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Stay classy, Piketty

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In the first text of our "Debating Inequalities" series published in partnership with *Public Books*, Erik Olin Wright brings a North American perspective to Thomas Piketty's *Capital in the Twenty-First Century.*

Reviewed: Thomas Piketty, *Capital in the Twenty-First Century*, (translated from the French by Arthur Goldhammer), Cambridge, Mass., Harvard University Press 2014.

At first blush, Thomas Piketty's book, *Capital in the Twenty-First Century*, harkens back to Marx. The title, after all, deliberately invokes Marx's *Capital* and much of the book talks about "capital" and "labor" as the two fundamental elements of the capitalist system. But for all of its nods to Marxism, Piketty's analysis neglects and obscures a crucial fact about class: the long history of exploitation and domination of labor by capital. It is not the case that Piketty is unaware of this history: on page one of his book, he tells the story of the bloody class struggle between miners and owners in Marikana platinum mine in August, 2012, in which thirty-four miners were killed by police. He uses this conflict to announce an overarching question:

> This episode reminds us, if we need reminding, that the question of what share of output should go to wages and share to profits – in others words, how should the income from production be divided between labor and capital? – has always been at the heart of distributional conflict.

He concludes the discussion of this event by writing:

> For those who own nothing but their labor power and who often live in humble conditions (not to say wretched conditions in the case of eighteenth-century peasants or the Marikana miners), it is difficult to accept that the owners of capital – some of whom have inherited at least part of their wealth – are able to appropriate so much of the wealth produced by their labor (p.49).

This is solid class analysis: the income generated in production is divided between antagonistic classes, capital and labor, and the part that goes to capital constitutes the appropriation of wealth produced by the labor of miners. Classes are understood relationally, and these relations involve domination and exploitation systematically connected to production.

But this relational understanding of class largely disappears after the opening of the first chapter.[1] When the term class is used at all, it is treated as simply a convenient way of talking about regions of the distribution of income or wealth – a top, upper, middle, and bottom. The owners of capital receive a "return on capital"; they are not described as exploiting the labor of workers. The distribution of income reflects a division of the national income pie into "shares"; it is not a real transfer from one class to another.

There is much of value in Piketty's empirical research and in his theoretical arguments about the long term trajectory of income and wealth in equality that does not depend on a relational class analysis. But the absence of a sustained class analysis of the social processes in which income is generated and appropriated, which is what I mean by the term "relational class analysis," obscures some of the critical social mechanisms at work. Let me elaborate this point with two examples, one from the analysis of income inequality and one from the analysis of returns to capital.

Income Inequality

One of Piketty's important arguments is that the sharply rising income inequality in the United States since the early 1980s "was largely the result of an unprecedented increase in wage inequality and in particular the emergence of extremely high remunerations at the summit of the wage hierarchy, particularly among top managers of large firms." (p.298). This conclusion depends, in part, on precisely what is considered a "wage" and what is "capital income." Piketty adopts the conventional classification by economists and treats all of the earnings of top managers as "income from labor," regardless of the form the earnings take – whether it is ordinary salary, bonuses, or stock options -- or the specific mechanisms by which the level of earnings is determined.

This is obviously the correct way to classify these elements of earnings for purposes of tax law and the theories of conventional economics in which a CEO is just a well-paid employee. But this way of treating the earnings of CEOs becomes less obvious when we analyze the position of CEO (and other top managers) in terms of relational class processes. As Piketty points out: "top managers by and large have the power to set their own remuneration, in some cases without limit and in many cases without any clear relation to their individual productivity (p.24)." This is especially true for top executives:

> …at the very highest levels salaries are set by the executives themselves or by corporate compensation committees whose members usually earn comparable salaries……It may be excessive to accuse senior executives of having their "hands in the till," but the metaphor is probably more apt than Adam Smith's metaphor of the market's "invisible hand" (p. 331-2).

[1] Occasionally in the book a shadow relational class analysis appears. In one place, for example, Piketty invokes the idea of a *transfer* of income when he writes: "it is important to note the considerable transfer of US national income – on the order of 15 points – from the poorest 90 percent to the richest 10 percent since 1980. […] this internal transfer between social groups….is nearly four times larger than the impressive trade deficit the United States ran in the 2000s." But even here the "transfer" refers to shifts in income from the mass of people to the top, not between relationally interacting social categories. "Transfer" here simply indicates a division of the pie more favorable to the top of the distribution, not the actual appropriation of income from one class of people to another.

Now, what precisely does this diagnosis of CEO and other top executive salaries mean in terms of a relational understanding of class? Class relations are fundamentally power relations. To say that capitalists "own" the means of production and workers "sell" their labor power for a wage is to describe a set of power relations binding together the activities of capitalists and workers.

