Can the Sustainable Development Goals stem rising income inequality in the world?

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Income Inequality, past and present

Three days after the fall of the American banking giant Lehmann Brothers, and amidst the crisis or great recession of 2008, I gave my inaugural address at ISS. I concluded then: *The current crisis and the increased public concern for improved income equality might provide the basis for a renewed political coalition to make employment creation and fair income distribution again major objectives for economic policy-making. But it is far from clear whether in most countries such a coalition would have sufficient influence to drastically changing economic policy.* (van der Hoeven, 2010). I had sincerely hoped that the tide of growing income inequality would be turning, but sadly enough this is not the case in most countries, neither in the world nor among all citizens in the world, as I later will explain in more detail.

My concern for income inequality was not triggered by the crisis of 2008; actually it started much earlier in my academic live: end 1960s early 1970s, when I was studying econometrics in Amsterdam and where I was inspired by writings, and listening to, Jan Tinbergen and Jan Pen, who wrote and spoke with much conviction on inequality in the world and in the Netherlands. The beginning of the 1970s saw an increasing interest in income inequality, also for developing countries. This was not so obvious actually. Take for example the proposal for the first Development Decade of the United Nations (1960-1970) that stated: *It is true that the General Assembly resolution lays down a precise quantitative target only for the increase in aggregate incomes, and that there is no similar quantitative target for changes in income distribution. We can, however, take it for granted that the 5 per cent growth target established by the resolution also implies that the increment in income thus achieved should be wisely used for the benefit of the poorer sections of the population and should result in a degree of social progress which is at least in "balance" with the rise in aggregate national income (Meier, 1971, p.54).* This sounds familiar even these days isn't?

In the early 1970s however, more and more scholars and activists started to voice concern about growing inequality and enduring poverty, especially from Latin American countries where progress coincided with enduringly high or growing income inequality. The Prebisch report in 1970 advocated for example reduction of inequality and argued that reducing inequality would not hamper growth and economic progress (Prebisch, 1970). On the contrary: new analysis showed that more equal income inequality could lead to a more balanced growth, through which poverty could reduce faster. The International Labour Organization (ILO) carried out, in cooperation with development institutes in developing and developed countries, a number of targeted country analyses on employment and inequality and did put the issue of unacceptable high levels for inequality on the international agenda. It was even the major recommendation in policy advice for Colombia. (I was fortunate to use that material for my master thesis on *Income distribution and economic growth* and the ILO became for a large period in my career my employer). The ideas gathered by ILO and research groups in various countries resulted in 1974 in the publication *Redistribution from Growth* by the Institute of Development Studies in Sussex, in cooperation with the World Bank, in 1974 (Chenery et. al. 1974). This publication documented for several countries growing inequality and emphasized practical redistribution policies. Irma Adelman, the pioneer on inequality in the 1960s brought the idea of redistribution from growth further to *Redistribution before Growth*, based on successful development patterns in Taiwan and Korea. She argued, in a lecture at ISS in 1979, that redistributing factors of production (land, better education, investment capital) before these would become scarce in a strong growth phase of the development process, and thus would command higher wages and prices, would be a superior way to achieve a more equal income distribution during the course of development. This idea was similar to those in Nobel laureate and ISS honorary fellow Tinbergen's 1975 book on inequality, which explained inequality as a race between technological progress and education. If technological progress grew faster than education, those who could master technological progress could receive larger rents than those who could not, leading to higher income inequality. (These discussions are echoed recently for developed countries in what is now called by the American political scientist Jacob Hacker (2011) *pre-distribution*: an example how the developed countries can take examples from (good or bad) experiences in developing economics, and then I am not referring to Greece only...).

The attention to greater equality in the mid-1970s also led to the so-called basic needs approach to development, partly based on previous development plans in India after independence. It became a focus in various development institutes like IDS and ISS, and a lead concern for ILO. The logic was as follows: If the satisfaction of basic needs would be a main objective of development, then more attention to redistribution is warranted in order to arrive faster at providing basic needs (Hopkins and van der Hoeven, 1983). This approach, however, was not entirely accepted. According to some developing countries the basic needs approach focused too much on the poorest developing countries, and gave too little attention to international measures to foster national economic growth (van der Hoeven, 1988). Basic needs were thus interpreted as a distraction from the 1970s debate on a New International Economic Order (NIEO) that envisaged reforms in the international relations so that developing countries could grow faster. This fear was fed by the fact that the World Bank became also interested in the basic needs approach, however, more as a social planning instrument without redistributive elements, than as a strategy to large structural changes within countries and between countries. Those who had argued initially for the basic needs approach argued that the basic needs approach was not anti-growth and produced evidence that emphasizing basic needs is not anti-growth, calculating how international reform could stimulate growth and satisfaction of basic needs.

However, while these discussions were going on, structural adjustment programmes (SAPs) started to dominate in various of circles development thinking and financing. After two oil crises in the 1970s and an increase in foreign debt in many developing countries – caused by the abundance of petrodollars on the world market – and after the debt crisis of Mexico in 1982, the World Bank and the IMF introduced these programs, where the focus was on budgetary cuts, liberalization of markets and active promotion of exports, aiming at stimulating growth and at strengthening capacity in developing countries to repay debts in foreign currency (Addison, 2002). Attention to social problems and domestic income inequality moved to the background.

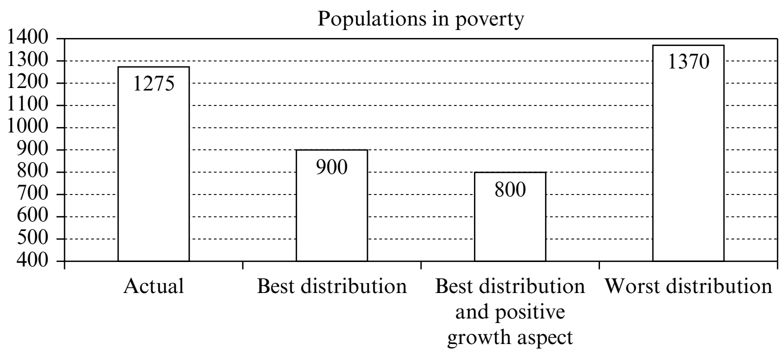
Middle and late 1980s saw a countermovement. Critics saw the SAPs, because of their liberal economic policy, as a major cause for increasing inequality and other social problems, especially in those countries that were obliged to take part in the program. Critics were led by national politicians, NGOs, scientists from the South and the North and by organizations in the UN system itself. These were not only organizations with a more social mandate, such as UNICEF, ILO and UNRISD, but also regional economic organizations such as, ECA and ECLAC, as well as the trade and development organisation UNCTAD. The criticism of the structural adjustment programmes rose, not only from the social angle, but also more and more from the economic angle, because the programs often did not lead to accelerated growth and reduction in debt. (A special program for debt forgiveness in poorer countries – HIPC – had to therefore also to be set up in the 1990s). It would take until the middle of the 1990s until more social objectives of development cooperation gained traction again.

Early 1990, the UNDP launched its annual *Human Development Report*, based on the ideas of Nobel Prize laureate and ISS honorary fellow Amartya Sen, asking for more attention to human development and also acting as a counterpart for the already existing World Development Report of the World Bank. The UN itself has organized a number of world summits on development issues. After the Berlin Wall fell, cold war issues no longer dominated the discussions in the UN. One of those was the Social Summit in Copenhagen in 1995 (World Summit for Social Development), which dealt with the problems of, and gave policy recommendations for poverty reduction, employment and social inclusion. The Social Summit contained explicit recommendations for the reduction of political, legal, economic and social factors that promote or maintain inequality in income.

