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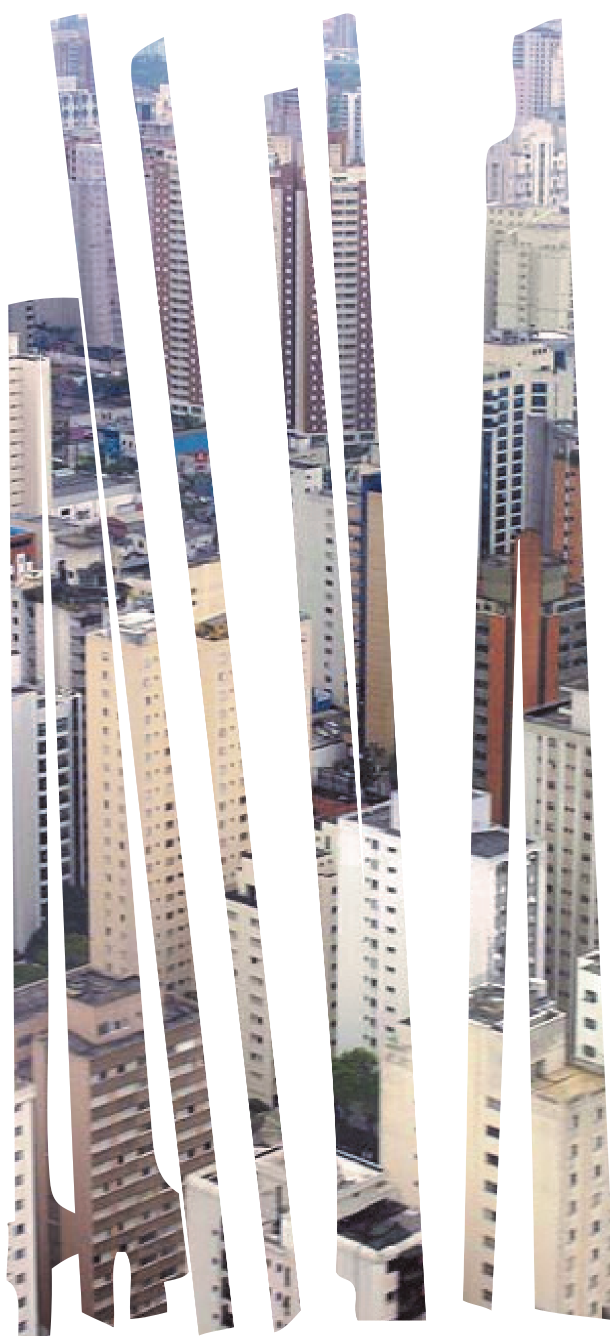
Is More Equality Possible in Latin America?
A Challenge in a World of Contrasted but Interdependent Inequality Regimes

Robert Boyer



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Is More Equality Possible in Latin America?

A Challenge in a World of Contrasted but Interdependent Inequality Regimes

Robert Boyer[1]

Abstract

Three contemporary paradoxes deserve explanations. First, in America, the finance-led growth regime has brought about a rupture with the Fordist Golden Age, causing a surge of inequality, because of quite specific spill-over effects from the economy to policy, whereby diverse social science research has convincingly concluded that the cost of inequality has become excessively large. Second, the Euro-zone crisis is often perceived as reflecting the limits of universal welfare states and the ideal of social equality, but some social democratic countries have resisted and continue to exhibit a complementarity between an extended welfare system, moderate inequalities and a dynamic innovation and production system. Third, Latin America, which used to be the continent with the highest inequality, has reversed its previous dynamics and seems to exhibit a growth pattern based upon inequality reduction, while still relying heavily upon the strong international demand for commodities. To resolve these paradoxes, a common socioeconomic approach is proposed, based upon the concept of inequality regimes. It is then applied to investigate the durability and likelihood of such a U-turn for Latin America. Conventional interpretations stress the universality of the mechanisms which widen individual inequalities within each nation-state but reduce the hierarchy of national standards of living. This analysis, however, concludes that Asia, North America, Europe and Latin America do not follow the same trajectory at all, since they have developed contrasting regimes of inequality that co-evolve and are largely complementary at the world level. This could be an alternative to the hypothesis of an irreversible globalization of inequality. As a consequence, the future of more inclusive Latin American economies depends on the interaction between new domestic democratic advances and the reconfiguration of the international economy.

Keywords: inequality regimes | growth and equity | welfare and innovation systems

Biographical Notes

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Contents

1. Introduction: A Turning Point in the Economic History of Latin American Countries? 1

2. China: A Modern Industrial Revolution, and the Kuznets Curve Revisited 4

2.1. The Outcome of Productive Modernization and Fast Growth 4
2.2. Economic Reforms Erode the Collective Institutions that Used to Limit Inequality 5
2.3. Large Regional and Urban Inequalities 6
2.4. The Marketization of Agriculture Seems to Have Reduced Inequalities but Capitalist Industrialization has Drastically Increased them 7
2.5. The Threats to Social Stability Call for the Establishment of Modest but Efficient Welfare 8
2.6. Building Nationwide Welfare Runs against the Logic of the Core Chinese Institutional Form: Local State Corporatism 9
2.7. The Primacy of Competition is an Obstacle to Society-wide Welfare 10
2.8. The Specificity of the Chinese Inequality Regime 11

3. The US: From the Golden Age to the Explosion of the Income of the Super-Rich 12

3.1. The Surprising Post-WWII Growth Regime: Stable and Reduced Inequality along with Technological Dynamism and Growth 12
3.2. A New Neoliberal Orthodoxy: Increasing Inequalities are Necessary for Growth Recovery 14
3.3. The Rupture in the Alliance between Managers and Wage Earners under the Pressure of Internationalization and Finance 15
3.4. The Explosion of Credit to Households as an Alternative to Increasing Wages and Fully-Fledged Welfare 17
3.5. Financialization Enables a Huge Income Transfer to the Super-rich 19
3.6. Power Asymmetry in the Economy is Converted into the Ability to Design Economic Policy and to Block any Regulation 21
3.7. The Joint Consequence of Full Liberalization: Wider Inequalities and Financial Crisis: Karl Polanyi Was Right! 23
3.8. The US and Chinese Inequality Regimes are Different but They Express Complementary Growth Patterns 24

4. The European Crisis: False Attribution to Welfare of the Dysfunctionality in Eurozone Treaties 26

4.1. Europe: Homeland of Bismarck and Beveridge 26
4.2. A Limited and Uneven Rise of Inequality in Europe, But Growing Financial Unbalances in Welfare Regimes 28
4.3. A Neglected Defense of the European Pursuit of Equality: Social Insurance Contributes both to Welfare and Competitiveness 29
4.4. The Financial Constraints Generated by the Crisis are a Threat to European Welfare: An Erroneous Interpretation 31
4.5. The Resilience of Social Democratic Capitalism 33
4.6. Defense of Rights to Economic Security is Crucial for the Emergence of a Virtuous Growth Regime with Stable and Reduced Inequalities: A Hidden Precondition for the Danish Flexi-Security Model 34
4.7. Every Inequality Regime is the Outcome of a Long Run Trajectory, Melting Ideas, Political Intermediation and Economic Specialization 36
4.8. The Extended European Welfare Systems and Regimes of Limited Inequality are Challenged by Global Finance and Eroded by Chinese Competitive Pressure 38

5. Latin America: Paradox or Historical Bifurcation? 39

5.1. A Continent Not So Poor, but the Most Unequal 40
5.2. The Surprising 2000s: A Rather General and Significant Reduction of Inequality 42
5.3. The Causes of this Improvement: A Complex Web of Economic, Social and Political Factors 43
5.4. A Tentative Synoptic Representation of the Determinants of the New Latin American Inequality Regime 48

6. From a Global and Universal Approach to the Complementarity of Contrasting Socioeconomic Inequality Regimes 51

6.1. Measuring Inequality at the World Level: The Need for a Plurality of Concepts 51
6.2. The 2000s: A Historical Reversal of Inequality? 52
6.3. The Kuznets Curve Revisited: Do General Laws Govern Growth and Inequality at the National Level? 55
6.4. From the Original to the Extended Kuznets Curve Model: The Novelty of the Contemporary Period 55
6.5. An Interdependent and Multipolar World of Inequalities: An Alternative Paradigm? 56

6.6. The Three Paradoxes Explained: How Academia, Economy, Polity and Geo-polity Interact 57

7. Conclusion: A Watershed in the Evolution of Inequality Regimes 61

7.1. Paradigms and Ideologies Matter 61
7.2. The Complex and Multiple Determinants of Inequalities 61
7.3. Fordism and Social Democratic Regimes have Anticipated Inclusive Growth in Latin America 62
7.4. Less Globalization of Inequality than Coevolving Contrasted Inequality Regimes 62
7.5. Inequality: When Economic Power Shapes Political Processes 63
7.6. Inclusive Growth: An Unfinished Agenda 64
7.7. Do Not Forget Latin American Idiosyncrasies 65

8. Reference List: Thematic Presentation of Sources 66

8.1. General Literature on the Relation between Growth and Equity 66
8.2. General Historical and Statistical Analysis of Inequality 68
8.3. Comparative Historical Analysis of the Emergence of Welfare States 70
8.4. Social Justice and Dynamic Efficiency According to *Régulation* Theory and Related Theories 71
8.5. Why a Domestic Led and Less In-Egalitarian Growth Regime is so Difficult in China 73
8.6. Analysis of the Transformations of the American Growth Regime and Inequalities 74
8.7. Recent Latin American Advances in Understanding and Promoting the Synergy between Growth and Permanent Growth Reduction 74
8.8. The European Crisis is Not the Consequence of its Extended Welfare 76
8.9. Institutional and Historical Analysis of Latin American Trajectories, Including *Régulation* Theory 78

1. Introduction: A Turning Point in the Economic History of Latin American Countries?

The explosion of inequalities across the world has attracted the attention of many social scientists and it is becoming a central issue in contemporary political debates. In academia, sociologists, political scientists, economists, epidemiologists, and historians have delivered new and somehow converging analyses and interpretations of inequality. In many countries, public opinion and social movements have pushed the issue of widening inequality to the top of the political agenda. A well-respected mainstream conservative journal has dedicated two issues entitled "Asia's Next Revolution: Reinventing the Welfare State" (*The Economist* 2012a) and "The New Politics in Capitalism and Inequality" (*The Economist* 2012b). The issue of inequality, welfare and contemporary capitalism is again on top of the agenda in most societies. Therefore, even if this work was and still is concerned with the likelihood and form of an inclusive Latin American development (*crecimiento con equidad*) it might still be useful to develop a panorama of the world economy in terms of inequality and emerging growth regimes. Are there powerful and common mechanisms shaping all national trajectories or are they largely specific in response to the interplay between domestic social and political processes and the structural transformation of international relations? The task is challenging because the analyst is facing three apparent paradoxes.

(1) First paradox: Is bad inegalitarian capitalism driving out more virtuous forms?

Since nearly three decades, i.e. the demise of the post-World War Golden Age, generally, income and wealth inequalities have drastically increased, to levels similar, for instance, to the ones observed just before the 1929 American Great Depression. Simultaneously, and quite independently, different researchers belonging to various disciplines in social science have converged toward a common understanding and conclusion: the structures that govern the economy and the polity and their mutual relations are breeding a series of mechanisms that exacerbate inequalities among citizens within the same country. They have proven that inequalities are bad for social cohesion, economic efficiency and political participation (Wilkinson and Pickett 2010: 20, 21, 52, 53, 82, 160, 225). But then, how can it be explained why such poorly performing societies tend to impose their logic and reforms on better ones?

(2) Second paradox: Is the deep crisis of the European Union counter-evidence against the superiority or even the viability of welfare capitalism?

Actually, the very idea of a state protecting the well-being of the citizens had emerged from the two world wars and the depression of the 1930s, when William Henry Beveridge and John Maynard Keynes were, along with Henry Ford, the founding fathers of a new national and international order. During the first phase of the subprime crisis, European integration and the euro seemed to have protected the old continent from the vagaries of the world economy triggered by the excess of financial liberalization and globalization. But since spring 2010, the whole European integration process is at risk and many foreign observers and international organizations blame European leaders for not having curbed further the surging costs of welfare. De facto, under the pressure of public and private international financial institutions Greek, Portuguese, Spanish and Italian governments had to implement significant cuts in many welfare benefits. The past synergy between economic performance and social security seems to have vanished and is now turning into an open conflict. *Nolens volens*, the citizenry had to accept more inequalities and even the rise of poverty as a precondition for restoring the confidence of international investors. This is a related puzzling issue to be investigated.

(3) Third paradox: Why is the most unequal continent, Latin America, now exploring a new strategy of development built upon reducing inequality?

This evolution is challenging many previous attempts at theorizing about built-in inequality and strong path dependency originating from colonial times, the curse of specialization in the extraction of raw materials, and partial and late industrialization, all of which features have been exacerbated by the pressure of globalization. Most of the statistical indexes point out a significant inflexion during the last 10-15 years: higher growth rates, formal employment creation and surprisingly enough the benefits of better macroeconomic performance have been distributed to low income groups and not only restricted to elite and upper middle classes. All the traditional measures of inequality suggest a possible bifurcation in Latin American history. What are its drivers and will they last sufficiently long to open a new epoch? Facing this difficult question, which analytical tools are available?

The objective of this paper is to possibly explain these three paradoxes by a common analytical framework. It starts from the major findings of comparative analysis of national growth regimes and extends a political economy approach inspired by *Régulation* Theory (see Boyer 1994) to the issue of inequality. China has attracted considerable attention

due to its spectacular development, large population and ascending geopolitical role. Given the present configuration of competition and labor laws, the coexistence of less poverty and more inequalities is not a real surprise (Section 2). Next, I turn to North America as the second continent, since its evolution is frequently presented as a benchmark and an anticipation of the future of modern societies. Many converging socioeconomic investigations propose a convincing diagnosis about the reasons of demise of the post WWII capital-labor compromise and the explosion of inequalities in favor of group of super-rich: opening to world competition, high international capital mobility and financialization all contributed to an explosion of income at the top (Section 3).

The old continent used to be the territory of Bismarck and Beveridge who launched the principles of modern welfare states. The related brands of capitalism are now under scrutiny: is not the Euro crisis a watershed in the history of welfare and negotiated capitalism? Most European governments now consider some degree of inequality is necessary to bring back economic dynamism (Section 4). In this context, the inflexion of Latin-America societies towards less inequality calls for an explanation. Genuine growth regimes and a new political configuration, specific to each country, shape a trajectory of inequality reduction (Section 5). Previous research has concluded that the various forms of capitalism and growth regimes were more complementary than in direct competition with each other. This hypothesis is here extended to the related inequalities, and the concept of regimes of socioeconomic inequality is elaborated and applied to each region of the world economy. We thus understand better why three regions of the world economy experience difficulties in reconciling development and social justice but why at the same time Latin America is exploring a new path, however uncertain the success might be. Building upon these findings, this analytical framework then delivers an explanation of the three paradoxes mentioned in the introduction (Section 6). Since it is too early to risk any prognosis about the durability of this U-turn, the conclusion summarizes the main results and proposes to extend some methodological advances by a more precise analysis of quite important Latin American idiosyncrasies that could not be taken into account by this comparative approach (Section 7).

2. China: A Modern Industrial Revolution, and the Kuznets Curve Revisited

The evolution observed since 1978 can be interpreted in the light of past historical experiences, as captured by the Kuznets curve hypothesis, but the origins of rising inequalities are also specific to the genuine institutional configuration of contemporary China.

2.1. The Outcome of Productive Modernization and Fast Growth

According to a seminal article (Kuznets 1955), the process of development exhibits first an increase and, after a preliminary phase, a decrease of economic inequalities. Two mechanisms contribute to an inverted U curve between income per capita and a measure of inequality. The early phase of take-off calls for heavy infrastructure and productive investment as the cost of an increase in standards of living. Similarly the transfer of labor from traditional rural sector to a modern industrial sector generates large productivity increases, and this gap in turn widens income disparity. When the basic infrastructure is built and the center of gravity of the economy has shifted to the modern sector, income inequality decreases through a mechanical process.

This simple hypothesis captures some features of Chinese growth pattern: the migration from traditional rural to modern urban sectors allows a surge in aggregate labor productivity given the huge differential in productivity levels (Table 1). The absolute gap in productivity levels between agriculture and industry was decreasing from 1991 to 2008 but only moderately, and thus the Chinese economy continues to move along the ascending part of the Kuznets curve. In effect, productivity differentials are converted into per capita income gaps and one observes a widening gap between rural and urban income per capita (Table 2), especially after 1991 when market liberalization reforms were extended from agriculture to industry.

Table 1: The Role of Extreme Productivity Differential in the Widening of Inequalities: China (1978-2008)

	1991		Relative productivity	2008		Relative productivity
	Value Added	Employ-ment		Value Added	Employ-ment	
Primary	7.1	48.8	14.5	6.5	39.6	16.4
Secondary	62.8	26.8	234.3	50.6	27.2	186.0
Tertiary	30.1	24.4	123.4	46.1	33.2	138.0
	100	100	100	100	100	100

Source: China Statistical Year Books (various years).

Table 2: The Urban/Rural Divide Measured by Average Per Capita Income Differential

1978	1991	2001	2008
2.57	2.40	2.90	3.31

Source: China Statistical Year Books (various years).

2.2. Economic Reforms Erode the Collective Institutions that Used to Limit Inequality

Clearly this is not the outcome of purely economic mechanisms, since the institutional and legal context also plays a key role. On one side, rural and urban workers do not have the same rights in terms of access to housing, health care and education, and this inequality is embedded into the implementation and enforcement of the dual *hukou* systems (in which rural migrants do not receive permission easily to establish official residency, and thus benefit eligibility, in the cities where they work), which is at odds with a common labor law and a unified welfare state typical of most industrialized economies. On the other side, the institutional and organizational transformations play a role in the evolution of income distribution. In 1978, private incentives were introduced in order to increase agricultural production, and a private rural sector was added to the previously obligatory collective forms of organization. In a second step, the mechanism was extended to some industrial zones and sectors, which created an economic momentum in the coastal regions, which attracted migrant workers from poorer inner regions (Table 3). Consequently, the relatively egalitarian, politically-coordinated collective organizations were being progressively challenged by firms run according to the logic of a myriad of other forms of property, and competition in

the market for goods. This structural change added another source for the widening of income differentials among firms, individuals and localities. China thus follows a pattern frequently observed in history: the early phase in the rise of markets has been associated with more inequ alities.

Table 3: The Two Sources of Inequality in China: Urban versus Rural, Public versus Private Property

Locality / Type of property	Rural	Urban
Collective	Pre 1978 configuration	Pre 1978 configuration
	1	2
	↓ A	↓ A
	3 —— B ——→	4
Private	Intermediate stage	2010 configuration

A: Change in the forms of property in direction of privatization
B: Migration of labor and persistence of rural and urban *hukou*

Source: Own elaboration.

2.3. Large Regional and Urban Inequalities

The very feature of this contemporary industrial revolution and the related dynamism of capital accumulation is spatially embedded: regional unbalances are the counterpart of unequal development of firms and polarization of income distribution. For instance, Beijing, Shanghai and Guangdong contribute massively to the rise of inequality (UNRISD 2010: 722) since in the first phase no or few public transfers from rich to poor regions were organized in order to compensate the violence of marketization.

Within the same province, the diverse localities do not exhibit the same dynamism and therefore inequalities seem to be largely fractal: at each observational level, new forms in the rupture of equality emerge. This is also true within the same city, because new social groups capture a larger fraction of income. Furthermore, in China the absence of a common citizenship builds another obstacle to the equality principle: the rural migrant workers do not have access to the same services as those who enjoy an urban *hukou* when they move and get a job in cities.

Some inequalities are manmade and embodied into laws, regulations, organizations and this open space for policies to reduce them: the gap between rural and urban *hukou* is becoming increasingly attenuated, and the Chinese authorities have finally taxed the richest provinces in order to subsidize lagging provinces, and bit by bit the pieces of a modest welfare state have begun to be built. Nevertheless the vigor of accumulation continues to generate widening inequalities and this raises an important theoretical issue: how can public interventions help the transition from one regime to another (see Section 2.5).

2.4. The Marketization of Agriculture Seems to Have Reduced Inequalities but Capitalist Industrialization has Drastically Increased them

The Chinese trajectory delivers an interesting hypothesis about the impact of market mechanisms upon inequalities: everything is up to the evolution in the degree of concentration they generate. When the liberalization of agricultural products is decided after 1978, quite all peasants seem to benefit from an increase in their real income and standards of living and collective property of land have been maintained: the Theil index (Galbraith 2007: 153) shows a mild decline of inequality within a dominantly rural society. By contrast the opening to modern techniques in experimental free trade zones creates a new dualism between old nationalized firms and joint venture with foreign multinationals, coastal and inner provinces: the Theil index then experiences a fast increase and the defeat of Tiananmen movement might have played a role in preventing the constitution of a countervailing power within Chinese civil society, that could have promoted a less unequal growth pattern.

The competition among firms of diverse forms of property (state, communities, joint venture, private, etc.) sets into motion a typically capitalist process of accumulation. This is ultimately the driver of widening inequalities, more or less in line with the evolution of the world economy. Hong Kong provides a good example of the pervasiveness of the sequence: liberalization and concentration of capital leads to a rupture in the past stability in income distribution at the domestic level. Inequality across nations is thus reduced but individual inequality increases domestically in nearly all societies (Bourguignon 2012). Productive capital mobility at the world level is crucial in generalizing this pattern: higher growth in new industrializing economies reduces their domestic poverty, partially closes the gap with mature economies but also generates a surge of inequality within each society, with only a few exceptions such as Latin America in the 2000s (see Section 4).

