The Neosocialist Delusion

foreignaffairs.com/articles/2019-12-10/neosocialist-delusion

Jerry Z. Muller, *Foreign Affairs*, January/February 2020

We are living, so we are told, in a neosocialist moment. From politicians such as the Briton Jeremy Corbyn and the Americans Alexandria Ocasio-Cortez and Bernie Sanders leading the charge, to celebrated academics inveighing against the sins of capitalism, to the hipster chic of the *Jacobin* crowd, a growing movement on the far left is trying to revive and rehabilitate a long-dormant ideological tradition.

The movement's obsession is the pursuit of greater equality, expressed primarily through punitive leveling. Things that contribute to inequality, such as income or profit or wealth, are considered public harms that need to be controlled—by taxes, regulation, and other government policies. The consequences for other priorities, such as sustainable revenue, economic growth, technological innovation, and individual freedoms? Not part of the equation.

Stay informed.

In-depth analysis delivered weekly.

Sign Up

Capitalism has strengths and weaknesses, and critiques of it are familiar—they've circulated widely ever since market-based economic systems started gaining ground in the eighteenth century. The force of those critiques, in fact, has helped fuel repeated reform movements over the ages, which have collectively transformed nineteenth-century laissez faire into the mixed welfare state economies of contemporary advanced industrial democracies.

Many on the left today are fighting for more of the same—continuing to pursue what used to be called "social democracy," using politics to control the private sector's excesses and harness its power for public benefit. That struggle is politically significant but theoretically uninteresting. The arguments for and against social democracy were worked out generations ago and still apply; take your pick.

The neosocialist movement is something different, however. Its roots lie not in social democracy but in democratic socialism, which seeks less to reform capitalism than to end it. And if its policies were ever put into practice, they would lead to disaster.

Rousseau Would have Loved a Wealth Tax

Concerns about the unequal consequences of free markets have a long history. In the mid-eighteenth century, thinkers such as Voltaire and David Hume regarded the spread of commerce as a boon to humanity. In place of poverty, hierarchy, and religious conflict, they argued, markets promoted prosperity, intellectual dynamism, and social peace.

Jean-Jacques Rousseau countered that humans were obsessed with their social status, and since competition for status was a zero-sum game, they were generally miserable. The gains that markets brought were distributed unequally and so increased the differences among people, making them still unhappier. In a commercial society, he claimed, "the privileged few gorge themselves with luxuries, while the starving multitude lack the bare necessities of life."

Adam Smith responded to Rousseau by arguing that under the right conditions, competitive markets could lead to "universal opulence"—by which he meant a respectable standard of living for everybody. That took care of the material problem, the starving multitudes lacking bare necessities. But it didn't get rid of the psychological problem, the anxiety about comparative social status.

The neosocialists seem to care as much about lowering those at the top as raising those at the bottom.

The neosocialists are descended from Rousseau. They downplay poverty and fetishize equality, focus on wealth distribution rather than wealth creation, and seem to care as much about lowering those at the top as raising those at the bottom.

The movement's signature policy proposal is a wealth tax, an annual levy on household assets. Touted by economists such as Thomas Piketty, Emmanuel Saez, and Gabriel Zucman, all associated with the Paris School of Economics, the concept has been embraced by both Sanders and Elizabeth Warren, U.S. senators from Vermont and Massachusetts, respectively, who are running for the Democratic presidential nomination. At first, Warren advocated a two percent tax on households worth more than $50 million and a three percent tax on billionaires. Later, pressed on how she would pay for her proposed universal health insurance, she doubled the billionaire tax to six percent. Sanders's plan starts at taxing $16 million in assets at one percent and tops out at an eight percent tax for assets exceeding $10 billion.

The radicalism of this approach is often underestimated. Many people conflate wealth taxes with higher income taxes or see them as mere extensions of a similar concept. But wealth taxes are fundamentally different instruments with much broader ramifications for economic dynamism and individual liberty.

The main effect of a wealth tax would be to discourage wealthy individuals from holding demonstrable assets. Any individual or household within shouting distance of the threshold would have to get its assets valued annually, imposing costs and creating a permanent jobs program for tax lawyers and accountants, whose chief responsibility would be to figure out ways around the law, including moving assets abroad.

A wealth tax would dramatically curtail private investment. The higher people rise on the economic ladder, the more of their resources go to investment instead of consumption. Those investments, in turn, often fuel innovative, risky ventures, which get funded in the hopes that they will eventually produce still greater gains. A wealth tax would upend the incentive structure for rich people, causing many to stop funding productive economic activity and focus instead on reducing their tax exposure and hiding their assets.

Warren contends that calculating one's wealth tax would be as easy as calculating one's property tax, but that is ridiculous. Take a firm that has a market value but no income—a frequent situation for startups but also common for established firms in various situations, such as a turnaround. Rich investors in such firms would have to sell their shares to pay the wealth tax or force the companies to disburse cash rather than invest in the future. Either way, the tax would discourage investment, reduce innovation, and encourage short-term thinking.

A wealth tax, finally, would force everyone whose assets were near its minimal threshold to give the government a full accounting of all those assets every year: homes, furniture, vehicles, heirlooms, bank accounts, investments and liabilities, and more. The result would be a huge expansion of the reach of government into citizens' lives, a corresponding reduction in citizens' privacy, and the accumulation and storage of vast amounts of highly sensitive data with few safeguards to prevent their misuse.