The results of the renewed attention to social issues led to preparations for the UN Millennium Summit in 2000 and to the subsequent formulation of the Millennium Development Goals, in which a 50 per cent reduction of poverty and improving several social targets at the global level were among the 8 goals (see Annex 1). In preparing an ILO contribution to the MDGs, Malte Luebker and I carried out a thought experiment on inequality: a *what if* experiment. We asked ourselves what if all *developing* countries would have in the year 2000 an inequality level, which was the lowest they had seen since the Second World War. So we did not propose something radical that would be out of reach for a country. We did not suggest, for example, that a highly unequal country Brazil should become as equal as Sweden etc. The outcome of this thought experiment was that *the number of poor people in 2000 could have been one third less if countries would have a level of inequality equal to that what they would have had in the past*. In a second thought experiment we added another fact, namely that a country with moderate inequality would grow faster than a country with greater inequality. Under this scenario the number of poor would have been reduced by almost 40 per cent (Figure 1).

Figure 1: Population in Poverty in the year 2000 according to actual and hypothetical best income distribution scenarios

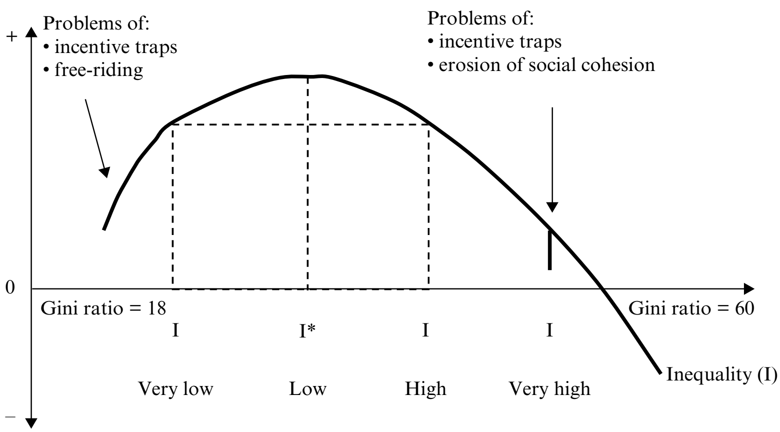
Source: Compiled from Luebker 2002



At the end of the 1990’s The Economic Research Institute of the United Nations (UNU-WIDER) started under its new director Andrea Cornia and deputy Tony Addison a large research program on inequality, growth, poverty and globalization. Globalization is characterized by greater integration in terms of trade and capital flows, made possible by new technologies but more so by international conventions and agreements that liberalised the rules governing external markets, as explained a.o. in the report of the World Commission on the Social Dimensions of Globalization of which Deepak Nayyar was a member, and for which I led the research secretariat.

One of the findings of the UNU-WIDER program was that too high income inequality hampers a kick off of growth, but also too little inequality, as happened in the former east bloc countries, (Figure 2). Income inequality is expressed in the form of the so-called Gini ratio, where absolute equality is zero and absolute inequality is one.

Figure 2: Inequality and growth: optimal scenarios
Source: Cornia (2004, p.45)



The project looked first at, what it labelled, the old explanatory factors of inequality (land inequality, poor education, poor infrastructure, urban bias) and found that, while these still explained the *level* of inequality, these could not explain well the *rise* in inequality. The main causes of the *increase* in national income inequality were the liberalization of trade and especially of capital markets, very much associated with globalization, the significantly increased financialization of national economies and of international relations, technological change, and the growing limitations of labour market institutions that had led to greater inequality between unskilled and skilled workers (Cornia, 2004, Shorrocks and van der Hoeven, 2004).

Despite these and various other analyses, the MDGs did not include reducing national income disparity in the targets for poverty reduction, and, for that matter, did not include reducing national inequality in other targets, such as those for education and health, as Jan Vandemoortele, who was involved in formulating the MDGs, has been arguing since the formulation of the MDGs. I will come back to this in the second part of my lecture.

In the early years of this century some major developing countries, now more appropriately called, 'emerging countries' showed strong growth in national income. These countries are *catching up* as Deepak Nayyar has phrased it so well in his latest book (Nayyar, 2013b). Also some poorer countries showed faster growth for the first time. However, income inequality rose in many countries, developing countries, emerging countries and developed countries alike. A number of countries in Latin America showed some decrease in income inequality, but this was not enough to get them out of the leading group of countries with the greatest income inequality in the world.

Halfway through the first decade of the new millennium a large number of reports from, among others, the UN, the World Bank, UNDP and ILO, appeared which all called for a reduction of rising or high income inequality, based on extensive research and data collections in this field. The validity of the Kuznets curve (which argued that during a process of development income inequality would rise and thereafter would decline, hence there would be no need for special attention) was rejected and valid arguments were put forward that a more equal distribution of income and assets did not have to lead to a decrease in economic growth.

After the financial crisis even the more traditional financial and economic circles sounded the alarm bell, fearing that large and rising income inequalities could affect the foundations of the free-market system. The number of items in the *Financial Times* about income inequality increased significantly. Piketty’s book on Capital in the Twenty First Century (Piketty, 2014) was well received and also on the ski slopes of Davos, where the annual World Economic Forum takes place, growing or large income inequality is the last two years one of the most important agenda items.

Globalization, at least the unrestricted globalisation that we see now, and income equality are clearly at odds with each other (see also Gunther and van der Hoeven 2004, van der Hoeven 2010, Vos 2010 and Bourguignon, 2015).

In 2010 Peter van Bergeijk, Arjan de Haan and myself organised a project looking, from a multidisciplinary perspective, at the financial crisis and the developing countries. Although all necessary data were not at hand, we sketched, in the introduction of the book emanating from that project, a picture how incomes of different groups in different country groupings were affected by the financial crisis originating in the USA and Europe (Table 1).

Table 1: Effects of financial crisis on various socio-economic groups in different country groupings
Source: Van Bergeijk, de Haan and van der Hoeven (2011, p.13)

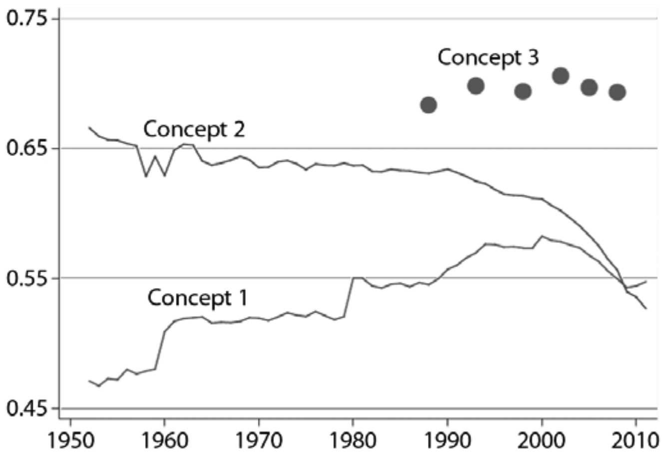
	Pre crisis	**Crisis**	**Postcrisis stimulus**	**Postcrisis fiscal austarity**
Developed countries				
Capital owners	++	–	++	+
Skilled workers	++	–	+	–
Unskilled workers	–	–	+	–
Excluded	–	0	0	–
Emerging developing countries				
Capital owners	++	+	++	+
Skilled workers	++	–	+	+
Unskilled workers	+	–	+	–
Peasant	–	–	+	–
Poor developing countries				
Capital owners	+	0	+	+
Skilled workers	+	–	+	–
Unskilled workers	–	–	+	–
Peasant	–	0	+	–

In effect, the poorer segments in the developed countries face a triple whammy: they did not profit from globalization, they were hardest hit in terms of unemployment and are now bearing the consequences of fiscal tightening following the massive stimulus and bank bail-outs. The situation for developing countries though is more complex. The growth path of the emerging developing economies shows similar movements as that of developed countries, but of less intensity and these economies were thus less affected by the crisis. However, except for some Latin American countries, the growing inequality which was building up or being reinforced, is not yet being halted, and wage shares in most emerging market economies are still declining, with a negative effect on domestic demand. The poorer developing countries, mainly in Africa, were less affected as their banking system was less developed, but still suffered from slower exports proceeds, remittances and lower aid levels.