2.5. The Threats to Social Stability Call for the Establishment of Modest but Efficient Welfare

China is emblematic of such a transformation: a massive reduction of poverty is a priori sustaining the legitimacy of first internal and then international (partial) liberalization but the explosion of income and wealth inequalities challenges the long term viability of this socio-economic regime.

(1) Economic growth has proceeded accompanied by unfair appropriation of past collective property, such as land, by private interests, personal enrichment of civil servants by corruption, inability of peasants to possess their land and a built-in two-tier citizenship, all of which are threats to the legitimacy of the political system. Accordingly, various NGOs report an explosion of demonstrations and protests at the local level, some of them quite violent. Strong social demands are thus addressed to the political system in the direction of accountability, more of a voice for public opinion and social justice. This is a first source for establishing a form of welfare and expanding social transfers, but two others are quite important.

(2) The level of income is not the only concern of the Chinese population, since the destruction of collective organizations.

(3) Actions promoting solidarity at the work place or community level has first generated the hope that markets would provide the required education, health care, housing or old age pension. This expectation was not fulfilled at all since the differential access to these services across regions, between different firms, urban and rural populations, has been widening, with dramatic consequence for the less privileged. The central government had to respond to this threat and decided to progressively build the possibility of access to some basic welfare to a growing fraction of the population.

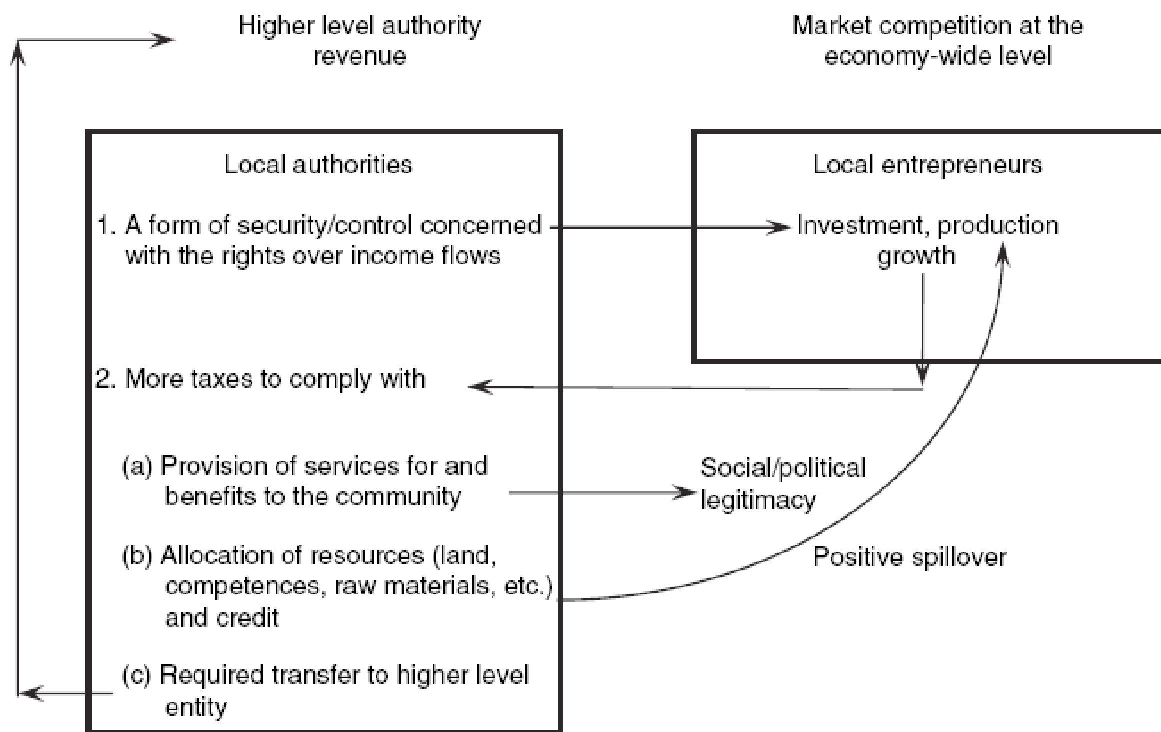
(4) The last structural and historical argument in favor of building a welfare state is that the very success of the new socio-economic regime destroys the past solidarity at the same time promotes a permanent transformation of techniques, products, localizations, and life styles, and thus it creates a state of insecurity, radical uncertainty and potential social chaos. Only the institution of adequate safety nets can stabilize expectations and everyday life continuity. This was Karl Polanyi's major insight and China seems to follow the pattern already observed in history. Since the mid-2000s, the government has decided to organize social transfers towards the

poorest regions, to experiment with an embryonic form of welfare and promote a minimum wage policy. Can these reforms succeed?

2.6. Building Nationwide Welfare Runs against the Logic of the Core Chinese Institutional Form: Local State Corporatism

A converging set of studies suggests that China has invented a way to align, at least partially, the interests of politicians and entrepreneurs: the development of a myriad of local state corporatist entities set into motion by competition-led accumulation (Boyer 2011a). In the absence of a full-fledged legal system and of a unique form of incorporation of firms, public authorities have the ability to define, at least locally and for a given period of time, the rights around the use of resources (land, raw materials, work force, talents, etc.) and to legitimize some rules in the appropriation of income flows. Under this umbrella, entrepreneurs may make decisions about production, investment, and technology. When they are successful, they are creating value that can be allocated for reinvestment, social and infrastructure expenditure, and contribution to the tax base of the related entity. Conceptually, this exchange may propel a virtuous circle involving bureaucrats and entrepreneurs. However, in isolation, such a system runs the risk of becoming more predatory and corrupt than efficient in value creation. There are two additional features of the local state corporatism. On the public side, each entity is partially accountable with respect to a higher rank entity that could correct the most detrimental forms of private appropriation. On the business side, if local entrepreneurs make wrong decisions they will be penalized in the competition with other businesses nurtured by many other localities. Thus, the local state corporatism has another relevant property: to articulate the various levels of Chinese society (Figure 1).

Figure 1: Local State Corporatism Hypothesis: A Synoptic View



Source: Own elaboration.

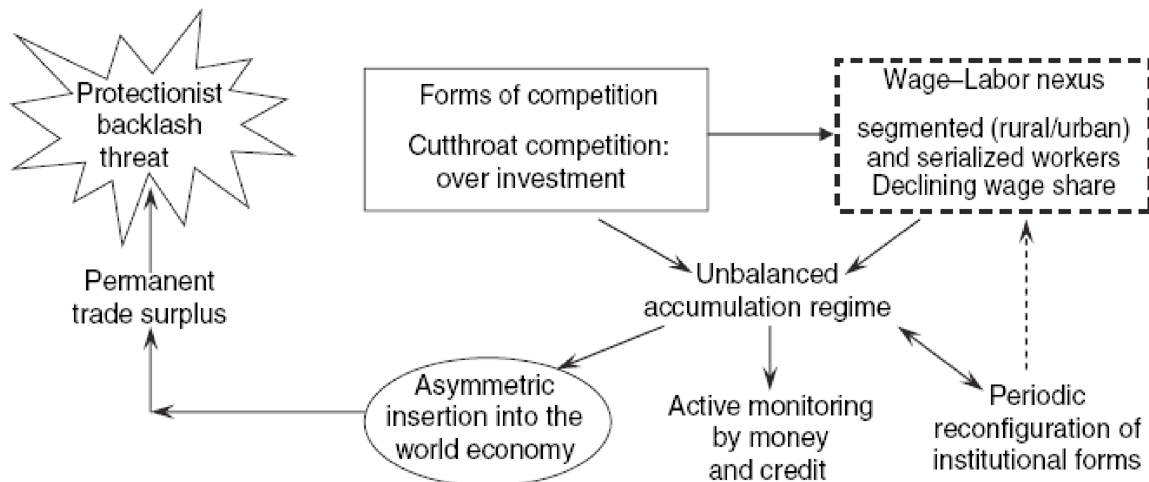
But in this case the central authorities in Beijing have no direct economic policy instrument in order to promote an extension and homogenization of welfare or a form of synchronization of minimum wage increases in order to foster a domestic consumption-led growth regime.

2.7. The Primacy of Competition is an Obstacle to Society-wide Welfare

In essence, the two founding social relations of capitalism are market competition and the capital/labor relation. Their conjunction implies that accumulation is the dominant feature of this socioeconomic regime. In this respect, the present institutional analysis suggests that the Chinese accumulation regime is basically competition-led. In fact, numerous entities with different legal status and localization (village, district, province, and so on) permanently compete to capture natural resources, capital, credit and, finally, product markets. Each local state-corporatist entity faces the equivalent of a prisoner's dilemma: it would like to benefit from the additional domestic market generated by wage increases and welfare implementation in other localities, without risking becoming less competitive. The logical outcome is to set local wage and welfare benefits at the lowest possible level and the overall macroeconomic equilibrium then sticks to the previous competition-led regime. Hence the central government has had

limited success in implementing a minimum level of welfare, a prerequisite for long term viability of Chinese society. To compensate the discrepancy between productive capacity fast growth and lagging domestic consumption, infrastructure investments and sales in foreign markets are used (Figure 2).

Figure 2: Competition: The Hierarchical Institutional Form in China



Source: Own elaboration.

This is a powerful original feature of the Chinese growth regime. Entry into international relations is not forced by the outside but was essentially a domestic policy decision. Quantitatively, the opening of the Chinese economy is impressive, but qualitatively, public authorities still have a remarkable amount of control over capital investments, credit allocation, the management of norms, interventions in the exchange market, and the building up of large reserves in order to prevent the equivalent of the 1997 Asian Financial Crisis. The present argument points out that the regime is not the expression of an ideological or doctrinal preference but the projection of the domestic accumulation regime into the world economy.

2.8. The Specificity of the Chinese Inequality Regime

Three core conclusions and a general hypothesis emerge out the present analytical framework. Firstly, Chinese inequalities are reminiscent of those of past industrial revolutions in Western countries and they seem to follow the typical Kuznets curve hypothesis. They originate from the structural heterogeneity intrinsic to productive modernization and a related mechanism has also been pointed out for Latin America by the founding analyses of the United Nations Economic Commission for Latin America and the Caribbean (ECLAC) (Pinto 1970). All societies do not belong to the same stage

of capitalist development and the same analysis cannot be applied indiscriminately. Secondly, there is a Chinese inequality regime that is also the outcome of specific social relations based upon the fierce competition among numerous local state corporatist entities, mixing polity and economy into a quite resilient trajectory. This explains why minimum wage and welfare policies have not yet fulfilled the expectations of Beijing about a smooth transition towards a consumption led growth. Thirdly, this inequality regime would not be sustainable without the opening of Chinese economy: the built-in productive overcapacity generated by the imbalance between wage and profit is partially overcome by the dynamism of exports to the US, European Union (EU), Latin America and Africa. Each of these entities in turn display quite different inequality regimes and generally speaking the internationalization makes (transitorily) compatible growth regimes that would be unsustainable within a closed economy. In other terms, globalization is the vector of contrasted national regimes of inequality. Let us provide some evidence of this hypothesis by studying the US (Section 3), the EU (Section 4) and finally Latin America (Section 5).

3. The US: From the Golden Age to the Explosion of the Income of the Super-Rich

Clearly in the contemporary American economy, inequalities have been soaring but the mechanisms involved are different compared with those that shape the Chinese trajectory. Not only has the productive paradigm shifted away from Fordism, but also a hectic process of financialization has challenged the previous determinants of functional and personal income distribution. A brief retrospective analysis brings several kinds of evidence to light concerning this new Great Transformation and its crisis.

3.1. The Surprising Post-WWII Growth Regime: Stable and Reduced Inequality along with Technological Dynamism and Growth

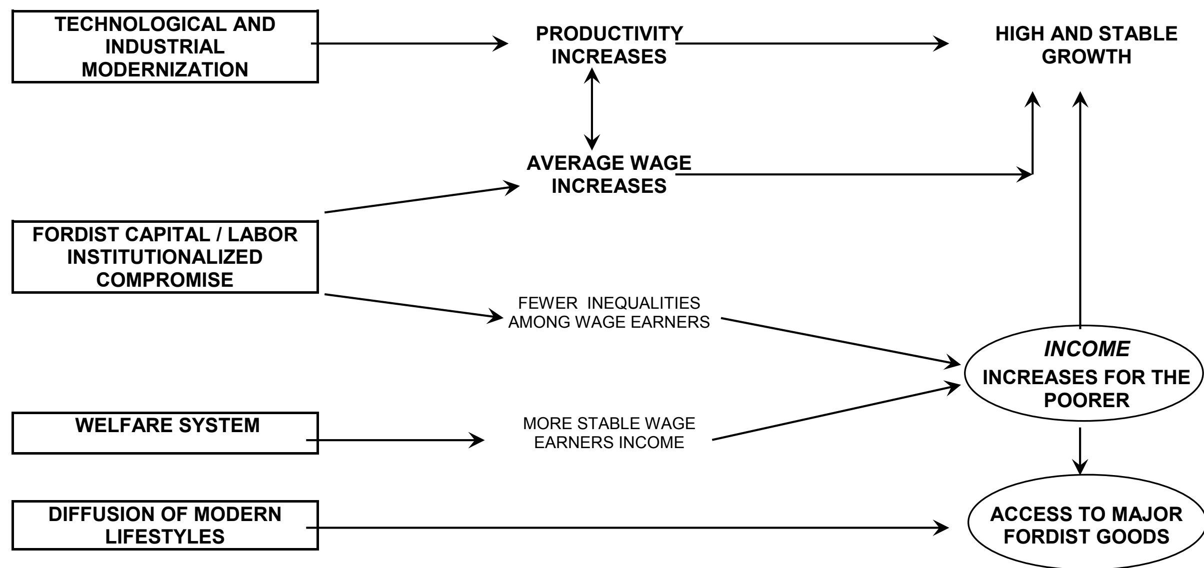
After the traumatic episode of the Great Depression and the large transformations generated by the war, many American analysts were anticipating a possible repetition of the interwar sequence, first a rapid reconversion and economic recovery and then a new period of stagnation and /or instability. Both Keynesian (Hansen 1947) and Marxist (Baran and Sweezy 1966) economists shared this prognosis about the built-in feature of mature economies to generate overcapacity and involuntary unemployment. On the other side of the academic spectrum, modern general equilibrium theoreticians pointed out an irreconcilable trade-off between economic efficiency and social justice: any discrepancy between marginal productivity and remuneration would be paid for by

a loss of welfare compared with the Pareto optimum of a pure market equilibrium. This vision was made popular by seminal textbooks (Samuelson 1948).

The exact opposite was observed from 1945 to 1973: a long period without any depression, fast growth and a remarkable reduction in economic inequality, as shown by Figure 3 below. The American economy changed dramatically with respect to the interwar period and a new growth regime had been explored and implemented. Mass production techniques were converted from the military to the civilian sector, i.e. the mass production of consumer goods; the related increasing returns to scale allowed reductions in relative prices and/or increases in real incomes. Precisely the tendency to build excess capacity was overcome and did not trigger the price wars seen in the 1930s because stronger bargaining power of labor entitled unions to negotiate collective agreements that in effect codified an explicit indexing of nominal wages to inflation and productivity (Figure 3).

Unions also were also stabilizing the hierarchy of remuneration among wage earners of different skills and responsibility, including higher management. In a sense income was largely collectively determined and it was no longer a pure market variable. Nevertheless, this change was largely underestimated by conventional economic theories and it was the starting point of *R*égulation theory (Aglietta 1979). Furthermore these collective agreements also provided the coverage of unemployment benefits, health care, old age pensions, and a contribution to housing; these welfare components thus stabilized lifelong earnings. Welfare was a contribution to the resilience of this Fordist growth regime since it favored the maturation of a modern life style; the complementarity of wage formation and welfare has been sustaining a virtuous circle from mass production to mass consumption and conversely. Not only was poverty largely eradicated but inequality was reduced: this epochal change played a major role in the legitimacy of the post WWII new economic order: social justice/fairness and capitalism were no longer automatically antagonistic.

Figure 3: The Institutional Transformations at the Origin of the post-WWII Growth Regime and Inequality Reduction



Source: Own elaboration.

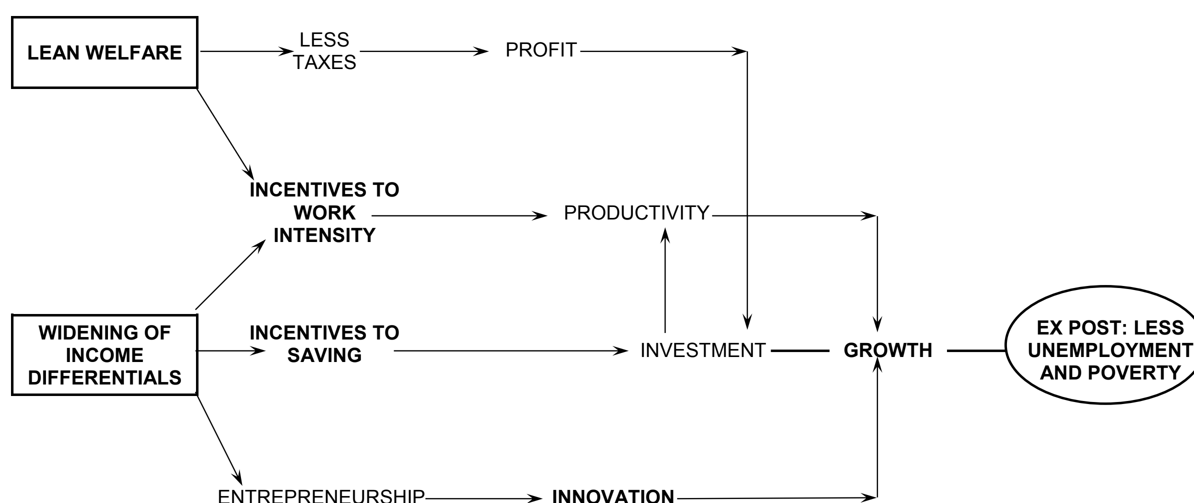
3.2. A New Neoliberal Orthodoxy: Increasing Inequalities are Necessary for Growth Recovery

No socio-economic regime can last forever: its unfolding and success also trigger various transformations that cumulate and finally threaten its structural stability. During the 1960s inflation rates sped up, stagflation occurred during recessions, public deficits were no longer sufficient to fight unemployment, and foreign competition is hollowing out the economy in the form of an external trade deficit, destabilizing the virtuous circle of the past. These macroeconomic disequilibria offered an avenue for a conservative backlash that uses the historical limits of Fordism to propose a radical intellectual alternative: the widening of inequality and the rolling back of welfare are presented as the absolute requisite for a revival of growth. This is presented as necessary to reduce poverty, the only legitimate objective for conservative social policy (Figure 4).

In this conservative vision, inequality is setting the "correct" incentives for a market economy. It is the condition for fostering entrepreneurship, innovation and hence growth. Since the rich save more than poor people, they set the pace of investment via their savings; this is a return to pre-Keynesian conceptions of the investment/saving equilibrium. The large scale of income differentials is also an incentive for work intensity and personal commitment of workers to the objective of the firms. It is also an invitation to human capital formation in order to acquire the competencies required by new technological paradigms. Low taxes and a lean welfare state (actually a workfare

policy) are the complements of this new conception for modern economic socio-economic regimes. Last but not least, economic theorizing gives some justifications for this counter-revolution: the implicit social constructivism typical of the post WWII era is replaced by the motto: “getting the market incentives right” and inequalities are the logical outcome of this strategy. Finally, deepening inequalities is the condition for poverty alleviation, which is both a puzzling convergence with the contemporary Chinese configuration and a distinct rupture with the Golden Age of Fordism.

