

## WHAT STIGLITZ AND STOCKMAN HAVE IN COMMON

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The role of government in the economy has been a major public policy issue for more than two centuries. Critics of capitalism, at least since Karl Marx, have argued that the system is skewed to benefit the political and economic elite at the expense of the masses: the proletariat over the bourgeoisie, as Marx put it, or the 1 percent over the 99 percent, as the Occupy Movement that began in 2011 put it. Two recent books have looked at these issues, one from the vantage point of the political left and the other from the political right. Joseph Stiglitz, a Nobel laureate economist and frequent commentator on the political left, discusses the way the system is skewed to support the 1 percent over the 99 percent in his book *The Price of Inequality* (2012), while conservative writer and former Michigan congressman and budget director in the Reagan administration David Stockman addresses these same issues from the political right in *The Great Deformation* (2013). Considering their political leanings, it is worth emphasizing how much their books have in common when describing the causes of the major economic and political problems they perceive in the United States.

Both Stiglitz and Stockman argue that corruption of the U.S. political system is damaging both the economic system and democracy. This article documents the commonality of ideas in their two books

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while recognizing the significant differences in their policy recommendations.

## Views on Crony Capitalism, Rent Seeking, the Fed, and Democracy

In Chapter 1 Stiglitz outlines the problem he sees, which, as the title suggests, is inequality, and he offers some data to back up his claims.<sup>1</sup> Chapter 2, titled “Rent Seeking and the Making of an Unequal Society,” places much of the blame for inequality on government policy. Stiglitz (2012: 39–40) argues: “We have a political system that gives inordinate power to those at the top, and they have used that power not only to limit the extent of redistribution but also to shape the rules of the game in their favor.” Stockman (2013: 169) agrees, saying that public policies to try to regulate the market “fail to recognize that the state bears an inherent flaw that dwarfs the imperfections purported to afflict the free market; namely, that policies undertaken in the name of the public good inexorably become captured by special interests and crony capitalists who appropriate resources from society’s commons for their own private ends.”

Discussing the lawyers and accountants hired by the elite, Stiglitz (p. 53) says, “They help write the complex tax laws in which loopholes are put, so their clients can avoid taxes, and they then design the complex deals to take advantage of these loopholes.”<sup>2</sup> Regarding the market power that the elite use to enhance its income, Stiglitz (p. 54) writes, “The simplest way to a sustainable monopoly is getting the government to give you one.” Stockman (p. 181) says, “Like in all instances of crony capitalism, economic outcomes are as much a gift of the state as they are the fruits of capitalist virtue.” Stiglitz (p. 40) agrees, saying capitalists write the rules in their favor “to extract from the public what can only be called large ‘gifts.’”

<sup>1</sup>Piketty’s (2014) best-selling book emphasizes inequality also, but the big difference between Stiglitz’s analysis and Piketty’s is that while Stiglitz argues that government policy is the major cause, Piketty argues that growing inequality is an inherent characteristic of capitalism. A review of additional literature below suggests that Stiglitz’s view is more widely held, at least among U.S. economists.

<sup>2</sup>A more pessimistic view of this type of activity is presented by Schweizer (2013: 4), who states, “Hiring a lobbyist aligned with a powerful politician is more important than hiring a lobbyist with a certain expertise or experience. Hiring a former staff member or family member is better still. It’s the favor that matters.”

Stiglitz (p. 59) argues that the rules are being written by the 1 percent for their benefit. “It’s one thing to win a ‘fair’ game. It’s quite another to be able to write the rules of the game—and to write them in ways that enhance one’s prospects of winning. And it’s even worse if you can choose your own referees.” Discussing government regulation in various sectors of the economy, Stiglitz contends, “The problem is that leaders in these sectors use their political influence to get people appointed to the regulatory agencies who are sympathetic to their perspectives.”<sup>3</sup>

Stiglitz (p. 62) says, “It doesn’t have to be this way, but powerful interests ensure that it is.” Stockman (p. 560) agrees, saying, “We have a rigged system—a regime of crony capitalism—where the tax code heavily favors debt and capital gains, and the central bank purposefully enables rampant speculation by propping up the price of financial assets and battering down the cost of leveraged finance.” Stockman’s (p. 606) dismal view is that “In truth, the historic boundary between the free market and the state has been eradicated, and therefore anything that can be peddled by crony capitalists . . . is fair game.”

