

BOOK REVIEW

Title: Efficiency and Equity in Welfare Economics

Author: PierCarlo Nicola

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by Flavia Cortelezzi

Pier Carlo Nicola, a member of the prestigious Accademia Nazionale dei Lincei, is one of the leading Italian scholars in General Equilibrium Theory and the author of a number of books on modern Mathematical Economics. As a Professor of Mathematical Economics at the Università Statale of Milano, he has taught and supervised for more than four decades hundreds of students forging a generation of economists and applied mathematicians.

“Efficiency and Equity in Welfare Economics” is his fourth book over a period of almost two decades with the prestigious German publisher Springer-Verlag. All his books are linked by a common approach. The author employs a rich set of mathematical tools to analyze specific economic dimensions in a general equilibrium framework and offers the reader some key elements to familiarize with the implications of complex models.

The overriding question is why one should be concerned with efficiency and inequality. The standard answer is firmly linked to the ethical approach of distributional questions (Sen and Foster 1997).

The latter is in turn related to individual concerns and views. On one hand people care about distributional fairness through their own behavior in experimental settings (Charness and Rabin 2002, Fehr and Fischbacher 2002, 2003), on the other, policy makers are continuously faced with taking allocative decisions in circumstances in which some gain and other lose.

The central place that Ricardo attributed to the subject of income distribution in the 19th century Political Economy is appropriate also in the 21st century Socio-Economics.

Although distributive justice is often considered to be out of scope in economics, there is actually an important strand of literature that addresses normative issues in social and economic justice. In the last fifteen years there has been, in fact, a renewed interest of economists in these themes driven partly by recent results in economic theory and partly by major contributions in the income distributions theory within many developed countries (Atkinson 1997).

Distribution effects are of great political interest at a time when the discussion about growing social dissimilarities is playing an increasing political role in public debates in Europe (Sen, 1997, Wilkinson and Pickett, 2010, European Commission, 2010, Stiglitz et al., 2009, Jackson, 2009).

Inequality is seen as a “socially corrosive threat to societies” (Wilkinson and Pickett, 2010). The Stiglitz Commission recommended that more prominence should be given to the distribution of income, consumption and wealth in society, because a rise in average income could be unequally shared across income groups, leaving some households relatively worse-off than others. Thus, average measures of income, consumption and wealth should be accompanied by indicators that reflect their distribution across persons and households (Stiglitz et al., 2009). Income forms the basis for consumption decisions by households, which decisively determines our well-being. Or as Pigou said: “The economic welfare of a community consists in the balance of satisfactions from the use of the national dividend (or, as we should say, national product) over the dissatisfactions involved in the making of it” (Pigou, 1932).

Moreover, political reforms can be enforced more easily when they are seen to include political measures that contribute to social justice.

Social justice is thereby always connected to the distribution of the material welfare. Society confronts choices that offer somewhat more equality at the expense of efficiency or somewhat more efficiency at the expense of equality. In the idiom of the economist, a trade-off emerges between equality and efficiency.

In this sense, “Efficiency and Equity in Welfare Economics” is a timely publication, catering for a large public, and filling a vacuum in the editorial landscape. It is timely not only because there is a widespread concern that economic growth has not been shared fairly, but also because the current economic crisis further widens the gap between rich and poor. New OECD data show that the global economic crisis has squeezed incomes from work and capital in most countries. Excluding the mitigating effects of the welfare state, via taxes and transfers on income, inequality has increased by more over the past three years to the end of 2010 than in the previous twelve.

The author has the strong merit of presenting a clever analysis and, at the same time, a passionate attempt to link welfare functions to the study of efficiency in income distribution and to inequality and poverty. The author is seriously concerned for the increasing efficiency in generating national income and improving equity in its distribution among economic agents is at the forefront of priorities of most modern economies. The aim is that of exploring the tradeoff between efficiency and inequality, with the scope of fighting poverty without impoverishing society as a whole.

“Do unto others as ye would that others do unto you” is the common thread of the entire book. The author considers this sentence as the greatest statement on fairness and reciprocity, and in the light of this Golden rule the author focuses his analysis on the possibility of the existence of an egalitarian system.

The style of the book is concise and straightforward. It is technical, being written for an economic literate reader, but, at the same time, it states the solutions proposed in a comprehensible way. The book is addressed to a wide public of scholars, academics and current or future policy analysts who want to increase their capacities in analyzing the welfare effects, in terms of social welfare and inequality, of development policies. On these grounds, economists and practitioners working in public administrations, professional organizations or consulting firms will find this book helpful for the richness of the references material and cited sources.

“Efficiency and Equity in Welfare Economics” helps the reader familiarizing with the complexity of the literature on social welfare. Through the book, the vast literature on the subject is summarized in a unitary framework. It does not attempt to be a complete survey of the existing results, but to give a critical assessment of the main axioms and relevant information. Social welfare functions are formally defined together with closely related concepts. In a more recent contribution (see Nicola, 2013), the author further specifies an individual social welfare index, easy to obtain and compute, which allows for a better international comparison of income per capita.

The book also contributes to document and reinforce the implications, in terms of policy, of different social welfare functions in order to design a fair trajectory for the economic development. To illustrate the relevance of the analysis proposed, a selected results on the Italian case are presented.

The structure of the book is the following. Chapter one provides a general overview; chapter two discusses different social welfare functions and income distributions. Chapter three looks at different definitions of inequality and poverty indexes. In Chapter four, the author links inequality to the production sphere of the economy, in order to focus on the possible connection between technical efficiency and the problem of

inequality. Chapter five simultaneously considers social welfare and efficiency and Chapter six tries to propose the possibility that a Public Administrator design an incentive scheme that is both equitable and efficient. Finally, chapters seven through nine explore, by means of a series of simulated numerical examples, the tradeoff between efficiency and inequality/poverty, in order to verify when a greater degree of inequality can improve the economy's total productivity, hence also the income and consumptions of the less favored.

I enjoyed very much reading this book and recommend it as a useful comprehensive introduction to all those, scholars, policy-makers who are interested in fostering "social justice". This book contributes to summarize the current debate and to present fresh and promising new ideas.

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