It is not only successful individuals who draw the neosocialists' ire; it is also successful companies. If a firm grows big enough to become famous, it becomes a potential target of vilification; if it grows too big, it becomes a target for destruction. Sanders, Warren, and Ocasio-Cortez, a Democratic representative from New York, accordingly, have all pledged to break up Amazon, Facebook, and Google.

The wealth tax would discourage investment, reduce innovation, and encourage short-term thinking.

Here they can draw on a venerable antimonopoly tradition in American political culture from the trustbusters on, rooted in the assumption that the further away you move from Smith's ideal of perfect competition among many small firms, the more the public is hurt. The economist Joseph Schumpeter, however, argued that Smith had greatly underestimated both the dynamism of capitalism and the role of entrepreneurs in driving it. Capitalism's manifold benefits didn't just happen; they were created, by a relatively small group of people responsible for introducing new products, services, and business methods. Entrepreneurs sought the big profits associated with temporary monopolies and so were driven to create whole new industries they could dominate.

Large companies, Schumpeter realized, acted as engines of innovation, plowing back some of their profits into research and development and encouraging others to do the same in the hopes of becoming an acquisition target. He would have been delighted with Silicon Valley, viewing technology giants such as Apple, Facebook, Google, and Microsoft as poster children for the enormous benefits to consumers that entrepreneurs generate.

Companies such as Amazon and Walmart, meanwhile, maintain their position through furious competition in service and price, contributing to the virtual elimination of inflation in the American economy. And yet it is precisely these dynamic, successful, customer-oriented companies that the neosocialists want to tax heavily, burden with regulations, and cut up for parts.

THE SKY IS NOT FALLING

What is the cancer that requires such deadly radiation to cure? Supposedly, that median earnings per household in the United States have stagnated for several decades and, for the lower deciles of the income distribution, even declined. The implication is that most people's standard of living has flatlined or dropped over the last two generations. But this is just not true.

The first thing to note is that statistics about income brackets don't map neatly onto individual lives, because the people inside the income brackets keep changing. Those billionaires the neosocialists want to soak are not fourth-generation patrician trust-fund babies but self-made entrepreneurs, and the lower brackets at any time include many young people and recent immigrants, who tend to move up later.

Second, the rich have indeed gotten much richer—at a higher rate than those in the middle, and with those at the bottom improving the least—and inequality has certainly increased. But that does not mean the nonrich haven't improved their condition, too. As a recent study by the economist Bruce Sacerdote concluded, "Meaningful growth in consumption for below median income families has occurred even in a prolonged period of increasing income inequality, increasing consumption inequality and a decreasing share of national income accruing to labor."

Beware the games that can be played with statistics. Households today, for example, are smaller than they were a generation ago, with more people living alone or with a single parent. Even if household income is stagnant, therefore, per capita income may have risen. Then there is the changing age structure of society. As more people live longer, the share of the retired elderly is increasing, and since they have less earnings, this has led to a decline in average household income. Income, moreover, should be understood to include not simply wages and salaries but also benefits. And employers have spent ever more in recent decades on the costliest of benefits, health care—money that should be considered part of earnings. Add government transfer programs, which lower incomes at the top and raise incomes and expenditures at the bottom, and the picture changes again. It is not one of dystopian immiseration.

Capitalism has proved extraordinarily fertile and dynamic in finding ways to improve living standards.

The intellectual heirs of Smith, as opposed to those of Rousseau, are interested less in capping inequality than in raising the standard of living of the population at large—finally achieving that "universal opulence" that Smith so presciently predicted free markets could deliver. Capitalism has proved so extraordinarily fertile and dynamic in finding ways to improve living standards, in fact, that it is difficult to track them.

Schumpeterian creative destruction has changed life in ways that are literally immeasurable. As the economist Russell Roberts has noted, even objects that are nominally the same, such as televisions, have evolved so much as to be incomparable over time. An average American television in 1973 showed half a dozen channels on a screen no larger than 25 inches wide. Today, the screens are larger and better, there are hundreds of channels available, and the unit is less a television than a digital hub. Personal computers used to be science fiction. Then they became ubiquitous. Now they seem to be ancient technology compared with the even more ubiquitous and powerful smartphones that bring the interconnected digital world to anybody, anywhere. Communication today is instantaneous and cheap; shopping is easier and better informed; everybody can watch or listen to what he or she wants, when he or she wants to; and nobody ever gets lost.

At one point in *Monty Python's Life of Brian*, a revolutionary in ancient Jerusalem asks his followers, “What have the Romans ever done for us?” His audience keeps shouting answers, until the speaker finally pleads, “All right, but apart from the sanitation, the medicine, education, wine, public order, irrigation, roads, the fresh water system and public health, what have the Romans ever done for us?” (“Brought peace!” offers a final heckler.)

The neosocialists scorn billionaires and attack Big Tech, asking, “What have Amazon, Apple, Facebook, Google, Microsoft, and the rest ever done for us?” Only made possible all the modern digital wonders we increasingly take for granted. Have Bill Gates, Jeff Bezos, and the other entrepreneurs partially responsible for such blessings profited from their success? Absolutely. But so have the rest of us, and vastly more—in improved lives, to be sure, but even as a result of their companies' supposedly threatening corporate growth, since those companies are mostly owned by us, the broadly dispersed shareholders of their common stock.

TURNING OFF THE ENGINE