



# THE BENEFITS OF INCOME INEQUALITY

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## **Abstract**

*In this essay, we maintain that income inequality has positive effects on the economy. This is so because it leads to an increased quality of life, decreases poverty, and maintains the freedom of the individual. For all too many people, even experts who really should know better, reducing income inequality is the best, perhaps, even, the only, way to reduce poverty. We take the diametric opposite position: as Smith (1776) saw so clearly, a necessary and sufficient condition for increasing the “wealth of nations” is via adherence to private property rights, the rule of law, and free enterprise. To say this is a contentious claim would be an understatement of the year. However, the present essay is an attempt to help right the balance in this important debate. All men of good will wish to wrestle poverty to the ground; the main disagreement concerns the appropriate and efficacious means to that end.*

**Keywords:** *Egalitarianism, income inequality, justice, poverty, liberty.*

## **1 INTRODUCTION**

One of the most contentious and prominent topics in the world of political economy today is income inequality. One of its benefits is that members of that society can choose their ways of life. A person who goes his way in this regard does so based on his talents, therefore, distinguishing himself from others. This freedom leads to specialization, the division of labor, more innovation, and increased quality of life for all. There are complaints from the mainstream media and socialist politicians about the 1% and their supposed hoarding of wealth. If a government official forced equality of income

and equal job distribution then there would be less opportunity to get ahead and make one's self a unique individual. Income inequality is beneficial in a free market society because it leads to an increased quality of life, decreases poverty, and maintains the freedom of the individual.

In section II we discuss how well we are all doing, economically, including the poor. The burden of section III is to discuss the popularity of income inequality. Section IV is given over to our thesis: the positive effects of income inequality. In section V we explore the role of economic freedom and maintain that it leads to income and wealth inequality. In section VI we criticize Rawls, who is perhaps the most important egalitarian, philosophically speaking. We conclude in section VII.

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## 2 THE WELL-TO-DO POOR

Americans continue to invest in themselves and material things, and their quality of life continues to grow. Products are easier and cheaper to obtain than ever before.<sup>1</sup> Companies like Amazon can deliver packages in one day. Big technology companies like Apple release a new iPhone every year or so. The only difference that can be seen in the new model is usually only the camera quality. Americans are quick to ditch the old iPhone for the new one because it is trendy. The quality of life in America is high because of the freedom to be an entrepreneur or to specialize. The innovations that are being made because of the specialization of labor are enjoyed by all. But this is all part and parcel of inequality. If we continually had to iron our matters so that equality could be maintained, none of this would be possible. Buchanan (2014) states:

“Among American families in poverty today, 1 in 4 have a freezer. Nearly half have automatic dishwashers. Almost 60 percent have a home computer. About 2 in 3 poor families have a clothes washer and dryer. Eighty percent have cell phones”.

The rich are getting richer; however, that does not mean that the poor are getting poorer. It is quite the opposite.<sup>2</sup>

There is nowhere in American history where the poor were treated better. Steve Jobs, Steve Wozniak, and Ronald Wayne all founded Apple, the company that produces iPhones and other trendy tech gear. Sure, they increased the division of wealth inequality but they “also improved the well-being of tens of millions of people who are less wealthy” (Henderson, 2018). Not only did the founders of Apple invent new and improved technology they also created thousands of

employment slots. Steve Jobs’s net worth was \$7 billion<sup>3</sup> before his death.<sup>4</sup> His wealth was earned from his perseverance in creating something that millions would enjoy.

## 3 THE POPULARITY OF INCOME INEQUALITY

The topic of income inequality has grown in popularity among mainstream media, politicians, and the average American citizens who read about it in newspapers or online. The argument against income inequality increasing the quality of life begins with the idea that no one should hoard all their wealth. Simply put, no one should be that rich. The counterarguments become based not on economics but morals and ethics. Senator Bernie Sanders, a Democratic Presidential Candidate in 2019, told the Bennington Banner, a Vermont newspaper in 1971 that it was “immoral” to be a millionaire and that they represent, “-the interests of corporations and big businesses,” (Chasmar, 2019). This claim “does reveal a real problem, which is the reduced aim of our society from virtue to material abundance,” in the view of Weinberger (2017). However, the average low-income American’s quality of life is better than ever before in American history. All of us, rich and poor, enjoy the products and innovations of those entrepreneurs with the initiative to create something that enriches our daily lives.

## 4 THE POSITIVE EFFECTS OF INCOME INEQUALITY

Income inequality has positive **effects** on the economy as a whole and helps low-income Americans greatly. We are not all equally talented. Each person fashions and establishes their unique contribution. But this necessarily leads to inequality, given human differences.<sup>5</sup>

<sup>1</sup> In saying this we abstract from the temporary economic glitch caused by the Covid 19 and the government’s response to it.

<sup>2</sup> See on this Stossel, 2019; Money Tips, 2018; Mitchell, 2019; Rector, 1990.

<sup>3</sup> Steve Jobs. (2011, September 1). Forbes Magazine Profile.

