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Capitalism and COVID-19: Crisis at the Crossroads

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Abstract: Existential threats, such as the COVID-19 pandemic, have historically engendered intellectual paradigm shifts, and even systemic transformations in the economy and polity. This paper focuses on two inter-related phenomena: rising economic inequality and the diminution of liberal democracy, a feature common to both developed and developing countries set in the context of a ubiquitous and globalized capitalism. In the post-pandemic world, we need to harness the positive dimensions of the powerful capitalist system to lower inequality and build a newer world akin to an earlier golden age of capitalism.

Keywords: pandemics, inequality, globalization, capitalism

The COVID-19 pandemic is a truly stupendous human tragedy, not only due to the mortality it is causing, but also because the greatest global recession since the 1930s may be about to ensue, and the unprecedented scale of the disruption to movements of people, goods and services. The consequence is the immiserization of vast swathes of humanity, particularly endangering the lives and livelihoods of the marginalized and vulnerable across the globe. Such existential threats have historically engendered an intellectual climacteric, and occasionally, gradual systemic change. Whether such behavioural and mind-set alterations do actually materialize in the future is a matter for history, however, there is no dearth of opinions about how the present crisis should be managed, and what the ideal

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complexion of the world that follows, should be.¹ This paper focuses on two inter-related phenomena: rising economic inequality and the diminution of liberal democracy, a feature common to both developed and developing countries, set in the context of a ubiquitous and globalized capitalism, which, as a system, has triumphed over all alternatives.

1 Pandemics in History

Earlier pandemics have produced or set in train transformations in the sense of Polyani (1944). The Black Death (*magna pestilencia*) of circa 1348–50, heralded the demise of the feudal economic system (Scheidel 2017; Routt 2008), a process which was to last three centuries, ending with the cataclysmic 30 Years War of 1618–48 (Hobsbawm 1954). The decimation of the population following the Black Death made land more abundant relative to labour, increasing the wage-rental ratio. This had the impact of lowering inequality, a tendency moderated by the falling price of grain in the late 14th century. It also altered the composition of output, leading to less grain production, increased animal husbandry, and the pattern of Europe-wide trade in woolen products, halting the hitherto flourishing Silk Route trade (Routt 2008). There was also political turmoil, with peasant revolts in Belgium prior to the Black Death, in England in 1381, and in Germany in the early 16th century (Scheidel 2017). These may have had some levelling effects. The feudal system, however, lingered till the end of the 30 Years War (Hobsbawm 1954), which also produced intermittent epidemics. Hobsbawm (1954) characterized the 17th century as a period of crisis in Europe. The conclusion of that catastrophe radically altered the global economic system in many ways, chief of which was the decline of Venetian Mediterranean trade. Citing detailed evidence from the devastated German city of Augsburg, Scheidel (2017) outlines the “equalizing” consequences of physical devastation, particularly through the proscription of the richest segments of society. The impact of the 30 Years war and the plague epidemics of the 17th century are also discussed by Caruso (2020).

Voigtländer and Voth (2013) point to wars and war-related epidemics from the Black Death up to the 18th century arguing that the decrease in population caused an increase in per-capita income, as the stock and productivity of land were left unaffected. This provided rulers with a taxable surplus, which they invested in armies and armaments, producing more war.

¹ In the words of Terence, who lived in second century B.C. Rome: *Quot homines, tot sententiae* (there as many opinions as there are men). <https://www.merriam-webster.com/dictionary/quot%20homines%2C%20tot%20sententiae> (accessed 10 May 2020).

Using an apocalyptic, Biblical, analogy Scheidel (2017) speaks of “four horsemen” which have acted as the great (economic) levelers throughout history: total war necessitating mass mobilization, state collapse, pandemics and political revolutions.² All of these phenomenon are in reality inter-related and endogenous to each other. The present pandemic’s impact on wealth and income inequality is yet to emerge, but what must be borne in mind is that in present-day production labour is more substitutable than ever before due to artificial intelligence, providing scope for the capital-labour ratio to rise, even though stock market and commodity prices have plummeted, and the prospects for de-globalization loom large.

2 Twin Crises of Capitalism: Inequality and Populism

One of the greatest challenges of our day is the growing world-wide tide of inequality in income and wealth (Stiglitz 2012; Piketty 2014) since about 1980. This development has occurred against the backdrop of accelerating globalization. A degree of inequality is acceptable to most as an outcome of incentivization mechanisms, and as a reward to risk taking, effort and prudential decision making. The inequality thus produced is an inequality of outcome. But, high and persistent inequality produces inequality of opportunity.³ Disadvantaged groups are unable to advance themselves by making the right life choices and exerting effort, due to the structural barriers presented by inequality of opportunity. Most agree that inequality of opportunity is undesirable, even immoral, and needs redressing; where opinions diverge is over the existence and pervasiveness of these unequal opportunities.

