The universal basic share and social incentives

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Posted On: 30 Sep 2016

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In the previous article in the series, Debraj Ray proposes a simple amendment of the universal basic income called the universal basic share. In this article, Debraj Ray and Karl Ove Moene (University of Oslo), discuss how the universal basic share combines social considerations of fairness with incentives for the collective good.

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Here is another story for all two-handed economists. On the one hand, the relentless advance of automation; on the other, the endless quest for putting human beings to work on ever more complex and ‘human’ jobs that machines apparently cannot perform: which one will win? Will there always be enough tasks to occupy 7.5 billion people, or will machines inexorably take over, perhaps even in the ultimate task of self-design?

We cannot pretend to answer this question. We do know, however, that the dystopia of a highly unequal economic future is plausible enough that we need to start thinking about income guarantees.

In this context, universal basic income (UBI) is a good idea. Briefly, everyone would have access to a flow of income per month - provided without conditionalities of any kind. One may or may not supplant that flow with additional income-generating work. For instance, starting 2017-18, Finland will trial UBI on a test group - the monthly amounts involved will be on the order of €560 per person, tax free.

In this article, we examine a simple amendment of UBI called the universal basic share, or UBS (see Ray (2016), for a proposal along these lines, and a discussion of antecedents to the idea). Simply put, the UBS is a commitment that is expressed, not as a sum of money, but as a share. Specifically, we propose that we commit a fixed fraction of our GDP (Gross Domestic Product) to the provision of a universal income for all. Thus UBS is country-neutral. It can be introduced into every country, rich or poor. It scales up or down with country-level income. It works equally well in India as in Norway.

UBS also allows everyone to share in the prosperity of a country. To us, this aspect of equity sharing is - in the longer run - the most fundamental feature of the UBS. It creates good incentives for collective cohesion. In this article, we remark on how the UBS combines social considerations of fairness with incentives for the collective good - effects that (non-proportional) UBI schemes do not have.

Some quick numbers
To see how the use of a share cuts across countries, compare a UBS commitment for India and Norway.

Norway has a GDP of NOK 3.15 trillion (US$380 billion) and a population of 5.2 million. Subtracting the
number of children between zero and 17 years, the adult population is just over 4 million. A UBS of 9% of GDP would give each adult person around NOK 70,000 (US$8,500). Raising that number to 12% of GDP would give each adult person around NOK 93,300 (US$11,300). Now, the poverty line in Norway is high: it is 60% of the median income, amounting to NOK 207,400 (US$25,100). A UBS of 9% would give each person one-third of the poverty line, while a UBS of 12% would give each person almost half of this high poverty line.

Meanwhile, 12% of India’s GDP would take us to around the poverty line there. India’s GDP was around US$2.09 trillion in 2015. The monthly poverty line proposed by the 2014 Rangarajan Committee was Rs. 972 (rural) and Rs. 1,407 (urban). With rural population shares accounted for, that is a bit over Rs. 13,000 (US$200) per year per person. Multiply by India’s population of 1.25 billion to estimate that UBI would cost 12% of India’s GDP. As a robustness check, 9% of Indian GDP would buy us around Rs. 10,000 per year, or about US$150.

While we can never compare the absolute numbers, a comparison of shares is not outrageous. It makes sense as a comparison of the relativism of a country’s commitment to basic income. It underscores the fact that UBI need not be a preoccupation of the rich.

The UBS facilitates social cohesion
Think about different ‘domains’ on which a UBI can be indexed: a fixed commitment, a share of government tax revenues, a share of labour earnings, or a share of GDP as we propose here. We claim that fixing UBS as a share of GDP is the best policy from the view of promoting social incentives.

For instance, suppose that all workers (or all citizens) obtain a share of labour earnings as their UBI. Then that share becomes an extra tax on labour income, biasing the choices of inputs in production. Moreover, this would further exacerbate tensions between employers and employees, as the latter would have even more incentive to raise labour income, and the former to suppress such raises. In general, different domains on which a UBI may be conditioned will have varying properties in terms of worker-capitalist solidarity or confrontation. Expressing the commitment as a share of GDP has a particularly neutral feel to it: the same share of profits and of labour earnings go to basic income for all. It is revenue sharing at the macro level that is neutral to the choice of employment and technology. Each citizen and each collective of citizens (workers as well as employers) now have some interest in increasing the nation’s national product.

