The problem with billionaire consumption

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Modern societies have granted capitalists the right to profit, but cannot extract from them a duty to invest, specifically during times of economic recessions. In contrast, workers have no right over the very aspect of spending — investments — that affects their employment and living standards

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A decorated Rolls-Royce car carrying guests leaves Antilia, the house of Indian businessman Mukesh Ambani, on the day of his son Anant's wedding in Mumbai, on July 12. | Photo Credit: Reuters

The lavish and extended wedding celebrations of billionaire Mukesh Ambani's youngest son has brought to the forefront the question of "conspicuous consumption" of the rich. In a capitalist society beset by high levels of inequality, how do we make sense of such displays of private wealth by the elite? Does billionaire consumption in an unequal society hinder or aid economic expansion? What are some of the ethical and economic issues involved? The issues discussed here do not pertain solely to the Ambanis, but attempt to tackle some broader questions regarding the question of private consumption by the rich.

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A defence of billionaires' consumption would run as follows: in a liberal capitalist democracy, there are no restrictions on what one chooses to do with one's private property. Assuming that market processes are fair, billionaires' consumption expenditure — no matter how lavish — is a legitimate exercise of their private freedoms and cannot be faulted. The existence of inequality is not their concern, but the manifestation of flawed policy that restricts market freedom and curtails pure competition. Increasing market access, in this view, would ensure that everyone has adequate wealth.

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On the opposite end of the political spectrum, the Marxist view holds that since value is created solely by labour, profits represent an unfair extraction of value. Thus, all forms of billionaire consumption is illegitimate, since private riches are generated through a denial of the rightful claims of workers. The co-existence of a large working class with low wages and a small number of billionaires does not arise because of a faulty market mechanism, but is an undeniable feature of capitalism itself. The rights over private property enshrined in liberal societies hide deep structural imbalances that serve to continually enrich a few at the expense of the many; in this framework, there can be no way to justify billionaire consumption.

The impact on the economy

Another defence of billionaire consumption is that regardless of the ethical issues involved, as long as consumption is done domestically, the expansion of purchasing power leads to an increase in demand for locally-made goods, and an increase in domestic employment and incomes. In economies like India where the generation of suitable employment is a matter of grave concern, private consumption of the rich ensures a vital boost to aggregate demand. Yet this represents a second-best solution to the problem of demand, since what is required for growth in living standards is investment, not consumption.

Consider two sectors in an economy, a consumption sector that produces clothes, and an investment sector that produces sewing machines. Assume that every year, the local billionaire spends a given amount of money to purchase clothes, but does not put in any order for new sewing machines. The demand for clothes generates employment, but the capital stock — represented by the sewing machines — does not change, and hence neither does labour productivity. Since per capita incomes depend on labour productivity, living standards do not rise. There might be employment, but no growth.

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If the billionaire was to purchase sewing machines, this investment would generate employment not just in the investment sector — as workers are hired to produce sewing machines — but also in the consumption sector, since these newly-hired workers would purchase clothes. Consumption spending does not necessarily generate investment spending, but investment spending, through the working of the multiplier effect, necessarily increases demand in the consumption sector as well.

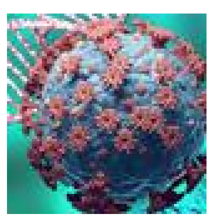
Moreover, investment would ensure the capital stock is upgraded with the latest machinery, increasing the productivity of labour and per capita incomes. Long-run growth crucially depends on investment spending, which is the domain of the rich, since working classes do not control the operations of businesses and have no say in the prospects of capital expansion.

A “social contract”

According to the celebrated British economist John Maynard Keynes, capitalist societies rest on a peculiar social contract. The capitalist classes are allowed greater wealth, control of production and a substantial share of net output produced each year, provided they ensure high levels of investment that generate sufficient employment and rising productivity. They must also ensure that prices are not increased drastically so that real wages do not fall. This can be the only grounds for an unequal distribution of resources in a capitalist society from a Keynesian perspective.

The greater the share of profits invested, the greater is economic welfare. Keynesian growth theory specifies that the rate of growth is highest when the entire share of profits is invested (for given technical conditions). In mainstream growth theory, the level of per capita consumption is highest when the entirety of profits is invested; this is known as the “Golden Rule”. Conspicuous consumption out of profits can therefore be seen as reducing the amount available for investment, and hence reducing welfare.

What rising inequality means



Herein lies the peculiar problems that affect modern capitalism. Since profits accrue privately, the decision to invest is also taken privately. In certain instances, capitalists may wish not to invest, for the risks would certainly outweigh the potential benefits. They may also choose to engage in pure consumption and lavish ceremonies, and liberal societies allow them the uncontested right to do so. But this represents a loss for the working classes, since it draws resources away from the expansion of the capital stock, reducing employment and labour productivity growth. Modern societies have granted capitalists the right to profit, but cannot extract from them a duty to invest, specifically during times of economic recessions. In contrast, workers have no right over the very aspect of spending — investments — that affects their employment and living standards.

This takes added significance in the presence of monopoly, where even if investment occurs, working classes are affected through the imposition of monopoly prices that reduce real wages and purchasing power.

The purpose of this piece is not to point fingers at specific instances of conspicuous consumption, but to place some economic issues in context. As opposed to a Marxist analysis, a Keynesian understanding would hold that lavish consumption of the rich is a problem only if enough investment is not forthcoming to absorb those searching for jobs and if the consumption of working classes is curtailed through high monopoly prices. In the context of high youth unemployment, stagnant real wages and a significant loss of jobs in the informal sector, the stark inequalities on display represent a very real public policy problem that we have shown an inability and unwillingness to confront.

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