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Taking On Adam Smith (and Karl Marx)

By STEVEN ERLANGER APRIL 19, 2014

PARIS — Thomas Piketty turned 18 in 1989, when the Berlin Wall fell, so he was spared the tortured, decades-long French intellectual debate about the virtues and vices of communism. Even more telling, he remembers, was a trip he took with a close friend to Romania in early 1990, after the collapse of the Soviet empire.

"This sort of vaccinated me for life against lazy, anticapitalist rhetoric, because when you see these empty shops, you see these people queuing for nothing in the street," he said, "it became clear to me that we need private property and market institutions, not just for economic efficiency but for personal freedom."

But his disenchantment with communism doesn't mean that Mr. Piketty has turned his back on the intellectual heritage of Karl Marx, who sought to explain the "iron laws" of capitalism. Like Marx, he is fiercely critical of the economic and social inequalities that untrammeled capitalism produces — and, he concludes, will continue to worsen. "I belong to a generation that never had any temptation with the Communist Party; I was too young for that," Mr. Piketty said, in a long interview in his small, airless office here at the Paris School of Economics. "So it's easier in a way to reopen these big issues about capitalism and inequality with a fresh eye, because I was too young for that fight. I don't have to justify myself as being pro-communist or pro-capitalist."

In his new book "Capital in the Twenty-First Century" (Harvard University Press), Mr. Piketty, 42, has written a blockbuster, at least in the world of economics. His book punctures earlier assumptions about the benevolence of advanced capitalism and forecasts sharply increasing inequality of wealth in industrialized countries, with deep and deleterious impact on democratic values of justice and fairness.

Branko Milanovic, a former economist at the World Bank, called it “one of the watershed books in economic thinking.” Paul Krugman, winner of the Nobel in economic science and a columnist for The New York Times, wrote that it “will be the most important economics book of the year — and maybe of the decade.” Remarkably for a book on such a weighty topic, it has already entered The New York Times’s best-seller list.

“Capital in the Twenty-First Century,” with its title echoing Marx’s “Das Kapital,” is meant to be a return to the kind of economic history, of political economy, written by predecessors like Marx and Adam Smith. It is nothing less than a broad effort to understand Western societies and the economic rules that underpin them. And in the process, by debunking the idea that “wealth raises all boats,” Mr. Piketty has thrown down a challenge to democratic governments to deal with an increasing gap between the rich and the poor — the very theme of inequality that recently moved both Pope Francis and President Obama to warn of its consequences.

Mr. Piketty — pronounced pee-ket-ee — grew up in a political home, with left-wing parents who were part of the 1968 demonstrations that turned traditional France upside down. Later, they went off to the Aude, deep in southern France, to raise goats. His parents are not a topic he wants to discuss. More relevant and important, he said, are his generation’s “founding experiences”: the collapse of Communism, the economic degradation of Eastern Europe and the first Gulf War, in 1991.

Those events motivated him to try to understand a world where economic ideas had such bad consequences. As for the Gulf War, it showed him that “governments can do a lot in terms of redistribution of wealth when they want.” The rapid intervention to force Saddam Hussein to unhand Kuwait and its oil was a remarkable show of concerted political will, Mr. Piketty said. “If we are able to send one million troops to Kuwait in a few months to return the oil, presumably we can do something about tax havens.”

Would he want to send troops to Guernsey, the lightly populated tax haven in the English Channel? Mr. Piketty, soft-spoken, barely laughed. “We don’t even have to do that — just simple basic trade policy, trade sanctions, would do the trick right away,” he said.

A top student, Mr. Piketty took a conventional path toward the French elite, being admitted to the rarefied École Normale Supérieure at 18. His doctoral dissertation on the theory of redistribution of wealth, completed at 22, won prizes. He then decamped to teach economics at the Massachusetts Institute of Technology before returning two years later to France, disappointed with the study of economics in America.

"My Ph.D. is mostly about pure economic theory because that was the easiest thing to do, and I was hired at M.I.T. as a young assistant professor doing economic theory," he said. "I was young and successful at doing this, so it was an easy way. But very quickly I realized that there was little serious effort at collecting historical data on income and wealth, so that's what I started doing."

Academic economics is so focused on getting the econometrics and the statistical interpolation technique correct, he said, "you don't really think, you don't dare to ask the big questions." American economists too often narrow the questions they examine to those they can answer, "but sometimes the questions are not that interesting," he said. "Trying to write a real book that could speak to everyone meant I could not choose my questions. I had to take the important issues in a frontal manner — I could not escape."

He hated the insularity of the economics department. So he decided to write large, a book he considers as much history as economics, and one that is constructed to lead the general reader by the hand.