Drivers of Income Inequality

What are the drivers of inequality? In order to answer that question we must first define income inequality more precisely. But first another issue: I have been talking until now about income inequality within countries. One may say: should we not have a more cosmopolitan approach, especially given the strong growth of several emerging economies, and rather look at inequality in the world? Several authors have done so in detail, e.g. Milanovic (2012) and van Bergeijk (2013). UNDP (2013) in a recent report has demonstrated what this entails (Figure 3).

Figure 3: Gini Index of global Income inequality
Source: UNDP (2013) Box 3.1



If we treat each country as a unit (concept 1), average incomes across countries have actually become more unequal. However, if population size is taken into account (Concept 2) incomes across the world become more equal. But if we take incomes of all households individually into account (Concept 3 for which much less data are available) the Gini Index of global income inequality is around 0.7, much higher than the level of income inequality found within any individual country. Despite the convergence in the average income of some big emerging countries, rising income inequalities within these countries resulted in overall global inequality not going down. On the contrary: it showed some increase during the globalization era from the mid-1980s to the early 2000s (UNDP 2013).

Now let me define national income inequality more precisely: The classical economists paid attention mainly to the distribution of income between labour and capital, the main factors of production. This type of inequality is therefore called factor income or functional inequality. This distinction between labour and capital income drove the great classical debates for many years In the post Second World War period, however, less attention was given to this type of inequality, as neoclassical production functions often assumed a constant capital share under the assumption that wage increases follow productivity increases. Attention shifted to personal income or household income distribution.

One can interpret household income distribution in three ways (van der Hoeven, 2010):

- *Primary* income distribution: the distribution of household incomes consisting of the (sometimes cumulated) different factor incomes in each household, before taxes and subsidies as determined by markets and market institutions.
- *Secondary* income distribution: the distribution of household incomes after deduction of taxes and inclusion of transfer payments (i.e. as determined by fiscal policies).
- *Tertiary* income distribution: the distribution of household incomes when imputed benefits from public expenditure are added to household income after taxes and subsidies. This interpretation of household income is particularly relevant for developing countries as different services and government services are often provided for free or below market prices.

Most policy discussions on inequality though focus on secondary household income distribution (take home pay, rents, interest earnings and profits after taxes).

More recently attention is shifting back to factor income distribution.[1] Daudey and Garcia Penalosa (2007) argue that the distribution of personal or household income depends on three factors: the distribution of labour endowments, the distribution of capital endowments, and the way in which aggregate output is shared between the two production factors.

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[1] The IMF (Jaumotte, and Tytell 2007) investigated the effect of globalization on the labour income share in developed countries as did the OECD (Bessani and Manfredi, 2012) while UNDP (Rodriguez and Jayadev, 2010) and ILO (2011) and (2012) carried out several analyses on a broader set of data encompassing all countries in the world.

The factor distribution of income is a statistically significant determinant of the personal distribution of income[2]: a larger labour share is statistically associated with a lower Gini index of personal incomes. It is therefore important to also (re-) consider the factor distribution of income.

The focus on factor income inequality points to the importance of better understanding the changing position of labour in the production process in order to correctly interpret inequality trends, as labour has been losing ground relative to capital over the past 20 years (ILO 2011). Furthermore, experience has shown that it is not possible to reduce primary household income inequality without addressing how incomes are generated in the production process and how this affects factor income inequality (van der Hoeven 2011). The great British scholar Tony Atkinson (2009) argues convincingly that there are at least three reasons to pay again greater attention to factor income distribution:

- To make a link between incomes at the macroeconomic level (national accounts) and incomes at the level of the household;
- To help understand inequality in the personal distribution of income;
- To address the social justice concerns with the fairness of different returns to different sources of income.

Also the too early deceased Andrew Glyn (2009) argued that factor income distribution matters to people for at least two reasons. Firstly, despite broader access to capital among households, wealth, and especially high-yielding wealth, is still extremely unevenly distributed as Thomas Piketty (2014) has reminded us so eloquently last year. Therefore redistribution from labour to property still has a significant effect in raising household income inequality. Secondly, the fact that profits may be rising much faster than wages, conflicts with widely held views of social justice and fairness.

[2] Other variables used are manufacturing share, GDP per capita, openness, civil liberties and, human capital.

More recently Trapp (2015) has argued that dynamics in the factor income distribution are of particular relevance for developing countries, especially in their effort to fight poverty. Regressive redistribution of factors and their remuneration will be felt strongly in these countries, due to weak social safety nets and limited access to capital by the poor. The main asset of the poor certainly is labour. As such, the labour income share can serve as an indicator in designing policies for social protection and tax systems as these usually target the factor income distribution (minimum wage policies, tax concessions for investments, etc.).

It is therefore important to be more explicit about the drivers of factor income distribution, as well as the drivers of primary, secondary and tertiary household income distribution and the relation between these. There are many drivers that affect the different types of income distribution. One can distinguish between drivers that are largely exogenous (outside the purview of domestic policy) and endogenous drivers (i.e. drivers that are mainly determined by domestic policy). However, a clear line is difficult to draw, because even drivers that at first sight may appear to be exogenous or autonomous are often the outcome of policy decisions in the past or the outcome of a domestic political decision to create international institutions (for example the creation of WTO to establish trade liberalization or the decision to invest in technical progress). With increased globalization, exogenous drivers gain in importance. As a consequence more is expected from national policy drivers to counteract the effect of the more exogenous drivers. Table 2 shows the interactions between the various exogenous and endogenous drivers and the various types of income distribution.

Table 2: Interaction between main drivers and various types of income distribution
Source: UNDP (2013) Table 3.8

	Distribution type				
	Factor income distribution	**Wage distribution**	**Primary household income distribution**	**Secondary household income distribution**	**Tertiary household income distribution**
Drivers					
Exogenous Drivers					
1. Trade globalisation	X	X	X		
2. Financial globalisation	X	X	X		
3. Technical change	X	X	X		
Endogenous Drivers					
4. Macroeconomic policies	X	X	X		
5. Labourmarket policies	X	X	X	X	
6. Wealth inequality	X	X	X		
7. Fiscal policies: Taxation and Transfers	X		X	X	X
8. Govt Expenditure					X

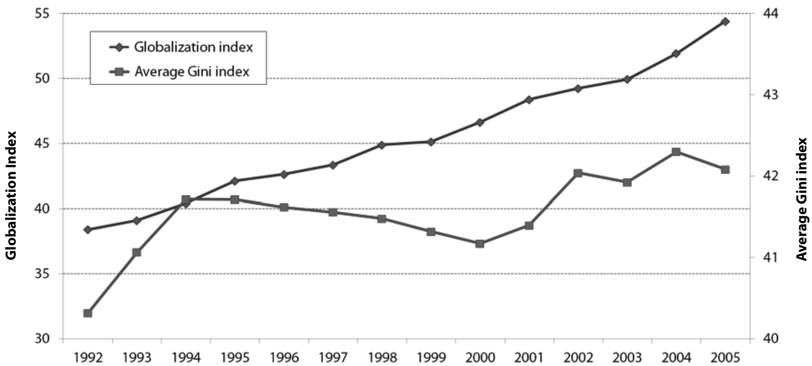
The crosses in the table indicate were the effects of these various drivers is the strongest. We see that exogenous factors (globalisation) affect mainly factor income and primary household income distribution (upper left quadrant of Table 2), while endogenous drivers affect both factor income and various types of household income distribution (lower left and right hand quadrants).

