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Review Paper

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SOCIAL DISTORTION EFFECTS IN THE GLOBAL ECONOMY

ЕФЕКТИ СОЦИЈАЛНЕ ДИСТОРЗИЈЕ У ГЛОБАЛНОЈ ЕКОНОМИЈИ

Summary: *The paper presents the dynamics of inequalities in the distribution of wealth between countries at the global level as well as through an analysis of the Gini coefficient in a selected number of countries. Legality, created as a result of globalization and liberalization, has led to divisions in most societies into two narrow groups, ie. „at the top" and "others". There is no more division into three layers of society – i.e. "top, middle and bottom". On the other hand, this trend creates distortions in the economic and in the social field. This is expressed through the principle: 'the more money remains concentrated at the top, the bigger decrease in aggregate demand'. Consequently, total demand in the economy is lower than the supply, and it causes the growth of unemployment, which leads to a decline in consumption and demand. This process creates deflationary pressures and causes fluctuations in foreign exchange markets, creating the crisis. To prevent such a scenario and to recover the global economy, it is necessary to make the intervention and do the redistribution of wealth through fiscal and other economic measures.*

Keywords: *inequality, the Gini coefficient of wealth redistribution, fiscal policy*

JEL classification*: F60, E62*

Резиме: *У раду се презентује динамика неједнакости расподјеле на глобалном нивоу између земаља, као и путем анализе Гини коефицијента у одабраним земљама. Савремени тренд је извјесна законитост настала као резултат глобализације и процеса либерализације, а то је да подјела у све већем броју друштава није више на оне са „врха, средине и дна", него на уску групу на самом врху и "све остале". Са друге стране поменути тренд ствара дисторзије у социјалној области, али и на економском пољу. То је изражено кроз принцип "што више новца остаје концентрисано на врху, то изазива пад агрегатне тражње". Стога, укупна тражња у привреди је мања од њене понуде, а то значи да расте незапосленост, што поново доводи до новог обарања потрошње итд. Поменути процес ствара дефлаторне притиске и изазива флуктуације на девизним тржиштима, што изазива кризе. Да би се такав сценарио спријечио нужно је потребна интервенција редистрибуције богатства кроз фискалне системе, у циљу опоравка глобалне економије.*

Кључне ријечи: *неједнакост, Џини коефицијент, редистрибуција богатства, фискална политика*

ЈЕЛ класификација: *F60, E62*

1. INTRODUCTION

The degree of inequality is expressed by the relevant percentage of the population and the percentage of their income. In graphic terms, this is represented by the Lorenz curve in the square, where the horizontal axis shows the percentage of the population, and the vertical axis percentage of income. Inequality can be expressed by the Gini coefficient, which is equal to the area between the actual curve and the curve of absolute inequality of income equality multiplied by two. The Gini coefficient has a higher value if the inequality of income distribution is higher. (Un)equal distribution across countries varies significantly, depending on the economic and social structures. Economic inequality is most commonly expressed through two key variables - wealth or income. Economic theorists make the distinguishment between these variables, explaining that the first (wealth) represents the size of the state, (stock), while the second has the character of high-quality cash flow (flow).

2. LITERATURE REVIEW

In the early seventies there was a series of papers that indicate the seriousness of the problem of inequality (and the related poverty) in many developing countries, as well as the failures of economic growth to contribute to solving this issue. The article of Fishlow, a "Brazilian Size

Distribution of Income", published in Papers and Proceedings of the American Economic Association 62, issued in May 1972, was investigating the structure of poverty in developing countries, with the example of Brazil in 1960 and the measures undertaken by the Government of Brazil and the results of those measures that were visible in the later period. In the paper of author Bardhan, the discussion on whether economic growth reduces poverty or increases it is developed (Bardhan 1975).

Osberg (Osberg 1984, 9) argues that behind the two aforementioned variables (wealth and income) there is the same concept, the "control over the use of scarce resources of society". Kuznets (Kuznets 1955), on the other hand, showed that the increase in per capita income (i.e., economic growth), after a certain "turning point" leads to a narrowing of disparities among different groups in society. Crucial importance for a new approach to the distribution of income issue, had a study of a group of authors, led by H. Chenery (at that time the chief economist of the World Bank), entitled "Redistribution with Growth", published in 1974, which elaborated the measures to be taken in the area of income redistribution, while supporting economic growth. If less developed countries liberalize trade and tax policy it is to expect that entrepreneurs from developed countries would invest in such countries, expecting better yield on invested capital in the less developed country. This does not have to happen if the investment risk is greater and that is why this mechanism often does not work (known as Lukas's paradox). Rajan (2010) points out that inequality is intensifying financial crisis cycles. Berg and Ostry (2011) prove, that during couple of decades and a large number of countries, equality helps to maintain growth. Many authors through their research (such as Benabola 2000; Bleaney et al. Kneller 2001) point out that some categories of government spending, for example, public investment in infrastructure, spending on health and education, and social security - can be oriented towards pro-growth and pro-equality. Scientist Okun argues that other categories may include detorieration or compromises with other shortcoming.

