What are the most important economic effects — good and bad — of forced redistribution? How should this inform government policy?

Redistribution refers to the transfer of holdings between persons or groups (Barry 2018). This transaction may occur between two individuals or between groups that may be defined by their existing possessions (via a quintile system[1] which segregates the population1) or by the rigid social system (the Whites and the Hispanics). Such a redistribution is said to be 'forced' when the transaction is made compulsory by the government. Monetary and fiscal policies like changes in the tax rates, government spending and fixed exchange rates are the main instruments used for the purpose. The phrase "forced redistribution" can, at first, seem a very direct take-and-give policy, however, the distribution mostly occurs in an indirect manner through a system of taxation and reallocation of resources by the government.

Merit, public, and free goods always produce positive externalities in the economy, but if left to the market forces, are always under-produced and under-consumed because of irrationality of the consumer and imperfect information in the market (Colin Bamford 2015). For this reason, most governments use a progressive taxation system, wherein the tax rate increases as the amount payable in taxes increases. The tax revenue generated is used to give out corrective subsidies, unemployment benefits, or directly provide goods and services. Governments either take control of firms that produce these commodities (State owned enterprises) or they fund private companies in the form of Pigouvian[2] or corrective subsidies (Daron Acemoglu 2015). This is known as the private production of public goods and is a major mechanism of redistribution in economies.

Additionally, a forced provision of, for example, education increases the availability of skilled labour and attracts foreign investment. In 2017, the USA spent an average of $12,800 per student on public education (Felon 2019). As a result, the literacy rate in America is 99% leading to a low unemployment rate of 3.5% in 2019. Although these goals can only be achieved in the long run, they lead to a substantial economic development in a country. (CIA 2010)

The word "inefficiency" is used a lot in economic contexts, it is useful to define the term with respect to how forced redistribution increases it. Inefficiency occurs when there is a loss in surplus due to higher costs of production, this generally happens when the market is not functioning in its *natural* equilibrium. The departure from the market equilibrium due to government intervention (like forced redistribution) leads to opportunity costs in terms of a loss to the producers, consumers, and social surplus in general.

Indirect or direct, the "quality" of efficiency gain is often fragile in such redistributive systems. A more robust way to have efficiency gains in terms of social and economic value is to provide goods and services that benefit the economy in the long run (through dynamic efficiency). For example, providing good quality education is more beneficial to the

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[1] A five-tier distribution of holdings over the population depending upon GDP per capita.

[2] Pigouvian or corrective subsidies are designed to induce agents who produce positive externalities to increase quantity towards the socially optimal level.

economy than distributing food grains as higher literacy leads to greater employment in the long run.

Indirect redistribution is inevitable in the form of taxation, the idea is to implement sustainable redistribution using a system of selective pressures, incentives, and constraints such that the redistribution occurs via “private” hands[3].

The purpose of forced redistribution is to create an egalitarian society. When inequality is already high, any further increases in inequality would only cause a reduction in social surplus. This could be for multiple reasons: a very high inequality could create distortions by preventing some people to compete with others on a levelled playing field. The government can achieve greater social equality, but only at the expense of greater inefficiencies. Hence, there is an opportunity cost involved. On the other hand, at extremely low levels of inequality, the social surplus decreases because of the deadweight loss from government taxation. This equity-efficiency trade-off represents the basis of the tiff between the so called “capitalists” and “socialists.” (Daron Acemoglu 2015)

Importantly, redistribution is not some form of socialism or communism. In reality, it helps the economy yield the greatest benefit from its public property. Pope Francis once described it as “humane micro-capitalism.” Unrestrained capitalism is not “too many capitalists,” but it is “too few capitalists.” (Hunt III 2014). Hence, the idea of paternalism[4] encourages the rational consumption of goods and services although the consumers do not have a choice. (Daron Acemoglu 2015)

In 2017, US Senator Elizabeth Warren, claimed that from 1935 to 1980 when America was coming out of the great depression, the country invested in education, infrastructure, and research. This is how the middle class was built — that is, 90 percent of the population who account for 70 percent of the income earned in the country (Kessler 2015). So, the GDP kept going. However, after the 1980s the GDP was still growing because of the robust multinational companies, owned by a few Americans, making large profits in the world economy. However, this was only the top 10% of the people. This leads to economic hardships for the middle class because the remaining Gross domestic product is distributed between the huge 90 percent of America’s population (CIA 2010). Forced provision of merit goods would, therefore, be beneficial for such people because they would have the greatest benefit.