Figure 4: The Anti-Egalitarian Paradigm Shift of the 1980’s: Inequality-Led Growth



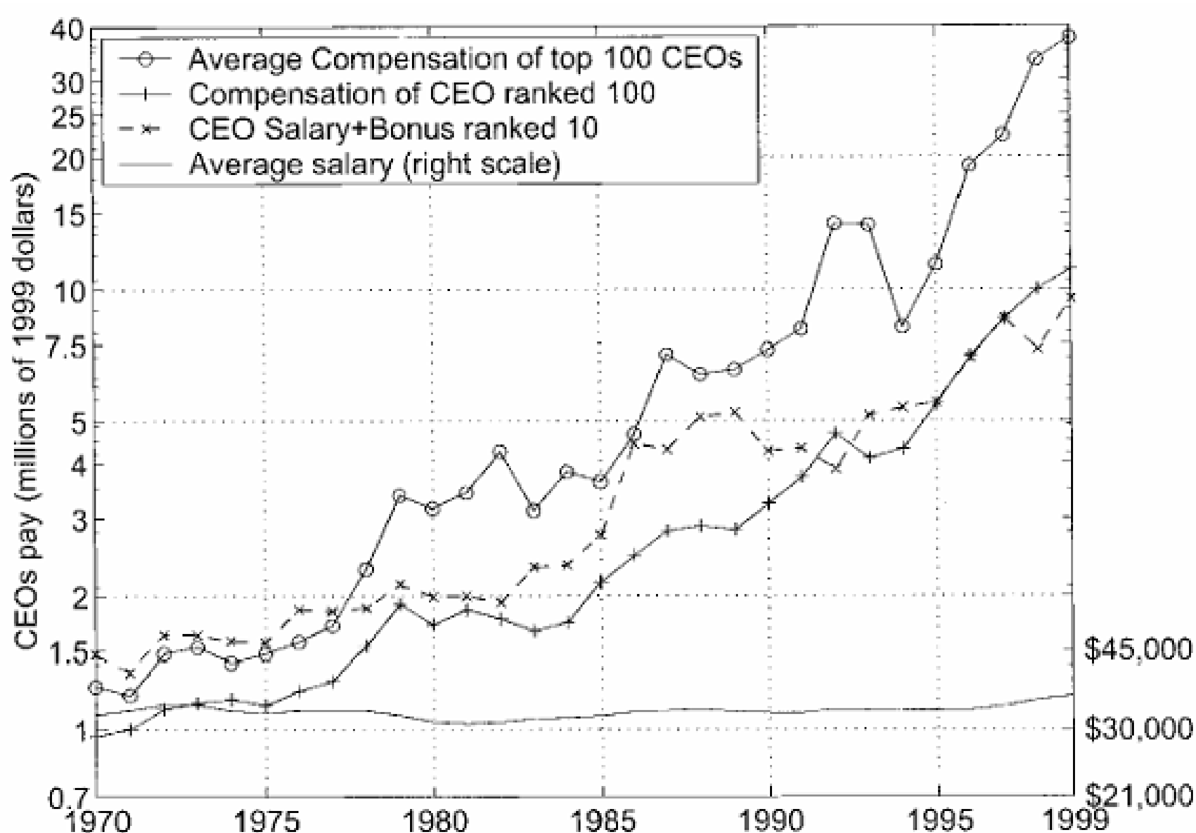
Source: Own elaboration.

3.3. The Rupture in the Alliance between Managers and Wage Earners under the Pressure of Internationalization and Finance

The conservative backlash has not been limited to academic research and ideological discourse. The attack against wage-earners’ power and protection has been consistently pursued under the banner of deregulation of previously protected sectors with high union density. Consequently, most of the coordinating mechanisms for wages via institutionalization have been cancelled and international competition has been the driver towards a complete redesign of remuneration systems. Cancellation of any automaticity in indexing clauses, decentralization of wage formation, wide diffusion of performance-based remuneration, and individualization and diversification of labor contracts were typical features of the 1980s and 1990s. Basically, the firm becomes “a nexus of contracts” and competition among divisions, departments and individuals is organized within the large firm in order to internally mimic market competition. Seniority payment is less and less the standard, and promotions are decided after organizing tournaments in which “the winner takes all” logic diffuses further.

The stability of the remuneration hierarchy within the firm is no longer possible since all these changes make large divergences in income evolution likely: the same skills and competences are no longer rewarded equally across sectors, regions, firms and even within the same firm. The macro-corporatism implicit in Fordism has yielded its primacy and it is being replaced by a series of micro-corporatist systems, in which the remuneration and fate of a worker relies mainly upon the performance of the firm he/she is working for. Fractal inequalities experience an unprecedented rise. Nevertheless, a major and common stylized fact emerges from American income statistics: given the quasi stagnation of total factor productivity, average real salaries have been nearly constant over two decades but the compensation of top level managers has exploded, largely because they have been linked to profit increases and the stock market valuation for listed companies (Figure 5).

Figure 5: The Widening Gap between CEO and Average Wage-Earners Remuneration



Source: Piketty and Saez (2003: 33, Figure 11). Used with permission.

This is the expression of an epochal change in socio-political alliances at the society wide level. Previously, top managers emerged out of an internal selection process among wage earners, and they still considered themselves to be part of the salaried

work force. Since the mid-1980s, they adhere primarily to shareholder value creation and their remuneration is aligned with the assessment of financial markets: financial bubbles periodically boost Wall Street indexes, in strong contrast with the poor progression of productivity in the real economy. This is a second and important factor in the explosion of top incomes and it expresses the alliance of managers with financiers; they no longer belong to the pool of the wage earners that contribute collectively to firms' performance, in contrast to that relationship which continues to prevail in German capitalism.

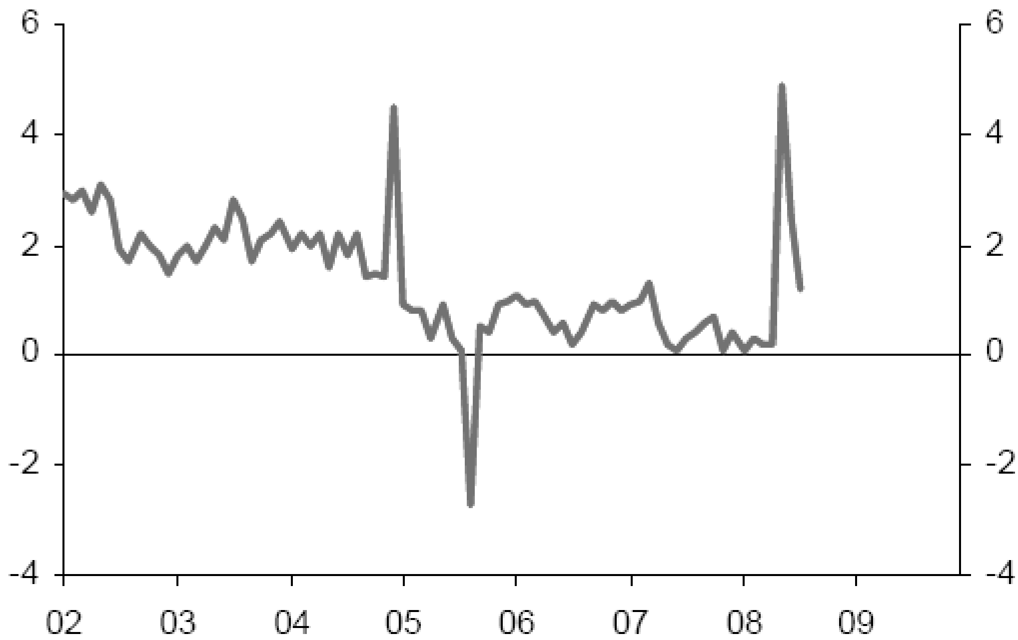
3.4. The Explosion of Credit to Households as an Alternative to Increasing Wages and Fully-Fledged Welfare

The corresponding growth regime is a priori structurally unbalanced: how can rank and file workers sustain consumption that continues to expand at its previous rate if the real wage remains virtually stable? Within each family, more members are having a job, and each of them work longer hours (Schor 1992) but these two strategies have limits in reducing the gap between unit real wage and household consumption trends. Here comes the other side of the rise of finance: the deregulation, globalization and the induced innovations propel new financial instruments such as subprime credit and securitization that allow easier access to credit even for the poorest fractions of the population. Not only does borrowing pay for housing and modern consumption goods but with credit they also can afford the costs of health care and university education. Given the blocking of an extended welfare system by the tax cut policies decided under the Reagan and Bush administrations, bank credit was a partial substitute for a collective organization of social security. A lax credit policy was in fact the compensatory device used to limit the adverse consequences of explosive inequalities of income upon the viability of this new regime.

A second feature has to be added in order to capture the novelty and specificity of the North American inequality regime. With the growing reluctance of firms to pay for a "pay as you go" pension with defined benefits, insurers and financiers propose and workers unions have to accept the transition towards defined-contribution pension funds, with all the risk associated with this individualization and exposure to the ups and downs of the stock market. The corresponding legislation ERISA (Montagne 2006) propelled a massive inflow into the American financial system and generated a succession of bubbles (internet, real estate, stock market) in which households feel as if they are rich due to portfolio wealth and house prices which in turn are used as collateral for getting even more credit. Thus in the 2000s, the household saving rate converged towards zero (Figure 6) and the constant rise of the debt/disposable income ratio (Figure 7) allowed

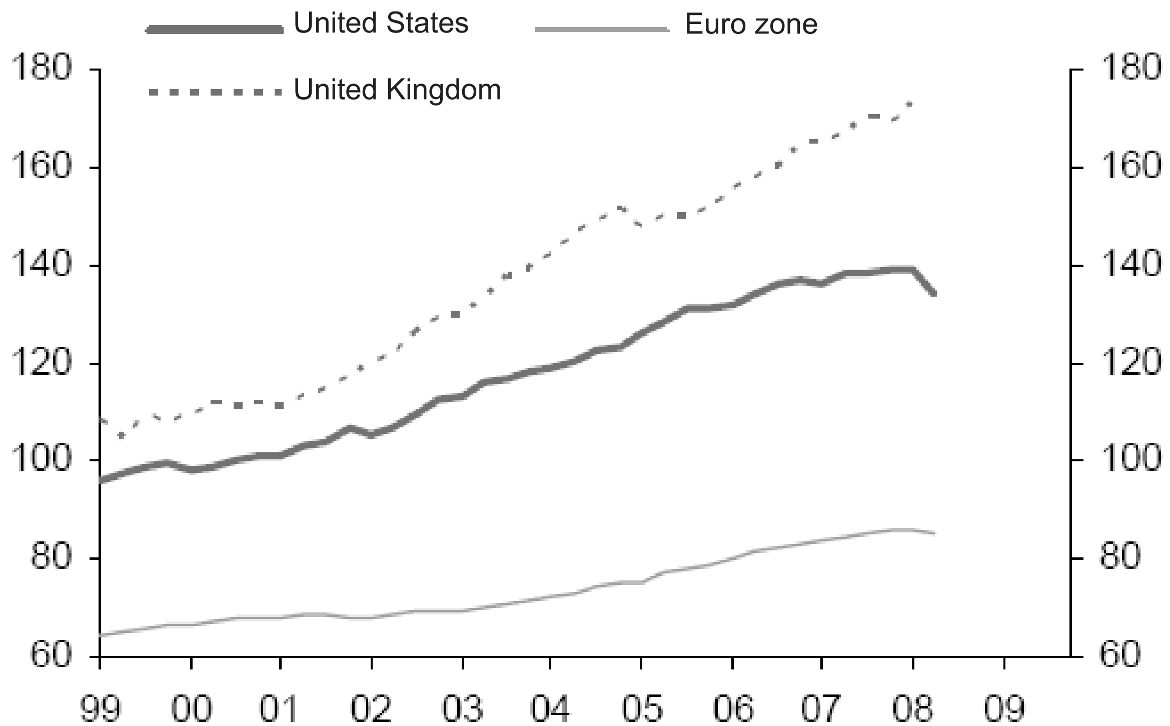
for a remarkable, but unsustainable, disconnection between income, consumption and investment in real estate.

Figure 6: Very Low Savings Rate of American Households



Source: Artus (2008: 2). Used with permission.

Figure 7: Debt as % of Income Growth



Source: Artus (2008: 2). Used with permission.

This explosion of credit and sophisticated financial instruments allowed a new economic regime but then quickly undermined the stability of the ratio of financial wealth to GDP observed until the mid-1980s. Consequently, the financial sector was no longer simply shifting profits from one productive sector to another, but it is appropriating for itself an increasing fraction of national aggregate profits (Crotty and Epstein 2008). These profits in turn tend to be distributed via bonuses, stock options and dividends, hence accentuating the gap between top incomes and median incomes which are mainly dependent on wages. A significant part of these extra profits originate in the relaxation of financial regulations which eased credit access for the less wealthy part of the population. This configuration reveals a striking paradox: the financiers have found a new source of profit by giving credit to the poor. Hence inequality is extended at the two extremes of the income distribution and the two evolutions are closely linked.

3.5. Financialization Enables a Huge Income Transfer to the Super-Rich

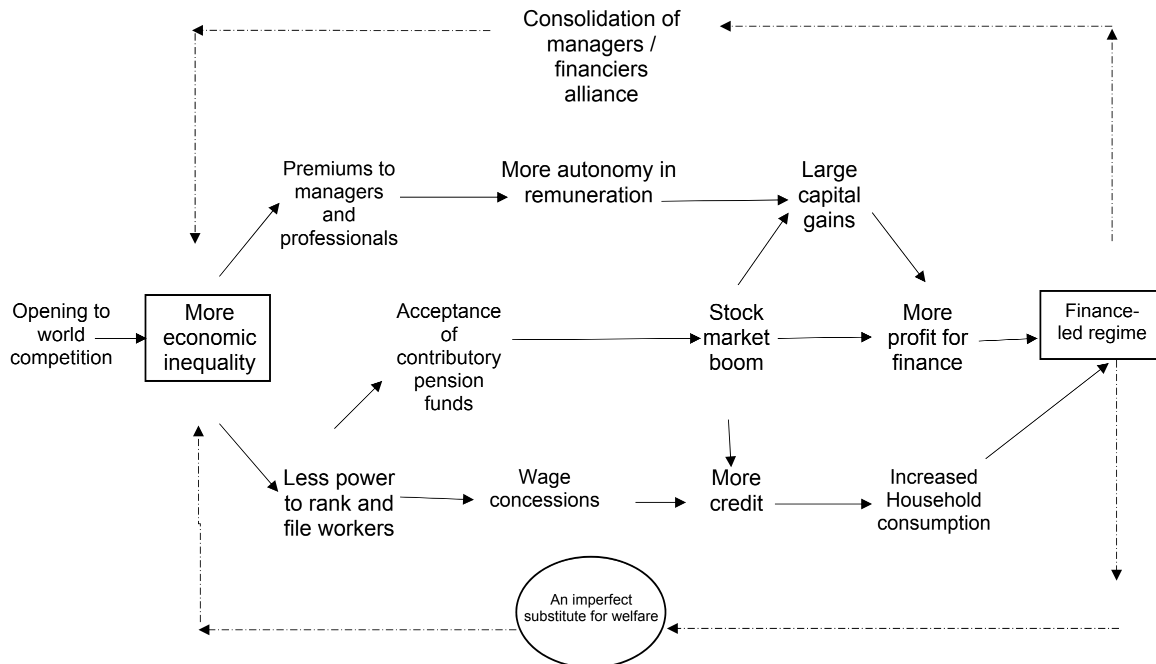
Finance clearly not only was and still is the driver of macroeconomic activity, but it is also the origin of an unprecedented polarization of personal income since the 1930s (Figure 8, below).

(1) In the lower part of the distribution of personal income, an easier access to credit makes tolerable the stagnation or even decline of the less skilled workers, severely hit by the delocalization of typical mass production, and the rise of tertiary jobs poorly unionized. Clearly it allows the ongoing progression of consumption, itself the driving force of the US economy. In a sense financial innovation is a countervailing factor against the negative impact of more acute foreign competition.

(2) In the upper part of the income distribution, the multiplication of new financial instruments and the alliance of top managers with financiers trigger a rapid rise of capital income and gains and this strengthen the impact of remuneration individualization along a “the winner gets all” the logic. The depth and fluidity of deregulated financial markets enables a rapid concentration of wealth among the best informed and dominant actors, compared with the slower motion of productivity and other performance indexes in the manufacturing and service sector.

Consequently the opening to world competition and then financial innovations define a new growth regime that is structurally unbalanced: income and wealth inequalities are functional to this new social configuration (Figure 8). By the way, let us note how different are the sources of inequality in the US and China (see Figure 2 above).

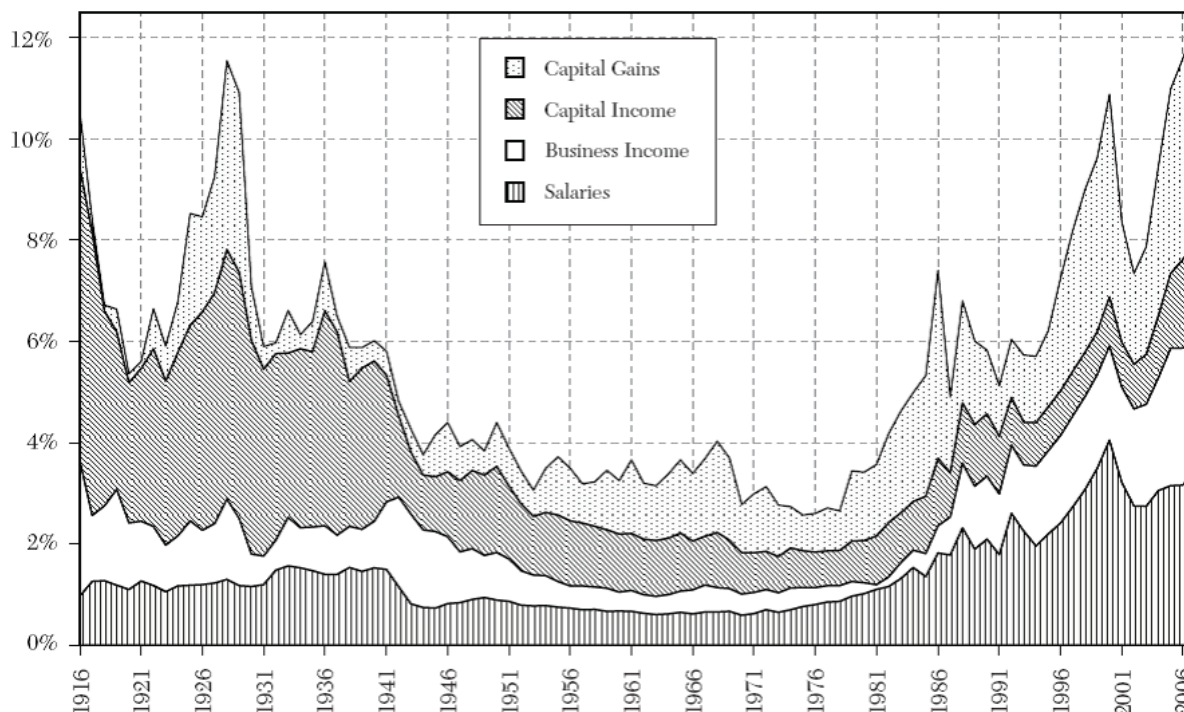
Figure 8: How Inequality Favors Finance and How Finance Exacerbates Inequality: The Contemporary American Inequality Regime



Source: Own elaboration.

This framework explains why recent studies do not consider only the traditional distribution according to deciles but also point out the concentration of income increases in uppermost percentiles. Compared with the Golden Age, the highest percentile has tripled its share of income from the 1980s to the mid-2000s, and both performance-related salaries and capital gains contributed to this explosion. This is partially reminiscent of the 1920s, but then capital income was the leading factor (Figure 9).

Figure 9: Capital Gain and Income are the Main Sources of the Rise of Inequalities from the Top of the Distribution (Higher percentile)



Source: Atkinson, Piketty and Saez (2011: 8). Used with permission.

3.6. Power Asymmetry in the Economy is Converted into the Ability to Design Economic Policy and to Block any Regulation

In typical liberalism and still more within ordo-liberalism, the rules of the game are set and kept independent from the lobbying of the most powerful actors. By contrast, in the present phase of neo-liberalism, the winners are able at will to alter the rules to their benefit. For instance, in the US, maintenance of a progressive personal income taxation would have certainly mitigated the rapid rise of top incomes. But in fact, the beneficiaries of the post Fordist, competition and finance-led regime have been able to convince officials of the United States Government, Congress and Senate that a non-progressive, flat tax rate was essential for innovation, growth and job creation (through conversion of their wealth into investment) in order to convert their wealth into investment, innovation and finally growth and job creation. The conservative counter-revolution to the Golden Age contributed also to the legitimation of this new fiscal paradigm (see Figure 4, above).

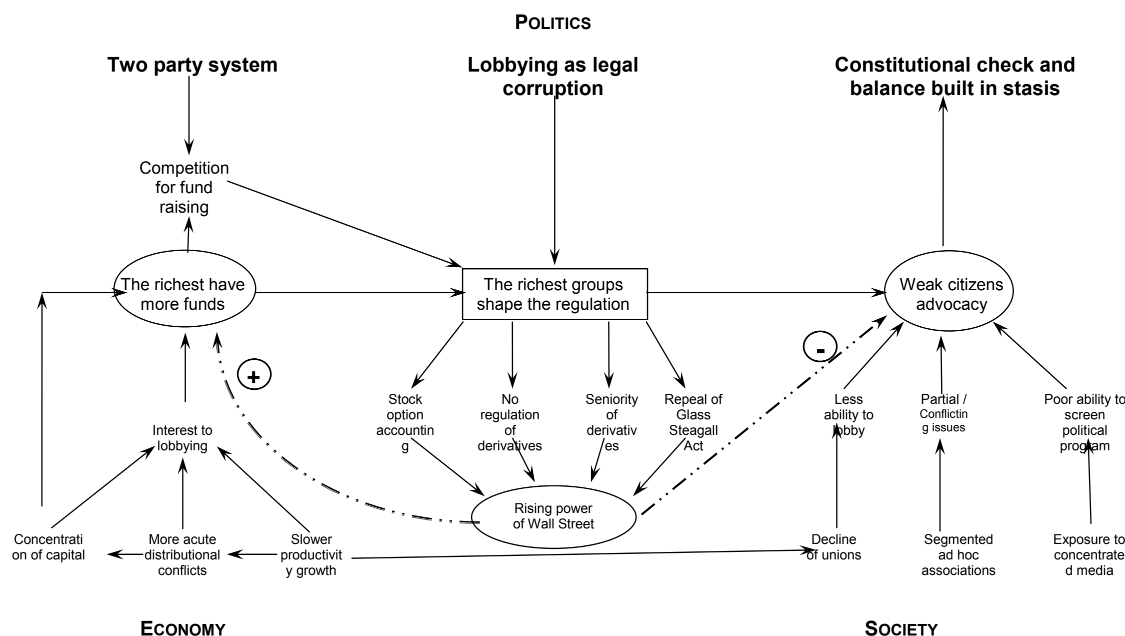
The change in taxation principles is impressive indeed when one compares the 1960s with the mid 2000s. The highest 1% now enjoys the same flat rate for income tax as the

highest 10%: the revision has mainly benefited the super-rich with some concessions to the middle class; this political coalition has been successful in redesigning the whole regulatory and legal American system (Piketty and Saez 2007: 12). Thus the change in the American inequality regime was politically driven and not the mere consequence of external and exogenous economic forces. The opening to competition shifted the bargaining power away from unionized labor; financial liberalization has been presented as a normal follow up of product and labor deregulation; in turn, the extreme capital mobility and the construction of large and deep financial markets has justified a drastic decline in the taxation of profit and capital gains. Such are the spill overs from economy to polity and from geo-polity back to economy.