On the other hand, inequality can affect positively the growth by encouraging innovation and entrepreneurship (Lazear and Rosen 1981); use savings deposits for investment (Kaldor 1957); and perhaps especially relevant for poor countries, allow individuals to accumulate the minimum capital required to start a business and obtain adequate education (Barro 2000). But inequality may be harmful for growth, because it deprives the poor of ability of health preservance and the accumulation of human capital (Perotti 1996; Aghion et al. 1999); it generates political and economic instability that reduces investment (Alesina and Perotti 1996); and hinders social consensus needed to adjust to shocks and maintain growth (Rodrik 1999). The relationship between inequality and growth can be non-linear, as in the theoretical model presented by Benhabib (Benhabib 2003), in which the increase of inequality at a low level gives rise to increasing growth, while at some point in this process there is encouragement of capital renting which reduces growth. Milanović (2000) showed that using direct measures of redistribution supports Meltzer-Richard hypothesis: greater inequality of society "pulls' greater redistribution. Numerous articles that are focused on whether the higher level of income is associated with higher and lower levels of inequality, have reached some sort of consensus that there is no overall net effect (Dollar and Kraay 2002; Dollar Kleinberg and Kraay 2013).

3. REDISTRIBUTION OF GLOBAL WEALTH

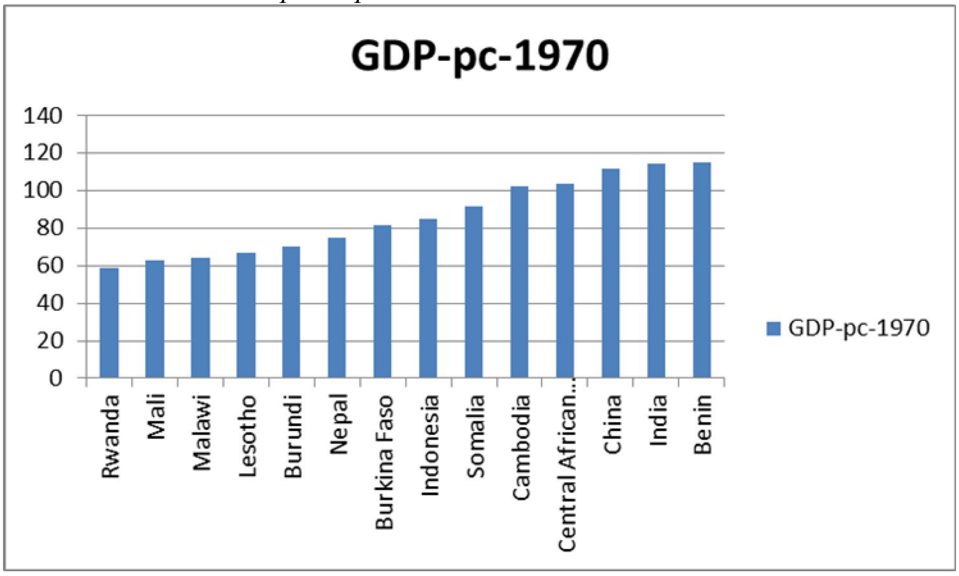
The liberalization of trade relations and free flow of capital should make conditions under which the capital of industrialized countries would be invested in developing countries, leading to industrialization in these countries and by that resulting in income increase. However, capital markets are imperfect - banks and investors give funds only if profitability is visible and risk minimized, which is less and less certain in modern turbulent conditions. Therefore, the investment in the developing country has become risky due to: political factors, climate disturbances or inadequate human resources for the management of investment projects. The result is that an increase in income in developing countries is not adequately anticipated. i.e. it is below expected level of increase.

3.1. Inequalities between countries

From the dawn of civilization and various forms of society there has been a gap between them. However, over the last 50 years the gap between the developed and the developing has reached unexpected proportions. This has largely contributed to the process of globalization and liberalization, through the Washington Consensus and the model of neo-liberalism and market fundamentalism.