Income Inequality and Globalization

Many aspects of globalization can be seen as drivers of income inequality, especially the factor and primary household income inequality (van der Hoeven 2009). Traditionally, most attention has been given to the effects of trade and trade openness on income inequality, but more recently financialization and technical change (particularly in relation to its effect on wage differentials) have also been the focus of much attention. The impact of these globalization drivers on income inequality depends however also on national macroeconomic and labour market policies, which can either counteract or intensify their effects.

In Figure 4 the Gini index of household income is plotted against the Globalization index[3]. The Globalization index[4] is the most widely based index of globalisation as it combines the major *de facto* indicators of globalization (trade, FDI stocks, portfolio Investment, and income payments to foreign nationals) with various *de jure* indicators (hidden import barriers, the mean tariff rate, taxes on international trade and capital account restrictions).

Figure 4: Income Inequality and Globalization across the World, 1992-2005
Source: UNDP, 2013, Figure 3.6



[3] For details see: Ragab,A 2013, *Technical note on income inequality and trade and financial globalization trends*, UNDP, New York

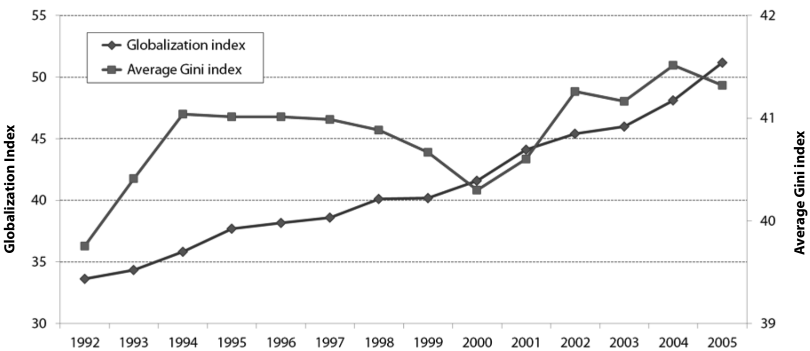
[4] For detailed definitions of index components and weights see Dreher, Gaston and Martens (2008) http://globalization.kof.ethz.ch/

In a sample of 102 countries (30 high income countries, 72 lower and middle income countries), the rise in the Gini index coincided with an increase in globalization. For countries in this sample the average level of inequality increased by 4% during the period, while the index of globalization increased by 42%. The correlation between the two measures is above 70 percent.[5]

This strong correlation for all countries holds also when high income (developed) and developing countries are considered separately. The correlations between the two indicators in each group are 68% and 67% respectively (see Figures 5 and 6 below). But in high income economies there is an already high level of globalization at the beginning of the period with a slow rise thereafter (from 61 in 1992 to 68 in 2005) while lower and middle income economies start at a much lower level of globalization and have a much steeper rise (from 34 in 1992 to 52 in 2005).

Figure 5: Income Inequality and Globalization across Developing Countries, 1992-2005

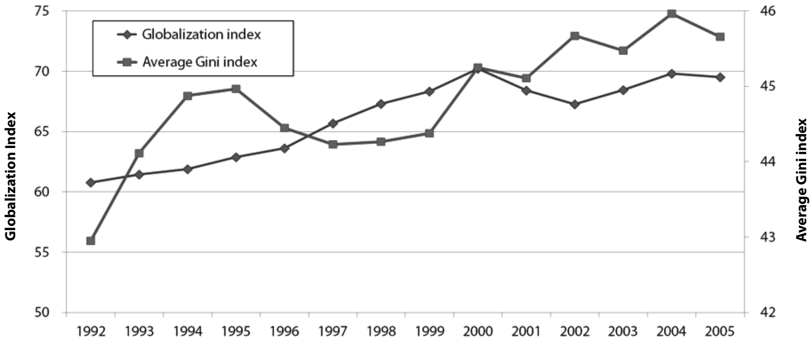
Source: UNDP, 2013, Figure 3.7



[5] Analysis with other more restricted indices or variables of globalization (such as trade openness or financialization) gave similar results, See Ragab, A. 2013, Technical note on income inequality and trade and financial globalization trends, UNDP, New York)

Figure 6: Income Inequality and Globalization in High Income (Developed) Countries, 1992-2005

Source: UNDP, 2013, Figure 3.8



Grouping countries by income status and looking at period averages gives also some quite interesting insights (Table 3). Among developing countries, indicators of income inequality and of globalization increase uniformly for each level of income status group. Upper middle-income developing countries score higher on both inequality and globalization than lower middle-income countries, and lower middle-income score higher on both measures than low-income countries. Among the subgroups of countries that changed income status classification during the period, the group of countries that graduated from low to lower middle, and the group that graduated from upper-middle to high income (developed) had a strong positive correlation in the trends of both globalization and income inequality.

Table 3: Average Gini index and Globalization Index by income status groups
Source: UNDP (2013)

Income status group	Gini Index	Globalization Index
Low-income	*39.6*	*49.2*
Lower-middle income	*43.5*	*54.4*
Upper-middle income	*50.9*	*60.3*

Globalization and factor income inequality

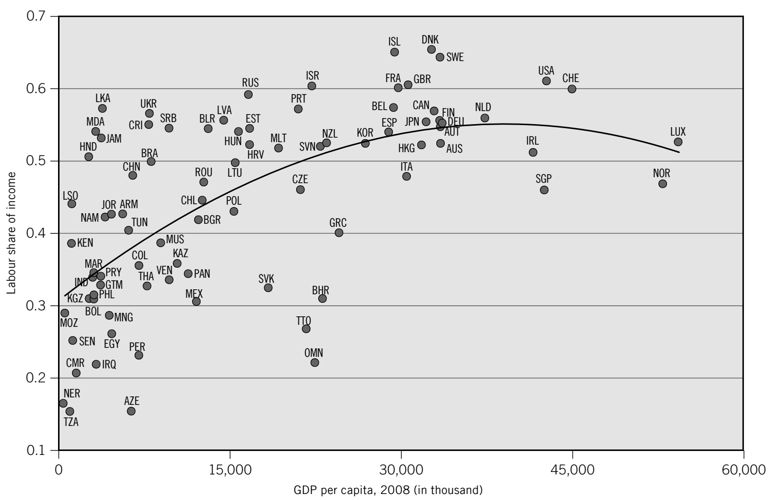
The decline in labour income shares during a phase of globalization, is not limited to specific sector but is an economy wide phenomenon. Rodriguez and Yayadev (2010) investigated by means of a large panel dataset for 135 developed and developing countries whether the secular decline in labour income shares is due to the decline of the labour income share in particular sectors or whether the decline in labour income share is economy wide. By matching national economy wide results with results for the labour income share at the 3 digit industry level they conclude that the decline in labour income shares are primarily driven by decreases in intra-sector labour shares opposed to movements in activity towards sectors with lower labour income shares. *This suggests that the decline in labour shares is driven by economy wide phenomena and therefore, national policies rather than industry specific policies are needed to reverse it*.

The downward trend of the labour income share is even more pronounced in many emerging and developing countries, with considerable declines in Asia and North Africa and more stable, but still declining, labour income shares in Latin America (ILO 2011). ILO 2013 and Stockhammer 2013 have used an enlarged panel dataset encompassing developed, developing and emerging economies to investigate the drivers of declining labour income shares. The average of labour shares in a group of 16 developing and emerging economies, declined from around 62 percent of GDP in the early 1990s to 58 percent just before the crisis.