Stiglitz (pp. 104–5) argues that “When one interest group holds too much power, it succeeds in getting policies that benefit itself, rather than policies that would benefit society as a whole. When the wealthiest use their political power to benefit excessively the corporations they control, much-needed revenues are diverted into the pockets of a few instead of benefiting society at large.” Why does this happen? Stiglitz tells us that interest groups hold too much power and use it to get policies that benefit the wealthiest.

Echoing Stiglitz’s message, Stockman (p. 672) says our government “is no longer a system of democratic choice and governance: it is a tyranny of incumbency and money politics.” He argues (p. 692) that “the gangs of crony capitalism will fight tooth and nail to preserve their slice of an imperiled pie, thereby disenfranchising even further ordinary taxpayers and citizens who have no voice in the Washington policy auctions.”

In Chapter 9, titled “A Macroeconomic Policy and a Central Bank By and For the 1 Percent,” Stiglitz finds fault with the Federal Reserve for monetary policies that subsidized banks and boosted the

<sup>3</sup>Economists will recognize that Stiglitz is referring to Stigler’s (1971) capture theory of regulation.

stock market, aiding the elite at the expense of the masses. He criticizes the bank bailouts, saying (pp. 307, 309), “More broadly, the bailout strategy put the interests of the banks (and especially the large banks) and bankers ahead of the rest of our economy. . . . The big banks can thus prosper not because they are more efficient or provide better service but because they are in effect subsidized by the taxpayers.” Stockman (p. 22) discussing the bailouts during the financial crisis, offers a similar message: “The Washington bailouts rescued the perpetrators, not the victims.”

Stockman (pp. 658–59) agrees with Stiglitz on Fed policy:

The Bernanke Fed has showered speculators with windfalls again and again in the various risk asset classes, yet the problem is not merely the unfairness of these massive unearned rents and the resulting further skew of societal wealth to the top 1 percent. In truth, the Fed’s radical financial repression policies cause vast economic deformations, even as they generate gratuitous upward redistributions of the wealth. . . . Never before had so much cash been hauled home by speculators—literally hundreds of billions—for so little value added.

Chapter 5 is titled “A Democracy in Peril.” Stiglitz (pp. 148–49) argues:

Politics is the battleground for fights over how we divide the nation’s economic pie. It is a battleground that the 1 percent have been winning. . . . In earlier chapters we saw how markets are shaped by politics: politics determines the rules of the economic game, and the playing field is slanted in favor of the 1 percent. At least part of the reason is that the rules of the political game, too, are shaped by the 1 percent.

Stockman (p. 52) agrees: “Trying to improve capitalism, modern economic policy has thus fatally overloaded the state with missions and mandates far beyond its capacity to fulfill. The result is crony capitalism—a freakish deformation that fatally corrupts free markets and democracy.”

Stiglitz (p. 225) thinks Warren Buffett was correct when he stated: “There has been class warfare going on for the last 20 years and my class has won.” In Stiglitz’s opinion (p. 102), rising inequality, to a large extent, “is the result of government policies.”

Stockman is not optimistic that the increasing cronyism he sees can be reversed. One might think that the Republican Party would be the political party that could reverse the trends he sees, but Stockman (p. 551) emphasizes that “there is no conservative party left in America—at least not one that is willing or able to defend sound money, free markets, and fiscal rectitude. So the drift into the crony capitalist end game will now accelerate, suffocating what remains of free market prosperity and honest political democracy.” Agreeing with Stiglitz’s message in Chapter 5, “A Democracy in Peril,” Stockman (p. 614) concludes;

A government which is responsible for every bob and weave of the entire national economy will quickly succumb to pure crony capitalism, a regime which cannot avoid eventual fiscal insolvency and the destruction of any semblance of a free market economy. . . . Most importantly, it means a fatal corruption of political democracy.

In sum, Stiglitz and Stockman see a system of cronyism, where government policies are designed by the economic and political elite to benefit themselves at the expense of the masses. Both use the language of the Occupy Movement to describe how the 1 percent rigs the system to increase their power and wealth. And both show how crony capitalism, rent seeking, and Fed bailouts have damaged the market economy and democratic government.

### Other Critics of Cronyism and Special Interest Politics

Stiglitz and Stockman offer good examples of the similarity in the way the left and right perceive the causes of problems that face the economic and political systems, but a substantial literature shows that they are not unique in describing a political and economic system characterized by cronyism and skewed to promote the interests of the political and economic elite. Holcombe and Castillo (2013) look at cronyism outside the United States dating back to the early 20th century, and Holcombe (2013) discusses a strong foundation for this line of reasoning in the economics literature.

