding fathers of liberalism, an inheritance tax close to one hundred percent is indispensable, in order to ensure equal starting opportunities for all young people.

4. Wealth, Property, and Classes: The Early and Utopian Socialists and Marx

4.1 The Utopian Socialists

In the 19th century, social tensions increased in the wake of the industrial revolution. The extreme contrast between the wealth of a few and the misery of many spurred socialist ideas. The growing wealth of the rising class of capitalists and factory owners made the misery of workers much more visible and harder to bear.

8 On this subject, Kurz (2001, S. 274) rightly points out that the degree of freedom in the issue of distribution initially postulated by Mill is not present in the wage-fund doctrine also represented by Mill. However, after the contradiction was pointed out to him, Mill later withdrew his wage-fund doctrine, thereby returning to a view "closer to Adam Smith's power-related theory" (ibid., p. 276).

9 As Spahn (2001, p. 240f.) remarks, one can see this openness either as an advantage, as the particularities of a historical-specific situation can thereby be taken into account, or on the contrary as a lacking specification of the model of a capitalist economy.

With increasing wealth and paraded luxury consumption, a number of alternative concepts to a capital society were proposed. The early or utopian socialists, as they are called today, suggested various radical alternatives. They all shared the view that property, and wealth based on property, were objectionable.

The utopian socialists followed a long tradition, going back to early Christianity and before (see Kurz 2016, p. 43). Over the course of history, many schools of thought argued against wealth and luxury for ethical reasons: the Greek stoics saw wealth as a contradiction to the ideal of a bare and simple life. Devout Christians strove for a life of austerity. The puritans, for their part, feared that wealth and luxury would cost them their salvation (see Pöll 1980, p. 12).

In the view of the early socialists, it was unacceptable that certain people accumulated riches while others lived in poverty. Their premises were the equality of all people, requiring the equal distribution of income and wealth. Varying political demands were made to achieve this goal (see Eißel 2002, pp. 201-3): St. Just and Babeuf, for example, strove to achieve an absolutely equal distribution of income, Saint-Simon and his followers demanded the abolition of the right of inheritance, and Fourier and Louis Blanc proposed the creation of production cooperatives.

Simonde de Sismondi (1773–1842), a strong critic of the classical British economists, is of particular interest here. According to Eißel (2002, p. 191), Sismondi laid down the "roots of a 'classical' criticism of the unilateral accumulation of riches from a social and economic point of view". For Sismondi, the distribution problem is socially of crucial importance. He made ethical arguments against excessive inequality and the concentration of power. He argued for reinforced worker's protection legislation and appealed to the moral responsibility of the wealthy towards the poor. Sismondi, however, is also important as an economic theorist, as he developed a theory of demand deficiency arising from unequal distribution – an early under-consumption theory. He pointed out that when workers are limited to their subsistence wages the supply of goods rapidly growing in the wake of industrialisation could face a lack of (consumption) demand. The sales of goods then stagnate, "leading to […] a lack of harmony in the demand for products" (ibid., p. 203). 100 years before Keynes, Sismondi recognised the vulnerability to crises of a market economy if income and wealth inequalities are far too high. The taxation of the wealthy was therefore considered an appropriate instrument to correct inequalities.[10]

[10] Keynes (1883–1946), who considered unemployment and the "arbitrary and inequitable distribution of wealth and incomes" the "outstanding faults of the economic society" of his time (Keynes 1936, p. 372), warned however against an unduly high taxation of the wealthy. For one thing, it would drive them towards tax evasion, and for another, "for a large proportion of this growth we are dependent on the savings of the rich out of their superfluity" (ibid.).

4.2 Karl Marx

Karl Marx had thoroughly studied Adam Smith and valued his scientific achievements. Unlike those representatives of classical economics who recognised a distribution problem at all, however, Marx and the labour movement that succeeded him did not see the remedy in redistribution of wealth, but only in the revolution of social relations. According to this view, wealth, private property and power enjoyed by a few privileged individuals could only be abolished in a society without classes. Until then, the capitalists still had their historical duty to fulfil:

> “The development of the productive forces of social labor is the historical task and privilege of capital. It is precisely in this way that it unconsciously creates the material requirements of a higher mode of production.” (Marx, vol. 3, ch. 15, p. 51).

Here we encounter again – in another form – Adam Smith’s central argument. An “invisible hand”, “behind the backs” of the actors, ensures that their selfish behaviour, namely striving for profit, has a social use: the continuous accumulation of capital and development of new technologies lead to an increase of labour productivity. Capital, ownership of assets and the corresponding wealth therefore also have a (temporary) distinct and useful function in the Marxist system. According to Marx, however, this growth process would eventually collapse, as the ever-expanding productive forces would inevitably be against the relations of production. Profit rates, decreasing in the long term, would ensure that the accumulation force of the capitalist system would eventually come to a halt.

