On Redistribution and Human Capital Investment Policies

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Societies have always attempted to realize economic growth. Growth can bring greater wealth and opportunities to a nation's citizens. However, with this growth, complex issues regarding social equity and government efficiency emerge. These may be spread over a broad spectrum, creating a need for governments to address them with two groups of policies: Redistribution of wealth and investment in human capital. Today, both groups serve indispensable functions to ensure that governments run properly. They also put guardrails so that an economy's balance is not tipped overly towards specific populations.

In history, the concept of a "tax," the most common form of a redistribution policy today, predates that of an investment in human capital. Historians agree that the ancient Egyptians systematically experimented with a tax as early as five millennia ago. After Egypt became unified, the kingdom required an increasingly complicated government to carry out its duties of supervising agricultural yield and warfare. The taxes back then differed significantly in their form from their modern versions. Papyrus scrolls inform historians that taxes were paid with livestock, gold, silver, and linens. These taxes served a much simpler purpose than any kind of wealth redistribution – they existed to ensure that the government under the pharaoh could operate and protect the kingdom from foreign foes.

The birth of educational institutions, the central pillar behind investment in human capital, occurred one millennium later. Around 2000 B.C.E., Mesopotamian civilizations created schools to train individuals for certain essential government positions, such as the scribe. These schools, though rudimentary, planted one cornerstone for any educational institution – the idea to invest in human capital to increase work efficiency and effectiveness.

In the eighteenth and nineteenth centuries, the instruments of tax and the initiative of human capital investment became linked with the values of social equality and equity. At the time, as the effects of the Enlightenment and Industrial Revolution set in on European nations, governments discovered the urgency to use these tools to tackle the emerging social issues of inequality. In the Netherlands, for example, the government created a new kind of tax on wealth. The idea of a wealth tax was pioneering. It marked an early systematic attempt by a government to redistribute wealth through tax. The Dutch also implemented educational reforms to expand access to education and improve the quality of schooling. They realized that investment in human capital might be a powerful tool to boost long-term economic and social development in that tumultuous era.

Today, the policy directions of redistribution of wealth and nurturing the intellectual capacities of the individual are still the guiding principles to achieve a society where economic growth is more broadly shared. Governments have more tools in their toolboxes for both directions. For instance, aside from taxes, minimum wages, which act as a binding price floor in the labor market, have been discussed as another redistribution policy. Additionally, a government can pursue a plethora of human capital investment projects. The question is: Which group of policies is more cost-effective for the government?

This question pokes at a crucial metric to determine whether any policy would be worth implementing: The cost to the government. The common perception is that human capital investment is more costly than a redistribution policy such as a tax. Most government programs to build schools and improve college education require immense funds. On the contrary, a government can earn revenue by employing any tax. However, while such a consideration might possess some merit in the short run, other factors come into play in the long run. Namely, when a government considers what policy to enact in the long run, it must also consider any potential benefits it might receive due to implementing that policy.

Many kinds of investment in human capital catalyze behavioral responses. People's behaviors create impacts. Some of these might be implicitly positive fiscal externalities. Suppose the government invests a sum into a project aiming to lower the tuition of public universities. One of the immediate consequences might be that more students can receive higher education. Then, due to an increase in college students, the government can expect increased income tax revenue as these students are likely to earn higher incomes. There is a positive fiscal result at the end of this chain reaction.

In 2020, Nathaniel Hendren and Ben Sprung-Keyser, two economics scholars, published a paper comparing the net costs of 133 government programs in the U.S., mainly focusing on policies in social insurance, taxes, and education. The definition of the "net cost" of a program is the initial cost of implementing the program minus the final fiscal earnings of the program. Such a calculation factors in the behavioral responses of individuals affected by these policies. The two scholars conclude that human capital development programs have lower or negative net costs, meaning that the U.S. government earned more than it initially spent. In comparison, redistributive policies such as cash transfers, unemployment insurance, or various taxes have much higher net costs. The researchers explain that investments in human capital eventually generate tax income that covers short-run costs. On the other hand, many plans to redistribute wealth, such as unemployment insurance, might disincentivize people to find an occupation that would lead to more income.

However, while human capital investments have a much greater utility in the long run, it is dangerous to reject policies to redistribute wealth for a reason of lower utility. Today, they are more necessary than ever for people in need. Without progressive taxes or minimum wages, there would be no safety net, and income disparities would be bound to widen dramatically. Furthermore, the claim that redistributive policies are always costly is somewhat arbitrary. For instance, when there is a period of macroeconomic prosperity and job opportunities abound, unemployment programs' net costs might be lower as people are more incentivized to find a job.

Both redistributive and human capital developmental programs aim to reduce income inequality and build a socioeconomic scenario where the boons of development can be shared more equitably. In the past, one glaring factor that led to widening inequality gaps was the inability of education to follow the advancement of technology. Data shows that from the 1950s to the 1980s, the average years of schooling for a person aged 30 in America grew much slower. Meanwhile, technological progress accelerated exponentially. As a result, in factories and other workplaces, many workers who did not acquire the necessary skills to keep up with the progress of technology gradually lost to machines in efficiency. As workers were paid less, income became more unequally distributed as the few people who gained the skills to compete with technology monopolized wage earnings.

Today, artificial intelligence marks another technological revolution. To ensure that income gaps do not gradually widen, governments must rely on both redistributive policies and investment in human capital. For one, governments should strengthen social safety nets with minimum wage policies. For another, more importantly, governments must divert more energy and funds to invest in primary and secondary education. As argued in another essay, the students of today and tomorrow must be exposed to AI at an earlier age and be equipped with the skill sets to navigate the digital world. From the age of the ancient Egyptians and Mesopotamians, taxes and efforts to improve education have helped human societies transition from one era to another. The world should be confident that these ideas will continue to be effective in a future that might yield unprecedented boons for humankind.

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