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Considering Thomas Piketty's *Capitalism in the Twenty-First Century*

Essay by Richard Kuisel, Georgetown University

"In my mind this book is as much a work of history as of economics," Thomas Piketty declares (p. 33). But his study is economic history animated by both moral indignation and commitment to political advocacy. It draws "lessons from the past" in order to illuminate the evolution of capital so that informed electorates can take charge of capitalism and make better choices about the future. Despite (or because of) this agenda *Capital in the Twenty-First Century* is of immense value to French historians. Advocacy aside this is a readable, if formidable—in both size and content—historical treatise. Its theory, terminology, and statistics are easily understood. And the economic analysis is flavored with examples drawn from the novels of Balzac and Jane Austen, from movies, and even from television series like *Mad Men.*

The author tends to side with historians and to chide his fellow economists (he once taught economics at MIT) for their scientific pretentions, their pointless theoretical speculation, and their neglect of history when "historical experience remains our principal source of knowledge" about economics (p. 575). He prefers labeling his discipline "political economy," which expresses its political, normative, and moral purpose and links it to other social sciences such as history. Conversely he also chides those historians who are allergic to numbers or dismiss all statistics as mere social constructs. A quantitative understanding of capital over the last three centuries, which demonstrates long term trends and capitalism's basic laws, he contends, is essential to correcting its shortcomings. He bases much of his theory on one such law, the formula $r > g$ or the rate of return on capital is greater than the growth of output and incomes, which he designates as the "central contradiction of capitalism" (p. 571).

Piketty has his critics—they detect flaws in his data, his definitions, his theoretical explanations, his concerns about capital accumulation, his policy prescriptions, and even his provocative language. None of these issues, which have been reviewed by economists and other experts, are my task.[1] I want to address only his historical account.

What can *Capital in the Twenty-First Century* teach French historians? Beaucoup. French history is central because French data such as tax records, compared to that of other nations, is older, more continuous and homogeneous, and its experience is more representative of global trends say than that of the U.S. Thus this study contains a brief history of French taxation. The French have also struggled with the tension between legal and economic inequality longer than others—ever since the French Revolution. Piketty charts the history of capital accumulation in France from 1700 to 2010, narrating

Note: Page number references in this essay refer to the English edition of the book: Thomas Piketty, *Capital in the Twenty-First Century,* trans. Arthur Goldhammer (Cambridge, Mass.: The Belknap Press of Harvard University Press, 2014).

[1] Tyler Cowen, "Why a Global Tax on Wealth Won't End Inequality," *Foreign Affairs* 93 (May-June 2014), 158-164; Lawrence H. Summers, "The Inequality Puzzle", *Democracy: A Journal of Ideas* 33 (Summer, 2014), accessed December 4, 2014, http://www.democracyjournal.org/33/the-inequality-puzzle.php?; Paul Krugman, "Why We're in a New Gilded Age," *New York Review of Books,* May 8, 2014, pp.15-18; Steven Erlanger, "Taking on Adam Smith (and Karl Marx)," *New York Times,* April 19, 2014; John Cassidy, "Is Surging Inequality Endemic to Capitalism," *The New Yorker,* March 31, 2014; anon., "Bigger than Marx," *The Economist,* May 3, 2014, p. 67.

the evolution of its composition and its owners, and demonstrating its innate tendency toward inheritance and inequality. His story begins with the ancien régime when the top decile owned 80 to 90 percent of national wealth. Two hundred years later this stratum possessed the same level of affluence so there was little difference in this respect between the Bourbon Monarchy and the Third Republic.

The peak of inequality in wealth and income came during the Belle Epoque. It was this maldistribution of capital, according to Piketty, that helps us understand the lavish life style and artistic achievements we associate with the era 1900-1910. In these years the top decile owned not only 90 percent of wealth but also 50 percent of national income. Much of their portfolio, now consisting of financial investments, passed from one generation to the next. Income generated by these holdings paid for the literary salons, the patronage of the arts, the fashionable luxuries, and the expenses of writers and artists. For example, the wealth of Marcel Proust's family subsidized his indulgences and his creativity.