From the social preconditions and effects of the accumulation and development process in capitalism, Marx, however, arrived at completely different conclusions from Smith. Smith was dismayed by the conditions of the working class, but he did not give the workers an active role in his system. Although he considered labour to be the source of all wealth, only the activity of the capital owners brings this property to the light; the latter therefore play the leading role. For Smith, the working class may be economically productive, but politically dammed to passivity. From the labour theory of value which characterises the entire classical approach, Marx concluded on the contrary, that the workers would one day oppose the appropriation by the capitalists of the surplus value they create, and thereby create a class and property-free society through revolution.

5. Income Generation, Welfare, and Fairness in Marginalism

With the emergence of marginalism (so-called neoclassical economics) in the 1870s, the question of the principles of growth and distribution was less important. Instead, the issue of scarce goods and production factors became the central issue of investigation. The emergence of marginalism changed the determinants of value and price, and in so doing of distribution as well. With the disappearance of social classes from the new economic theory, the focus was on the production factors labour, land, and capital. In marginalism, the income of these production factors corresponds to their marginal product, which is why this (essentially microeconomic) income theory is nowadays called the marginal productivity theory of distribution. Under certain assumptions about the properties of the production function, in the case of perfect competition the product is divided between the production factors according to their marginal value contribution. All factor incomes are determined simultaneously and correspond to their respective marginal products.

At the heart of the microeconomic marginal productivity theory, it is, however, a case of determining the demand according to the individual production factors and the corresponding production factor markets; in the proper meaning of the word, it cannot therefore be called a primary theory of distribution. The individual factor prices (real wage, profit rate, rent) are also calculated simultaneously to the determination of the factor demand. As opposed to classical economics, the fundamental principle of the factor price determination is identical for all production factors.

The remuneration of each of the production factors fulfils the criteria of justice of performance. In the reference case of perfect competition, exploitation is impossible. Distribution is determined to a certain extent by the technical conditions of production and thereby removed from social or political disputes. In principle, there is no room for conflict and power in distribution.

Alfred Marshall (1842–1924) was possibly the most important protagonist to help the breakthrough of the economic revolution, i.e., the paradigm shift from classical economics to marginalism, with his *Principles* of 1890 (see Streissler 1981, p. 41). Marshall strove to “depoliticise” economics. This was also a reaction to the looming labour movement and the success of social and Marxist doctrines. The fundamental principle of quasi-natural-law determination of wages, described by the “Iron Law of Wages” (Ferdinand Lassalle) that Böhm-Bawerk so vehemently defended in his well-known essay on *Power or Economic Law*, was accepted in the context of the microeconomic production theory. Production and distribution theory were (again) presented as two sides of the same coin. Only the laws of the market achieve the result of distribution;

distribution therefore follows quasi-natural laws. Consequently, as the influences on wages from outside the market or other distribution variables lead to damages such as unemployment, the issue of fairness does not need to be addressed any more. We shall see at a later point that Friedrich August Hayek in particular was a dedicated representative of this view.

However, the question of fairness of income generation in the market process and thereby the legitimation of wealth as well as the necessity of redistribution was later discussed even by neoclassical economists. They arrived at very different conclusions, however: John Bates Clarke (1847–1938), for example, considered a wage rate determined by the market process as fundamentally fair. On the contrary, an open minded neoclassical economist such as the influential Paul A. Samuelson (1915-2009) represented the view that the market could indeed achieve an *efficient* result, but that an assumption of *distributional fairness* could not be derived from this (Samuelson 1965).

Within the spectrum of marginalism, the utilitarians such as Edgeworth and Pigou had a particular role to play in that they argued for the redistribution of wealth for welfare-theoretical reasons. Their basis was the principle that the marginal utility of an increasing income is always decreasing. In this, Francis Y. Edgeworth (1845–1926) saw himself as a representative of an "exact utilitarianism". Although the comparison of utility between two individuals has theoretical difficulties, in practice it is supposedly acceptable, according to Edgeworth. If the individuals have the same preferences to a certain extent, a more equal income distribution would lead to more welfare in society. According to this approach, excessive individual wealth prevents "the greatest happiness for the greatest number".