These results confirm of Diwan's earlier observation (Diwan, 2001) that currency crises are associated with sharp declines in the labour income share, reiterating that the cost of financial instability affects labour disproportionally. More recent analyses (Stockhammer 2013 and ILO 2013) find decline of the welfare state and weakening of labour market institutions in addition to financialization, globalization and technical change as drivers of factor income inequality.

The decline of the labour income share in developing countries is the more worrying as, according to past patterns of development, the labour income shares in developing countries should actually rise with increasing per capita GDP (Figure 7).

Figure 7: The unadjusted labour income share and GDP per capita in 2008
Source: ILO (2014) Figure 8.2



Note: The labour share of income is measured as the ratio of compensation of employees to GDP at factor cost in 2008. GDP at factor cost is measured as GDP at market prices, minus the difference between taxes, less subsidies for production and imports. Source: Authors' own calculation based on data from the United Nations Statistics Division; China: National Bureau of Statistics; Penn World Tables.

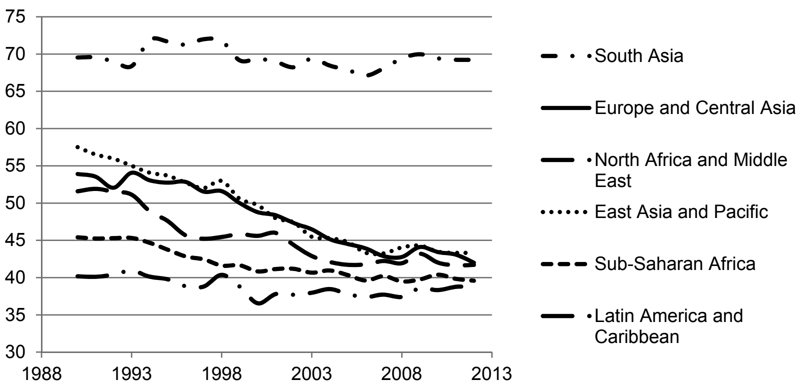
More recent data confirm the trend of a declining labour income share observed before the crisis of 2008. In a recent study, using an augmented data set, (distinguishing labour income share in the corporate sector and in the whole economy) Karabarbounis, and Neiman (2015) found that the global corporate labour share has exhibited a relatively steady downward trend, from a level of roughly 64%, reaching about 59% at the end of the period, while labour's share of the overall economy also declined globally from 58 % to 53% (Figure 8).

Figure 8: Decline in Global labour income share: Corporate sector and Overall Economy

Source: Karabarbounis and Neiman (2015) Figure 1 p.70

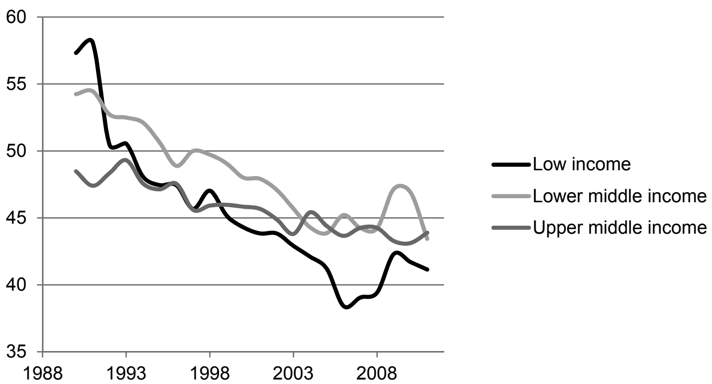
Trapp (2015) used an original way to determine changes in the labour share in developing countries, by collecting social accounting matrices (a research methodology well developed at ISS in the 1970s and 1980s by Rob Vos and others) of a large number of countries to estimate labour income shares in these countries. Her finding confirms the other analyses mentioned above of a downward trend of the labour income share in most developing regions (Figure 9). East Asia and the Pacific is the region that experienced the fastest decrease (on average 14 percentage points since 1990), closely followed by Eastern Europe and Central Asia (both about 11 percentage points), and Latin America and the Caribbean (both about 10 percentage points). A considerable decline also occurred in Sub-Saharan Africa, where labour income shares fell by 6 percentage points between 1990 and 2011. Exceptions to the downward trend are in South Asia, the Middle East, and North Africa, where labour income shares fluctuated, but on average remained stable, (note that labour income shares in these regions actually should have increased, as mentioned earlier, given the positive growth in GDP in these regions).

Figure 9: Labour Income Share by region, 1990-2011
Source: Trapp (2015) Figure 6



Looking at different GDP per capita groups (according to World Bank country classifications) one notices that the negative trend occurs in all income groups. However, it is more pronounced in low-income countries, followed by lower middle-income and upper middle-income countries (Figure 10).

Figure 10: Labour income shares by GDP classification 1990-2011
Source: Trapp (2015) Figure 7

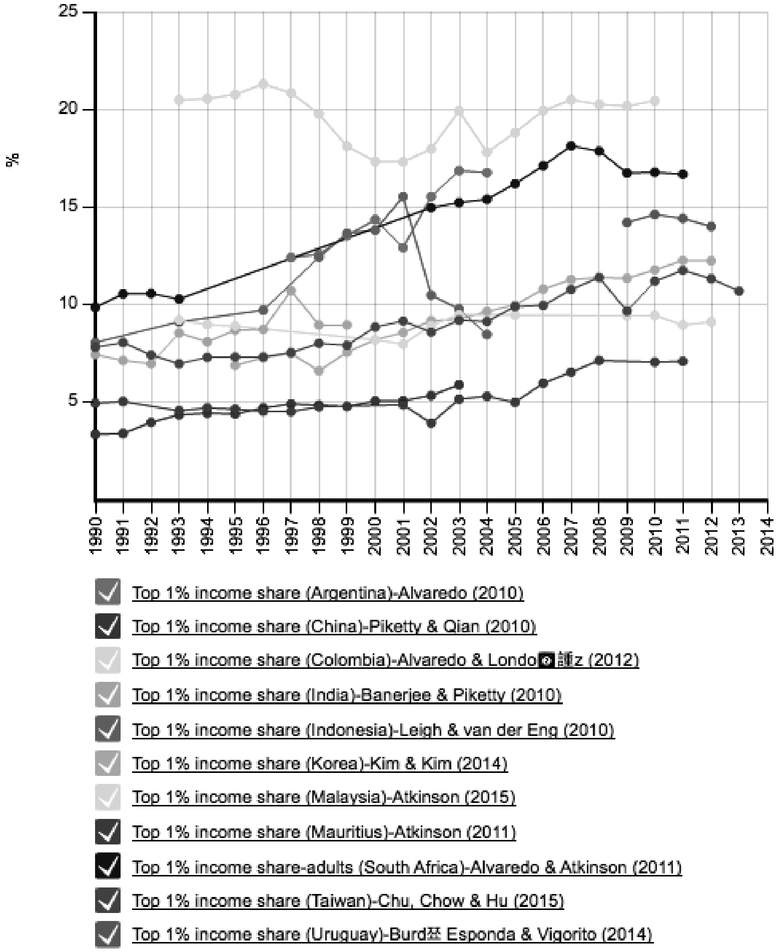


The last two set of analyses range until 2011/2012, i.e. they include and well extend beyond the financial crisis and its immediate aftermath. *It is clear from these analyses, that the decline of the labour share has not halted or been reversed after the financial crisis. And also do not attest to the sometimes-heard thesis that the financial crisis did hit capital owners harder than ordinary workers and their families*. We actually see that the share of the top 1 per cent is increasing in almost al developing countries, a consequence of the declining labourshare and of greater inequality between wages themselves.