Most of American inequalities are thus collectively made by explicit strategies of dominant economic groups in a successful strategy to build an institutional order convenient for the preservation and defense of their private interest. This is the expected conclusion from a political science approach (Hacker and Pierson 2011). One novelty is that a growing fraction of economists have become persuaded of the same diagnosis: an entrenched economic power has been converted into the ability to shape collective organization, including via the diffusion of a free market ideology and active lobbying in favor of deregulation and the absence of any collective control over financial innovations (Stiglitz 2012).

Many features of the US political system combine their effects and explain the emergence of Wall Street power to prevent any effective public control over their dangerous but highly profitable financial innovations (Figure 10). First, the two-party system implies a competition for fund-raising for each election and typically the rich part of the population usually outspends the advocacy groups defending citizens and consumers. Second, on top of the electoral process and on an everyday basis, the leading economic groups have the resources to pay lobbyists in order to be sure that laws and regulations will take their interests into account. Under U.S. election regulations, these contributions and expenditures are disclosed to the public. This transparency actually hides what should be labelled as corruption in most other societies since it runs against the principle of equality of the expression of all citizens whatever their income. Third, after the Lehmann Brothers collapse and the major economic crisis, American presidents have been unable to impose a drastic re-regulation of finance since the check and balance principles, embedded into the division of power between the legislature, courts and the President, have preserved the heart of the influence of financiers: their lobbies continue fighting against any more restrictive legislation such as the Dodd-Frank Act, and until now they have been successful.

Figure 10: How the Capture of the State and Political Arena by Key Economic Groups Has Allowed the Explosion of Inequalities in the United States



Source: Inspired by Jacob S. Hacker and Paul Pierson (2011: 163-306).

In spite of recurring scandals (insider trading, golden parachutes, Libor fixing by collusion…) and the unpopularity of Wall Street among citizens who lost their homes and jobs, top managers' remunerations still defy the law of gravity. It is the very consequence of American core political institutions and not the outcome of any invisible hand promoting pure and perfect competition. Again, as in China, but differently, the American inequality regime is manmade.

3.7. The Joint Consequence of Full Liberalization: Wider Inequalities and Financial Crisis: Karl Polanyi Was Right!

In retrospect the macroeconomic regime, described by Figure 8 above, proved itself to be unsustainable as soon as the price of housing stopped rising, but this could also have been anticipated well before the crisis: the poorest could not service their debt given the erosion of their purchasing power (Boyer 2000a). Hence the adhesion to neoliberalism has set into motion two destabilizing processes. On one side, the share of income held by top 10 % shifted from 34 % in the 1970s to nearly 50 % just before the crisis, i.e. a configuration equivalent to that of the 1920s. Such trends could not last forever, for clear social and political reasons. The other side of the coin is the unfolding of a bubble that is bound to burst out as soon as any bad news twists overly-optimistic

expectations into a panic, only stopped by the complete guarantee granted by the Central Bank and Treasury to the financial sector.

Long run historical data confirm the relevance of this analytical framework (Moss 2010). The explosion of credit feeds a boom, a concentration of income and the illusion of a new and unprecedented regime devoid of any crisis. This occurred in the 1920s and it has been repeating in the 1990s with the collapse of the New Economy financial bubble and finally with the subprime crisis in the 2000s. Then bank failures speed up and top incomes experience a steep, but temporary, decline. Consequently, the American financial and then economic crisis is also a symptom for an unfair and unbalanced society.

Hence the commodification of labor (wage tends to become again a pure market variable, welfare is converted into workfare) and the privatization of money (by the ease in the creation of highly liquid financial instruments) put the American economy at risk. If ones adds the marketization of nature (carbon emission trading, valuation of bio-diversity, options linked to climate), the basic intuition of Karl Polanyi is quite relevant for our times: such a society is not viable and should generate vigorous social movements to stop unlimited marketization.

3.8. The US and Chinese Inequality Regimes are Different but They Express Complementary Growth Patterns

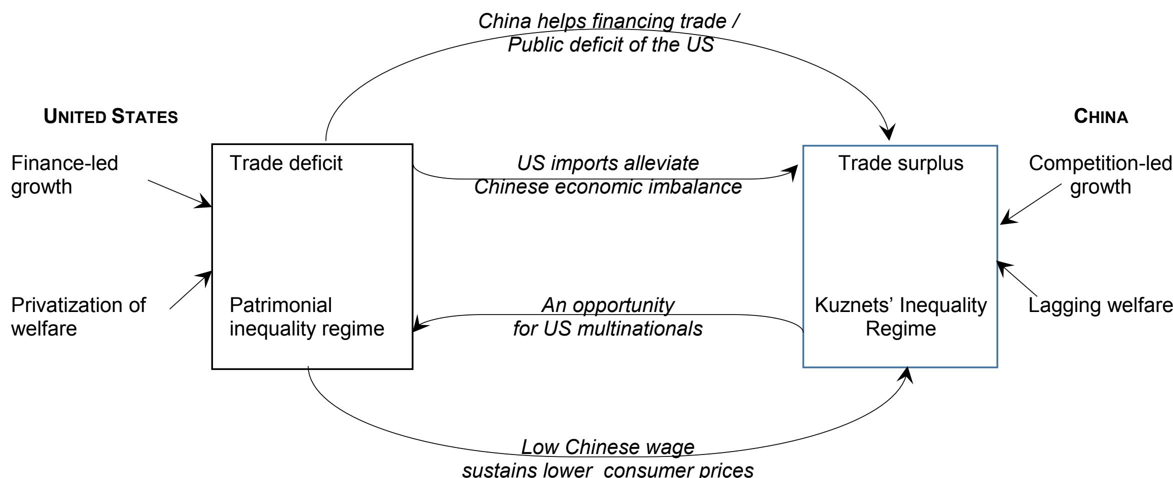
This rather long analysis shows that these two societies are contemporary but they do not display the same accumulation patterns and inequality regimes, but they seem to be unable to operate without their opening to the world: in a sense, their mutual exchanges are contributing to their viability that would not be warranted within a close economy context (Figure 11).

(1) In terms of growth regimes, the dynamism of American consumer demands, associated to an intensive delocalization of productive networks, generates a cumulative trade deficit, while the hegemony of finance implies tax cuts that favor a permanent government budget deficit. A symmetric configuration is observed in China: transformed into the manufacturing base of the world, the economy generates a large trade surplus since the competition-led growth regime implies a permanent overcapacity. This feature of China, in turn, enables the financing of the American economy via purchase of American Treasury bonds. None of the two economies is closed any more since they have become more and more interdependent and the viability of their growth regimes is up to the management of this interdependence.

(2) By correlation, the American patrimonial inequality regime and the Chinese Kuznets inequality regime are interrelated. On the American side, the permanent rise of manufactured goods imported from China contributes modestly but consistently to improvement in standards of living, and the inflow of Chinese saving permits lower interest rates and the easy terms for higher-risk loans and as well as the public deficit. The American inequality regime is thus made acceptable and viable as far as a real estate bubble persists. On the Chinese side, rapid productive modernization triggers an explosion of inequalities but the dynamism of investment and of exports after 2000 reduces drastically poverty and diffuses the expectations that upward mobility opens an avenue for becoming rich to Chinese people. Metaphorically, the poor welfare of Chinese workers helps sustaining the American way of life for the poorest fraction of the population unable to pay for private insurance and access to welfare.

Let us extend this general hypothesis to two other zones of the world economy, Europe and Latin America.

Figure 11: The American Patrimonial Inequality Regime and the Chinese Kuznets' Inequality Regime are Complementary



Source: Own elaboration.

4. The European Crisis: False Attribution to Welfare of the Disfunctionality in Eurozone Treaties

There is no better counterexample against the common hypothesis about the convergence of institutional configurations under the pressure of globalization. In the US, the perception that inequalities are a threat to the cohesion of society has permeated the political arena and led to ultimately successful calls for a reform of health care coverage. The Chinese authorities have recognized the social and ecological unsustainability of their modernization strategy and have begun to study and implement safety nets in the direction of a genuine welfare state. By contrast the Euro zone crisis has induced a dramatic reappraisal of the merits of universal welfare systems: cuts in health care, education, unemployment benefits have been imposed by the European Commission in most Southern Europe societies. How to explain these diverging trajectories? A brief historical retrospective might explain this apparent paradox.

4.1. Europe: Homeland of Bismarck and Beveridge

The first industrial revolution took place in England and diffused with a lag to Germany and France, which triggered a process of organizational and social change that brought an economic insecurity and inequality widening. The related issues then triggered open conflicts about capital/labor relations in order to limit wage decreases during periodic crises, to insure industrial accidents collectively, to fight against infant mortality, to implement old age pensions, safety nets against unemployment and finally family allowances. This is precisely the pattern observed in Germany that was a pioneer in the promotion of a redistributive system that would deliver workers' security and reduce the inherent trend of capitalism towards greatly increased inequality. This early welfare system is labelled as Bismarck's contribution to the emergence of a specific brand of capitalism. The British trajectory is different in its timing and precise organization and financing of a welfare system aiming at making viable and acceptable industrial capitalism: Beveridge proposes an integrated system based on general taxation and not social contributions that organizes the solidarity only among wage earners, a corner stone of Bismarckian welfare systems. An international comparison suggests two major lessons: first, fighting against insecurity and inequality is a long historical process that requires a permanent adjustment to changing technological, social and political conditions; second, each society has found its own way and method for organizing its welfare system (Table 4).

Table 4: The Construction of Welfare Systems: A Long National Historical Process. Dates in the Creation of Various Insurance Regimes

Countries	Industrial accidents	Health	Pensions	Unemployment	Family
Germany	1884	1883	1889	1927	1954
France	1898	1930	1910	1914	1932
	1946	1945	1930	1959	1945
			1945	1967	
Italy	1898	1886	1898	1919	1936
		1928	1919		
		1943			
United Kingdom	1906	1911	1908	1911	1935
	1946	1946	1925	1920	
United States	1930	1965	1935	1935	
Canada	1930	1971	1927	1940	1944

Source: Own elaboration.

The foundation of these social security systems opened a new epoch for European societies. Public spending that represented 8.7 % of German GDP in 1881 rose to 43.1 % in 1930 and then 46.9 % in 1977 (André and Delorme 1983) and social expenditures grew from 0.7 % of GDP to 30.4 % and finally to 32.0 % in 1977. The bulk of public spending occurred in response to the rise of social welfare expenditures: they represented less than 7.7 % of total public expenditure in 1880 but 68.9 % at the end of the same period (André and Delorme 1983: 11). The timing is different for the United Kingdom (André and Delorme 1983: 30) but the trend is the same: the contemporary societies are welfare state capitalist ones, since public transfers are providing basic social services (health, education, pension, family, unemployment insurance): they are the core of the interventions of modern states.

These institutional transformations seem to have played some role in the remarkable reduction of income inequality from 1940s to 1980s both in the UK and Germany. Nevertheless, with the opening to world competition and the rise of international finance, this configuration has experienced various strains that have stopped the reduction of inequalities.

4.2. A Limited and Uneven Rise of Inequality in Europe, But Growing Financial Unbalances in Welfare Regimes

As already pointed out, the United States had in the 1920s experienced a concentration of top incomes and this feature had some role in the macroeconomic unbalances that led to the Great Depression of the 1930s. Canada and Ireland followed the same pattern. The crisis and the aftermath of WWII exhibit a large decline of the share of income at the top; the institutional transformations shown in Figure 3 contributed to this change and opened the Golden Age of Fordism in which social justice and economic efficiency were no longer antagonists, but this genuinely new configuration was subsequently eroded by the ongoing deregulation of markets for products and labor, and eventually, for financial services. Progressive income inequality then reached the level of the 1920s. The UK and other English speaking countries follow the same trajectory, with the exception of New Zealand (Atkinson, Piketty and Saez 2011).

The conventional wisdom would then infer that globalization diffuses the process of deregulation, decentralization and individualization of remuneration makes the English pattern the benchmark everywhere around the world. Continental Europe and Japan define interesting counter examples: income distribution does not shift in favor of the rich or, if so, only moderately (France for instance). A rather limited labor market deregulation, a personal income tax system that remains progressive and a multifaceted and extended welfare have contained the explosion of inequality with the possible exception of Germany that has implemented a slimming down of welfare benefits since the 1990s (Piketty and Saez 2007). Thus societies may continue to express their preferences for equality but it has a cost, i.e. a large public financing by social contributions and/or taxes.

Unfortunately since the 1990s, slow growth has been the rule in Europe and this has generated a widening gap between the financial resources allocated to welfare and the further evolution of benefits, especially for health insurance and unemployment coverage. The Lisbon Strategy was aimed at speeding up technological change and growth in order to sustain the high European level of welfare, but it largely failed, and dramatically so for southern European countries. Public deficit spending and even more public debt were used to compensate the erosion of their competitiveness and growth potential in the long run. When the subprime crisis was converted into the threat of a world depression, European economies initially benefited from the automatic stabilizers of an extended public sector and welfare state. Unfortunately, this was not a typical business cycle since it meant the entering of a long lasting systemic crisis, especially for the Eurozone institutions. The partial recovery was stopped by the

diffusion in 2010 of austerity policies that intend to first restore sound public finances. Higher taxes accompanied cuts in public employment, reductions in education and health expenditures, i.e. the core component of the past socio-political compromise upon an extended welfare state.

In some weak economies, the sustainability of welfare itself is at stake: public opinion is strongly attached to equality but economic resources no longer sustain the welfare and tax systems that pursue this objective. Nevertheless, the scarcity of public financing is not the only reason for this contemporary threat to European welfare.

4.3. A Neglected Defense of the European Pursuit of Equality: Social Insurance Contributes both to Welfare and Competitiveness

The ideological and theoretical representations of welfare have an impact upon the direction of reforms. Since the Beveridgian systems impose growing costs on labor and deteriorate competitiveness and employment, this is presented as a justification for welfare cuts. Similarly, Bismarckian systems are facing the tax revolt of middle classes and the erosion in their tax bases due to high financial capital mobility. Social security is analyzed as a pure cost without any positive and significant contribution. This reductionist accounting-based vision totally neglects that social security promotes wellbeing through better security that it generally reduces inequality and it may also be the catalyst for dynamic economic efficiency. This trilogy was first pointed out for interpreting the “Dutch miracle” (Visser and Hemerijck 1997) and can be summarized by a synthetic diagram (Figure 12).

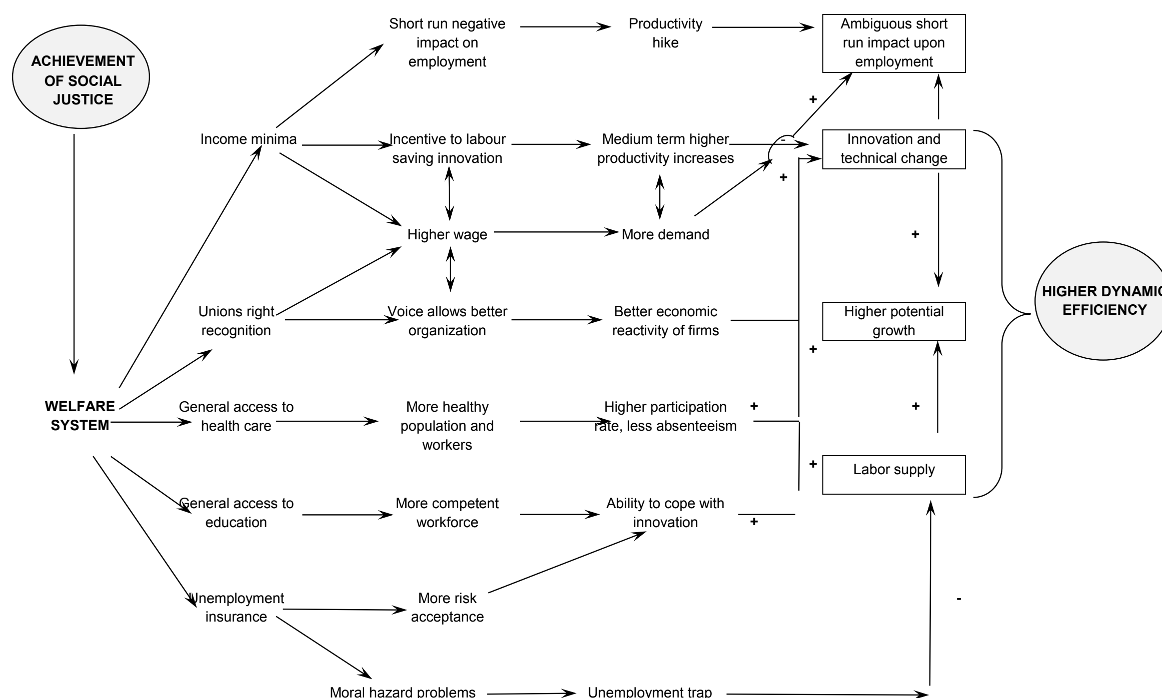
(1) Education means nurturing learned citizens, a health care system delivers longer life without major diseases, unemployment benefits and minimum wage reduce the poverty among wage earners: wellbeing has been improved even if this contribution is not measured by current methods of calculation of national accounts.

(2) Since the provision of education, health and insurance against economic risks are collectively organized and financed by society-wide contributions, the welfare and tax systems exert a clear redistributive impact and they are tools for promoting a limitation of inequalities. *A contrario*, the individualization of insurance contracts, the decentralization of many components of welfare and the rise of pension funds are sources for diverging trajectories among individuals with quite similar initial characteristics.

(3) The feedbacks from welfare to the economy are numerous and can make clear contributions to innovation, growth and economic performance. A dynamic policy for minimum wage increases might temporarily hurt less productive firms but it is an incentive for labor saving innovations and a long run increase in productivity. Furthermore, within wage earner societies, salaries are key determinants for consumption and global demand and thus they may compensate the labor saving bias by a co-evolution of demand. In a sense, the conceptions of Schumpeter and Keynes are more complementary than opposed (Dosi 2009). Health expenditures contribute to better health, less absenteeism and a longer life expectancy which in turn allow for a higher return of the investment in education and training. Education, conceived as acquisition of the ability to learn how to solve problems for the majority of the population, brings a key ingredient to the dynamism of national systems of innovation. Nordic countries have pushed one step forward the hints derived from the Dutch polder model and they recurrently adjust the complementarity between their welfare and innovation systems (Boyer, forthcoming). They propose a similar update concerning unemployment benefits: they do not generate any unemployment trap if a generous replacement rate is complemented by an active training policy in order to reallocate manpower to sunrise, fast growth and high productivity sectors.

Thus, outside Nordic countries, the rationales for a universal welfare state in symbiosis with the national innovation system have been abandoned in favor of a crude accounting approach to cost reduction, in complete disregard of the adverse effects upon population wellbeing, long run productive capacity and ability to innovate and explore an upgrading of economic specialization.