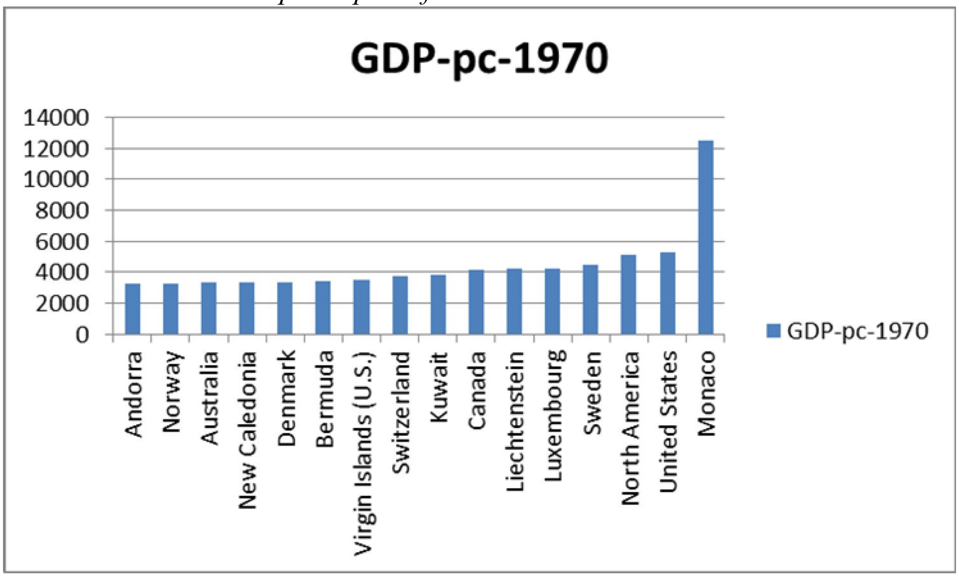
Charts 1 and 2 show a significant disparity between underdeveloped and developed countries recorded in the year 1970. While in developed countries GDP per capita ranged between 60-118 dollars, in developed countries this ratio is between USD 3,000 and 12,000, which represents 50 to 100 times higher income in developed countries.

Chart 1 GDP per capita - last 14 countries on the list in 1970



Source: calculation of authors based on data of the World Bank/indicators

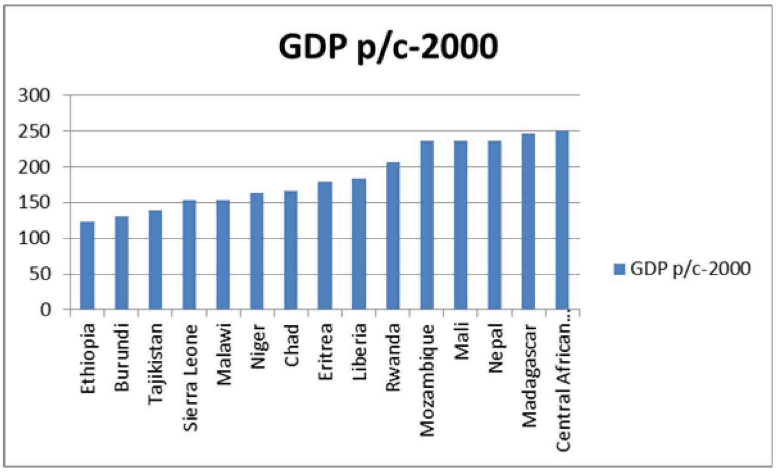
Chart 2 GDP per capita - first 16 countries on the list in 1970



Source: calculation of authors based on data of the World Bank/indicators

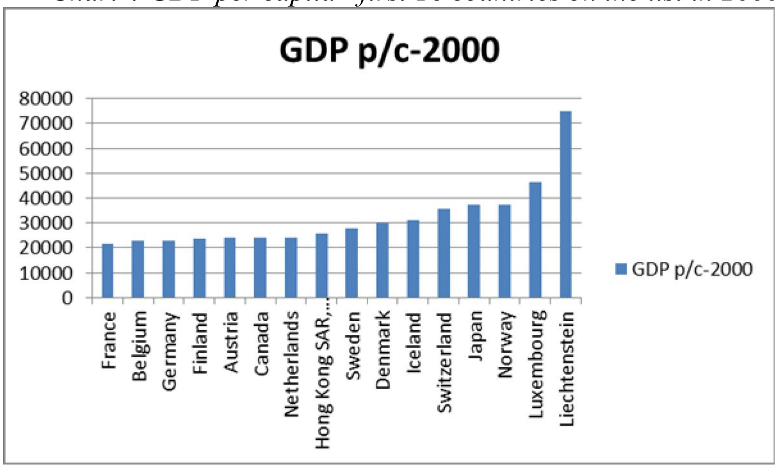
Charts 3 and charter 4 show *per capita* disparity between countries in the year 2000. It is observed that per capita in developing countries ranges from USD 120 to 250, while in developed countries it ranges from USD 20000 to 72000. An increase in developing countries is over 100%, and in developed countries it is over 600%. This suggests that the developed countries are more rapid, which significantly widens the gap.