Following the First World War, however, shocks to inherited fortunes and income meant the *rentier* class had to "eat into their capital" making their former lifestyle less and less affordable. What ruined capital between 1913 and 1950 was a combination of the physical destruction of world wars, the loss of foreign portfolios, e.g., expropriations like those of the Bolsheviks, low rates of savings, the wreck of stock- and bond-holders during the Depression, the sale of assets at low valuations, and finally policies like those of progressive taxation. These years marked the bottom of Piketty's "U curve" of capital, the valley or the "euthanasia" of capitalists, between two long periods of prosperity (p. 149). Indeed the interwar years ended a century of monetary stability. The purchasing power of a government bond when *Swann's Way* appeared in 1913 was virtually equivalent to one acquired after the Napoleonic Wars. But by 1950 the same bond had lost 99 percent of its value. Historians writing about the political, social, and cultural life of the 1920s, 1930s, and 1940s who try to explain the uprootedness, uneasiness, and uncertainty of the French during these years need to be mindful of how these apprehensions reflected anxieties about wealth.

Piketty helps French historians think both comparatively and over the *longue durée*. He identifies in quantitative terms what was typical and what was unique about France. It was representative in its growth rate of 1 to 1.5 percent during the nineteenth century and in experiencing the U curve of the twentieth century that hollowed out capital. France followed other general trends like the shift in capital's structure from agricultural land and government bonds to real estate, equity, and financial instruments. However, compared to other national histories France was special in several respects. The Age of Empire made the French (along with the British) unusually wealthy. In 1913 French national income was 5 to 6 percent higher than its domestic product because of its exposure to foreign capital. It was atypical in averaging 13 percent annual inflation from 1913 to 1950. And in contrast with the Anglo-Americans, the French relied on inflation to liquidate massive public debt, i.e., in the wake of the French Revolution and two world wars. Moreover in recent decades, unlike the Anglo-Americans, but more like continental Europeans, the French have curtailed rather than tolerated extreme inequality.

A long term perspective such as Piketty's reveals the thirty years following the Second World War as an interruption in the history of capital. France enjoyed a rather exceptional period of catch up after 1945, the celebrated *trente glorieuses* that featured low returns on capital and high growth rates. It rested on the bottom of the U curve and represented a moment when wealth and income became distributed more equitably and a "patrimonial middle class" emerged. But the French of 2014 mistakenly now view these years as an escape from the history of capital accumulation and yearn for their return. According to Piketty nostalgia for this halcyon era is misplaced. By the 1980s growth rates retreated to their historic low levels of around 1 percent, the return on capital resumed its normal pace of 5 percent, the redistribution of wealth and income stalled, and an age of inheritance reemerged. Soon 60 to 65 percent of wealth once again belonged to the top decile.

Piketty's narrative raises at least one major question for French historians. Why did France become more egalitarian between 1910 and 2010? Why did France and the U.S. reverse places over the century so that the extreme inequalities of wealth and income that once characterized the Belle Epoque now describe contemporary America? (The irony is Americans in 1910 were more egalitarian than the French.) He argues the reversal in France can be attributed to changing norms which informed public policy. For example, the Third Republic during the Belle Epoque, according to Piketty, hypocritically justified its rejection of an income tax on the pretext the Republic guaranteed legal equality. By the Fourth Republic, however, new attitudes made former levels of inequality intolerable. He leaves it to others to explain the development of such new norms. How can one account for mid-century policies like the 1945 tax on capital, a minimum wage, nationalizations, income subsidies, pensions, family allowances, indeed the whole panoply of the welfare state that brought a redistribution of income? In more recent years governments of the Left, appalled by the extravagant severance packages of super managers, limited some forms of remuneration such as stock options in the name of fairness and solidarity. And President Hollande wants companies to pay a 75 percent tax on salaries over a million Euros. The French in the last century become less tolerant of inequality posing an explanatory problem for historians: how, when, and why did this happen?