Figure 12: How Some Welfare Systems Enhance Dynamic Efficiency



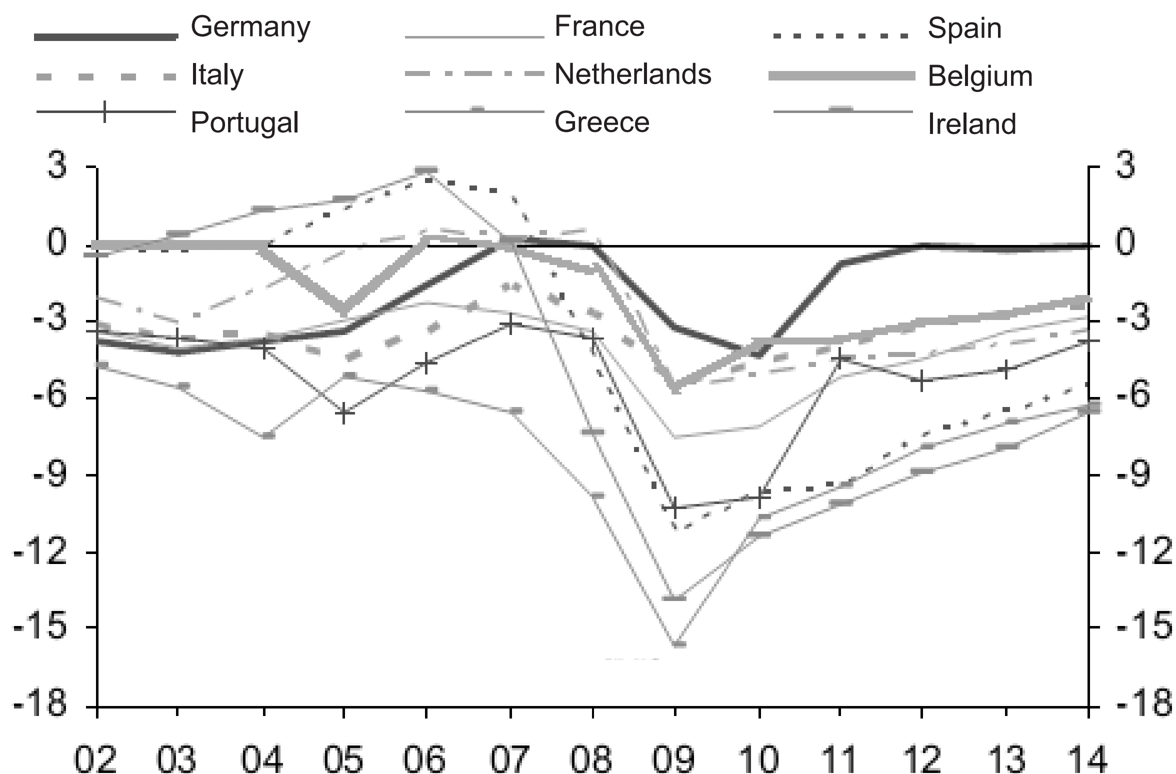
Source: Own elaboration.

4.4. The Financial Constraints Generated by the Crisis are a Threat to European Welfare: An Erroneous Interpretation

A second misinterpretation relates to the diagnosis made by European leaders about the origin of the Eurozone crisis: excessive public deficits are thought to be the only cause of financial speculation about the end the Euro; therefore austerity policies are the cure to be administered. Unfortunately this statement confuses the highly specific Greek crisis with the overall mechanisms that led to the Euro crisis. Basically it was the unexpected outcome in the transmission of Lehman Brothers collapse to American macroeconomic activity and finally to the rest of the world including the European Union. Given the size of public spending and social transfers in GDP, automatic stabilizers limit the severity of the recession at the cost of larger public deficits. Actually, for the majority of the members of the Euro, the crisis is not at all the consequence of lax and badly conceived public policies: just before September 2008, Germany, Spain, Ireland and Belgium even enjoyed slight public surpluses. In Germany this was the consequence of an early slimming down of welfare benefits by the successive Hartz programs and for other countries an intense real estate bubble fuelled by very low interest rates was the cause of this good but artificial health of public finance (Boyer 2011b). The cure should have been searched for by the restructuring of the real estate sector and the fast recapitalization of ailing banks. By contrast, the financial markets

have been attacking the Treasury bonds of the countries that exhibited the larger public deficit, whatever its cause, thus confusing a typical bad public management in Greece with the spill over from finance to public deficit (Figure 13).

Figure 13: Ireland, Spain, Belgium and Germany: Public Budget Surplus/GDP (%) before 2008



Source: Artus (2013a: 5). Used with permission.

This largely erroneous diagnosis has a logical outcome: the way out of negative expectations by financiers about the Euro viability is then to cut down public spending – public infrastructures, education, health care and even research – and to slim down welfare benefits. These are precisely the components of welfare-led dynamic efficiency (Figure 12, above) that were supposed to be the drivers of the Lisbon Strategy in order to reconcile social cohesion and innovation dynamism. Furthermore the very extension of public and welfare expenditures explains the hollowing of public deficits in reaction to the sharp decline in world trade and then domestic GDP: automatic stabilizers play their role but most experts and governments interpret them as an evidence for an over extended and/or mismanaged welfare. Austerity policies are imposed by European authorities and reiterated even after 2013, when their negative impact upon growth and employment is recognized by most macroeconomists from academia and the IMF (Blanchard and Leigh 2013). A vicious circle is thus unfolding from slow growth to public

deficits, from welfare cuts to recession and finally from low investment to sluggish productivity and capacity reduction. Ex post, welfare appears to be unaffordable given the depressed domestic economy. Nevertheless most citizens continue to defend their rights to security and decent living conditions. This leads to an open political instability in the most severely hit member states of the European Union (Boyer, forthcoming).

4.5. The Resilience of Social Democratic Capitalism

Is the European model built upon moderate inequalities limited by an extended welfare, progressive personal taxation and regulations governing wage formation passé? Not necessarily, since when correctly understood, adequately implemented and periodically reformed, welfare capitalism can prosper even in the epoch of intense world competition (Fellman et al. 2008; Pedersen 2008).

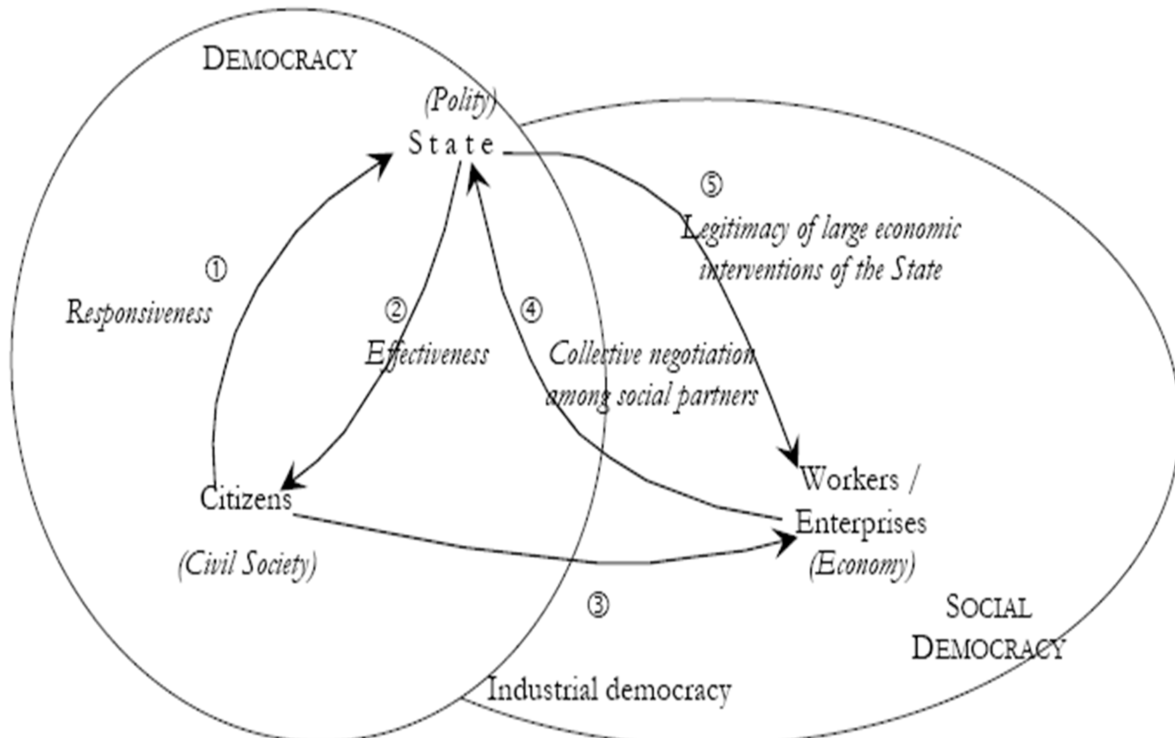
(1) On one side, the Nordic countries continue to take seriously the possible contribution of welfare to national competitiveness: at each period, policy makers have searched for a compromise among firms, wage earners and citizens in order to activate some of the relevant mechanisms that link the welfare regime and the innovation system (Boyer, forthcoming).

(2) On the other side and by contrast, Southern European countries have been unable to organize such a complementarity, especially in terms of innovation-friendly labor legislation and welfare: with the Euro, given the loss of the use of periodic devaluations as a compensating valve for poor structural competitiveness, they are unable to sustain their relatively limited but dysfunctional public sector and welfare as soon as international credit stops financing their trade deficit. In fact, contrary to the conventional view, Greece, Portugal, Spain, and to some extent Italy and France, suffer from their distance from the ideal European welfare capitalism, and not at all from its intrinsic failures.

A political economy analysis brings another argument in favor of the better resilience of social democratic configurations: compared with typical liberal capitalism they allowed a much more moderate widening of inequalities. Basically, the strengthening of workers' rights in the economy gives them many tools to defend welfare and entitles them to be more active citizens in the political arena. This complementarity of the two spheres feeds back into a virtuous circle where by citizenship and wage labor nexus are both transformed by the implementation of democratic principles. Consequently, in spite of a wide opening to world competition, economic, social and political inequalities are contained in most social democratic countries (Figure 14). The distribution of power

among firms and wage earners, the government and citizens, contrasts sharply with the configuration observed in market-led capitalisms (see Figure 8, above).

Figure 14: Why the Social Democratic Citizenship Protects the Rights and Power of Wage-earners, thus Limits Inequalities



Source: Own elaboration.

4.6. Defense of Rights to Economic Security is Crucial for the Emergence of a Virtuous Growth Regime with Stable and Reduced Inequalities: A Hidden Precondition for the Danish Flexi-Security Model

A third factor appears as crucial for understanding this institutional divide among the various European economies: a technocratic approach has prevailed over the understanding of the political processes that reconcile social justice and economic performance. Actually, the Nordic countries have been the implicit benchmark adopted by the "open method of Coordination" elaborated in the 2000s in order to turn the old continent into the most innovative region in the world while preserving the traditional values of social cohesion (Rodrigues 2002; 2009). The simple fact of comparing the various labor market institutions and welfare was supposed to generate emulation by all of the governments, thus transforming significantly the domestic context in favor of major reforms. This assumed that the polity had mainly the purpose to implement

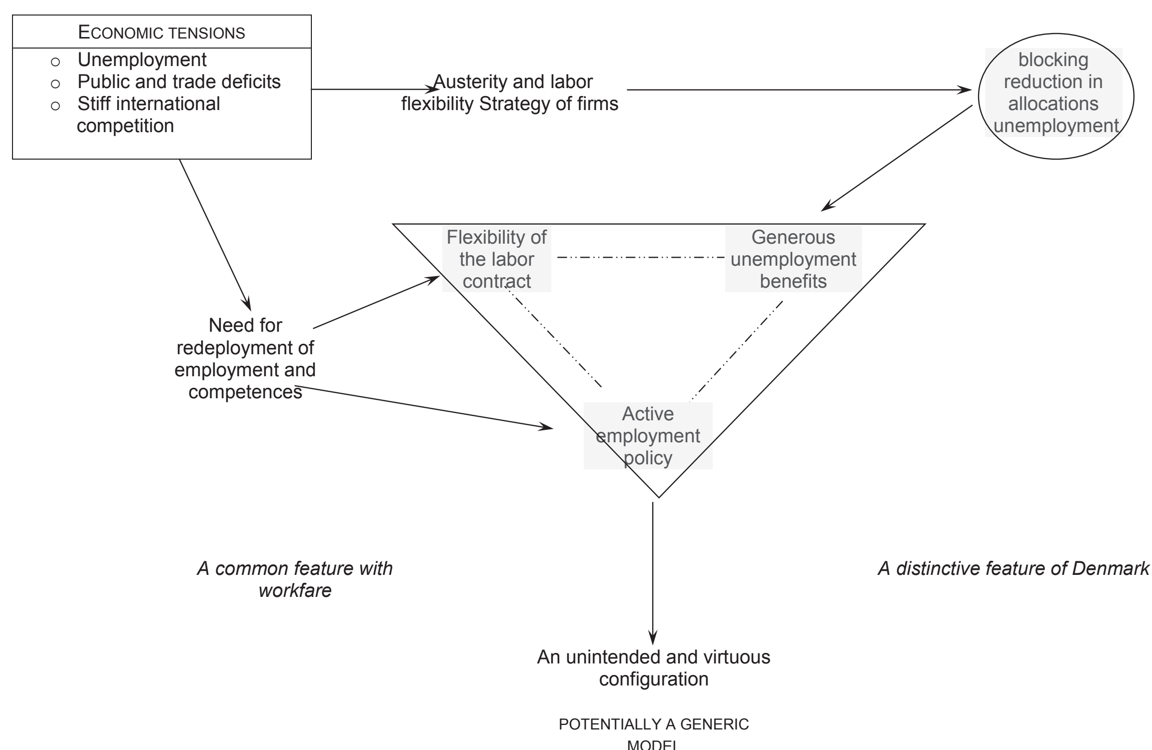
economic rationality, defined abstractly by the synthesis elaborated by the European Commission of the best practices collected across the member states.

The very history of Welfare Nordic capitalism falsifies this quite optimistic vision and there is no better example than the emergence of the so called Danish flex-security model (Campbell et al. 2008; Madsen 2006; Fellman et al. 2008). Back in 1993, Denmark suffered a loss of competitiveness, a large public deficit and a high unemployment attributed to a far too rigid labor market. No surprise if the business association was asking for less labor market regulations in order to quickly adjust employment and recover profitability. But workers unions strongly opposed and asked for the preservation of employment security, thus blocking the demands for lower unemployment benefits. This frontal conflict of interests seemed bound to end in a dead end, i.e. a victory either of business or of wage earners, as usual in many labor conflicts. Nevertheless, as soon as the two collective actors agreed that the redeployment of employment was necessary for preserving future high wage jobs and firms' economic viability, the protection of existing jobs was traded against an active employment policy – that was proposed and financed by the state along with the preservation of decent standards of living for the unemployed, thus taking on board the issue of labor security. The flex-security model was born and it was the unintended consequence of the interactions of three and not only two actors: business, labor and the state (Boyer, forthcoming). Many such conflicts have been recurring in other societies but they did not deliver the same institutional innovation, because their history has been instead governed by strong and persisting ideological oppositions between capital and labor, for instance in France, or by conceptions that self-regulating markets are by nature efficient and fair, as observed in the US (Figure 15).

The contribution of the flex-security model to moderate inequalities is thus threefold. First the primacy of a good and democratic education system gives to almost the entire Danish population the ability to forge core competences, such as the ability to learn how to learn (Lundvall 2011) that are subsequently mobilized as informed citizens and polyvalent workers. Furthermore, lifelong learning periodically updates precise capabilities required of workers by world competition and technical change. Second, long term employment is the exception and low unemployment is the rule and this means an equal access to jobs, at odds with the traditional juxtaposition of insiders and outsiders in many other segmented labor markets such as Germany. Last but not least, a significant progressivity of personal income and extended free public services for education and health do introduce a large redistribution towards less inequality. Thus Denmark displays a slightly higher Gini coefficient than the US for primary

income distribution (0.49 versus 0.47), but it is drastically reduced after tax and welfare redistribution (to 0.29 versus 0.34) as shown by Carlos Telo (2012).

Figure 15: The Danish Flex-Security model: The Unintended Consequence of an Unemployment Crisis and the Conflict of Opposing Interests and Rationales



Source: Own elaboration.

4.7. Every Inequality Regime is the Outcome of a Long Run Trajectory, Melting Ideas, Political Intermediation and Economic Specialization

Many analysts might be convinced by the previous argument: from the point of view of wellbeing, economic performance and ecological sustainability, the social democratic configuration is superior to the liberal one typical of market-led capitalism (Artus 2009; Wilkinson and Picket 2010; Fukuyama 2012). Then why have Americans not tried to adopt and transpose it to their continent? The discussion about the failure of Southern Europe to cope with the Lisbon Agenda has already delivered an answer and the contrasting inequality regimes in China and United states suggest that the hypothesis of one best way towards which all societies should converge does not fit with the historical record.

For instance, when one compares Denmark and the United States over the formative years 1880-1933, the present gap in their welfare organization can be traced back to

the layering of differences in labor mobility, conceptions of society and government, political parties structuring, moral valuation of solidarity versus responsibility, Grundtvig enlightenment versus Lockean liberalism or divergence in the process of union formation (Table 5). Their contrasting inequality regimes are the coalescence of their respective history. Thus the complexity of the related complementarities makes nearly impossible the import or even the hybridization of any foreign model. The more so, the more idealized and misunderstood the configuration to be emulated.

Table 5: Welfare as a Part of a Social and Ideational Long Run History: Denmark versus United States

1880-1933	Denmark	United States
Labor	Relatively immobility makes possible local solidarity	High expectation of mobility mutes political conflicts
International legacy	Guilds transformed into trade unions	Difficult construction of unions out of successive immigration waves
Conceptions of State / Government Society relations	Quasi fusion between "Society" and "Government" Institutional pragmatism Grundtvig enlightenment	Liberty and democracy have to be defended against the expansion of government Social nationalism, self-regulating system, Lockean liberalism
Political configuration	Social Democrat as third way between Left and Right, Socialism and Liberalism	Socialism was never an option, nor a challenge
Economic argument pro/against Welfare	An extension of community help to self help at the national level	Welfare reserved to "worthy poor" The cost of welfare may hinder economic dynamism
General conception of Welfare	Continuation and updating of widely recognized principles	A threat to individual liberty and founding principles
Conclusion	Welfare is a part of a long tradition of mutual responsibility	Welfare may undermine personal responsibility

Source: Freely inspired from Daniel Levine (1978), Tom Knudsen and Bo Rothstein (1994), Ove Korsgaard (2000), Robert Henri Cox (2001), Margaret Somers and Fred Block (2005).

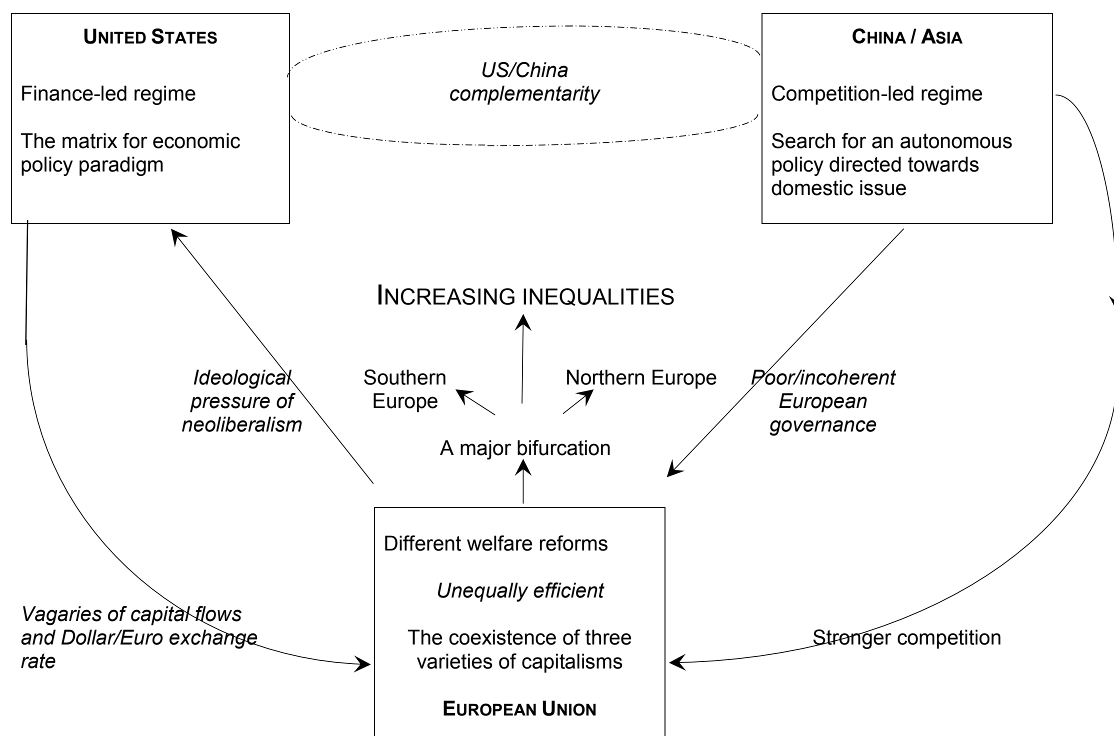
4.8. The Extended European Welfare Systems and Regimes of Limited Inequality are Challenged by Global Finance and Eroded by Chinese Competitive Pressure

Not only are inequality regimes the expression of different development modes/growth regimes modes, but they are also interdependent. Thus the evolution of the European Union has to be related to the trends generated by the US/China dyad presented above (see Figure 11, above). Clearly given the fuzzy governance of the EU, the old continent appears as very dependent on the impulses originating from North America and Asia, the two key players of the international economy (Figure 16).

On one hand, the repercussions of financial liberalization and globalization have revealed the institutional weaknesses of the Eurozone. They have first been fuelling an easy credit to governments and propagating real estate bubbles in Spain, Ireland and then, after the Lehman Brothers collapse, they triggered sudden outflows of private highly mobile capital away from the weakest member states. This divide between northern and southern economies has implied a reversal of the catching up of standards of living within the EU: rather moderate unemployment and resilience of welfare on one side, with an explosion of youth employment and significant slimming down of social benefits on the other. Intra-European inequalities are thus rising again. Furthermore, the Washington consensus and IMF adjustment programs that had dramatically failed in Asia and Latin America are rejuvenated by the European Commission under the joint pressure of international financial investors and the German government. Preserving social cohesion and formation of social capital is no more the priority of governments and the very origins of the European model are being forgotten.