Increasing share of top 1% income groups in developing countries

If the labour income of the top 1 per cent of income earners were excluded nation wide, the decline in the labour income share would probably have been even greater than what we observed in Figure 10. This reflects the sharp increase, especially in English-speaking developed countries, of wage and salaries (including bonuses and exercised stock options) of top executives, who now cohabit with capital owners at the top of the income hierarchy (Atkinson, Piketty and Saez, 2011). The proportion of wage earnings in the top segments of household income also increased, to various degrees, in other countries including Japan, the Netherlands, Canada, Italy, Spain and the United Kingdom – though not in Sweden, Finland or Australia (Atkinson, Piketty and Saez, 2011). Data for the share of top incomes in developing countries are much scarcer, but for 11 developing countries, for which data are available, a similar trend as in developed countries can be observed (Figure 11). The share of the 1 per cent top income group in Colombia reaches 20 per cent, a level similar to that in the USA. It is increasing also for all other countries in the sample, except for Indonesia.

Figure 11: The incomes of the top 1 per cent (11 developing countries)
Source: The World Top Income Database. http://topincomes.g-mond.parisschoolofeconomics.eu



Millennium Development Goals and Sustainable Development Goals

Let me now turn to the question of whether the Sustainable Development Goals can stem this growing income inequality. The 17 Sustainable Development Goals (see Annex 2) have been adopted last month at the UN Sustainable Development Summit in New York. These goals come into force as of January 1, 2016 and are the successors of the Millennium Development Goals (MDGs) which were adopted in 1991 and whose target date is the end of 2015.

In order to understand the making of the SDGs, we have to see briefly how the MDGs came about. An enthusiastic group in the secretariat of the UN developed them on the basis of the UN Millennium Summit declaration of 2000[6]. The MDGs reflected the wish of many development practitioners to have, at a global level, clear goals and measurable outcomes of a number of desirable development challenges, without proscribing a fixed sets of policies, as this would have led, in the wake of the dissatisfaction with structural adjustment policies of the 1980s and 1990s, to great controversy and to a rejection of an otherwise generally accepted policy document (Vandemoortele, 2011). However, the absence of a well-founded development theory meant that in practice for most countries development policies remained business as usual, considerably influenced by the Poverty Reduction Strategies, the successor of the Structural Adjustment Policies of the World Bank. As Saith (2006) puts it: *'Poverty reduction is somehow detached from the constraints imposed by structural inequalities and anti-poor and anti-labour policy biases. The answer is held to lie in the simple equation: external assistance + technological fixes + good local governance = poverty reduction'*.

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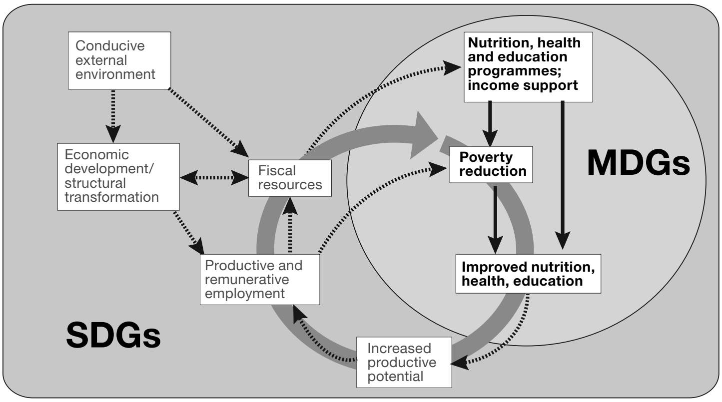
6 These were based on early conceptualization of development goals by the OECD and drew on the Millennium Declaration, accepted by all Heads of State at the Millennium Summit of the UN in September 2000. The Declaration itself has a longer and higher set of aspirations, and should not be confused with the very specific and time-bound set of indicators which comprise the 8 MDGs and 21 targets through which progress towards the MDGs are measured (Melaned, 2012, p.4)

UNCTAD (2014) argues that the MDG approach was essentially a linear one, focusing mainly on human and some environmental development goals and programs, targeted directly at meeting those goals. By focusing on outcome goals, to the exclusion of the means for achieving them, the MDGs encouraged reliance on specific programs aimed at improving the targeted indicators that were mostly financed by Official Development Assistance (ODA). Ensuring sustainability depends, however, critically on reversing vicious circles of development, in which especially many least developed countries find themselves (UNCTAD 2014). Economic development has thus a major role to play in achieving human development goals, and a still more critical role in sustaining advances in human development over the long term. Employment is a critical linkage in this process, especially when it is accompanied by rising labour productivity (Nayyar, 2013a). An economic development process is needed that creates productive and remunerative jobs allowing people to generate the income needed to escape poverty, while also generating the public revenues needed to finance health services and education. This in turn requires an international economic system that supports such development processes. If the post-2015 agenda is to be successful in achieving the adopted SDGs, it needs to encompass all of the elements presented in Figure 12: economic transformation, employment creation, the generation of fiscal resources and a favorable global economic environment, also called structural transformation, a necessary condition for long-term growth of per capita income (Ocampo et al., 2009). Indeed,

> "(i)t is associated with two types of dynamic efficiency, accelerating the growth of productivity, output and employment over time. The first is a Schumpeterian efficiency effect, whereby those sectors with the highest rates of productivity growth and capacity expansion lead the innovation process and drive productivity gains. The second is a Keynesian efficiency effect, whereby the pattern of specialization shifts towards sectors that benefit from faster growth of domestic and external demand, generating positive impacts on output and employment. These two types of efficiency generally go hand in hand, as the more knowledge-intensive sectors also tend to face stronger domestic demand growth in the long run, and tend to be more competitive in international markets" (UNCTAD 2014)

Figure 12: Context of the SDGs
Source: UNCTAD, 2014, Chart 22



UNCTAD (2014) found that in the case of the LDCs overall growth rates closely reflect sectoral changes in employment: economic growth is negatively correlated with the share of agriculture in employment, but positively correlated with the shares of industry and services, a clear case of structural transformation. Moreover, *the LDCs that have experienced the greatest structural transformation are also those that have made the greatest progress towards attaining the MDGs*. Also, economic growth has been much more strongly correlated with MDG performance in countries with above-average structural transformation than those with less structural transformation.

The 2014 LDC report of UNCTAD considered two critical aspects of human development: poverty (MDG 1) and enrolment in primary education (MDG 2). Figure 13 presents the performance of all LDCs relative to target 1A of MDG 1 (halving the poverty headcount ratio at the $1.25-a-day poverty line) against the Structural Transformation Index[7].

7 The Index is thus calculated as the simple arithmetic sum of the direct productivity term measuring gains in aggregate output per worker due to increases in productivity within each sector, and the reallocation term capturing the effects of changes in employment shares between sectors UNTAD, 2014 p.81

It suggests a strong and positive association between structural change and progress in halving poverty: countries that achieved faster transformation performed better in terms of poverty reduction than those where transformation was slower. Asian LDCs such as Bhutan, Cambodia and Nepal, which have experienced rapid transformation of their economic structures over the past two decades, have also been among the highest achievers in reducing poverty A similar result holds for educational attainment: as depicted in Figure14, progress in primary school enrolment appears to be strongly associated with structural transformation. UNCTAD, 2014 finds this pattern generally replicated across other MDG targets, suggesting a significant positive association between structural change and the average progress across all the MDG targets.