Chart 3 GDP per capita - last 14 countries on the list in 2000



Source: calculation of authors based on data of the World Bank/indicators

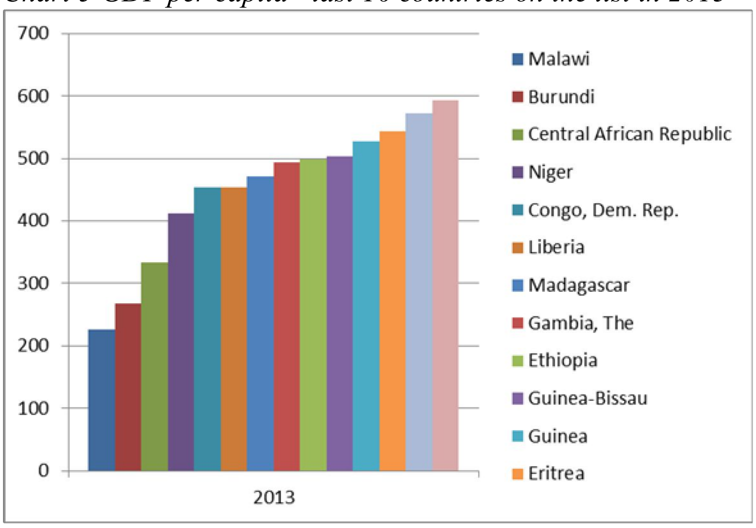
Chart 4 GDP per capita - first 16 countries on the list in 2000



Source: calculation of authors based on data of the World Bank/indicators

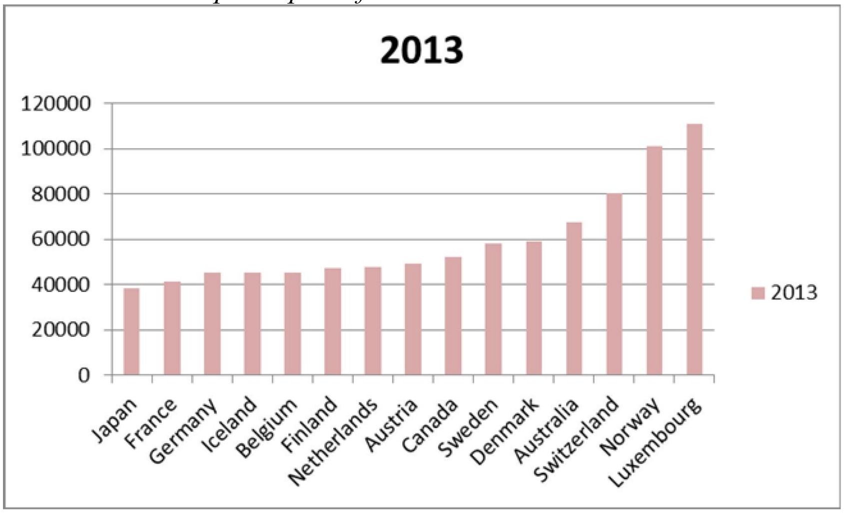
Charts 5 and 6 show the gap between developed and developing countries in 2013. The range in developing countries was USD 220-590, while in developed it was from USD 39,000 to 115,000. The last observed period recorded a decline in growth in favor of the disparities, which is the result of international capital movements and the process of de-industrialization of the developed countries in favor of developing countries, in the interest of higher profits of big and wealthy corporation.

Chart 5 GDP per capita - last 16 countries on the list in 2013



Source: calculation of authors based on data of the World Bank/indicators

Chart 6 GDP per capita - first 16 countries on the list in 2013



Source: calculation of authors based on data of the World Bank/indicators

Table 1 shows the ratio of selected positions on the charts of the best and worst ranked countries according to the criterion of GDP per capita. It is evident that the disparity in all the analyzed categories was highest in 2000 and reduced in 2013, as explained above, the gap is more pronounced in the final ranking positions, with a significant reduction to the oposite positions of the scale.