On the other hand, the competition led development of China and its structuring role in the reorganization of Asian and international division of labor generate another bifurcation within the EU. Germany and Nordic countries continue to experience trade surpluses given their specialization in top quality, high skills and large value added products; thus their welfare and innovation and productive systems remain compatible if not fully complementary and this limits both dis-industrialization and inequalities rise. The opposite is observed in Greece, Portugal, Spain, Italy, and to some extend in France. Public opinion highly values the present welfare system but poor economic performance makes its financing increasingly difficult. Most governments are torn between their compliance with European rules of the game in order to have access to financial bailouts and a vibrant opposition of workers, pensioners, and welfare dependents.

Figure 16: The Ability to Pay for Welfare is Reduced by the Fallout of the Subprime Crisis and the Loss of Competitiveness and Attractiveness: The European Inequality Regimes at Risk



Source: Own elaboration.

Let us summarize the major findings gathered until now. Firstly, the nature and evolution of inequality are historically and geographically embedded within various regimes that are significantly different. Secondly, these inequality regimes are mixing ideologies, political compromises and economic specializations and they thus display a significant path dependency. Thirdly, the North American, Asian and European regimes cannot be understood in isolation since they are interrelated and some of them are complementary.

5. Latin America: Paradox or Historical Bifurcation?

Let us then apply these analytical tools and findings to Latin America: why has there been a reduction of inequalities since the 2000s, at odds with the opposite trends observed elsewhere? This paradox can be explained, but the sustainability of this reversal is still at stake at the present stage of the crisis that opened in 2008.

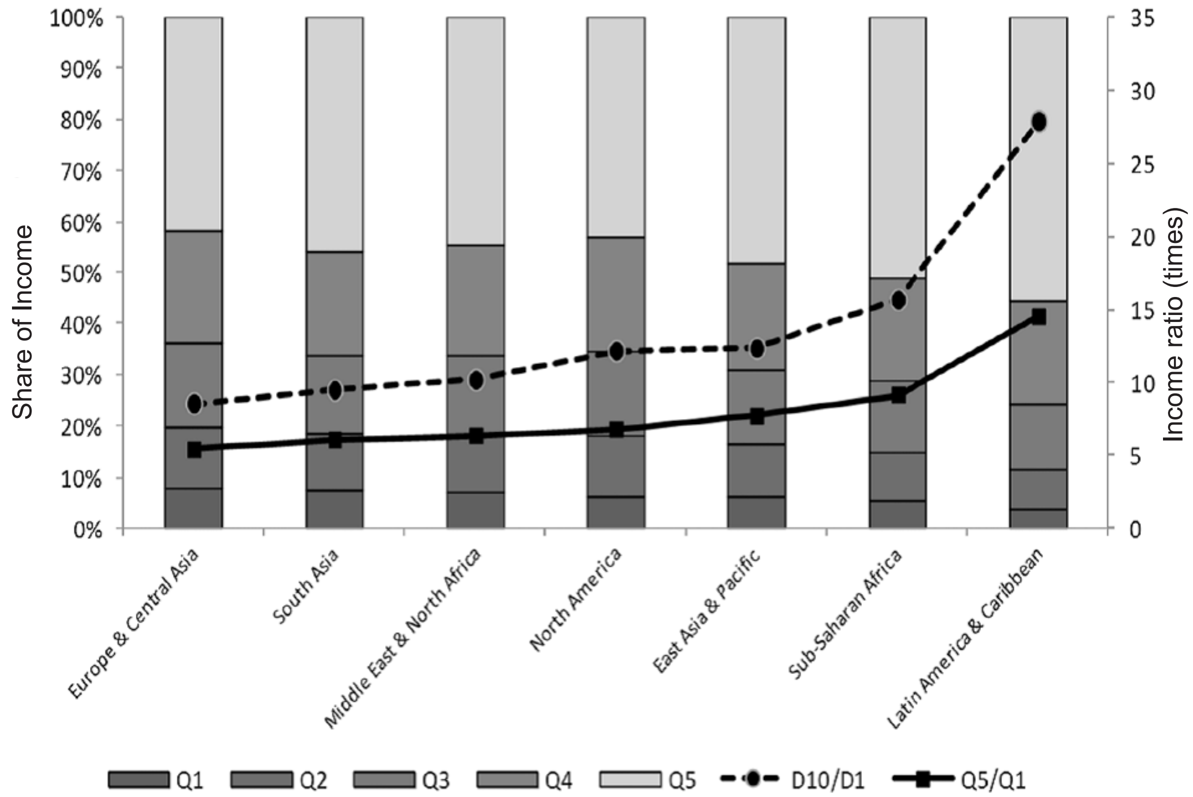
5.1. A Continent Not So Poor, but the Most Unequal

A priori, Latin America and Caribbean countries are at the extreme opposite of Europe since they define the most unequal region, surpassing even the poor Sub-Saharan Africa. This zone has the highest appropriation of national income by the top decile in comparison with the lowest (Figure 17), and this extreme social divide is a persistent feature of Latin America even though median income is far higher than in Africa. Poverty persists in the midst of relatively societies richly endowed in terms of natural resources and in some cases even industrialized economies such as Brazil suffer from the same challenge.

Nevertheless, simply belonging to the same region of the world or geographical proximity does not imply a convergence of inequality measures: Uruguay and Venezuela enjoy quite moderate polarization, with inequality indices nearly the same as in Europe, while by contrast, inequality is far larger in Brazil and in Bolivia and Honduras that are located at the extreme range of inequality (Figure 18). In spite of common features in terms of colonial history and economic specialization, the particular contours of national social and political intermediation still matter, and this was also observed within the European Union.

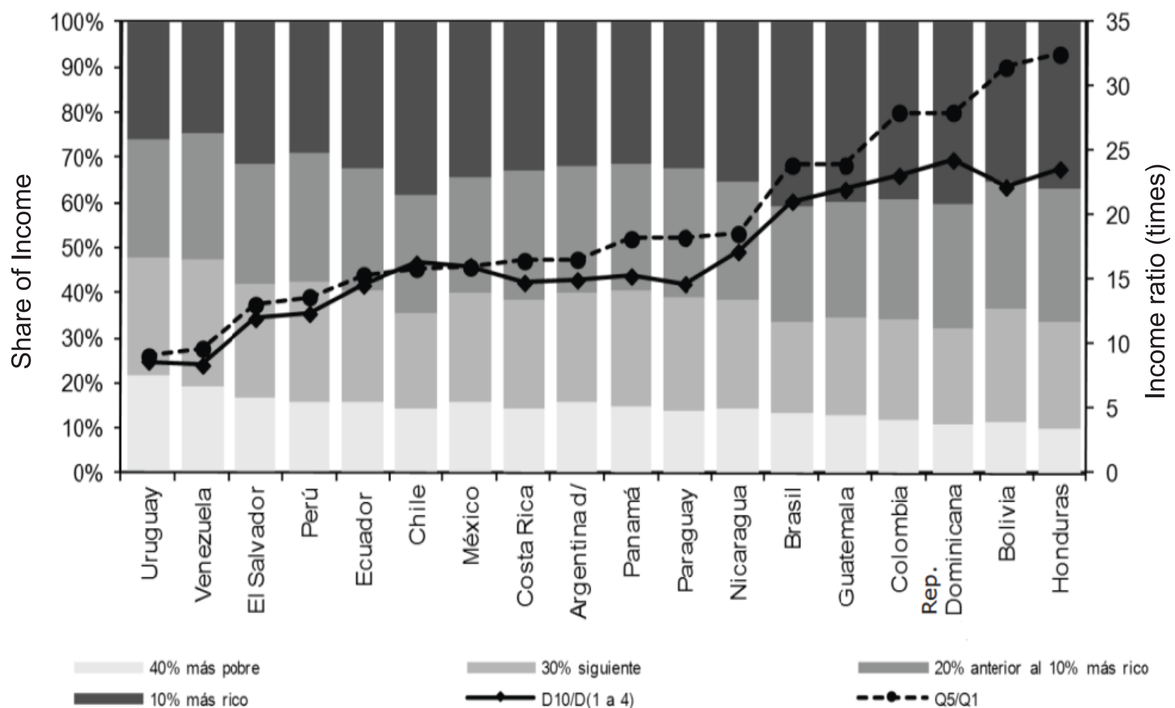
On the surface, such a long lasting social polarization in Latin America seems to substantiate a path dependency hypothesis. Hence the (logical but erroneous) prognosis that in the 2000s, income inequality should have become worse in the context of rising inequalities in most regions of the world economy.

Figure 17: Latin America and Caribbean are Extremes in Terms of Inequalities. Distribution of Income near 2009 (% and Multipliers)



Source: Juan Pablo Jiménez and Isabel López-Azcúnaga (2012: 5). Used with permission.

Figure 18: High Diversity of Income Distribution by Deciles within Latin America (% and Multipliers)

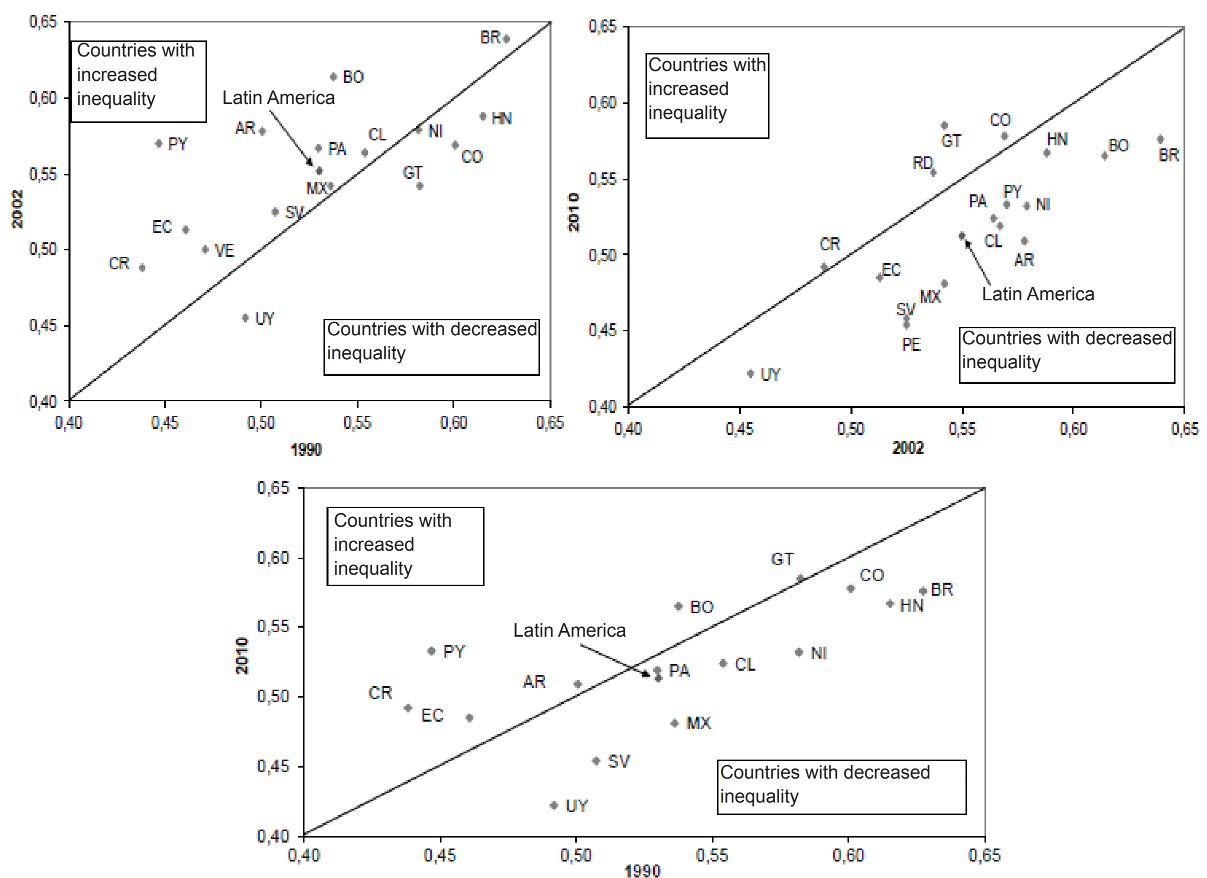


Source: Juan Pablo Jiménez and Isabel López Azcúnaga (2012: 6). Used with permission.

5.2. The Surprising 2000s: A Rather General and Significant Reduction of Inequality

Latin America in the 1990s had actually experienced a strengthening of inequality throughout the decade with few exceptions, but the 2000s shows an U-turn in Gini coefficients for a vast majority of Latin America economies: Brazil, Argentina, Mexico are good examples of this change whereas Uruguay exhibits a constant improvement from period to period in the fairness of income distribution; this is a new evidence about the relative autonomy of domestic social and political processes.

Figure 19: The Evolution of the Gini Index for 16 Latin American Countries 1990-2010



Source: Juan Pablo Jiménez and Isabel López Azcúnaga (2012: 3). Own translation. Used with permission.

Nevertheless, are there common factors that propel this reversal and will they persist and create a major historical bifurcation in the history of the region? Are they related to a common insertion into the world economy or to more internal transformations, for instance a better response to financial crises and the invention of new policies aiming at social inclusion?

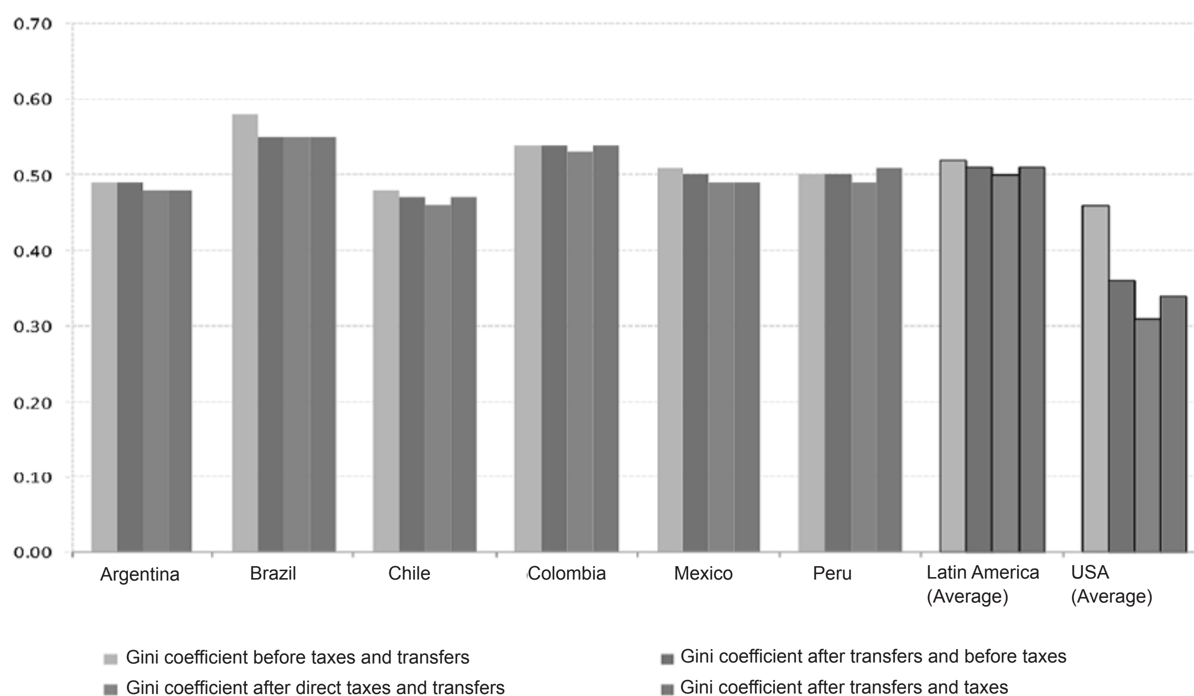
5.3. The Causes of this Improvement: A Complex Web of Economic, Social and Political Factors

The concept of inequality regime suggests that no single factor is powerful enough to trigger its transformation and therefore a list of likely candidates, driving forces has to be screened.

(1) No Major Impact of the Redistributive Role of Fiscal Policy.

Many specialists of inequality point out the strategic role of taxation and redistribution, for instance the move towards a flat tax in many liberal capitalist countries (Atkinson, Piketty and Saez 2011; Piketty and Saez 2003; 2007) is not devoid of responsibility in the changing inequality regimes of the US, but the resilience of a progressive taxation in Nordic countries such as Denmark (Boyer 2006) shows the relative autonomy of governments with respect to expectations of convergence. Under this respect, Latin America is a remarkable example for the extreme modesty of redistributive policies that aim at poverty reduction more than they explicitly fight against inequality. The only exception is Brazil, but even there the redistributive effect is far inferior, compared to that typical of the European Union (Figure 20). In 2006, the Gini Index for Brazil falls from 0.56 to 0.54 after taxation and social transfers, but from 0.46 to 0.31 in the EU. Nevertheless two polar cases are insightful. The most common configuration (UK, Ireland, Spain and Denmark) exhibits quite a high inequality of primary income distribution, rather similar to the average level observed in Latin America, but redistribution massively reduces *ex-post* inequality (Telo 2012: 279).

Figure 20: Major Differences between Latin America and OECD Countries: The Redistributive Impact of Fiscal Policy on the Gini Index



Source: Goñi, Lopez and Serven (2008), own translation. Used with permission under License: Creative Commons Attribution license (CC BY 3.0)

According to these data, the core challenge for Latin America would be for governments to overcome the reluctance of the elite and middle class to pay taxes high enough to extend the transfers to the poorer and not so much productive and labor heterogeneity (ECLAC 2012a). Until now, only Brazil has significantly increased the tax burden to a level comparable with that of average OECD countries.

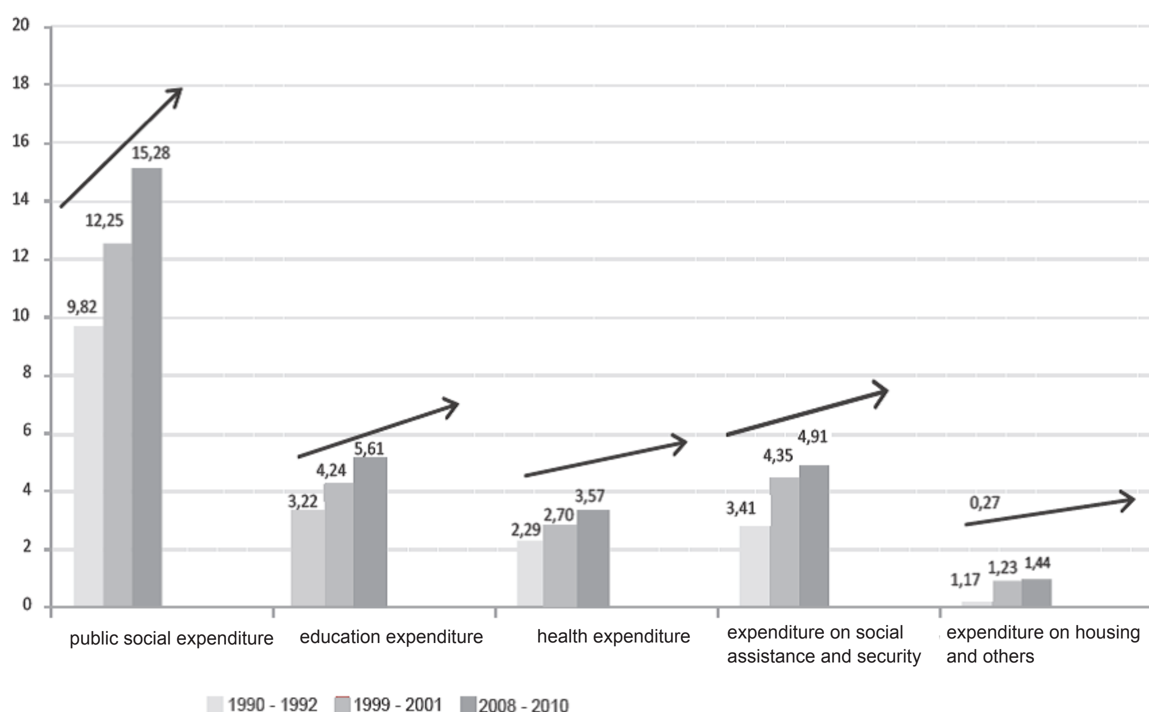
(2) Learning from the Previous Crises and a Modest Improvement in Social Expenditures but not so Much in Education

Many statistical and econometric studies have shown that high macroeconomic volatility and financial crises reduce well-being and generally widen the pool of poverty and thus deepen inequality from below, whereas bubbles augment them from above. This applies to Latin America (Panigo 2008). Since Mexico and many other Latin American economies have been the first to endure modern financial crises generated by large capital inflows and sudden stops, the successive governments have painfully learned not to repeat the same mistakes again and again (Boyer et al. 2004). Clearly Latin America has been faring far better in the post 2008 financial turmoil than during the 1980s and 1990s crises. No IMF-type adjustment was necessary and, however difficult to quantify, this better macro-economic management—moderate public debt,

large currency reserves, better anticipation and so on—has mitigated the impact of the world crisis, and consequently kept active transfer policies.

This has created more space for a modest increase of social expenditure but still is limited in terms of supply of public education, health care, subsidies to housing, all factors that should contribute more to inequality reduction and long growth capability (Figure 21). Actually, Latin American welfare is quite limited given the trend towards the privatization of these public services and goods; this places an obstacle to further inequality reduction. For instance in Brazil, during the summer 2013, some popular movements have protested against the difficult access to poorly organized urban transport and the inequality of other public services for the poor, meaning that cash transfers are not the panacea: they and are only one step in the direction of a real welfare (Miranda do Nascimento 2013) .