The causes of inequality are well known. First, unskilled labour saving technical progress; secondly, financial globalization; thirdly, less regulated labour markets, including informal and precarious employment. The nature of global manufacturing production has become increasingly fragmented, with components produced and shipped to different locations across the globe, turning nation states into regions. Financial globalization and the greater mobility of capital contribute to greater inequality by lowering the bargaining power of labour under the threat of economic activities locating overseas (Furceri, Loungani, and Ostry 2017). These

² Milanovic (2016) speaks of these as the malign forces of income equalization.

³ Discrimination, based on personal or group characteristics, such as race, ethnicity, religion, sexual orientation can also produce inequality of opportunity.

developments also mean that there is a tendency for capital's share in total product to rise (see the evidence cited in Milanovic 2016). Piketty (2014) demonstrates the rising ratio of the value of capital to national income in a number of countries. And, as everyone knows the ownership of capital is much more concentrated compared to labour income. In a global context, (Milanovic 2016, figure 1.8) demonstrates that the share of billionaires wealth relative to global GDP was under 3% in 1987; this had increased to more than 6% by 2013. Accompanying this, the national income share of the middle class (defined as having an income in the range of 25% above and 25% below median national income) declined over this time period in nearly all Western democracies, with the United States exhibiting the lowest middle-class share, and the UK not far behind with the fourth lowest share (Milanovic 2016, figure 4.8).

When we come to trends in global inequality three factors come to mind. The first relates to the famous Kuznets hypothesis that inequality first increases with growth and then declines, as growth proceeds further. Milanovic (2016) suggests that there may be Kuznets waves. Inequality in various industrializing and industrialized countries first rose and then declined in the 1820–1970 period. The peak in inequality was invariably at some point during the first epoch of globalization (1870–1914), and inequality tended to decline in most advanced industrialized economies after the First World War until about 1980. Once again, as globalization gathered pace during its second historical phase post-1980, inequality crept up again; this time developing countries, especially emerging market economies, have also been participants. Thus, the two historical episodes of increasing globalization are associated with rising inequality. Note, that as average income rises it is theoretically feasible to have greater inequality due to the increased distance between subsistence income and average income (Milanovic 2016).

Next, we have the concept of “global” inequality, developed mainly by Branko Milanovic (Milanovic 2016, for example). In recent years, the greatest beneficiaries of changes in the global income distribution have been the world's super rich (the top 1% in the income distribution) along with the middle classes in emerging market economies; the greatest losers have been the lower middle and low income groups in developed countries. Global inequality can be further decomposed to inequality within nation states, as well as the inequality between countries based on their average incomes. The inequality within nations has been rising everywhere, despite a short brake on inequality during the tenure of progressive regimes in Latin America. The other component of global inequality is the inequality between nations, and here we can focus on the population differences in per-capita income between nations. We would expect global inequality to fall as average income in the most populous developing countries (China and India) catches up

with rich countries, and indeed this has been the case. But when we combine the two factors that make up global inequality, most of present-day global inequality still continues to be attributable to between country inequality, that is the inequality which stems from differences in average income between rich and poor nations. How rich or poor an individual is, depends on their position in the hierarchy of occupational incomes, but is more attributable to where they reside and work. A bus-driver may be poor because of his disadvantaged place in the wage league table, but more importantly it depends on where he is a bus-driver (a rich or poor country). Thus, according to Milanovic (2016) there is a *citizenship rent*, and consequently a *global inequality of opportunity*.

Finally, rising inequality alters the political landscape moving it inexorably towards greater plutocracy in both advanced democracies and the elected authoritarian regimes in the developing world. This tendency has been driven, in no small degree, by the creeping importance of money in ensuring electoral success (Milanovic 2016, 2019). The median voter thesis of Downs (1957) whereby the interests of middle classes dominate in a democracy has been replaced by the clout of the super rich. National policies serve to further the interests of the owners of internationally mobile capital and skills. This manifests itself, chiefly, in the nation state being obliged to follow policies of fiscal austerity and wage compression, lest national participation in the globalized economy be jeopardized. It also frays the domestic social contract, and leads to the diminution of social protection. By contrast during the era of more limited globalization prior to the 1980s, the interests of the rich and the median income group did not necessarily conflict; it was an era of growing social protection, the provision of public services like education and health, employment rights, declining inequality and consensual democracy. Mizruchi (2013) points out that in the early post-war era (1945 to the 1970s) the corporate elite in the United States exhibited ethical considerations of civic responsibility and enlightened self-interest, unlike at present. In short capitalism, can be both benign or malign, depending on the epoch.