Among the powers of capitalists in these relations are the power to offer employment at given wages, to issue orders to employees about what work they must do, and to dispose of the profits – the surplus generated by the firm – for alternative purposes. Other powers can be added to this list, but it should already be clear that what we call the capital/labor relation is actually a very complex multidimensional bundle of power relations.

In the modern corporation, many of the powers-of-capital are held by the top executives. This means that they cannot reasonably be described as simply "labor" within the firm, only much better paid. They occupy what I have called contradictory locations within class relations, meaning that relationally they have some, but not all, of powers of capitalists.[2] This has direct implications for how we should think of the super salaries of CEOs: a significant part of the earnings of top managers and executives should be thought of as an allocation by the executives themselves of profits of the firm to the personal accounts of managers rather than a wage in the ordinary sense. They exercise their capitalist-derived power within the class relations of the firm to appropriate part of the corporation's profits for their personal accounts. If this is correct, then a substantial part of their earnings should be thought of as a return on capital, albeit of a different form from dividends derived from ownership of a stock.

The implication for Piketty's overall analysis of the trajectory of income inequality in recent decades is that a significant part of the increase in remuneration going to "super-managers" should be attributed to the capital-share of total income rather than the labor share. This means that you cannot estimate capital shares and labor shares simply by taking at face value the categories of national income accounts. And this claim, if accepted, also calls into question one of Piketty's key conclusions: "…this spectacular increase in inequality largely reflects an unprecedented explosion of very elevated incomes from labor, a veritable separation of the top managers of large firms from the rest of the population" (p.24). To be sure, the explosion of inequality does represent the explosion of very high incomes of top managers, and this certainly does create a "separation of the top managers of large firms from the rest of the population," but this should not be treated as entirely due to increasing inequality in incomes *from labor*.

Returns to Capital

The absence of a relational class analysis is also reflected in the way Piketty combines different kinds of assets into the category "capital" and then talks about "returns" to this heterogeneous aggregate. In particular, he combines residential owner-occupied real estate (homeownership) and capitalist property into the aggregate category "capital." This is a pretty important issue, for homeownership comprises somewhere between about 40 and 60 percent of the value of all capital in the countries for which Piketty provides this breakdown. Combining all income-generating assets into a single category is perfectly reasonable from the point of view of standard economic theory, in which these are simply alternative investments for which a person receives a return. But combining these two kinds of economic processes into a single category

[2] For my approach to these issues see *Classes* (Verso, 1985) and *Class Counts* (Cambridge University Press, 1997).

makes much less sense if we want to identify the social mechanisms through which this return is generated.

Owning a home generates a return to the owner in two ways: as "housing services" which are then valued as a form of imputed rent and as capital gains, if the value of the real estate appreciates over time. In the United States in 2012, about two thirds of the population are home owners, and roughly 30 percent of these own their homes "free and clear" while another 51 percent have positive equity but are still paying off their mortgages.[3]

The social relations in which the economic returns are linked to these patterns of homeownership are completely different from those within capitalist production relations. Of course, there are important social and moral issues linked to homeownership and access to affordable housing, and so inequalities in this form of "capital" matter. But they don't matter for the same reasons that inequalities in capitalist property matter and they don't operate through the same causal processes. As a result, the social struggles that are unleashed by inequality in homeownership on the one hand and by inequality in the ownership of capitalist capital on the other are fundamentally different. And, crucially, the public policies that would help remedy the harms generated by these different kinds of "returns to capital" would also be different: for example, eliminating the tax deduction for interest payments on mortgages for expensive homes, or reducing the tax deductions progressively for high income homeowners would significantly affect the inegalitarian implications of housing-based "returns to capital." Piketty's proposed global tax on capital is a plausible element in a policy designed to respond to the inequalities linked to the global mobility of capital, but this seems to have little relevance to the harms generated by inequality in returns to homeownership.

In sum, Thomas Piketty and his colleagues have produced an extraordinary dataset on income and wealth inequality that includes data on the wealthiest of the wealthy. And by making these data publicly available in such an accessible, user-friendly way they have performed a wonderful service to the academic community.[4] What we still need is a systematically relational class analysis of these data in order to identify the diverse mechanisms generating economic inequality. Because if we are ever to undo the historical and ongoing legacies of capitalist inequality—or even prevent them from further deepening—we have to put class exploitation and domination at the center, not the margins, of the discussion.

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[3] Source: Zillow.com, 10 January 2013.
[4] Much of this dataset is available at *The World Top Incomes Database*