Arthur C. Pigou (1877–1959) supported the idea of redistribution with the goal of more equality and also justified this with the law of decreasing marginal utility. He limited the meaningfulness of redistribution, however, in that it could not run contrary to the principle of welfare maximisation postulated by Alfred Marshall. Pigou is of interest because he claimed there was a possibility of "exploitation", even in a neoclassical system in which the factor incomes are principally determined by marginal productivity. For Pigou, the marginal productivity theory can only be applied under strictly limited conditions, which are rarely found in reality. In the real world, deviations from perfect competition and thereby power influences would only need to be taken into account in a few exceptional cases. Depending on the extent of the price elasticity of the offer or demand, it would be conceivable for a factor not to be remunerated according to the marginal productivity. In this case, exploitation in the sense given by Pigou is possible, which could affect all the factors. In this way, the capital could also be "exploited" by the workers, for example.

Finally, reference must be made to an empirical observation on the nexus between individual wealth and general increases in welfare by Simon Kuznets

(1901–1985). This correlation is well-known today as the Kuznets curve. Based on empirical data in the USA between 1913 and 1948, Kuznets (1955) concluded that growing wealth of individuals is a necessary side-effect at the beginning of a long-term economic development process. This corresponds to the widespread idea of the so-called '*trickle-down effect'* whereby the wealth of a few is beneficial to all members of a society, because even the less wealthy will see an increase of their income and wealth after a certain period of time. The stylised development illustrated by the bell-shaped Kuznets curve implies that per-capita income and inequality are low in the early stages of development. Moreover, the number of wealthy people is relatively low. In the wake of industrialisation (more generally: of economic development), characterised by gradually increasing per-capita income and a general growth of wealth, a small group of people moves into the rapidly growing new economic sector with rapid income growth. This group typically consists of especially daring entrepreneurs, pioneers, risk-taking individuals, or people with a coincidental advantage. Their income rapidly stands out from the rest of the economy. While the gap between rich and poor increases in this stage, large parts of society also benefit from a certain increase of their incomes. This process continues for a certain time, until inequality eventually reaches its maximum. Although per-capita income continues to increase, inequality abates as more and more people move into the quickly developing sector.

In this context, Kuznets did not develop a special and formulated distribution theory. As an empiricist, he considered he had observed this development in the data, and tried to give an explanation for it that seemed plausible to him. He conceded the lack of reliability of his empirical basis and the vagueness of the theoretical justification of the correlation between wealth and growth:

> "The paper is perhaps 5 per cent empirical information and 95 per cent speculation, some of it possibly tainted by wishful thinking." (Kuznets 1955, p. 26).

With respect to the history of economic thought the Kuznets curve has been an important alternative draft as it represents an optimistic counter-proposal to the stagnation-dominated development theories of the classical economists. The simple message of the Kuznets curve is that inequality and the affluence of a few are the inevitable and ultimately desired condition of a general increase in welfare. Economic and social inequality would only be a temporary phenomenon that would disappear by itself. Paradise awaits in the future!

In the introduction to his book *Capital in the Twenty-First Century*, Thomas Piketty (2014) extensively analyses the Kuznets curve. Based on a much broader database, Piketty shows that the right-hand side of the Kuznets curve indicating a decline in inequality has not manifested in developed economies. According to his research, rising per-capita incomes in industrialised countries are not associated with lower but with continuously increasing economic inequality. According to his reasoning, under certain circumstances (for example, the rate of profits in excess of the rate of economic growth, as has mainly been the case in the history of humanity) wealth will continue to be more and more concentrated. According to Piketty, the individual wealth of a small group –the already very wealthy capital owners at the top of the wealth distribution – will continue to grow in the future unless there is active taxation.

6. Wealth and Justice in Neoliberalism

6.1 Friedrich August Hayek

Friedrich August Hayek (1899–1992), whose views are presented here alongside those of the US-American economist Gregory Mankiw as representative of the neoliberal position concerning wealth, gave an interview in February 1981 to a leading German business magazine.[11] A month before the publication of this interview, Ronald Reagan took office as the 40th US- President. Two years before, the leader of the Conservative Party, Margaret Thatcher, had become the British Prime Minister. The early 1980's mark the beginning of the era of neoliberal economic and social politics, of which the main protagonists often referred to Hayek's liberal philosophy and radical free-market views. With their policies, Thatcher and Reagan provided de-regulation and privatisation as well as their massive tax reduction programmes for a worldwide shift towards supply-side economics, the economic and political effects of which were felt far beyond Anglo-Saxon countries. In terms of income and asset distribution, this was the beginning of the so-called "Inequality Turn" (Atkinson 2016, p. 3, pp. 80-1).