<sup>4</sup> Every penny he earned from the market from these sales enriched him. But the people with whom he dealt, suppliers, employees, customers, lenders, and landlords, also gained, at least in the ex-ante sense, otherwise, necessarily, they would not have dealt with

him. In other words, in enriching himself, he did precisely the same for all these others. Without him, they would have been poorer. The market is not a zero-sum game. Parker Brothers’ game, “Monopoly” in contrast, is a zero-sum game. When you land on Broadway and stay at the hotel perched on that property, you lose, and the owner of that property gains. In sharp contrast, if you stay a night at a Trump hotel, both parties gain, almost always ex-post, and necessarily ex-ante.

<sup>5</sup> See this claim Block, 1990, 2000, 2014A, 2014B; Buchanan, 2014; Cathey, 2020; Engelhardt,



A free nation allows us to use our abilities most effectively. The more industrious and talented a person is, the more he will excel and reap greater rewards. 'Inequality...is rooted in the biological nature of man,' said James Fenimore Cooper," (Henderson, 2018). The invisible hand, a concept coined by Adam Smith (1776) more than two hundred years ago, allocates resources efficiently; however, that does not mean that they are distributed equally. Many of those who oppose income inequality would like to redistribute wealth; however, social programs like those are costly and weaken the motivation to work hard. Winston Churchill delivered a speech in 1945 to the House of Commons in London and famously said, "The inherent vice of capitalism is the unequal sharing of blessings. The inherent virtue of Socialism is the equal sharing of miseries." If there was no willingness to work to raise yourself higher on the economic ladder, then there would be no improvement in society or innovation. "High inequality provides the incentives to work harder, invest and undertake risks to take advantage of high rates of return" (Mirrlees, 1971). High inequality like that in the United States "fosters aggregate savings, and therefore capital accumulation, because the rich have a lower propensity to consume," (Kaldor, 1956). When the government issues policies to make "the distribution of income more equal, it distorts incentives, alters behavior, and makes the allocation to resources less efficient," (Mankiw, 2015).

When in history has government intervention ever acquired positive results? The most corrupt industries in America are healthcare and education. Yes, when the state throws tons of money in any one narrow direction, bloom occurs; but this does not demonstrate overall benefit. In contrast, in the market, every interaction benefits both parties ex-ante, without exception.

"The top 1 percent of U.S. earners pay nearly 40 percent of U.S. income taxes. The top 10 percent pay 70 percent. The top 50 percent pay more than 97 percent of income taxes. The poor pay nothing," (Buchanan, 2014). The income inequality gap shrinks if one compares consumption instead of income. The gap closes

somewhat since income taxes are disproportionately taken from the most productive. "Tax high incomes or wealth heavily and you will have fewer people trying to make high incomes and get wealthy," (Henderson, 2018). If politicians cared about the Americans living in poverty in the United States they would continue to "cheer for policies that lead to higher economic growth," (Henderson, 2018) instead of continuing to highly tax the rich. Redistribution is not one of these policies.

## 5 ECONOMIC FREEDOM

Economic freedom is what accounts for economic growth (Gwartney, et al, 1996). If every man or woman was the same in his or her abilities and tastes, then there would be no human improvement. As Murray Rothbard demonstrated in 1971:

"If men were like ants, there would be no interest in human freedom. If individual men, like ants, were uniform, interchangeable, and devoid of specific personality traits of their own, then who would care whether they were free or not? Who, indeed, would care if they lived or died? The glory of the human race is the uniqueness of each individual, the fact that every person, though similar in many ways to others, possesses a completely individuated personality of his own."

For there to be any improvement there needs to be a division of labor, which breeds not equality, but inequality. As Smith (1776) wrote, "the division of labor is limited by the extent of the market". For there to be a division of labor men and women that contribute to the economy need to specialize. There can be no specialization without individuality.

"The developed economy makes room for and encourages an enormously greater specialization and flowering of the powers of the individual than can a primitive economy, and the greater the degree of such development, the greater the scope for each individual," (Rothbard, 1971).

Specialization of trade creates new job slots and increases the quality of life for the individual. “Lest we forget, it is the freedom that produces inequality,” (Rothbard, 1970). Without the freedom to improve oneself individuality is gone.

Many mainstream politicians criticize the gap between the rich and the poor. Massachusetts Senator Elizabeth Warren (2019, Dec 16) opposed income inequality. During her run for the 2020 Presidential election, she continuously explained her plan to decrease the income gap in America. Part of her plan states:

“I’ve proposed a two-cent wealth tax on the wealthiest 75,000 families in America. I’ve proposed imposing a 14.8% payroll tax on wages above \$250,000 and a 14.8% tax on investment income for high earners as part of my Social Security expansion plan. I’ve also proposed returning the estate tax thresholds to their levels at the end of the George W. Bush administration and instituting more progressive rates above those thresholds,” (Warren, 2018).