It may seem fastidious to take exception to such a thoroughly researched, theoretically sophisticated, and forcefully argued study, yet some of its historical exposition may be debatable. Questions sometimes arise because of the brevity of explications, often only one or two sentences, and to some unconventional interpretations. Yet even if explanations are cursory, they deserve evaluation.

In his assessments of French public policy the author can be rather inconsistent, even arbitrary. On the one hand Piketty, the historian, stresses the strategic importance of government policies like taxation, subsidies, and spending. Thus in his account the vagaries of setting the level of the minimum wage from the 1950s to the 1980s either narrowed or widened inequality. Or the Popular Front reduced inequality by boosting wages for workers. And his therapy for remedying contemporary inequality is a global progressive tax on capital. He asserts that the history of income depends heavily on political choice and institutional arrangements rather than solely on economic laws. On the other hand Piketty, the economist, invokes economic laws and rules for explanation leading him at times to tilt toward economic determinism. State intervention during the years following the Second World War, he judges, does not deserve much "praise or blame" with respect to promoting growth (p. 98). Postwar France, Germany and Japan would likely have caught up with the British and the Americans "regardless of what policies they had adopted"—to which he amends "I say this with only slight exaggeration." "The most one can say," he concludes, "is that state intervention did no harm" (p. 99). Similarly the liberalization policies pursued by the Anglo-Americans under Margaret Thatcher and Ronald Reagan "neither increased growth nor decreased it" (p. 99). Some historians might disagree and argue that the shape and pace of postwar growth depended heavily on the state's actions. What was rebuilt first, how and when growth accelerated, and who benefited most—all depended on the Fourth Republic's decisions as embodied in its investment programs like the Monnet Plan. State policy determined the pattern of growth. Piketty tries to steer between crediting (or blaming) public policy and invoking economic laws for the evolution of capital : "the importance of capital in the wealthy countries today is primarily due to a slowing of both demographic growth and productivity growth, coupled with political regimes that objectively favor capital " (p. 42). But his specific judgments do not always convey the needed balance.

I would also register slight dissents from his mini-histories of wage divergence/convergence. Describing post-1945 reconstruction in France he observes, "at first no one seemed to care" about the inequality of wages between managers, engineers, and other skilled personnel and workers at the lower ranks of the wage scale. But "things changed suddenly in 1968" (p. 289). My reading of the situation would indicate that workers, trade unions, Communists, and many others both cared about and tried to elevate wages in order to keep up with inflation in the late 1940s and early1950s. The republic adopted, for example, a sliding wage scale adjusted to the cost-of-living in 1952. To no avail. The problem was less a matter of indifference about lagging real wages than it was the political inability of the Left to correct them. And the eruption of workers' discontent in 1968 may have seemed a surprise, but in retrospect tension over wages and working conditions had been longstanding issues which had sparked several major industrial strikes from the early 1960s on.

In a second instance Piketty addresses the question of wage convergence during the two world wars. At issue is explaining why workers at the lower echelon of the wage scale fared better in wartime. Low income workers, he argues, were better protected from inflation, thus elevating their relative position in terms of real wages. He asks why these workers were more generously treated than others, especially in the public sector, and answers, "Because workers share certain perceptions of social justice and norms of fairness, an effort is made to prevent the purchasing power of the least well-off from dropping too sharply, while their better-off comrades are asked to postpone their demands until the war is over" (p. 287). This interpretation seems too high-minded. In 1917 the government imposed a system of wage controls that set the criteria for wage differentials for all war-related industry. It is unlikely the ideal of equity inspired this arrangement, not when public authorities were responding to strikes and trade unions were demanding increases to meet the high cost of living. Wartime bargaining power determined wage levels as much as a sense of fairness. Under the Occupation and Vichy, setting wage scales followed the priorities of German and French authorities who did not privilege equity or burden sharing. In fact several million workers escaped French control and labored for German firms in either France or in Germany.