Hayek considered the classical liberal pioneer John Stuart Mill as one of the chief culprits of the sheer existence of the distribution issue. Mill, he claimed, who had introduced an analytical separation of production and distribution in economic theory, introduced a completely false idea to the world, namely that there was any leeway in distribution:

> "What we are experiencing today is the result of a fundamental confusion, that was introduced by the supposedly liberal British thinker John Stuart Mill. In his 'Principles of Political Economy', Mill wrote a sentence that was the basis for all socialist ideas: 'Once the social product exists, one can do with it what one wants.' This completely overlooks the fact that the production process is not independent from the distribution process, which precisely

[11] In this interview, Hayek points out again certain views he had developed extensively in Hayek (1960) for example.

> means that one cannot do what one wants with the national product." (Hayek 1981, p. 16).[12]

For Hayek, it was obvious that the market process gives rise to inequality. He did not see this inequality as problematic, however, but as an important precondition for economic development, a central foundation for economic performance:

> "Inequality is not regrettable, instead it is most welcome. It is simply necessary. Unfortunately, the national product only exists because people are remunerated according to their productivity and are attracted to where they produce the most. It is precisely the differences in remuneration that lead individuals to do what the national product permits to arise. Through redistribution we paralyse this signalling device." (Hayek 1981, p. 16).

Hayek considered the term "social justice" entirely misplaced.[13] According to him, justice is only significant as a category of the legal system, as it allows the deduction of the equality of individuals before the law (formal legal equality). If this is not ensured, freedom, which is the greatest of all goods for Hayek ("the condition of all other values"), is destroyed. In the economy, on the other hand, justice does not have its place, as in Hayek's view, people do not have any leeway of action on the markets and therefore their actions cannot be evaluated in a normative sense. The demand for greater income and wealth equality would be futile, as distribution is only determined by the laws of the market. According to Hayek, production and distribution are therefore inseparable. From the perspective of economic liberalism, wealth is a justified result of efficient market processes. Hayek went a step further at this point, in that he rejected the question of the fairness of income distribution as nonsensical and therefore inadmissible, because:

> "[…] the distribution that arises from the market process is not the intended result of human actions. The term of social justice is therefore completely meaningless in an order of market economy with free choice of profession." (Hayek 1981, p. 16).

Hayek, who maligned the idea of social justice with such zeal, implicitly introduced a different concept of justice. In economic liberalism, he stressed, justice exclusively means performance-related justice. In this way, wealth can be interpreted and justified as follows: wealth is the expression of prior accumulation processes, based on fairly remunerated efforts and risks that have a

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[12] This and the following quotes from Hayek (1981) are own translations of the original German text.

[13] This sentence from the interview shows the zeal with which Hayek rails against the idea of social justice: "I have come to feel strongly that the greatest service I can still render to my fellow men would be that I could make the speakers and writers among them thoroughly ashamed ever again to employ the term." (Hayek 1981, p. 16).

positive effect for society as a whole. Accordingly, Hayek warned against the limitation of individual wealth, because

> "[…] those who attack the wealthy forget that most of them created jobs in the course of accumulating their wealth and have thereby helped more people than if they had given their money to the poor." (Hayek 1981, ibid.).

Hayek thereby made a connection to a fundamental thought of Adam Smith, according to which the accumulation of capital creates growth. He did not add, however, that wealth was not necessarily equated with the accumulation of capital and growth for Smith. At many points in his work, Smith indicated that there was the possibility of wealth being wasted on unproductive purposes (consumption, hoarding). In contrast, Hayek saw that even a playboy's wasteful life of luxury is a useful social model and therefore has a development function. Because they follow a way of life in which new leisure activities arise, this could prepare the way for the development of new mass markets:

> "[…] many of the toys and tools of sport that later became the instruments of recreation of the masses were invented by playboys." (Hayek 1960, p. 195).

For Smith, however, neither (wasteful) consumption nor the self-serving behaviour of a wealthy person was the guarantee of general social wellbeing. Only the embedding in corresponding social institutions that divert the self-serving behaviour of the individual into meaningful directions could ensure that the wealth of the individual could also be the wealth of the nation. And aside from Mill, other liberal classical economists of the 19th century saw a certain measure of freedom in the determination of distribution. Hayek's view largely exceeds the line of thought of his liberal predecessors.

6.2 Gregory Mankiw's "just deserts"

In a recent essay written in the wake of the post-financial crisis discussion on the enormous wealth increases among the top one percent of the US-American society, N. Gregory Mankiw represents a determinedly liberal economic view.[14] He argues against any politically motivated redistribution of income and wealth, as he thinks wealth generally arises from the accumulation of fairly-earned income.