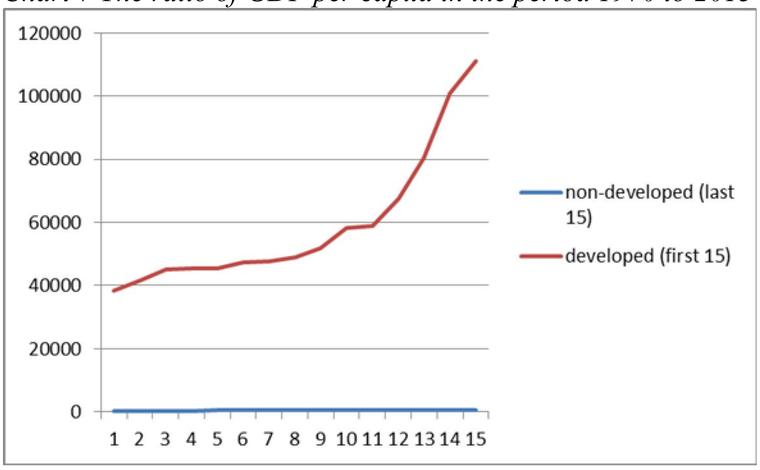
Table 1 The ratio of GDP of leading countries versus last ranked countries

Ratio	1970	2000	2013
Firts country : last country	1 : 213	1 : 612	1 : 491
First 5: last 5	1 : 98	1 : 331	1 : 282
First 15: last 15	1 : 53	1 : 181	1 : 125

Source: calculation of authors based on data of the World Bank/indicators

Chart 7 shows the curve of development of GDP per capita in the period 1970-2013 which shows a huge disparity. It is evident that tere is a huge disparity and pronounced slope of growth in developed countries, and nearly horizontal curve growth in underdeveloped countries. Considering all the previous graphs we can see different structures in both categories of countries during the observed period, with highlighted differences in undeveloped countries, which suggests that some countries have managed to significantly develop during this period and emerge from the group of the least developed (India, Indonesia, etc.).

Chart 7 The ratio of GDP per capita in the period 1970 to 2013



Source: calculation of authors based on data of the World Bank/indicators

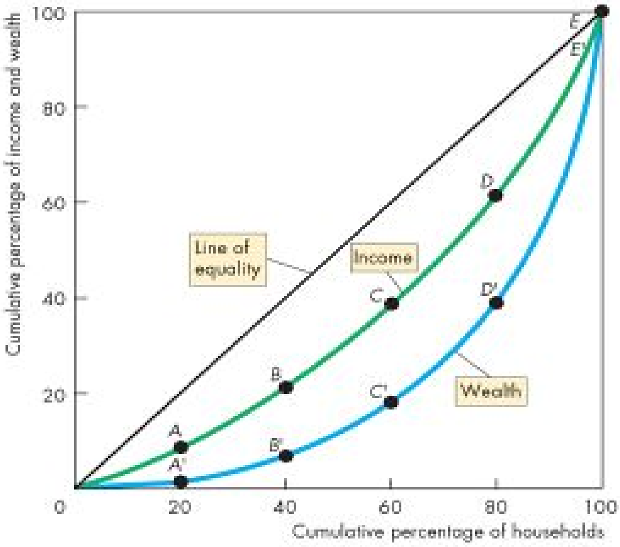
3.2. Gini coefficient

The Gini coefficient is displaying the trend of inequality. It is calculated as the ratio of the area between the line of equality and the Lorenz curve[1] and the entire area below the line of equality:

- in the case of perfect equality (LK is equal to the line of perfect equality) = Gini coefficient is 0
- if one person has all the income (wealth) = Gini coefficient is 1

Figure 1 shows the Lorenz curve of distribution of wealth. It is noted that the Lorenz curve is far from the line of equality, and compatible with the curve of wealth.