Figure 13: Performance of LDCs: Changes in poverty reduction index plotted against changes in progress in structural transformation index

Source: UNCTAD 2014, chart 32

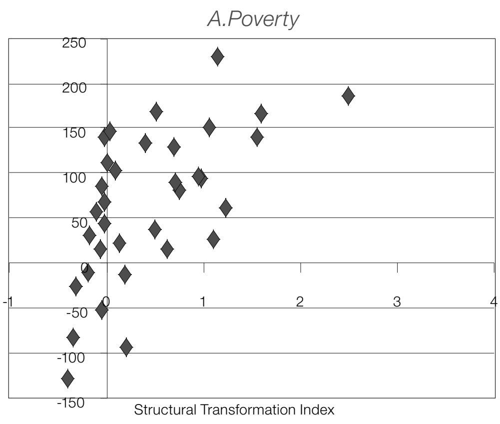
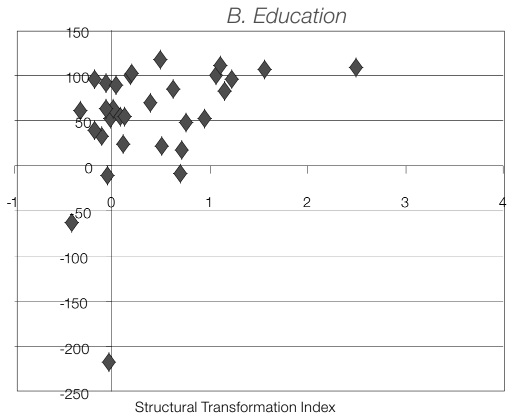


Figure 14: Performance of LDCs: Changes in education index plotted against changes in progress in structural transformation index
Source: UNCTAD 2014, chart 32



So there is ample justification for including goals on transformative economic policies and outcomes. The political climate for doing so has also changed: now that the Bretton Woods institutions are losing their monopoly in development financing (attested by the recent establishments of a BRIC bank and the Asian Infrastructure Investment Bank, see: AIV, 2014) the fear of Northern dictated structural adjustment programs is declining and hence development policies, based on the experience of structural transformation, which some of the successful emerging countries underwent, can lead to an international acceptance of a development agenda which is built around more Southern oriented structuralist development strategies.

Goals on structural transformation and sustainable growth then do become relevant: Firstly, because the MDGs, in which these goals did not figure, did not spur efforts on structural transformation, which they should have, and secondly, because countries that performed better on structural transformation, did also better in achieving the MDG goals.

Hence it is logical that in the preparation of the SDGs more attention was given to issues of sustainable growth and structural transformation. Actually, the list of SDGs reflects much more the principles and aspirations of the Millennium Declaration of 2000, and represents therefore a more integrated approach to development, in which economic, social and ecological concerns are more balanced. They contain, as Mkandawire (2004) formulated, a possible agenda for transformative social policies. If we classify the 17 goals as social, economic, environmental or general (an exercise which is open to multiple interpretations, as some goals can be typified by more than one term) we arrive at 5 social goals, 5 environment goals, 3 economic goals and 4 general goals.[8] This classification does also point to a rather balanced set of goals.

Inequality and Sustainable Development Goals

Various authors (van der Hoeven, 2010, Vandemoortele, 2011, Melaned, 2012) have argued that the MDGs, by emphasizing targets at a global level (and more and more also at national level), have ignored the inequalities that averages conceal. They suggest therefore that attention to inequality is imperative in any formulation of the SDGs and that targets for all SDGs should be broken down for different socioeconomic classes or for different income groups. These argumentations have been strengthened by recent analyses that conclude that greater equality and more equal access to government services will contribute to improved and sustained development in general (Wilkenson and Pickett, 2009). However, for a workable set of SDGs it is not only necessary to make the various impacts on poorer groups more visible and to suggest corrective measures in terms of public and development aid expenditures, but also to analyse and take action on what kind of economic or social processes are causing these enormous (often growing) inequalities.

[8] See annex 2 for all 17 SDGs; 5 Social Goals (SDG 1 ,2, 3, 4, 6), 5 Environmental Goals (SDG 7, 12, 13, 14, 15), 3 Economic Goals (SDG 8, 9 and 10), 4 General Goals (SDG 5, 11, 16, 17)

In the evaluation of the results of the MDGs it became clear that the lack of any reference to inequality was a great oversight in the MDGs. This mistake was exacerbated by the fact that currently most poor people, defined as those living on less than 1.25 a day, do not live any more in low income countries, as Andy Sumner made clear (Sumner, 2012). Various scholars and activist came to conclusion that tackling inequality is actually a greater challenge than tackling poverty. During the preparation of the SDGs, I joined a group of about 90 concerned scholars that in an open letter[9] urged the Secretary of the High-Level Panel of Eminent Persons on the Post 2015 Development Agenda that the SDGs should take inequality on board in all its aspects and adopt as a goal the reduction of the Palma ratio, which indicates how much more the income of the 10 per cent richest is, compared to 40 per cent poorest. As Palma has elaborated in a special issue of *Development and Change* (Palma, 2011) this ratio does not only gives a better picture of inequality, but also can shed light on the specific situation of the middle class. Palma correctly argued that differences in inequality are less an outcome of technical factors and more the result of the political process, where norms and habits determine the degree of inequality and where the attitude of the middle class plays an important role.

Which measures are necessary to stem the growing inequality? To answer this question it is useful to return to Table 2, which distinguishes between exogenous and endogenous drivers of inequality. Exogenous drivers of inequality are shaped by international trade and investment agreements as part of an improved system of global governance, giving developing countries more policy space and allowing them to set in motion a process of structural change. But equally important are the endogenous drivers of inequality.

It is on those endogenous drivers that I want to concentrate now. The literature has shown that domestic policies can have a great effect on inequality (Dagdeviren et al. 2004). Figure 15 gives the degree of redistribution that governments in countries at different levels of GDP per capita did perform. In all income groups there is great variation.

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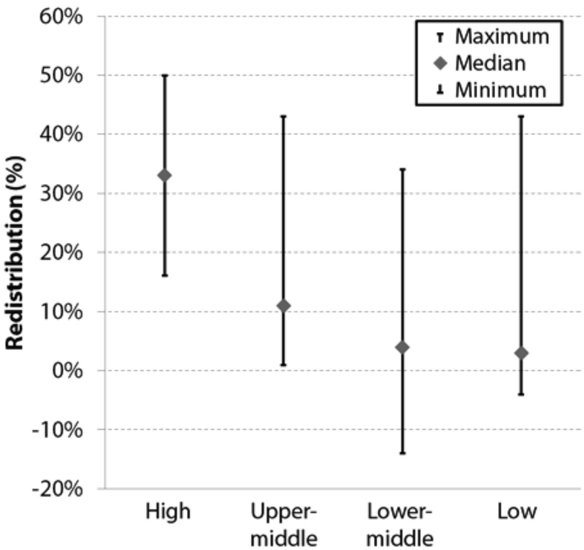
9 http://www.post2015hlp.org/wp-content/uploads/2013/03/Dr-Homi-Kharas.pdf

High income countries are on average better able to reduce primary or market income inequality, but we notice also for all income categories, huge variations in this reduction of primary inequality. National institutions and national policies can play therefore an important in reducing primary or market outcome inequality. Moreover, the degree of inequality reduction from primary to secondary distribution does not seem to be related to the level of initial primary or market outcome inequality.

Figure 15: The degree of redistribution in the late 2000's by GDP per capita group
Source UNDP 2013, Figure 3.13



To what extent do the SDGs take income inequality and redistribution into account? The most direct reference to inequality is in goal 10: reduce inequality within and between countries. However the targets related to domestic (within) inequality are rather weak. The first target states: *By 2030, progressively achieve and sustain the growth of the bottom 40 per cent of* *the population at a rate higher than the national average*, followed by targets calling to promote inclusion, and ensure equal opportunity a.o. by eliminating discriminatory laws. Another target is to adopt policies, especially fiscal, wage and social protection policies and progressively achieve greater equality.