He explicitly refutes the idea of an institutionalised system of income redistribution in accordance with Rawls' concept as a type of insurance against the social risks of life, and instead presents a so-called *just deserts*-perspective. For Mankiw, wealth is always *fairly earned*, because income that corresponds

[14] Mankiw, who wrote *Principles of Economics,* the best-selling economics textbook of the present day, was nominated in 2003 by the Republican US-President George W. Bush as chairman of the Council of Economic Advisers, the most important economic policy board in the US.

to the value contribution of the individual is always “deserved”, in both meanings of the word (just deserts). In this perspective, in a world of perfect competition without either public goods or external effects, there is no legitimate reason to levy taxes and redistribute income and wealth. Only in the case of a deviation from perfect competition (allocative market failure) and the occurrence of negative external effects is it necessary, as had already been suggested by Pigou, to levy taxes. For the financing of public goods – which may include the absence of poverty – taxes are also appropriate. A progressive tax system, however, would only be justified according to the solely legal principle of equivalence if the wealthy also had a disproportionate benefit from public goods. Consequently, Mankiw considers the marginal tax rates that amounted to 91 % in the 1950s as “confiscation” of fairly-earned income by the state.

Concerning the tasks of the state in a market economy, Mankiw defends a radical free-market position, derived from his ultra-liberal view of justice. For Mankiw, as for Hayek, *performance justice* is the sole decisive evaluation principle for the distribution of income. Mankiw’s statements, however, can be seen as a welcome contribution to the distribution debate, as he brings the normative element, which is usually excluded by representatives of the marginalist approach, back in:

> “I trust that these thoughts offer a vivid reminder that fundamentally normative conclusions cannot rest on positive economics alone.” (Mankiw 2013, p. 33).

If this view were to garner appraisal from the peers who are theoretically closest to him, this would be progress in the debate on the distribution of income and wealth.

7. Concluding remarks

Two principal approaches concerning the function of wealth can be observed in economic theories. On the one hand, wealth is a helpful – or even necessary – condition for economic development and the long-term increase of income of all members of society (“trickle-down effect”). Proponents of this view usually emphasize the positive incentives which only arise if it is possible to achieve a high level of income and wealth. They warn against paralysing the economic dynamic through measures such as wealth and income taxation and thereby destroying jobs. According to the liberal theory of justice, however, wealth is not only legitimised by its positive welfare effect. As long as there are sufficiently equal opportunities and fair, consistent rules of conduct, individual wealth is justified (see Hirschel 2004, p. 48). The existence of equal opportunities and social mobility in particular, is often only postulated by many liberal representatives and not corroborated. According to the liberal view, the terms wealth, ownership, and property are treated as an inseparable unit. The emphasis on economic freedom in this view implies the legitimate possibility of accumulating great wealth and having free disposal of it. Any attempt by the state to tax private wealth or its transfer in the form of donations and inheritance is called "expropriation" and is vehemently rejected (see Straubhaar 2015, Hank 2015). On the contrary, the state is given the task of guaranteeing the principally legitimate right of property and enforcing it if necessary; there is no natural upper limit for wealth based on private property:

> "Economic individualism's basic premise is that the pursuit of self-interest and the right to own private property are morally defensible and legally legitimate. Its major corollary is that the state exists to protect individual rights. Subject to certain restrictions, individuals (alone or with others) are free to decide where to invest, what to produce or sell, and what prices to charge. *There is no natural limit* to the range of their efforts in terms of *assets, sales, and profits*; […]" (Hessen 2008, p.1; my emphasis).

On the other hand, there is the view that excessive wealth hinders the development possibilities of a society. It is usually pointed out that high income leads to a higher level of savings, which removes consumption resulting in a lack of effective demand and weakening the growth dynamics of an economy. The assertion that wealth and inequality are preconditions for welfare growth is countered by the argument that the existence of a trickle-down effect is increasingly called into question by recent empirical studies which do not show any positive correlation between inequality and growth (see, for example, Cingano 2014). Opponents of individual wealth furthermore emphasise that wealth is also contrary to the principle of human equality. According to the Marxist view, unequal distribution of wealth goes hand-in-hand with private property. As class affiliation rather than individual performance decide on the distribution of income and wealth, equal opportunity and the performance principle are purely ideological constructs according to this view (see Hirschel 2004, p. 48).

The evaluation of individual wealth is also present in the economic theories in the context of general ethical and political principles. Who is considered wealthy, and whether one defends or rejects great individual wealth, are questions that can only be addressed in the context of fundamental ethical principles. Even the economic theories that pretend to be free of value-judgements cannot free themselves from an implicitly present assessment basis.

It can be assumed that the public debate and scientific discourse that have been revived due to the increased economic inequality in the recent past will present new findings concerning the creation, consequences, and assessment of individual wealth.

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