Figure 1 Distribution of wealth shown by Lorenz curve



Source : McTaggart et all 2014

The Lorenz curve is a useful tool in the analysis of economic differences, because it vividly expresses the degree of inequality in society. However, due to the limited possibilities to rank income distribution on the basis of Lorenz's criteria, as well as the fact that a number is more precise and concise than pictures, policy makers and researchers give priority to measures that provide a complete ranking of income distribution, because each distribution is awarded the appropriate number. In the literature there are lots of numerical measures of inequality, and the the Gini coefficient is most used as the most popular measure of inequality, which back in 1912 was suggested by the Italian statistician Corrado Gini (after whom it was named Gini, Gini: „Variabilita e mutabilita“, Cuppini, Bologna, 1912). The Gini coefficient is directly derived from the Lorenz curve. The Gini coefficient expresses the ratio between the surface of the Lorenz curve, which closes with the line of equality and the total area of the triangle below that line (Figure 1). The value of the coefficient theoretically ranges from 0 (total equality) to 1 (complete inequality). The Gini coefficient can be expressed in percentages (decimal notation can be easily converted to a percentage - multiplying by 100). Graphic calculating of the Gini coefficient Gini = A / (A + B). It is equal to the surface of A multiplied by 2 (The A + B = 0.5 (because the axis ranges from 0 to 1).

The following formula is applied to calculate the Gini coefficient:

$$G = \frac{1}{2n^2 \overline{y}} \sum_{i=1}^{n} \sum_{j=1}^{n} \left| y_i - y_j \right|, \tag{1}$$

[1] 100 years ago, in June 1905, a short article entitled Methods of Measuring the Concentration of Wealth appeared in the Publications of the American Statistical Association (the forerunner of the Journal of the American Statistical Association), proposing a simple method, subsequently called the Lorenz curve, for visualizing distributions of income or wealth with respect to their inherent “inequality” or “concentration.” Its author, Max Otto Lorenz, was about to complete his PhD dissertation at the University of Wisconsin. This article apparently remained his only publication in a scientific journal, and it made him famous.

where yi and yj are incomes of i-th and j-th individual, y is the average income, and n is a total number of recipients of income. Gini approach to measuring inequality is based on a comparison of each pair of incomes and collecting the absolute values of the measured difference in incomes. Inequality in the distribution of the whole is represented by the sum of inequality of income couples. Since each absolute difference is counted twice | yi - yj | (again as | yi - yj |) the whole expression is divided by 2. In order to obtain an adequate indicator, a sum of absolute income is divided by the square of the number of inhabitants, ie. participants in the distribution and by average income. Equation (1) shows that the Gini coefficient is equal to half of the average relative difference, which is defined as the arithmetic mean of the absolute values of the differences between all pairs of income, compared to the average income.

Table 2 shows the values of the Gini coefficient (in 11 countries with the lowest and highest coefficient) in the period 1970-2013. It can be seen that Gini coefficient is low in the Scandinavian countries, which traditionally have an effective social policy, through the allocation policy and fiscal systems with progressive rates. There are also Slovakia, Hungary, Belarus and Slovenia, which have managed to resist the challenge of transition, in the sense that the process of transition, "as a rule", led to an increase in social inequalities. On the other side is a group of countries with unstable political systems and with the exception of Brazil and Chile they are among the most underdeveloped countries.

Table 2 Gini coefficient for selected countries in the period 1970 to 2013

Country	Gini-min	Gini-max	Gini-average	Country	Gini-min	Gini-max	Gini-average
Denmark	23	27	25	Paraguay	41	58	52
Sweden	23	27	25	Zambia	42	57	52
Finland	22	28	26	Central African Republic	43	61	54
Slovak Republic	19	29	26	Chile	51	57	54
Belgium	25	33	27	Guatemala	51	60	55
Belarus	21	30	27	Honduras	51	59	55
Hungary	21	31	27	Panama	51	59	55
Norway	24	30	27	Colombia	51	59	56
Slovenia	23	31	27	Brazil	53	63	60
Austria	23	31	29	Botswana	54	65	60
Ukraine	23	39	29	Namibia	61	74	66

Source: calculation of authors based on data of the World Bank/indicators

Table 3 shows that all the observed countries in the region have a medium value of the Gini coefficient and that there is no significant social stratification (except in the case of Macedonia in a given period).