Increasing inequality in an epoch of hyper-globalization has fueled the flames of populist politics. Here it is important to distinguish between the liberal and electoral aspects of “democracy” (Rodrik 2017; V-DEM project 2017). A liberal society is one where there is respect for minority rights, constraints on the executive (and legislature), with an independent judiciary, and there is respect for the rule of law. The electoral process refers to (multi-party) electoral competition. There is no reason to always expect liberal values to be present in an electoral “democracy”. A purely electoral process may elect populist dictators or parties with scant respect for liberalism. Rodrik (2018) suggests that the rise in populism coincides with hyper-globalization. The vote share of populist parties since 2000 in

selected European and Latin American nations has exceeded 10% (Rodrik 2018, figure 1).

Indeed, it can be argued that in recent elections in the USA in 2016, the 2019 UK election and the Indian elections of 2019 the median voter resoundingly voted to become poorer. Despite the nationalistic rhetoric, the ultimate outcome of the policies of these elected administrations will further immiserize the already poor. Two explanations enable the rationalization of this irrationality. The first is cognitive dissonance. The second is to do with the “memetic” viral spread of ideas, leading to identity based nationalism triumphing over economic interests in the mind of the median voter, who is willing to sacrifice economic interests for the sake of nationalist identity based actions such as America First, Brexit or the proscription of Muslims.

3 What Needs to be Done

As an economic system, the powerful and productive capitalist mode of production is here to stay. In the past four decades capitalism has been creating greater inequality. Milanovic (2019) divides the capitalist world into liberal-meritocratic systems, as in the established old democracies in Western countries and the “political” capitalism best exemplified by China, with autocracy as its hall mark. The growing tide of authoritarianism in many “developmental” developing countries mirrors the latter image. At the present time, however, there is a degree of convergence between the two systems due to the rising tide of corruption in “political” capitalist states, and the plutocracy in the liberal states driven by the power of money in the electoral process.

We must resurrect the positive side of capitalism, as evidenced during its golden age (Marglin and Schorr 1989) after the Second World War. This means greater public spending on health, education, social protection and redistributive policies which redress inequality, which under the present depressed circumstances also serve to boost output and employment for the poor. We must seriously consider taxes on wealth, the possible distribution of capital to the less affluent segments of the population, and ways of engendering greater demand for unskilled labour via labour augmenting technical progress. In this connection, Dabla-Norris et al. (2015) and Ostry, Berg, and Tsangarides (2014) show that the recent growth experiences of a cross-section of developed and developing countries suggest that inequality is actually harmful to growth prospects, contrary to the received wisdom that inequality, by permitting the rich to save and invest more in productive capital, oiled the wheels of growth. Also, there is now ample evidence that redistributive policies, including social protection expenditures appear

to no longer crowd-out growth prospects (Ostry, Berg, and Tsangarides 2014). In other words the efficiency-equity trade-off (Okun 1975) no longer exists, or is very much weaker linked to new forms of market failure and extreme inequality. We must also consider ways of redressing the global inequality of opportunity by permitting greater migration of unskilled workers from the global South to the North. Novel methods of reducing conflict via buy-backs of weapons (Caruso 2020) also merit attention.

Criticism of “hyper-globalization” emanates from both the liberal and populist camps. Rodrik (2017) outlines the globalization trilemma, whereby the simultaneous achievement of national sovereignty, democracy and hyper-globalization is impossible. A more diminished form of globalization such as that which prevailed during the Bretton Woods era up to the 1970s may be desirable, with curbs on financial flows, and the rules governing the global economy subject to the nation state’s redistributive social contract. Populists too are wary of globalization, often motivated by their xenophobic search for scapegoats. There is evidence of de-globalization in the world economy (van Bergeijk 2019), highlighted by the aggressive trade policies of the USA since the inauguration of Donald Trump as President, and the COVID-19 pandemic is bound to disrupt global supply chains. There is a widespread expectation of a decline in the volume of international trade and transactions, and globalization generally. This is mainly down to hegemonic change, and the lack of global economic leadership recently displayed under President Trump. At present, there is a lack of international policy coordination, as was the case via the G-20 in 2008 following the financial crisis. The success of economic globalization hinges crucially on the ability of an economic hegemon (UK and the USA) providing leadership, policy coordination and being a lender of the last resort to prevent economic collapse. This does not seem forthcoming from the United States at present, and China seems still not ready to step into the global economic leadership shoes. But we must not allow de-globalization to proceed too far, so as to retain some positive features of the earlier liberal-internationalist order (Gleditsch 2008; Ikenberry 2018), which also coincided with the golden age of capitalism.

More than ever, the present crisis should serve to remind us that inequality is the mother of all forms of conflict, which demands amelioration.

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