Figure 21: The Evolution of Public Spending by Sectors from 1990-2012 to 2008-2010 (% GDP) in 21 Latin America and Caribbean Countries



Source: Own elaboration using CEPALSTAT.

(3) Changes in the Macroeconomic Context: Better International Prices, Lower Volatility, Higher Growth, Larger Tax Basis.

Whereas the total value of exports had been stagnating during the 1990s, from 2002 to 2007 they have tripled; this was generated by the simultaneous credit-led US boom and competition-led regime in China: they have triggered large price increases given the lag in adjusting capacities in the sector of commodity production (ECLAC 2012b: 68). Since most Latin American growth regimes are export led, GDP has been expanding and has provided the fuel for domestic consumption; it has also extended the tax base, for example some levies that are attached to exports of commodities, as decided by the government in Argentina after 2002 (Boyer and Neffa 2004; 2007). Some of this bonanza has been channeled into the fight against poverty, thus delivering political legitimacy and launching a transition towards consumption-led development as observed in Brazil (Boschi 2012).

Most studies in political science and economic sociology traditionally focus on issues of power, conflict and organization concerning the emergence and transformations of welfare systems. Nevertheless, they frequently forget to study how the macro-economy shapes the size of the base for redistribution: the positive and increasing sum game typical for a fast growing economy makes political compromises easier (in Latin America in the 2000s) than during a depression where nobody is eager to accept to share the burden (the Greek depression 2009-2013 or European 2013 recession).

A scenario exercise (ECLAC 2012a) considers that the mere extrapolation of the 2000s trends is quite unlikely: no return to pre-crisis employment level in the US, anticipation of a possible lost decade in the European Union, and a clear deceleration of Chinese growth combine their impact and it is thus prudent to anticipate a clear decline of the stimulus generated by the dynamism of the world trade, i.e. to err on the side of the pessimistic scenario (Table 6).

Table 6: Three Scenarios

Destination market	Optimistic Scenario		Neutral Scenario		Pessimistic Scenario	
	Volume	Value	Volume	Value	Volume	Value
Latin America and the Caribbean	4.4	9.0	3.7	3.5	2.0	0.0
China	18.3	24.1	16.4	9.9	8.9	-0.9
European Union	5.5	12.6	1.1	1.7	0.8	-3.6
United States	6.2	10.4	6.2	5.7	3.4	1.9
World	7.5	10.5	6.5	5.0	4.5	0.7

Source: Own elaboration.

(4) The Impact of the Return to Democracy and Larger Responsiveness to Social Demands

A growing literature now investigates the reasons for the (modest) U-turn of inequalities in Latin America; each discipline has its own favored interpretation As usual, macroeconomists privilege changes in economic policy and corrections of the errors of the past (Hausmann et al. 2005; Bresser-Pereira 2009). On their side, geopolitical approaches see Latin America moved by forces that are largely out of control of domestic actors, whatever the merits of more prudent economic policies. The specialists of anti-poverty policies point out the effectiveness of conditional cash transfers and attribute to this social innovation the inflexion of inequalities.

But other analysts stress that these cash transfers are not the major source of inequality reduction. Concerning for instance Brazil:

In a development that defies the dogmas of the minimal state, the labor market (employment and minimum wage) accounted for nearly 60% of the fall in social inequality; Social Security benefits contributed with 27%; and the Bolsa Família along with other safety net programs alike with 13%. The process of market inclusion was consequently the result of job growth coupled with a spreading out of monetary cash transfers, both contributory (pegged to the minimum wage) and non-contributory, a phenomenon that increased average income and enhanced commodification to compensate for government failures to provide basic services (Fagnani 2013).

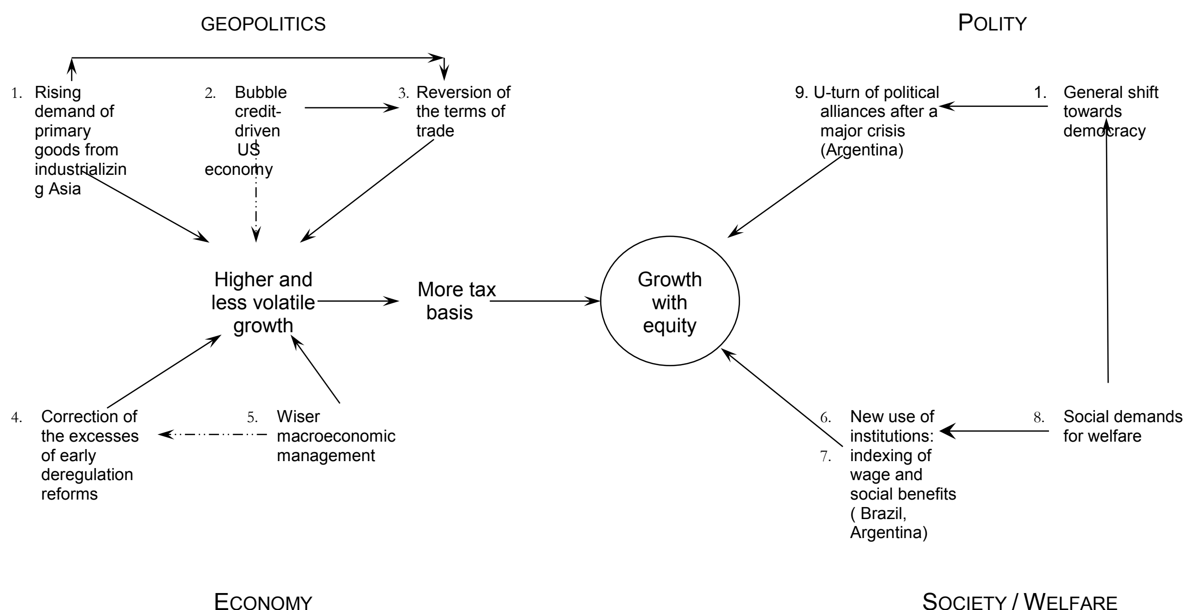
Furthermore demographic changes should be brought into the analysis: since fertility rate is inversely correlated to income in cross national analyses (Schultz 2005), its decline might have played some role in the poverty reduction observed in Latin America. Since welfare systems are complex organizations/institutions interweaving economy, family, civil society and state (Théret 1997), the nature of political intermediation should also be brought into the picture. Actually, the successive transitions towards more democratic constitutions and regimes has made governments more responsive to the demand of a large fraction of the population previously excluded from the concerns of the ruling elite (Gómez-Sabaíni et al. 2011).

5.4. A Tentative Synoptic Representation of the Determinants of the New Latin American Inequality Regime

A priori each of these explanations is rather compatible with or even complementary to the others, and they are neither exclusive nor contradictory. Logically, the absence of many of the related transformations would have prevented the inflexion of inequality and conversely when they are jointly operating, past determinisms can be altered towards a more inclusive growth (Figure 22).

For instance, good international perspectives may be wasted by a poor and short sighted macroeconomic policy and thus it may nurture a financial crisis quite detrimental to well-being and social inclusion.

Figure 22: A Systemic Approach to the Factors Contributing to a Reduction in Latin American Inequality



Source: Freely inspired among others by Juan Pablo Jiménez and Isabel López Azcúnaga (2012); Luis Miotti, Carlos Quenan, Edgardo Torija Zane (2012).

Second example, many social movements may ask for a better social protection but an authoritarian government defending some limited private interests can block these demands: democratic institutions usually help in the search for a more egalitarian distribution of income and wealth.

This shows that path dependency does equate with reproduction ad infinitum of a given mode of development and inequality regime.

Let us now compare Latin American societies with the inequality regimes of the other zones of the world economy, respectively captured by Figure 2 for China, Figure 8 for the US and Figure 16 for the European Union. Clear distinctive features appear:

(1) Firstly, an *integration into the world economy*, mainly via the export of primary commodities, was detrimental when their terms of trade were declining during the post WWII period with the domination of Fordism but it became a trump when China and Asia were industrializing and importing massively the natural resources required by their fast and steady take off.

(2) Secondly, whereas *democratic institutions* are well established in Europe and North America, they are quite recent in most Latin American societies and de facto this

political shift has entitled the expression of demands for social protection that, at last, have been taken seriously and partially fulfilled.

(3) Thirdly, the *succession of economic crises*, largely generated by a fast liberalization and opening to international capital flows, has promoted the emergence of pragmatic policies and reforms, correcting the adverse effects of the adhesion to the belief that market mechanisms alone were sufficient to propel development. The constitution of a moderate welfare system has now become perceived to be a condition for long term social sustainability and political legitimacy.

(4) Last but not least, the *limits of export-led development* were clearly perceived by experts and governments. In this context, the constitution of a welfare system and a labor policy synchronizing wages along with growth or productivity appear as key drivers in the direction of a more inward looking strategy (Saboia 2010). This is a clear opportunity for large size economies, such as Brazil, whereas it should be an incentive for others to join projects of regional economic integration in order to organize at the relevant level, the synchronization of welfare and production systems.

Given the implications of these transformations it is difficult to assess whether the institutional configurations have evolved towards new and more coherent growth regimes or if the recent good macroeconomic performance and inequality reduction are mainly the outcome of world bonanza that could be reversed. The slowdown of Brazil economy in 2013 and the economic and political tensions observed in Argentina since the early 2010s suggest that the jury is still out.

In any case, these four transformations shed some light on the Latin American paradox pointed in the introduction: the most unequal continent is exploring a “growth with equity” strategy that is replicating neither the US nor the European experiences, because of a genuinely distinctive economic, social and political history. Of course some other factors might be similar across the three regions. For instance in Latin America too, the evolution of finance has entitled credit to compensate slowly growing or stagnating household incomes and thus to sustain domestic consumption. Similarly poor people generally pay higher interest rates than the rich and this is a source of extra financial profit and widening of income and wealth inequality. Consequently, financial instability could strike again Latin America, originating domestically or internationally. Thus a major issue arises: how autonomous and resilient is this model of growth with social inclusion?

6. From a Global and Universal Approach to the Complementarity of Contrasting Socioeconomic Inequality Regimes

It is time to search for a synthesis and birds-eye perspective: how do the domestic arena and the international system interact in the genesis and evolution of economic inequality? Let us first review recent statistical results, then revisit the foundational Kuznets hypothesis and finally propose our own framework based upon the joint analysis of different inequality regimes and their co-evolution.

6.1. Measuring Inequality at the World Level: The Need for a Plurality of Concepts

From a global perspective, growth theory suggests to capture the impact of unequal development upon income per capita at the level of each nation-state, where statistics are available over long periods due to data collection by public authorities, and whose archives are subsequently revisited by economic historians. Century-long data then show that according to this first concept, inequality grows along the unfolding of industrial and capitalist revolutions, the only exception being the post-WWII period when various forms of developmental states have been counteracting the previous trends observed since 1820 (Milanovic 2007: 29).

Nevertheless such a measure does not take into account that the population size varies tremendously between Luxembourg and Switzerland on one side and China and India on the other. Therefore weighting each national income per capita by population size corresponds to a second concept for international inequality. The picture is not very different: a long term increase of inequality from 1850 to 1940 and stability during the Golden Age when both international and domestic inequalities were stabilized via the containment of market forces by institutions, organizations and the Bretton Woods system (Milanovic 2007: 30).

The internal inequality within each nation-state is not taken into account by these two indices, since the same average income is fictively attributed to each individual citizen of a nation-state. With the availability of individual income statistics for a growing number of countries since the 1980s, a third concept of global inequality can be given a measure and compared: the same weight is attributed to each individual with its actual income, converted into a common PPP index. No surprise, the global inequality measure shows larger inequality than the international one, but it seems that after 1990, this measure shows a mild decline. Since the statistical sources are different, this second set of data points out an interesting methodological issue: the

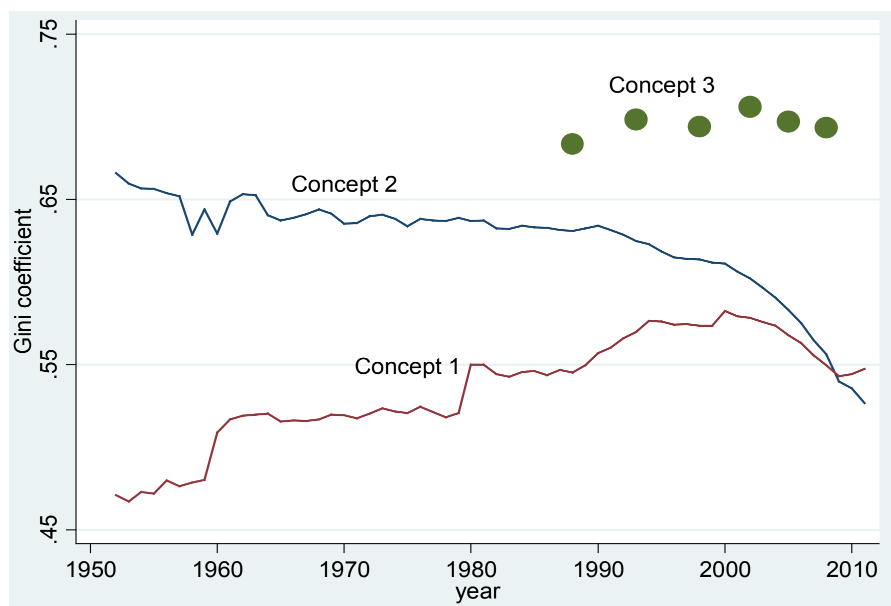
take-off occurring in India, China and other populous countries has reduced weighted international inequality, whereas the un-weighted index exhibits on the contrary a rapid increase (Milanovic 2007: 32).

6.2. The 2000s: A Historical Reversal of Inequality?

The updating of household surveys that recently have been extended to a growing number of countries, including Africa, delivers more accurate but still imperfect estimates of global inequality that enlighten the lively debate about the complex links between globalization and inequality with new findings. Basically the three concepts of inequality yield the same conclusion: since the 2000s, the decline in international inequality is because rich countries growth is now slow and economic dynamism is on the side of emerging economies with huge (China and India) or large (Indonesia, Brazil and Turkey) populations; thus weighted international inequality decreases still more rapidly; this upward trend of the average per capita income of these countries overcomes the widening of internal inequality that prevails for most of them. The defenders of globalization as a driver for development find here a long awaited confirmation of their hopes (Figure 23).

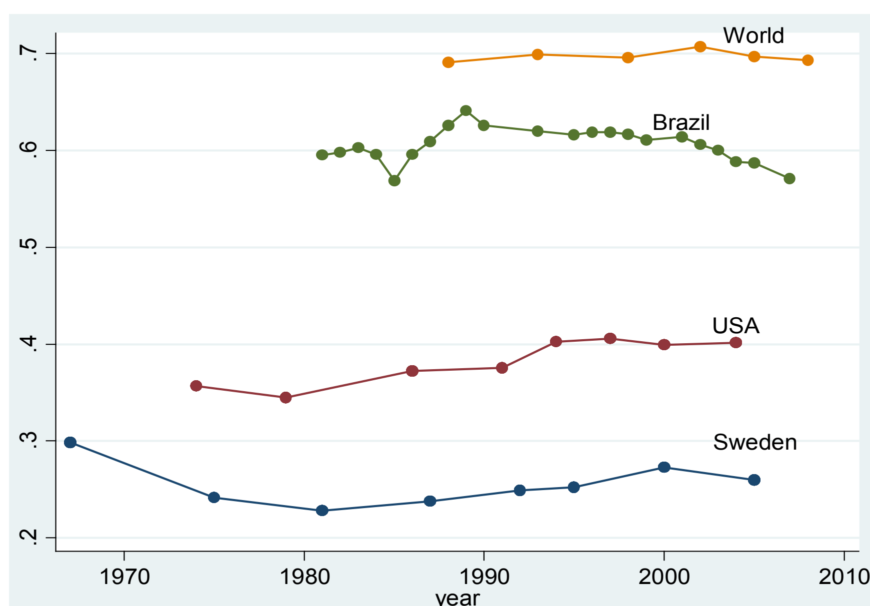
This is an invitation to compare the evolutions of this global inequality with some emblematic national trajectories. The difference of levels between Brazil and Sweden is striking, and the USA exhibit an intermediate Gini coefficient, increasing but moderately, at least compared with the gap with Brazil. Of course size matters: the most egalitarian nations are small (Sweden, Denmark, Uruguay, Switzerland,…) whereas continental economies are *a priori* quite heterogeneous: solidarity supposes trust and reciprocity and they are easier to nurture in densely connected societies. Hence a difficult theoretical question: at what level (the world, the nation, the locality or the community) and in what arena (the firm, the economy, polity, the access to basic public goods) are the conceptions of social justice forged? Consequently the various indexes are built by each researcher according to her/his own purpose: they acquire a social relevance only when collective actors use them in support for their demands to governments. In this aspect, the concept global inequality has so far attracted few supporters outside some ad hoc international organizations and a few individuals who perceive themselves to be “citizens of the world” ready to express their solidarity at this level by consenting to large and possibly long lasting transfers (Figure 24).

Figure 23: Two Measures of International Inequality versus an Assessment of Global Inequality. Gini Coefficient 1952-2011.



Source: Branko Milanovic (2012: 6),"Global Income Inequality by the Numbers: History and now", Figure 2. Used with permission.[2]

Figure 24: National Differentiation of Inequality across Nation-states, but Much Smaller than the Inequality among Individuals in the World. Gini Coefficient 1968-2005.



Source: Branko Milanovic (2012: 9),"Global Income Inequality by the Numbers: History and now", Figure 3. Used with permission.

2 Figures 23-25 are presented here with the permission of the World Bank: The World Bank authorizes the use of this material subject to the terms and conditions on its website, http://www.worldbank.org/terms.

Figure 25: A Historical Shift in the Source of Global Inequality: More Linked to Citizenship than Internal Social Stratification (Theil Coefficient).1870 and 2000

Source: Branko Milanovic (2012: 18), Figure 6. Used with permission.

This leads to a proposal: can available statistics decompose global inequality into one part related to citizenship in one country and another linked to the position of individuals within this country? Branko Milanovic calls the first "location" the other "class" (2012) and he analyzes the Theil index between 1870 and 2000. As far as the quality of data allows, inequality was mainly related to class in the 19th century, but today the discriminating factor is where individuals live, i.e. on average, location matters much more than occupation within each society. This result implies that national economies continue to be the place were solidarity is expressed and they are the outcome of a century-long process of institution building to promote the diffusion of gains from technical change (Figure 25).

Of course, several other regional entities are emerging and attempt to usurp some or all of the functions of nation-states (North American Free Trade Agreement (NAFTA), Association of Southeast Asian Nations (ASEAN), Southern Common Market (MERCOSUR), the European Union (EU)) but the process is far from mature enough to contribute to the emergence of inequality regimes at the regional level and even less at the world level. Growth and Inequality regimes are still embedded into the national social fabric.

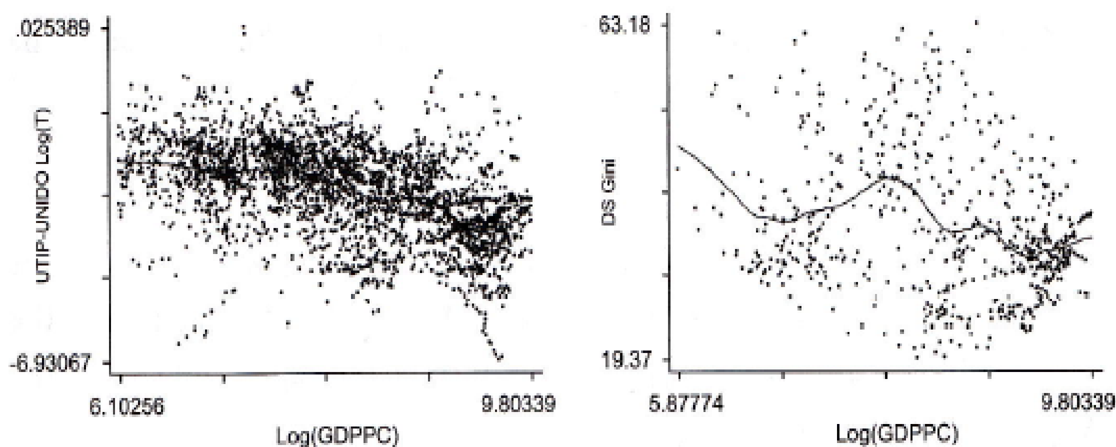
6.3. The Kuznets Curve Revisited: Do General Laws Govern Growth and Inequality at the National Level?

As previously presented (Section 2.1 above), the Kuznets hypothesis states that modernization first increases inequalities as it matures and then endogenous forces imply a reversal towards more equality. Nowadays, it can be tested over a large sample of periods and countries (Galbraith 2012) and a simple graphical analysis shows how fuzzy such a simple coevolution is (Figure 26). One could argue that each industrial revolution starts a new inverted U-curve and that some economies continue to explore the maturing phase of the previous industrial revolution while others climb a new Kuznets curve. Nevertheless the global picture becomes quite complex and given the intricacy of the factors that sustain growth, it is somewhat illusory to extract a simple relation between growth and inequality: it is at best a reduced form of a fully-fledged model and thus there is no reason to think that it needs to be invariant for all regimes.