Table 3 GINI coefficient of West Balkan countries

Country	Gini-min	Gini-max	Gini-average
Romania	23	30	28
Croatia	23	34	29
Montenegro	28	31	30
Bulgaria	23	36	30
Serbia	28	33	31
B&H	29	34	32
FYRM	28	44	38

Source: calculation of authors based on data of the World Bank/indicators

3.3. The wealth of individuals

Inequality between individuals was reflected throughout the history of civilization, through a particular social group, class, caste and so on. However, after the implementation of the liberalization process and acceptance of the neoliberal concept of the global economy, the gap is rapidly increased, both between countries and between individuals and at the global and national levels. For example, in 1968 the CEO of General Motors had personal income about 66 times more than the average worker in the corporation. Its present executive 'counterpart' in Wallmart earns 900 times the average employee. The wealth of the family of the founder of Wallmart in 2005 was estimated at 90 billion dollars, which is the total of the lowest 40% of the US population, or 120 million people (Sravni 2011, 21). President and Chief Executive Officer of Exxon Mobil Corporation, according to the American Commission for Securities and Exchange for 2007, received income which included a salary in the amount of 1.75 million dollars, 3.36 million bonus, 16 , $ 1 million prize and the right to preferential purchase shares of the company, $ 430,000 in other forms of compensation (among them 229,331 dollars for a personal insurance policy, and 41,122 dollars for the use of company aircraft). 85 richest people in the world have assets of as much as 3.5 billion which is equal to the poorest in the world assets (Oxfam 2015). In the same period of five years between 2003 and 2008 the poverty was reduced at 22% of employees in Germany, while the average salary of board members of 30 companies listed on the Dax, increased by 62% (Sravni 2008).

The table also shows that the number of billionaires in 2014 is 3.5 times bigger than in 2000, and their wealth increased by 6 times, despite significant decline during the crisis years. This emphasized increase of rent on capital and the enormous concentration of the huge property with a small number of individuals. This uneven relationship cost of capital and labor costs, shifts the poverty line, and further impoverishes the group which constantly has been selling their work to owners of capital cheaper and the gap is widening each year more and more.

Table 4 Number of billionaires and their wealth

Year	Number of billion.	Neto amount
2000	470	$898 billion
2001	538	$1.8 trillion
2002	497	$1.5 trillion
2003	476	$1.4 trillion
2004	587	$1.9 trillion
2005	691	$2.2 trillion
2006	793	$2.6 trillion
2007	946	$3.5 trillion
2008	1125	$4.4 trillion
2009	793	$2.4 trillion
2010	1011	$3.6 trillion
2011	1210	$4.5 trillion
2012	1226	$4.6 trillion
2013	1426	$5.4 trillion
2014	1645	$6.4 trillion

Source: Forbes

In 2012, the value of billionaires net equity was approximately the same as the GDP of 145 countries at the bottom of the scale of GDP. (GDP of mentioned countries amounted to USD 5.3 trillion, according to World Bank data Statistics).

4. THE ROLE OF FISCAL SYSTEM

After the Great Depression in 1929-1933, the Keynes' economic model advocates the development of social protection mechanisms. According to Keynes, the government directs the demand by adjusting the fiscal policy and supports economic growth and employment by the progressive taxation model. The model was recognizable by the slogan "tax and spend" meaning that the governments by increasing their costs, further "inject" and increase demand i.e. produces "multiplier effect". It should be noted that poor part of society is gaining from the fiscal redistribution. Needy categories are definitely winners of well-targeted transfers that increase their income. Such transfers are necessary in any society, but there are neither losers at these efforts. Seemingly affected by the redistribution as a major source of tax revenue, the middle class is the recipient of investment in education and health that enables social development, security and social mobility. In the controversy in scientific circles the neoliberals were on one side advocating the concept of "minimum", "neutral" or "entrepreneurial state" which, in greater or lesser extent, challenges the justification for redistributive policies of the state. On the other side are the authors who advocate the development of the concept of "new state/society of security and prosperity", "socially responsible state" or the "social investment state" (Giddens 1999, 16).

However, with the process of globalization and acceptance of non-liberal concept and market fundamentalism, the role of the state in the economy has been radically reduced. This leads to all the above mentioned. In recent years, many countries have abandoned the system of progressive taxation and thus reduced the redistribution of income. Contemporary fiscal systems are increasingly oriented to consumption tax, not income, which 'goes' in favor of capital, and to the "damage" of work. On the other hand, by intensification of the process of de-industrialization and relocation of production in underdeveloped countries, due to lower costs, a large number of countries is facing a budget deficit, leading to external borrowing. On the other hand, according to Stiglitz (2012) when too much money is concentrated at the top of society, the average American begins to spend less, or will cease to consume less in the absence of an artificial incentive to do so. Moving money from the bottom to the top reduces the overall consumption because rich people spend as part of their fortune, less than would be spent by those with lower incomes (if that part of the wealth had been transferred to them). It represents a certain pattern: the more money remains concentrated at the top, the aggregate demand is more in the fall. Unless something else happens through intervention (redistribution of wealth), total demand in the economy will be less than its offer, which means that unemployment will rise, which will then, in a circle, lead to the overthrow of the new spending.