He is also not afraid of literature, finding inspiration in the descriptions of society in the realist novels of Jane Austen and Balzac. Wealth was best achieved in these stories through a clever marriage; everyone knew that inherited land and capital was the only way to live well, since labor alone would not produce sufficient income. He wondered how that assumption had changed.

As he extended his work on France to the United States in collaboration with Emmanuel Saez, a professor of economics at the University of California, Berkeley, he saw that the patterns of the early 20th century — "the top 10 percent of the distribution was full of rental income, dividend income, interest income" — seemed less prevalent from the 1970s through the early 1990s.

"It took me a long time to realize that in effect we were returning slowly in the direction of the previous equilibrium, and that we were part of a long transitory process," he said. When he started working on the issue in the late 1990s, "there was no way this could be understood so clearly — having 20 additional years of data makes a big difference to understanding the postwar period."

His findings, aided by the power of modern computers, are based on centuries of statistics on wealth accumulation and economic growth in advanced industrial countries. They are also rather simply stated: The rate of growth of income from capital is several times larger than the rate of economic growth, meaning a comparatively shrinking share going to income earned from wages, which rarely increase faster than overall economic activity. Inequality surges when population and the economy grow slowly.

The reason that postwar economies looked different — that inequality fell — was historical catastrophe. World War I, the Depression and World War II destroyed huge accumulations of private capital, especially in Europe. What the French call "les trentes glorieuses" — the roughly 30 postwar years of rapid economic growth and shrinking inequality — were a rebound. The American curve, of course, is less sharp, given that the fighting was elsewhere.

A higher than normal rate of population and economic growth helped reduce inequality, along with higher taxes on the wealthy. But the professional and political assumption of the 1950s and 1960s, that inequality would stabilize and diminish on its own, proved to be an illusion. We are now back to a traditional pattern of returns on capital of 4 percent to 5 percent a year and rates of economic growth of around 1.5 percent a year.

So inequality has been quickly gathering pace, aided to some degree by the Reagan and Thatcher doctrines of tax cuts for the wealthy. "Trickle-down economics could have been true," Mr. Piketty said simply. "It just happened to be wrong."

His work is a challenge both to Marxism and laissez-faire economics, which "both count on pure economic forces for harmony or justice to prevail," he said. While Marx presumed that the rate of return on capital, because of the system's contradictions, would fall close to zero, bringing collapse and revolution, Mr. Piketty is saying the opposite. "The rate of return to capital can be bigger than the growth rate forever — this is actually what we've had for most of human history, and there are good reasons to believe we will have it in the future."

In 2012 the top 1 percent of American households collected 22.5 percent of the nation's income, the highest total since 1928. The richest 10 percent of

Americans now take a larger slice of the pie than in 1913, at the close of the Gilded Age, owning more than 70 percent of the nation's wealth. And half of that is owned by the top 1 percent.

Mr. Piketty, father of three daughters — 11, 13 and 16 — is no revolutionary. He is a member of no political party, and says he never served as an economic adviser to any politician. He calls himself a pragmatist, who simply follows the data.

But he accepts that his work is essentially political, and he is highly critical of the huge management salaries now in vogue, saying that "the idea that you need people making 10 million in compensation to work is pure ideology."

Inequality by itself is acceptable, he says, to the extent it spurs individual initiative and wealth-generation that, with the aid of progressive taxation and other measures, helps makes everyone in society better off. "I have no problem with inequality as long as it is in the common interest," he said.

But like the Columbia University economist Joseph E. Stiglitz, he argues that extreme inequality "threatens our democratic institutions." Democracy is not just one citizen, one vote, but a promise of equal opportunity.

"It's very difficult to make a democratic system work when you have such extreme inequality" in income, he said, "and such extreme inequality in terms of political influence and the production of knowledge and information. One of the big lessons of the 20th century is that we don't need 19th-century inequality to grow." But that's just where the capitalist world is heading again, he concludes.

Mr. Saez, his collaborator, said that "Thomas combines great perfectionism with great impatience — he both wants to do things well and do things fast." He added that Mr. Piketty has "incredible intuition for economics."

The last part of the book presents Mr. Piketty's policy ideas. He favors a progressive global tax on real wealth (minus debt), with the proceeds not handed to inefficient governments but redistributed to those with less capital. "We just want a way to share the tax burden that is fair and practical," he said.

Net wealth is a better indicator of ability to pay than income alone, he said. "All I'm proposing is to reduce the property tax on half or three-quarters of the population who have very little wealth," he said.

Published a year ago in French, the book is not without critics, especially of Mr. Piketty's policy prescriptions, which have been called politically naïve. Others point out that some of the increase in capital is because of aging populations and postwar pension plans, which are not necessarily inherited.

More criticism is sure to come, and Mr. Piketty says he welcomes it. “I’m certainly looking forward to the debate.”

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