A more careful analysis of this incentive property requires an analytical model. It is possible that a ‘constrained optimum solution’¹ that maximises social solidarity could be more complex than the one proposed here. At the same time, it is clear that UBS modifies the potential conflicts of interest and incentives relative to those that apply if some receive only wage income and some receive only capital income. With a GDP share, workers’ interests lie not only in increasing their wages, but in increasing profits as well. For instance, everybody gets something back from wage moderation to remain competitive in the world economy.

This common interest built into a system based on fairness is particularly important for organisations based on collective action. Far from replacing such organisations, UBS rewards encompassing organisations such as labour unions and employer associations. Everybody gets an interest in overall economic performance - across firms, sectors and regions - and not only in their own local
performance. Certainly, UBS does not do away with local and special interests, but it increases the opportunity cost of special-interest policies, and makes them less likely to pass.

Norway is a small open economy. It is heavily dependent on competitive performance in the world market. To remain competitive, workers in traded-goods sectors may have to accept wage moderation. With an appropriately calibrated UBS, all citizens - and not only employers - get something back from that wage moderation, as long as it serves to raise the GDP of the country. In the traded goods sector, workers now obtain more secure employment and are in practice remunerated with the UBS-share of the profits that wage moderation generates for their employers.

It is the same with automation and labour-saving technological change. When all citizens get a share of the benefits from new innovations, there are less (though not zero!) conflicts over technological development, because that development has consequences that are less inequitable. With a UBS everybody gets property rights in the robots, and potentially conflictual externalities are reduced.

**The UBS promotes fiscal health**

In the 2012-213 assessment year, a shade under 30 million individuals filed tax returns in India. This is under 3% of the entire population. In addition, the majority of these individuals had a zero balance: the number of actual payers was around 1%. That is a ridiculously low number, but it is not hard to see why. Agricultural income is exempt from taxation, for reasons that escape us and probably escape everyone else as well. And business dealings (including self-employment activities) are overwhelmingly conducted in cash.

With a responsibility to pay out 10–12% of GDP in basic income, this will and must change. Not only will the government be galvanised into expanding the tax base, it will receive immense support from the public and the media in doing so.

**The UBS shares risk**

Like all forms of UBI, a UBS is redistributive as it benefits low income citizens the most. It is also potentially redistributive in a functional sense between labour and capital: labour is less exposed to the consequences of an increasing profit share that so many fear.

But apart from its claim on national wealth, UBS can also have good insurance properties. UBI is a fixed commitment that, once approved, can hang like the sword of Damocles above a government. A breaking of that commitment in bad times could set a dangerous precedent, and not breaking it might mean a loss of fiscal prudence. In contrast, the UBS moves a government’s obligations in proportion to national income, and provides risk-sharing with all the citizens. The enormous advantage, of course, is that UBS permits sharing in the long-run on the upside and it is only to be hoped and expected that the long-run will, indeed, point upwards.

It should be noted that the UBS also transforms part of labour earnings from a source that may vary with both local and aggregate shocks to earnings that are only exposed to aggregate shocks. In most economies the aggregate shocks are small relative to local shocks. As long as most people are risk averse this implicit insurance in the UBS are potentially valuable even for people who in expected terms pay in more in taxes than they receive from the UBS.
The UBS empowers labour
And now, a word on the dreaded incentive effects of basic income. The idea is simple: with a source of basic income always at one’s disposal, people will be reluctant to work. There is, additionally, a comparison to be drawn between UBI and UBS. Specifically, a UBS is more worrisome than a UBI is on this matter of reluctance, when the economy is growing. After all, under a UBS, basic income will keep pace with that growth, leading to even greater reluctance to work. On the flip side, in a declining economy, the incentive to participate will outpace the UBI, which won’t decline with aggregate GDP.

We are going to return to this comparison in a moment, but let’s pause to directly address this whole business of ‘reluctance’. Yes, of course basic income will raise reservation wages, and empower the weaker groups in society. Why shouldn’t it? Are the voluntarily unemployed among the rich any less ‘reluctant’? Perhaps this is a matter of polemics, but we prefer the term ‘empowerment’ to ‘reluctance’. When vulnerable groups become stronger they can demand higher pay and fairer treatment. Indeed, estimates of the effects that welfare spending has on the lowest wages show clear positive effects. The gap between the wages in the ninth decile to the wages in the first decile (before taxes and transfers) declines with an elasticity of 1/3 when welfare benefits are raised (Barth and Moene 2015). These estimates are based on the performance in rich OECD (Organisation for Economic Co-operation and Development) countries. The impact on employment conditions in developing countries is likely to be even stronger, in particular in the informal sector.