Thomas Piketty (Piketty 2014, 570-573) reviewing the basic causal mechanisms in the light of his empirical findings that the rate of return on capital is higher than the rate of economic growth (r> g) and the consequences of this finding, sees that economic inequality is a barrier to economic growth. In fact, one of his conclusions is that, if nothing is done, the economic inequality inevitably magnified in the future, so it is reasonable to ask the question about prospects of economic growth. The main destabilizing force refers to the fact that the return on equity r can be significantly higher in long periods than the growth rates of revenue and the growth of production volume. Once collected, the capital is reproduced faster than the growth of production volume. Past is devouring the future. The consequences of the long-term dynamics of the distribution of wealth are potentially daunting, especially when you take into account that the yield on capital varies directly with the size of the initial deposit and the divergence of wealth going on globally. Piketty emphasized that in the last three decades, this trend is particularly pronounced, and that the workers' revenues are relatively stagnant or declining, while income from capital grow, particularly in the 1% of wealthiest population. The entire added value goes to the richest, and this leads to high imbalances. Piketty believes that the current tax systems are not effective, because wealthy individuals and companies can easily avoid them moving to another country. That is why he advocates the introduction of taxes at the global level, with a rate of 80% for wealth above EUR 10 million which could not be avoided. It is quite impractical solution.

5. CONCLUSION

Increasing inequality, the unequal distribution of income and high unemployment are the biggest challenges that the world faces today. The process of distribution of income has become inevitable preoccupation of economic theory, and therefore policy makers. In recent decades, an increase in income went to, in the highest percentage, only to a narrow layer of the rich people -at the very top of the pyramid. Significant interest in the academic and the political community in the problem of inequality, has contributed to a number of studies which recorded inequality as one of the key factors of today's global economic crisis. Inequalities arising from unequal starting position in society have a negative impact on overall economic performance. On the other hand, extreme inequality is causing social resentment and generating political instability. In this way, there is a process of strengthening the position of scientists who have been advocating protectionism and anti-globalization. An increasing number of inhabitants of the countries feel they are losers, while a small group of winners becomes richer and this leads to challenging the neoliberal concept through free trade and open markets. Economic inequality leads to unequal conditions of life, endangering the safety of people and producing social problems, which are usually expressed in rising poverty and unemployment.

As a result of global interdependence, there was a political and economic restructuring of the world and the transfer of authority from the national states to supranational authorities. A set of mega-corporations that are associated by the states that manage the economy, often relies on the power of the state to reduce the risk (Chomsky 2006, 112).

Economic inequality is a process that is expressed not only between states, but also within a society. The gap is becoming deeper and such a distortion in the social sphere is reflected through economic instability in the economies of individual countries. Cost of capital and the cost of labor in these circumstances obviously goes in favor of capital and greater wealth has been concentrated in the hands of the rich to increasing extent. The rich do not exist in vacuum. They need a society that works to maintain their position. Societies in which inequality is too large do not function effectively and their economies are neither stable nor sustainable. The evidence provided by history and experience in many parts of the world today, are unequivocal: at some point when inequality has reached unsustainable levels there began spiraling downward - the whole society sliding towards dysfunctionality, and when the company becomes dysfunctional, even the rich pay a high price for such a condition. The modern economic system is the imbalance between the goals of big business and the role of the state. For a stable economy and economically viable state, which would not need external borrowing, except in exceptional cases, it is necessary to regulate the system of income distribution and introduce efficient fiscal systems

New forms of social organization pushed away the nation state as the primary economic and political unit, where the state of relative equality and well-being transformed into the state of competition and inequality. The state (very often) turned from the service of citizens into service to "elite" and individual centers of power. There is no automatic link between inequality and political reaction, but first give impetus to another, especially when inequality is combined with instability, the financial crisis and the recession, which has resulted in a significant rise in unemployment (Top 192) The question is what kind of strategy should be taken to move inequalities and how to set them within limits that are socially tolerant and desirable? What strategy may be applied to achieve economic development and social stability?

Generally, the characteristics of the global economy in the future and national economies will be determined by certain invisible conflict between the interests of capital and interest and action of structures of individual countries. Modern key question whose answer will determine the future of economy is whether to abandon the neoliberal concept due to excessive turbulence of the market (as a result of oversupply relative to demand, ie. excessive concentration and offer of capital) and strengthen the role of the state in order to strengthen income redistribution.

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