Economic Inequality

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Rotary Club of West Marin
August 28, 2019
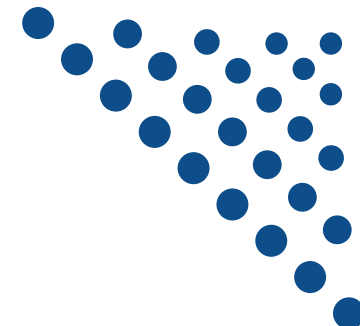
National Economic Education Delegation

- **Vision**
  - One day, the public discussion of policy issues will be grounded in an accurate perception of the underlying economic principles and data.

- **Mission**
  - NEED unites the skills and knowledge of a vast network of professional economists to promote understanding of the economics of policy issues in the United States.

- **NEED Presentations**
  - Are **nonpartisan** and intended to reflect the consensus of the economics profession.

Who Are We?

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  - 2 Fed Chairs: Janet Yellen, Ben Bernanke
  - 6 Chairs Council of Economic Advisers
    - o Furman (D), Rosen (R), Bernanke (R), Yellen (D), Tyson (D), Goolsbee (D)
  - 3 Nobel Prize Winners
    - o Akerlof, Smith, Maskin
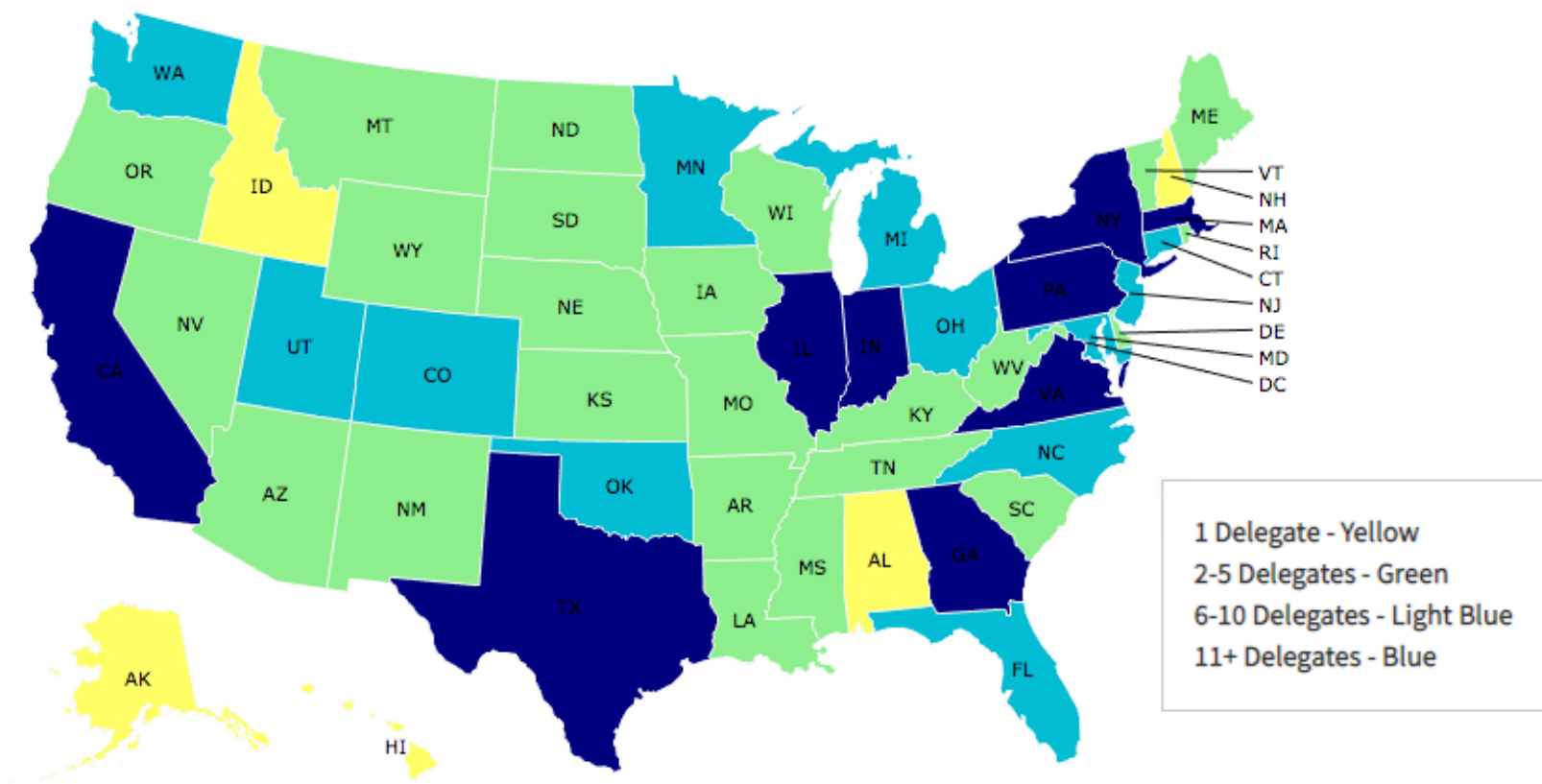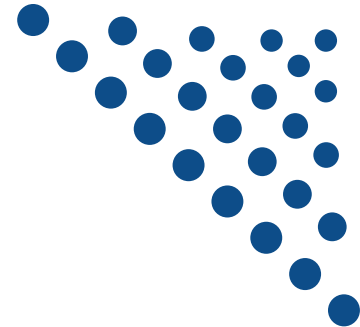
- **Delegates: 365 members**
  - At all levels of academia and some in government service
  - All have a Ph.D. in economics
  - Crowdsource slide decks
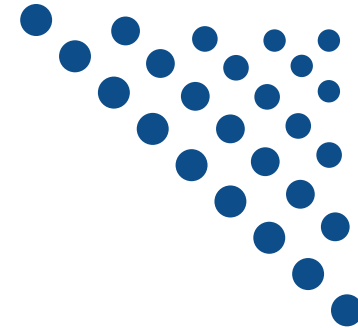 - Give presentations