Most informal low-paid low-productivity jobs are manned by vulnerable and low-skilled workers with few outside options. They are unable to retaliate, or to speak up against unfair treatment, in fear of the consequences of not having a job. Basic income can prevent some of this. It empowers vulnerable groups and - in the case of UBS - makes them continuously stronger as incomes in the rest of the economy grow. Thus UBS is a form of growth-led empowerment of poor groups - preventing them from being left behind both economically and politically.

This sort of empowerment generates homeostatic properties. When the economy overheats, generating a high growth of GDP, basic income will grow with it via the UBS, causing reservation wages to rise and acting as a stabiliser. The opposite is true when the economy goes down; it will increase labour force participation. We are not claiming that these supply-side effects are strong enough on their own to prevent cycles, but at least they do not exacerbate the amplitude of such cycles, and will likely serve to bring them down.

Finally, free-market wage choices could be inefficiently low in the first place. Suppose that worker effort varies with wages. While employers might choose wages with this consideration in mind, they will still set wages inefficiently low from a social perspective. For the profit-maximising choice of wage that occurs when the greater outlay of wages just balances out the gain from worker effort - employers will not want to pay any higher. But at that point, higher pay continues to generate higher effort and higher production, and this is better for the social surplus even though profits would decline.

With a basic income this sort of inefficiency becomes less likely, as the lowest pay that employer can force workers to accept becomes higher. It would also change the mix of jobs that employers offer. After all, the (private) profitability of bad jobs is high only when workers are weak and other wages are low. Empowering workers via basic income can put an end to this kind of employer dominance, transforming some of the bad jobs into good jobs.
UBS and sustainable development: A race to the top

The United Nations (UN) Sustainable Development Goals (SDGs) emphasise that we should “end poverty in all its forms everywhere” (goal 1), and “reduce inequality within and among countries” (goal 10). The UBS can help on both these fronts. As we have already noted, the level of pay generated by the UBS does not necessarily have to cover the cost of a decent life to begin with. Indeed, this modest entry point is what gives the UBS its political plausibility. But with a fixed share it will get there over time. In this sense, the proposal takes care - at least to some extent - of the debate that we “cannot afford it”.

We know a lot about races to the bottom: environmental damage, regional tax incentives, tariff wars are all well-known Prisoners’ Dilemmas in which equilibrium outcomes involve an excess supply of the ‘bad stuff’. In the face of such dilemmas, international organisations that oversee such matters as global pollution or free trade must constantly strive to provide checks and balances - and credible punishments - that avoid bad equilibria.

It is very different with UBS. Imagine exploiting the unique opportunity afforded by the UN development goals. All countries can be invited to commit a certain share to basic income, say 10% of GDP. If some commit there will be pressure on the others to follow suit. The idea is to convert UBS into a global prestige item (much like nuclear power). The more countries that join, the more costly it may become to stay outside. Affordability becomes less of an excuse. So does international competitiveness: effectively, countries can coordinate on raising labour costs via the UBS, and the arguments for sticking with stingy labour laws on the grounds of competition have less merit. Even Switzerland may want to revisit its recent negative decision once the proposal is differently framed as a UBS and as more countries join.

The UBS pays a social dividend

A good development path entails constant attention to the distribution between vulnerable and powerful groups, and it seeks the ongoing empowerment of vulnerable groups. UBS provides both. Slogans like ‘development first, redistribution later’, are based on promises that seldom are fulfilled. Because economic growth is an unending process, such slogans are notoriously prone to time-inconsistency. After all, the redistribution can always come later, preferably as late as possible.

A second reason for time-inconsistency in redistributive promises is that the tolerance for a particular level of inequality today affects the political ability to redistribute in the future. It is no secret that economic development creates economic interests that work to sustain the emerging distribution via the political process. Thus high inequality generates low support for redistributive policies. Postponing redistribution could imply eliminating it altogether.

If we are right that basic incomes have clear social gains for society in the form of empowerment and higher productivity, it must be important to start early. Postponement just means that the potential gains are wasted, that people are deprived of the benefits they could have had. A head start on UBS is therefore economically and politically advantageous. It can reap the benefits of empowerment and of higher productivity for a longer period. In addition, it can prevent those who have improved their income status from obtaining high political power and a low willingness to help others for the collective good of the great majority. The same UBS across countries, both rich and poor may work well both in Norway and India as it represents a common share, but of two different pies.
That is why no country needs to be rich before introducing UBS — but they may become rich by introducing it.

Notes:
1. This refers to the solution obtained upon optimizing (maximising/minimising) an objective function (example, utility function or cost function) with respect to some variables in the presence of constraints on those variables.
2. This refers to the tendency to maintain a condition of balance or equilibrium even in the face of external changes.

Further Reading