Is *Capital in the Twenty-First Century* a new edition of *Das Kapital*? Piketty's choice of title is certainly provocative, and one conservative has labeled it "soft Marxism." But the answer to the charge is "No." The French economist rejects what, according to Marx, was the central dynamic of capitalism that returns on capital would diminish to zero bringing about its collapse. Piketty says quite the opposite. He argues that a high rate of return has been the historic norm and that we are heading back in that direction after an interruption in the twentieth century. Moreover, he does not reject capitalism as a system or project an alternative like communism. In fact he defends inequality in so far as it spurs economic initiative. Piketty presents *Das Kapital* as a rather crude attempt at diagnosing capitalism and duns Marx on many counts, such as disregarding the possibility of durable technological progress, randomly applying statistical data, and omitting the remedial power of public authorities. Piketty thinks of himself as a member of the post-Cold War generation who were "vaccinated for life against the conventional but lazy rhetoric of anti-capitalism" (p. 31). Nevertheless, he believes the nineteenth-century German radical was intuitively correct about the self-destructive dynamic of capitalism. Piketty is not a Marxist, but his dark forebodings about the future of capitalism, his moral intensity, and his contentious style are reminiscent of the nineteenth-century socialist.

Piketty attacks many common misconceptions with zest. He manages to mix statistical analysis with the sting of an exposé. He critiques conventional wisdom like the Kuznets curve that supposedly proved capitalism's long term tendency toward shrinking inequality. He demolishes illusions about the alleged evils of taxation and social spending. Many of us, he argues, are also misinformed about the public debt. If European governments are burdened with debt and cannot spend on what they should, e.g. education, Europeans have never been richer. But wealth is so badly distributed that "private wealth rests on public poverty" (p. 567). He also upends the popular notion of entrepreneurial meritocracy. While he acknowledges that the income earned by entrepreneurs is indispensable for economic development and thus legitimate, he also insists there should be limits to their remuneration. There is no evidence, he contends, that the skyrocketing salaries of CEOs have generated higher productivity for their companies. Immense inequalities of wealth are not closely related to entrepreneurial élan and "are of no use in promoting growth" (p. 572). The justification for the fortune of the wealthy as a reward for entrepreneurial labor ignores the elements of "pure luck" and "outright theft" (p. 446). This French economist refuses to worship the Anglo-American idol of entrepreneurship. And he warns extreme concentration of wealth may one day provoke "significant political upheaval" (p. 422).

Piketty's principal challenge is to the illusion that the damage inflicted on capitalism in the twentieth century also transformed it. In many respects the past has returned, even if some aspects of capital, especially on the European continent, have been modified. But the hyper concentration of wealth and income and the importance of inherited wealth belong to the future as well as the past. The enormous fortune of Liliane Bettencourt, the heiress of L'Oréal, is one of his examples. The rate of return on capital has been, and will be, approximately five times greater than earned income. And as growth returns to historic norms, savings grow, capital accumulation accelerates. In short the twenty-first century at the global level will resemble the French Belle Epoque in egregious inequality. Citing Balzac's novel *Père Goriot*, Piketty recalls the advice of Vautrin, the old cynic, to the young, penniless go-getter Rastignac about the surest path to wealth: skip your studies and marry money. Given the return of patrimonial capitalism such advice, one might conclude, may still hold for young people today hungry for their fortune.

Piketty's history was a best seller for months after its publication, and it has stimulated a lively debate in the U.S. about inequality. French history can prosper if it takes a cue from *Capital in the Twenty-First Century*. French historians can simultaneously convey scholarly heft and attract a mass audience if we address important and relevant questions. Our research need not be confined to a small coterie of academic colleagues.

Richard Kuisel
Georgetown University
rfk@georgetown.edu

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