- **Global Partners: 42 Ph.D. Economists**
  - Aid in slide deck development

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Where Are We?
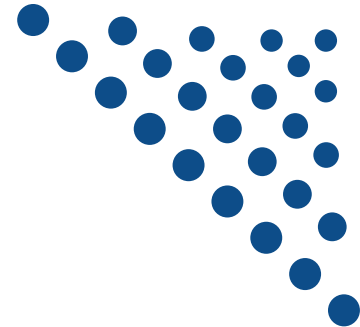
1 Delegate - Yellow
2-5 Delegates - Green
6-10 Delegates - Light Blue
11+ Delegates - Blue

Credits and Disclaimer

- **This slide deck was authored by:**
  - Jon Haveman, Executive Director of NEED
- **This slide deck was reviewed by:**
  - Timothy Smeeding, University of Wisconsin
  - Robert Wright, Augustana University
- **Disclaimer**
  - NEED presentations are designed to be nonpartisan
  - It is, however, inevitable that the presenter will be asked for and will provide their own views.
  - Such views are those of the presenter and not necessarily those of the National Economic Education Delegation (NEED).

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Outline
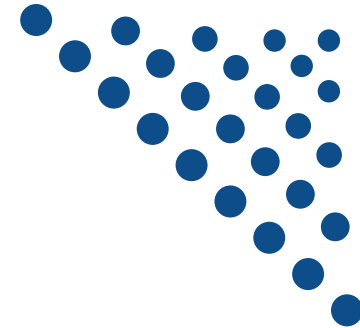
- **Definition**