Gabriel Kolko, a left-leaning historian, sees government as an organization that provides regulatory advantages to the economic elite. He discusses this in the content of Progressive Era policies that

are often viewed as favoring the general public over moneyed interests (Kolko 1977).

Peter Schweizer (2013) discusses in detail the negative effects of cronyism, but differs from Stiglitz and Stockman by arguing that the special interest political activity that often appears as bribery—interest groups bribing legislatures for favorable outcomes—is more accurately described as extortion. In this respect, he follows the lead of McChesney (1987, 1997): Legislators threaten businesses and other interests with harmful legislation, or threaten to hold up legislation they desire, until those interests make payments to the politicians. Still, Schweizer describes a system of cronyism that works for the benefit of the elite but imposes costs on the masses.

John Allison (2013), like Stockman, is a strong supporter of free markets and sees the Fed as a major contributor to the 2008 financial crisis, along with various government policies like deposit insurance and the taxpayer subsidy inherent in Fannie Mae and Freddie Mac as government sponsored enterprises. While he focuses more narrowly on the financial crisis, Allison sees the problems with intervention in a manner similar to Stockman.

While Schweizer and Allison write from the vantage point of the political right—or, more accurately, from a libertarian perspective—there is a substantial literature on the political left making similar points about cronyism. Larry Bartels (2008) calls the political privilege the elite enjoy at the expense of the masses the “New Gilded Age,” noting how the political process is skewed to benefit the 1 percent. Hacker and Pierson (2010) and Gilens (2012) argue along with Stiglitz that the growing privilege of the 1 percent is not due to market forces but to the political power of those at the top. Finally, Gilens and Page (forthcoming) offer a persuasive empirical analysis which concludes that government policy conforms to the preferences of the elites, and goes in the direction average citizens prefer only when their preferences correspond with those of the elites.

## Different Policy Recommendations

As far as specific solutions to the problems they perceive, both Stiglitz and Stockman come up with a list of desirable reforms. Their lists are different because Stiglitz sees inequality as the major problem while Stockman sees the major problem as the undermining of a free-market economy. Overall, Stiglitz calls for more

government oversight and involvement in the economy while Stockman calls for less.

Stiglitz lists more than 20 policy reforms he recommends to address the problems he and Stockman agree plague the economic and political system. His recommendations are not specific policies but rather policy goals. For example, under the heading of “curbing the financial sector,” he offers six reforms designed to curb excessive risk taking, make banks more transparent, increase the competitiveness of banks and credit card companies, make it more difficult for banks to engage in predatory lending, curb bonuses that encourage excessive risk taking, and close down offshore banking centers. Yet, Stiglitz does not offer any specific policies that would achieve those ends.

Stiglitz wants stronger competition laws, better corporate governance, an end to government giveaways and corporate welfare, a more progressive tax system, a more effective estate tax, better access to education, universal health care, and stronger social protection programs. Again, he does not recommend specific policies, but rather provides a list of what he views as desirable policy outcomes. Those outcomes are left-leaning: They would produce higher taxes, more government spending, and more government oversight of the economy.

The inconsistency between Stiglitz’s diagnosis of the problem and his recommended reforms is that he believes the problems are caused by government policy, yet he recommends more government as the solution. If government is the problem, the obvious solution would be less government, not more.

Stockman offers a list of 13 “crucial steps” he says are needed, including reforming the Fed, abolishing deposit insurance, developing a “super Glass Steagall” to separate commercial banking from investment banking, abolishing incumbency, requiring a balanced federal budget, separating the state from the free market, abolishing social insurance, ending bailouts and subsidies, eliminating 10 federal agencies and departments, establishing a cash-based means-tested safety net, abolishing the minimum wage, eliminating health insurance, imposing a 30 percent wealth tax to pay down the national debt, and repealing the Sixteenth Amendment.

In contrast to Stiglitz, Stockman recommends actual policies rather than the results he hopes to see from policies, and his recommendations in most cases call for smaller government rather than

bigger government. Both authors want to end corporate welfare, but Stiglitz wants to enhance the welfare state's support of individuals while Stockman wants to abolish that system and replace it with means-tested cash transfers. Stiglitz wants to increase the progressivity of the income tax; Stockman wants to eliminate the income tax. Both are pessimistic that the system that is controlled by the 1 percent can be turned around.