The formulations of these targets reflect the difficulty among the negotiators behind the SDGs to come to clear statements on inequality. *The only time bound target* (rate of income growth of bottom 40 per cent faster than national average) *is rather vague and completely misses the fact that increases in inequality are especially created at the top end of the income scale*. One can only deplore that the modest suggestion to use the Palma ratio, which is sensitive to more than proportionate increases at the top income scale, has not been taking into account in the current SDGs.

The other targets are calling for more policy attention to national inequality. In this respect it might be instructive to see what happened at the recent conference on Financing for Development (FfD), a preparatory conference this July in Addis Ababa setting policies and actions for final adaptation of the SDGs in September. Although the outcome document of the FfD conference, the Addis Ababa Action Agenda, mentions several concerns on growing inequality and urges national governments to increase fiscal resources, that can be used to counteract the growing income inequality stemming from globalization (see also Bourguignon, 2015), it fails to recommend fundamental changes in the International Financial System which could increase the fiscal capacity of developing countries to finance amongst others redistributive policies. Firstly, various developed countries prevented recommendations on changing the current global financial architecture in the Addis Ababa Action Agenda. A change would have led to less volatility in foreign flows and hence less need for developing countries to hold costly foreign reserves to face growing volatility. With less volatility, these foreign reserves could have been used by developing countries for national investment.

Nobel prize laureate Joseph Stiglitz has calculated that the effect of using foreign reserves for domestic investment in developing countries would have been a bigger contribution to the financing of the MDGs than current development aid[10]. Secondly, recommendations to set up an international tax body to stem the illicit outflow of resources from developing countries through tax treaties and transfer pricing etc., which would have greatly increased the fiscal situation in developing countries, were not accepted, as developed countries wanted to keep the discussion and measures on tax issues under the auspices of the OECD, an organisation dominated by western developed countries. Thirdly, sensible proposals to set up a Sovereign Debt Reduction Mechanism, the adoption of which would have avoided unregulated and ad hoc debt rescheduling, were not accepted, putting yet another strain on the fiscal situation in developing countries (AIV, 2014).

So on a first reading one could say that the SDGs and the Addis Ababa Action Agenda, in the way they have been currently formulated, will not be able to stem the growing inequality in the World. However, another issue that came to the fore during the preparation of the SDGs, is the active involvement of civil society. Civil society and some governments have achieved that the SDGs are now embedded in the Human Rights Declaration and in the other international instruments relating to human rights and international law and that a follow-up and review process should be an integral part of the SDGs. Here opportunities still exist. The Statistical Commission of the UN, in consultation with all stakeholders will set in 2016 verifiable indicators towards the targets of the SDGs, while member states are encouraged to develop national strategies, which will be part of a review process coordinated by the High Level Political Forum on Sustainable Development, based on SDG progress reports. These review processes will

[10] 'Developing countries earn at most 1 to 2 per cent in real return on their foreign reserves. They could invest these reserves locally with returns up to 10 to 15 per cent. Assuming a difference of 10 per cent between domestic and foreign returns, the opportunity cost of holding reserves is quite high, well in excess of $300 billion per year – more than 2 per cent of GDP. The total opportunity cost of reserves is roughly equal to the amount of funds needed by developing countries to finance necessary investments to meet the MDGs' (Stiglitz, 2006, p.249)

not only be informed by governments and international agencies, but also by civil society. It is in these processes that I see a continued and future challenge to put issues of inequality at the forefront of development policy. At various passages in the SDGs and in the Addis Ababa Action Agenda many lofty words have been said about reducing inequality. Active involvement of civil society can thus call governments and the UN system to task on growing national and international income inequalities and demand measures which go beyond the formulation of some of the time bound exact targets, but which follow the general language of the SDGs and the Post 2015 development agenda and which could then form the basis of a global social contract (van der Hoeven, 2011, Ghosh, 2015) for an effective development partnership.

It is also here that I look at ISS. On the hand, ISS has great capacity to analyze income and poverty trends and the effects of international and national economic policies, but on the other hand ISS has also great knowledge on how politics, laws and social policies work and how people and disadvantaged groups can make themselves stronger through more effective civic action. The SDGs provide for the ISS a continuing incentive to stay on this multidisciplinary path of solid analysis and of understanding national and international trends and policies, with policy and civic action to stem the growing inequality in the world.

Words of thanks

I come to the end of my lecture, but will not close before expressing my gratitude to all at ISS, with whom I had the pleasure of working. It is first of all a delight to be engaged with eight generations of students, who have shown me again and again how vibrant the world is. I worked with three rectors, Louk Box, Leo de Haan and recently Inge Hutter. They all, in their own way, gave me space at ISS to develop my ideas and to pursue my inklings, something which I very much have appreciated. Also members and ex-members of the board, notable Mohamed Salih, Freek Schiphorst and Wil Hout encouraged and supported me in all kind of matters. I have found a welcome home in the staff groups Work, Employment and Globalization, ably led by Freek Schiphorst and Irene van Staveren, and Economics for Development, where Peter van Bergeijk, Mansoob Murshed and Arjun Bedi made me realize that one is never too old to learn, as did ISS affiliated professors Rob Vos and Nico Schrijver. ISS can also be proud of its nonacademic staff, including all the librarians and ICT people and the secretariat, which helped me in carrying forward the mission of the ISS. In particular I benefitted from collaborating with Linda Johnson, executive secretary of the ISS, Femke van der Vliet, Sandra Nijhof, Jane Pocock, Annette van Geen and Sharmini Bisessar, some of whom helped me literally until the last minute today. I would also like to thank all my colleagues and friends from abroad, some of whom came from far to join this morning's seminar and who are all with us this afternoon. Your cooperation, insights, and friendship mean a lot to me.

However this all pales with the support I got from Marianne, Kees and Jorick. They gave me inspiration, and also their valuable and frank opinion on family and world affairs. It is not always easy with an often-away travelling husband and father. Marianne, Kees and Jorick thank you very much.

It is the tradition that a valedictory lecture in the Netherlands ends with ik heb gezegd. But to me that sound somewhat pedantic. Firstly because, as I sketched above, there are many opinions and mine is only one, and secondly ik heb gezegd sounds so definitive. I certainly will continue to speak my mind in the years to come. So let me end in a more English tradition: *Thank you for joining and for listening to me, I have appreciated that a lot.*

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Annex 1 Millennium Development Goals (MDGs)

1. Eradicate extreme poverty and hunger
2. Achieve universal primary education
3. Promote gender equality and empower women
4. Reduce child mortality
5. Improve maternal health
6. Combat HIV/AIDS, malaria and other diseases
7. Ensure environmental sustainability
8. Develop a global partnership for development

Annex 2 Sustainable Development Goals (SDGs)

1. End poverty in all its forms everywhere
2. End hunger, achieve food security and improve nutrition and promote sustainable agriculture
3. Ensure healthy lives and promote well-being for all at all ages
4. Ensure inclusive and equitable education and promote life-long learning opportunities for all
5. Achieve gender equality and empower women and girls
6. Ensure availability and sustainable management of water and sanitation for all
7. Ensure access to affordable, reliable sustainable and modern energy for all
8. Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all
9. Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation
10. Reduce inequality within and among countries
11. Make cities and human settlements inclusive, safe and sustainable
12. Ensure sustainable consumption and production patterns
13. Take urgent action to combat climate change and its impacts
14. Conserve and sustainably use the oceans, seas and marine resources for sustainable development
15. Protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification and halt land degradation and biodiversity loss
16. Promote peaceful and inclusive societies, provide access to justice for all, and built effective, accountable and inclusive institutions at all levels
17. Strengthen the means of implementation and revitalize the global partnership for sustainable development