At best, the idea of a" succession of phases à la Kuznets" is a pedagogical device in order to classify the results of national case studies and explicate that, within the same calendar time, China may explore the ascending part of Kuznets' curve, while Brazil enters a period of reduced inequality and the United States launches a paradigm shift that generates new sources of inequality (Figure 27). Another avenue for research is the test of multivariate regression, which simultaneously examines a long list of other variables in order to better capture the diversity of national experiences. For instance, inequality is better explained by the conjunction of income per capita when a trend is added to the variables, but it is probably a proxy for other missing variables (Galbraith 2007: 170).

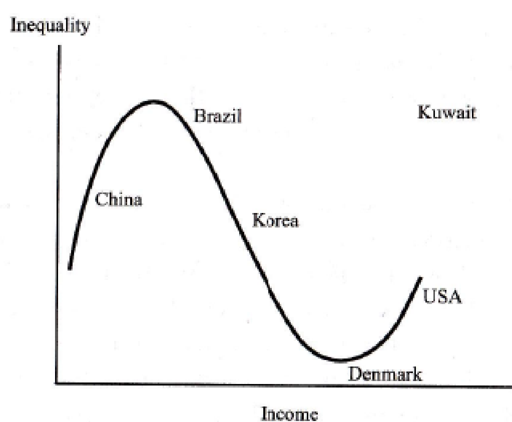
6.4. From the Original to the Extended Kuznets Curve Model: The Novelty of the Contemporary Period

Figure 26: An Interdependent World, Complementarity of National Inequality Regimes and Development Modes



Source: *Inequality and Instability. A Study of the World Economy Just before the Great Crisis* by Galbraith (2012: 65), Fig. 3.8. Used by permission of © Oxford University Press (USA).

Figure 27: A Stylized Augmented Kuznets Curve, with Selected Countries in Illustrative Positions



Source: *Inequality and Instability. A Study of the World Economy Just before the Great Crisis* by Galbraith (2012: 53), Fig. 3.1. Used by permission of © Oxford University Press (USA).

An alternative takes seriously the historical time, i.e. that of the transformations of social relations, organizations, institutions and technologies. Within a *Régulation* theory approach, social and political history shapes each national development mode and several configurations have emerged within the same epoch featuring a specific production and innovation paradigm (Boyer and Saillard 2001). Therefore the fuzziness

of the Kuznets curve is not a surprise but the projection of the diversity of inequality regimes, closely associated to contrasted development modes.

6.5. An Interdependent and Multipolar World of Inequalities: An Alternative Paradigm?

The present framework faces one major objection: if there is no single pattern in development modes and inequality regimes, how to explain their persistence? We have progressively shown that they are forming a rather coherent or at least compatible system at the world level (Figure 28).

(1) The explosion of top income within the finance-led growth in the United States is the symmetric of the widening of inequality generated by the fast productive modernization in China. This is not the only co-evolution within the world economy.

(2) The Euro crisis too and the threat upon extended welfare systems and defense of social solidarity are the consequence of the joint pressure of Chinese rapidly catching up in most industries; and the recurring global financial crises generated by the American victory in promoting liberalization and globalization of trade, capital, and finance.

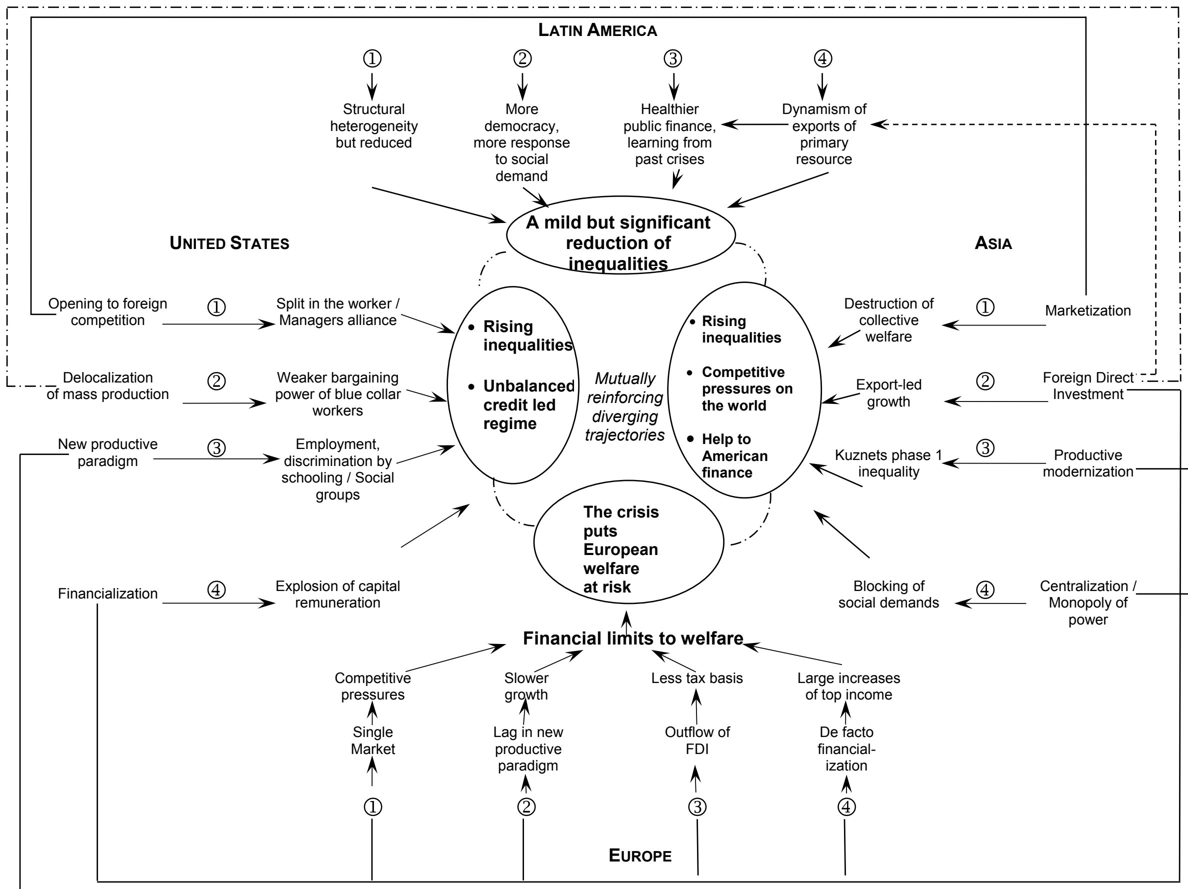
(3) The Latin American paradox – an atypical decline in economic inequality starting from an extreme social polarization – is also explained by its specialization that is complementary to that of China and the US, the ability to learn from the past financial crises and the transition to democracy as providing finally a positive response to demands for social protection.

The macro-economic imbalances, generated by the widening of inequality within each domestic economy, are symmetric in the US and in China and consequently only the compensating movements in international trade and finance allows the viability of socio-economic regimes that could not be sustained within closed borders: abundant credit to sustain the American way of living with stagnant average real income in the US, dramatic industrial overcapacity due to the squeeze of labor share in China; low American household saving rate versus Chinese high savings, partially channeled back to the US financial system.

Thus the internationalization of production, capital and finance makes compatible and viable contrasted inequality regimes, themselves embedded into complementary development modes. Furthermore, this explains the puzzling observation of opposite evolutions concerning inequality: less inequality between nations since globalization

entitles a variety growth regimes – credit led, export led, innovation led – but each of these regimes nurtures widening inequalities for individuals within the same nation-state, i.e. the two major stylized fact identified in Section 6.2.

Figure 28: An Interdependent World, Complementarity of National Inequality Regimes and Development Modes



Source: Own elaboration.

6.6. The Three Paradoxes Explained: How Academia, Economy, Polity and Geo-polity Interact

This analytical framework delivers also an interpretation of the puzzling observations made in the introduction (Table 7). The explanation combines a cognitive approach (how does *pure economic theorizing* analyze the links between economic activity and income distribution?), a positive study of the consequence of *asymmetric economic power* upon inequality, an investigation of the forces that shape *state interventions* and finally a recognition of the *hierarchical relations* that govern *the world economy.*

(1) First paradox: Is bad inegalitarian capitalism driving out more virtuous forms?

Why such an increase of inequality in most economies, in spite of the converging evidences from various social sciences that they are costly and detrimental to economic performance and wellbeing? Mainly because dominant economic interests have use a non-relevant theorizing of a pure abstract market economy to hide their ability to appropriate the rents typical of quite imperfect competition, to design complex and dangerous but profitable new financial products and finally to capture the state as their insurer of last resort, to the detriment of the rest of the society. The finance-led American capitalism is emblematic of this configuration and given its hierarchical position within the international relations, this vision has been exported to other continents and regions – frequently via international institutions – however different might be their actual modes of regulation.

(2) Second paradox: Is the deep crisis of the European Union counter-evidence against the superiority or even the viability of welfare capitalism?

If limited inequality is good for social cohesion and economic performance, how can we then explain the slow growth and the Euro crisis of the European Union, the homeland of welfare capitalisms: in the era of "globalization," are they passé? Basically most governments have forgotten why welfare can be an asset in the formation of social capital and hence competitiveness, the European integration has been almost exclusively built upon the promotion of competition with few or any solidarity between unequally advanced economies, and the transmission to Europe of the crisis of liberalized finance has falsely been interpreted as the consequence of excessive public deficits. Clearly national welfare systems have thus been challenged and destabilized, but weak European governance has been unable to promote and implement the required welfare state at the continental level. Nevertheless Northern Europe – Germany, Austria and Nordic countries – continues to show that an extended welfare system may still limit inequality and may contribute to economic resilience and success.

(3) Third paradox: Why is the most unequal continent, Latin America, now exploring a new strategy of development built uopon reducing inequality?

Why has Latin America, the territory of long lasting and wide inequalities, experienced a modest but significant reversal of income inequality since the 2000s? Actually a long history of costly financial and economic crises had finally the merit of repealing the Washington consensus and it has set into motion a more pragmatic learning process towards better macroeconomic management and reforms that would build

a modest but effective safety net. The polity is not absent in this process since the shift from authoritarian to more democratic regimes has led to a better response to social movements' demands for a modicum security. A genuine Latin American development theory might emerge, stimulated by the new international context, where primary resources and ecology are expected to become the major constraints upon the future of growth, both for mature and emerging economies. It is too early to diagnose whether the 2010s will mean a tipping point in the emergence of "growth with social inclusion" paradigm, since a lot is up to the evolution of the rest of the world. For instance will a South/South complementarity (between Brazil and China for instance) shape the future international system or will another North/South hierarchy (the US pivot towards Asia) emerge? Geopolitics should not be forgotten in any prognosis about a long term reduction of inequality in Latin America.

Table 7: The Three Paradoxes: The Outcome of Four Entangled Processes

	Academia Neo-Walrasian Economics	**Economy** Asymmetric power from imperfect market	**Polity** Capture of the state by dominant economic interest	**Geopolity** Changing world system
Paradox 1 Large cost of inequalities but they are rising	Triumph of ideology over scientific results	Privatization of utilities, appropriation of rents, onscurity of financial products	A minority (exporters, rentiers, financiers) imposes its socioeconomic regime	Larger impact of ideologies than scientific results
Paradox 2 European Union crisis: that of Welfare State	Inability to economically justify an universal Welfare State	Prevalence of market competition over social Europe building	Primacy of finance over national sovereignty, lobbying more than political deliberation	EU a second rank player, unable to conceptualize and diffuse its model
Paradox 3 Latin America: reduced inequalities in the era of global inequalities	Learning for past crises and errors, emergence of a new developmentism	More rent seeking and monopoly than entrepreneurship do limit inequality reduction	Positive role of democratization but still quite unequal access to the state	Progressive but relative autonomization with respect to the Washington Consensus

Source: Own Elaboration.

7. Conclusion: A Watershed in the Evolution of Inequality Regimes

This panorama of socioeconomic inequality regimes across the world allows some provisional conclusions and avenues for further researches.

7.1. Paradigms and Ideologies Matter

The demise of the Beveridgian and Keynesian intellectual consensus has played a role in the legitimation of and in some countries the acceptance of widening inequalities by a large fraction of policy makers. With the comeback of new classical, pre-Keynesian macroeconomic theories, the search for social justice has been again presented as intrinsically detrimental to economic efficiency, and this aggiornamento has started from the US and the UK, and diffused largely to the rest of the world. Of course, some socio-economists had developed a suggestive alternative theorizing according which a well-designed welfare could simultaneously enhance equity and dynamic efficiency, but the diffusion of this alternative paradigm was limited to Northern Europe, especially the Netherlands and social democratic Nordic economies. After the collapse of fully liberalized financial markets, the social demands for security by workers and families of emerging economies give a new chance to this alternative: a social security system might be the necessary complement to the turmoil generated by a fast social and technological transformation, as observed in China. An equivalent reappraisal is occurring in most Latin American nations.

7.2. The Complex and Multiple Determinants of Inequalities

Can it be said that there are universal laws governing inequalities? In the light of the last three decades, the Kuznets curve approach has not lost any relevance but has to be reassessed. On one side, the very rapid and intense productive modernization of China has been associated with a surge in sectoral, regional and individual inequalities, even if a long period of growth has drastically reduced poverty. Similarly, in developed economies, the erosion of Fordist mass production, its delocalization to emerging economies and the transition towards radically new productive paradigms – from information and communication technologies to sciences based biotech and even the new “financial industry” – have generated a new ascending phase in the Kuznets curve whereby growth and inequalities moved again synchronically. The domination of finance has reintroduced in the US wider inequalities, equivalent to those observed before the 1929 crash. Thus, financial fragility and rising inequalities go hand in hand. On the other side, Latin America has experienced a much more moderate productive modernization, but financialization has introduced other forms of inequalities compared

with those typical of *rentier* economies. The recent reduction of inequalities is not the "natural" consequence of invariant and universal mechanisms, but the outcome of a complex web of factors: a new dynamism of raw materials demands at the world level, learning from the previous economic crises, better response to social demands associated to the transition to more democratic regimes have made possible the search for an inclusive growth in Latin America.

7.3. Fordism and Social Democratic Regimes have Anticipated Inclusive Growth in Latin America

Past historical record falsifies the claim by neoclassical economists that growth with equity is impossible since the two objectives are contradictory. Studies inspired by *Régulation* Theory have shown that the impressive economic and social performances of the post-WWII Fordist mass production-mass consumption regime has been achieved by an institutionalization of wage formation, a reduction and stabilization of remuneration hierarchy and the implementation of universal welfare state covering a large variety of social risks (health, unemployment, training and retraining,…) and broad access to education. This has been observed in the US and most European countries and later under different forms in Japan and South Korea. These regimes entered a major crisis under the impact of the productivity growth slowdown, recurring struggles over income distribution, the internationalization of production and finally the domination of finance. Nevertheless, some social democratic societies, in Sweden, Denmark, Finland and Norway, have suffered equivalent world financial crises but the resilience of a basic political compromise has allowed reforms that have limited the explosion of inequalities. *A priori*, this is good news for contemporary Latin American strategies: inclusive growth is possible, provided stable socio-political alliances recurrently readjust the domestic institutional architecture and productive system to the changing social demands and the international context.

7.4. Less Globalization of Inequality than Coevolving Contrasted Inequality Regimes

The buzz word "globalization" is a dangerous and misleading concept since it suggests that the same economic, social and political processes are operating similarly across continents and various societies. Since the explosion of inequalities during the last two decades has been quite general, this would suggest looking for a general and universal explanation of this structural change. By contrast, all the previous analyses point out the diversity of the trajectories among nations: US versus China, Southern versus Northern Europe, Latin America versus Asia and so on. Clearly, domestic

socioeconomic compromises matter and therefore contemporary societies are exploring different stages or configurations in the permanent struggle between the intrinsic trend towards inequality put into motion by capitalist accumulation and the capacity of social movements to counteract them and defend community, solidarity and security principles in response to the radical uncertainty typical of an unfettered capitalist competition. The contemporary societies are at different epochs of Polanyi's dual movement. This analysis proposes to replace the concept of the globalization of inequalities by that of contrasting but interdependent inequality regimes. The finance-led inequalities in the US are associated to the "satanic mills" type inequalities occurring in China, and these two national trajectories do destabilize the welfare states of countries in the European Union. The stabilization of a more egalitarian growth in Latin America is up to the interplay of these three key actors: will the creeping Eurozone crisis turn into a complete breakdown or will the political contradictions in the US trigger a new financial meltdown and world crisis, not to speak about a possible major social and political crisis in China with devastating consequences for Latin America? Multiple, deep and contradictory interactions and entanglements, more than globalization, explain best the evolution of the world inequalities. This analytical framework also explains two major stylized facts: global inequality among individuals is reduced by the catching up of competition led growth strategies (China for instance) but increased within each nation-state given their specific inequality regimes.

7.5. Inequality: When Economic Power Shapes Political Processes

This embeddedness of individual inequality in specific national socioeconomic regimes is an invitation to overcome the methodological individualism implicit to most statistical analyses which frame inequality in terms of Gini or Theil indexes. Why not adopt instead a holistic individualism in which a set of basic social relations shapes the opportunities and constraints affecting individual strategies and consequently income and wealth distribution? This is precisely the objective of a lively multidisciplinary research program. Many researchers working within various sub-disciplines of social sciences – statisticians, historians, epidemiologists, sociologists, political scientists, socio-economists, political economists – now investigate the sources, evolution and consequences of economic, social, and political inequalities. Their efforts seem to converge towards *a* common understanding of the genesis of present inequalities. On one hand, large imperfections in markets are used by leading actors to exert oligopolistic and monopolistic economic power and appropriate a larger and larger fraction of national income and wealth. Thus, rising inequalities can best be seen as direct consequences of large asymmetries in the distribution of power in the economic sphere. On the other hand, the same powerful economic and financial actors, by their

access to political power, have acquired the ability to control the design of the regulations that shape their activity to their advantage, or conversely repeal any public supervision, regardless of the negative consequences for economic and financial stability or social cohesion. This framework is highly relevant for the US and UK societies that continue to be dominated by the power of Wall Street and the City of London. Nevertheless, this emerging theoretical approach is uniquely built upon the American and British cases. The precise processes operating in the US are not capturing the major factors that shape the evolution of inequalities in many other societies, for example in Germany or in Japan. The study of the interaction between economy and polity, politics and economics is also interesting for Latin America but specific investigations are required in order to detect the various processes that are not limited to the domination of financiers over nation-states, however important it might be elsewhere. How is power distributed in the different Latin American societies? This is the crucial issue for understanding the specificity of the large inequalities that have hampered the development of this continent, and might express themselves again if the inclusive growth strategy fails.

7.6. Inclusive Growth: An Unfinished Agenda

Precisely how can the permanent reduction of inequality launch a new growth pattern and define a long term and viable future for Latin America? Answering such a question would suppose a full understanding of the various processes and mechanisms that have generated the reversal of quasi secular trends. A survey of Latin American studies suggests that the ingredients have been multiple. Macroeconomists insist upon the positive consequences of the demand from industrializing Asian countries, since the export-led model has not been fully replaced by a domestic-led one, even in the case of Brazil, where the size of the domestic market and the degree of industrialization define the most favorable basis for the success of inward looking development. Other macroeconomists stress that governments have finally learnt from their recurring mistakes and they have adopted wiser policies that reduce the probability of a domestically generated major crisis. Welfare specialists point out the relative success of antipoverty strategies, but regret the absence of a fully-fledged welfare system, both in terms of stimulation of the domestic market and political legitimation of governments. Last but not least, political scientists argue that the transition to democratic regimes has been a precondition for most of the structural transformations previously mentioned. Within a *régulationist* approach, the viability of this new socio-economic regime depends on complementarity between the dynamism of the production and innovation system, the institutionalization of the wage labor nexus and the constitution of a welfare that would simultaneously provide a modicum of security for all and possibly enhance competitiveness. Specific studies are thus necessary in order to diagnose if

such a complementarity is actually emerging. In this respect, a comparative analysis of the process of emergence of modern welfare states could be enlightening for Latin American scholars and policy makers.

7.7. Do Not Forget Latin American Idiosyncrasies

The anxious concerns about the consequences of rising inequalities has generated a vibrant international academic community that has developed common concepts, methods, statistical indexes and understandings. Does this set of analytical tools fully take into account the most salient issues for Latin America? How should we deal with the opposition within the formal and the informal sector? What are the consequences of an urbanization that is increasing faster than industrialization, upon the methods for alleviating poverty and reducing inequalities? What have been the long term consequences of the conflicts between natural resources exporters and industrialists upon economic policy – for instance the choice of an exchange rate regime and a fiscal system – and the difficult constitution of the welfare system? How are social and economic inequalities exacerbated by the imperfections in the democratic process? Some promising studies on Latin America propose a class-based point of departure for an overarching analysis of the various sources of inequalities. If one is convinced that “classes matter”, then the investigation of the links between growth and equity should take into account the complexity of social classes in Latin American that cannot be reduced to the typical capital/ conflict or to the opposition between industrialists and financiers or to the distribution of talents and competence among individuals, as assumed by the current measures of inequality. It may well be, that one urgent task of Latin American researchers is to renew with the founding fathers of ECLAC in order to coin indigenous concepts, indexes and paradigms that would capture more accurately of the specificity of their fields. This would in turn be a step in the direction of a more general theory that is not hostage to concepts rooted in specifically European and North American configurations.

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