All the same, advocates of consumer sovereignty might argue that forced provision reduces choice for the consumer. For example, if the government nationalizes the education industry and provides the same kind of schooling for all, people who can afford to go to posh private or boarding schools will turn out to be the losers. They would have contributed more to the economy through their better-quality education, however, the forced provision of public education services by the government would prevent that. They would also say that just providing goods for free or at very low prices potentially leads to disincentive to

[3] Incentivizing corporate social responsibility leads to an increased private production of merit and public goods that would have otherwise been produced by the government.
[4] Paternalism is the view that consumers do not always know what is best for them, and the government should encourage or induce them to change their actions.

work and enterprise. Unemployment, therefore, rises as people do not have to work to procure commodities. Standard of life is also lower. Because the government is the sole provider, it does not have to face the fierce market competition, which forces firms to keep the quality of their commodities up to the mark.

The benefits derived from forced provision occur assuming that the government is not corrupt. If majority of the public funds are used for personal gain, the optimal allocation would be distorted. Bureaucratic governments work on the basis of directives instead on the basis on Adam Smith's invisible hand. Nepotism is also common in such economies, leading to the people closest to the politicians gaining the most. This inevitably leads to deadweight loss in the economy and the whole purpose of bringing equality is defeated (Colin Bamford 2015).

A government's policies are highly predicated on their stance on redistribution. If the government believes that effort and talent should be given the carrot and inefficiency should be given the stick, then its regime would have low redistribution and low taxes and capitalism would be promoted (A. a.-M. Alesina 2005). For example, in countries like China, and the Soviet Union, central planning is associated with the Marxist-Leninist theory, hence, favouring forced redistribution. On the other hand countries like Singapore and Hong-Kong have minimal government intervention and function on the basis of the market forces.

When people in a democracy, like the USA, choose their governments, their ideologies vary from person to person. For instance, someone "poor" will be in favor of forced redistribution since they would gain from it. However, this preference changes when such people gain form the redistribution and turn into the rich of the tomorrow. When this happens, the old "poor" are no longer willing to support the scheme (Alesina, Di Tella and MacCulloch August 2004). Likewise, the rich might support redistribution either because of altruism and good conscience or as a backup in case of future misfortunes.

The welfare state of the government refers to a set of insurance, regulation and transfer programs utilized to create a safety net, reduce poverty and to redistribute income from the rich to the poor. The largest factor that influences the government's budget for is the costs and benefits from giving such advantages. Merit goods create positive externalities in an economy. Ideally, the government should expand provision until marginal social benefits equal marginal social costs. This means that if the marginal social benefits exceed the marginal social costs for the next unit, it should be provided by the government. This happens when the demand for the good rises to a point that the market is in disequilibrium and hence government intervention is necessary. This standard cost-benefit logic[5] not only applies to merit goods but also to all insurance programs, education provision and infrastructure development. (Daron Acemoglu 2015)

In a more political sense, the government may favor redistribution and more socialist policies to win larger political support. The large middle class mostly favors such "democratic" approaches because their net gain is the highest (A. a.-M. Alesina 2005).

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[5] A calculation that identifies the best alternative, by summing benefits and subtracting costs, with both benefits and costs denominated in a common unit of measurement.

However, the Meltzer-Richard model showed how inequality may generate higher income taxes in political equilibrium and thereby more distortions in terms of efficiency. This means that the government needs to choose a balanced tax rate where increasing the rate does not lead to more evasions or a reduction in the tax base (Huber† 2009).

Government fiscal policy measures must ensure that inequality in income doesn't rise beyond control and very high taxes and government benefits do not lead to disincentive to work. Interestingly, there are opportunity costs associated with both sides of the coin. Hence, according to the state and structure of the economy, the government policy should be balanced and should not lead to inefficiencies in market. As Ray Dalio said, "The problem is that capitalists typically don't know how to divide the pie well and socialists typically don't know how to grow it well," (Feloni 2019) To put it very simplistic terms, extreme redistribution would not benefit a country's economy and neither would no redistribution; the key is reaching a pragmatic balance.

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