Mainstream and free-market economists do not agree on much; however, they both agree on one thing; Warren’s plan is radical. It would demonize rich Americans. If taxes were raised as high as her plan calls for, the wealthy would leave the country in droves. The once-rich would start earning less. They would save less money, work fewer hours, and there would be a higher risk of tax avoidance (legal) and evasion (illegal). There is a reason that big companies or intelligent people leave countries that have many restrictions on their companies and lifestyles. Ultimately, the inventions or services that are produced by these people are enjoyed by those in other countries.

Warren and her mainstream media politicians and friends miss the essence of the problem when they proffer plans such as this. Income inequality is not the most alarming problem in the United States. The difficulty is the income tax. It is corrupt, to say the least. Bedard (2010) states:

“It damages the economy. Income taxes are levied on work, savings, and investments. In essence, the government grows by taking money from what makes the economy grow.

Such a system retards capital formation, job growth, and a higher savings rate and, as such, stymies economic growth or recovery.”

The income tax undermines the hard work of American men and women. Income inequality that has been birthed by the free market pales into insignificance as a challenge that the United States faces in the present day. The biggest issue is big government and its even bigger hand in the back pocket of the American taxpayer. Many mainstream politicians get away with hurling the term “income inequality” as a charge of unfairness because it aggravates people who support the noxious notion of social justice. This phrase is then flipped on its back and turned into almost the only negative connotation in the media. Income inequality in America increases the quality of life of many Americans and is ultimately beneficial to the free market society.

Income inequality and the fact that not everyone has the same skills is an inevitable characteristic of our species. Nevertheless, beneficial in a free-market society because it leads to an increased quality of life, decreases poverty, and maintains the freedom of the individual (Rothbard, 1974). Not every man or woman is the same. Yes, whoever honed their skills and or has good luck travels up the economic ladder faster than others. The only way to make “people who are unequal in talents equal in rewards is to use government power to dispossess some and favor others,” (Buchanan, 2014). To put it simply, if one’s talents and quality of work were worth \$15 per hour then he would tend to be earning \$15.<sup>6</sup> It is disturbing that many governments and people have fallen for the trick of favoring a restricted market with socialistic tendencies. Governmental intervention always stamps out the individuality of man and specialization (Rothbard, 2014). “The New Leftist admires Che Guevara, Fidel Castro, and Mao Tse-Tung not simply because of their role as revolutionaries and guerrilla leaders, but more because of “their repeated attempts to leap into communism as rapidly as possible” (Rothbard, 2011). Income inequality harbors improvement and always assumes opportunities to improve. If every person was equal, there would be no

<sup>6</sup> In equilibrium, he would be grossing precisely that amount. True, we are never in equilibrium. But the economy is forever moving in that direction.

incentive to work hard and no reason to save money. The United States GDP would fall rapidly and the America that many once knew would cease to exist.

## 6 RAWLS

One of the most famous and powerful arguments on behalf of egalitarianism was penned by Rawls (1971). He argued under the “veil of ignorance” that if people were to choose their role in life in advance, they would want a society if not of absolute equality, then something very close to that. To wit, no one should have any more wealth than the poorest, unless that would improve the economic welfare of the most poverty-stricken. But Nozick (1974) put paid to that argument with his Wilt Chamberlain example. Wilt is willing to show us his skills on the basketball court. We are willing to pay him \$20 to witness the exhibit. There are 1000 of us. We strike a deal. Mr. Chamberlain is now \$20,000 richer than before. We are all out of pocket that \$20.<sup>7</sup> However, inequality has now reared its ugly head. What to do about this horror? Get Wilt to return the money to the rest of us? But then he wouldn't have agreed to the performance in the first place, and our economic welfare plummets. Nozick's brilliant point against Rawls is that any egalitarian scheme faces an overwhelming roadblock. It is incompatible with human freedom. Any plan that obviates “capitalist acts between consenting adults” (Nozick, 1974, p. 163) of this sort is hardly worth serious consideration.

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<sup>7</sup> But we valued the experience more than that amount, so we, too, gained.

Another argument on behalf of stealing money from the rich and giving it to the poor stems from the diminishing marginal utility of money. A rich man's last \$100 bill is the difference between lighting his cigar with it, or not. Whereas, for the poor man, that amount of money spells the difference between a full belly and going to bed hungry. Thus, if we transfer this sum from the former to the latter, there is a gain in utility. But this argument founders on the shoals of interpersonal comparisons of utility. There is no scientific way to compare the enjoyment garnered by these two men from that amount of money. Maybe the wealthy man would invent a cure for a disease with that \$100, and the poor man would just use it to attain an alcoholic stupor. If so, it is difficult to maintain this argument.

## 7 CONCLUSION

Finally, there is the charge of hypocrisy. Many advocates of redistributionism are college professors. They earn an upper-middle-class level of income, and sometimes more. They have fine houses, cars, wristwatches, clothes, money for travel, etc. If they held fast to their supposed principles, they would divest themselves of these luxuries, and enrich the poor with the savings thereby afforded. In contrast, the principles of the free-market supporter are merely to refrain from violating rights (such as robbing the wealthy), and they are quite able to adhere to these.

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