### The Road Ahead: The War of Ideas

Stockman sees no hope. He says (p. 672), "Alas, none of these solutions are even remotely possible within our now fully corrupted constitutional framework. The latter is no longer a system of democratic choice and governance; it is a tyranny of incumbency and money politics." Stiglitz is slightly more optimistic. He notes the importance of ideas, saying (p. 183), "The fact that the 1 percent has so successfully shaped public perception testifies to the malleability of beliefs. When others engage in it, we call it 'brainwashing' and 'propaganda.'" But the 1 percent controls the media and controls people's perceptions. Regarding the present state of affairs, Stiglitz says (p. 186), "I show how the 1 percent has used these advances to alter perceptions and achieve its aims—to make our inequality seem less than it is and more acceptable than it should be." He continues (p. 233), "We've seen how the powerful manipulate public perception by appeals to fairness and efficiency, while the real outcomes benefit only them." The way out, then, is to win the war of ideas.

Dani Rodrik (2014) says the same thing, echoing Keynes's (1936: 383) famous statement that "the ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else." Academics reading this article will be sympathetic to the notion that ideas trump interests, but therein lies the big tension between Stiglitz and Stockman. They identify the same problems, attribute those problems to the same causes, and agree on the same pernicious results. But they offer very different solutions. Stiglitz argues for bigger government and more government oversight of the economy to address the problems caused by faulty government policy, whereas Stockman argues, in the main, for the opposite.



Public policy recommendations, however, should take account of the incentives of policymakers and the information available to them to make informed public policies (Holcombe 2012). Both Stiglitz and Stockman do this when diagnosing the problems, and they should extend this methodology to designing policies to address those problems.

## Conclusion

This article has demonstrated the similarity of the ideas of the political left and right on the causes of contemporary political-economic problems and their consequences, using Stiglitz as the spokesman on the left and Stockman on the right. A brief reference to other scholars on the left and right shows that their ideas are representative across the political spectrum.<sup>4</sup> There is substantial agreement that faulty U.S. government policy that systematically favors the elite over the masses is damaging the market system and democracy.

Stiglitz and Stockman both believe their policy recommendations represent the interests of average Americans, and neither believes that the policies they recommend favor the 1 percent over the 99 percent. Yet, the fact that their recommendations are so different points to the political challenges working against reform.

It would be easy to argue that Stiglitz and Stockman both overstate the degree to which ordinary Americans are harmed by government policies that favor the 1 percent. Gilens and Page (forthcoming) offer a more optimistic view. After undertaking an empirical study that shows the influence of the preferences of elites and impotence of the preferences of ordinary citizens, they find that “this does not mean that ordinary citizens always lose out; they fairly often get the policies they favor, but only because those policies happen also to be preferred by the economically elite citizens who wield the actual influence.”<sup>5</sup>

<sup>4</sup>A recent exception is Piketty (2014). While Stiglitz, Stockman, and a number of other authors noted earlier focus on faulty government policy as the problem, Piketty argues that the inequality he and Stiglitz view as the primary problem is inherent in the nature of capitalism. Like Stockman, Piketty argues for a wealth tax, although Piketty’s wealth tax would be an annual progressive tax whereas Stockman’s recommended tax would be a one-time tax at a much higher rate.

<sup>5</sup>Note the similar conclusion drawn by Beard (1913), who offered a similar message of elite opinion trumping the masses in the writing of the U.S. Constitution.

The degree to which the elite control the political process is certainly open to question. The highest income earners face a marginal income tax rate of 40 percent or more when considering federal and state taxes while the bottom half of the population pays almost no income taxes. The U.S. corporate income tax rate is the highest in the world, while more than half of government spending goes to transfer payments. But set aside the question of whether Stiglitz and Stockman and others have exaggerated the influence of the elite. Their agreement that government is the cause of the problems they cite makes a powerful argument for limiting the scope and power of government. The fact that there is agreement on the left and the right on these problems and their causes is worth noting. That points to the policy question of what should be done to address those problems.

A government run by an omniscient benevolent dictator could implement the policy proposals that Stiglitz or Stockman recommend (but not both, because many of their recommendations are in conflict). In fact, government policies are created and implemented through a political process in which people who have more political power are naturally inclined to use it for their benefit. If these authors are correct in diagnosing the problem as being created by the abuse of government power, the only real solution is to constrain the the power of government. To think that increasing the scope and power of government will make government more benevolent is wishful thinking.

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