- **Measurement**

- **How does it happen?**

- **Does it matter?**

- **Is it a problem?**

- **What to do about it**

Economic Inequality: Income
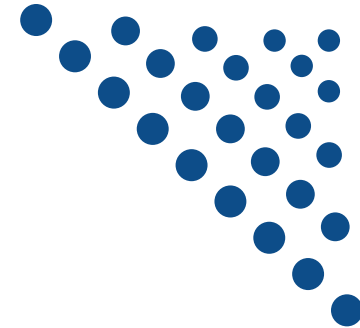
- **Definition:**
  - The extent to which the distribution of income deviates from complete equality

  - The dispersion of income throughout the economy
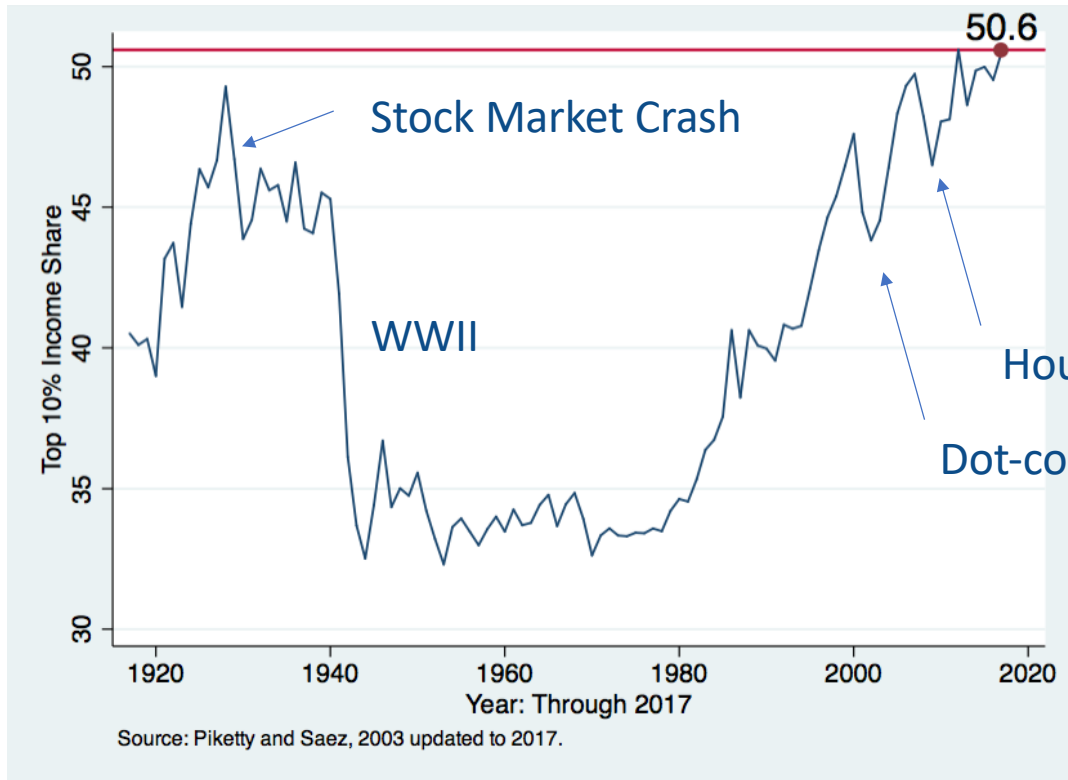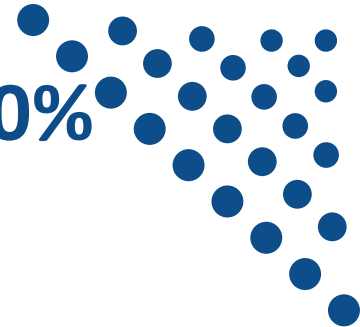
Different Ways of Thinking About Inequality

- **Income Inequality**
  - Before taxes and transfers
  - After taxes and transfers

- **Wealth Inequality**

- **Consumption Inequality**

National Income Inequality: Share of Top 10%

Stock Market Crash

WWII

Housing Bubble

Dot-com Bubble

50.6

Source: Piketty and Saez, 2003 updated to 2017.
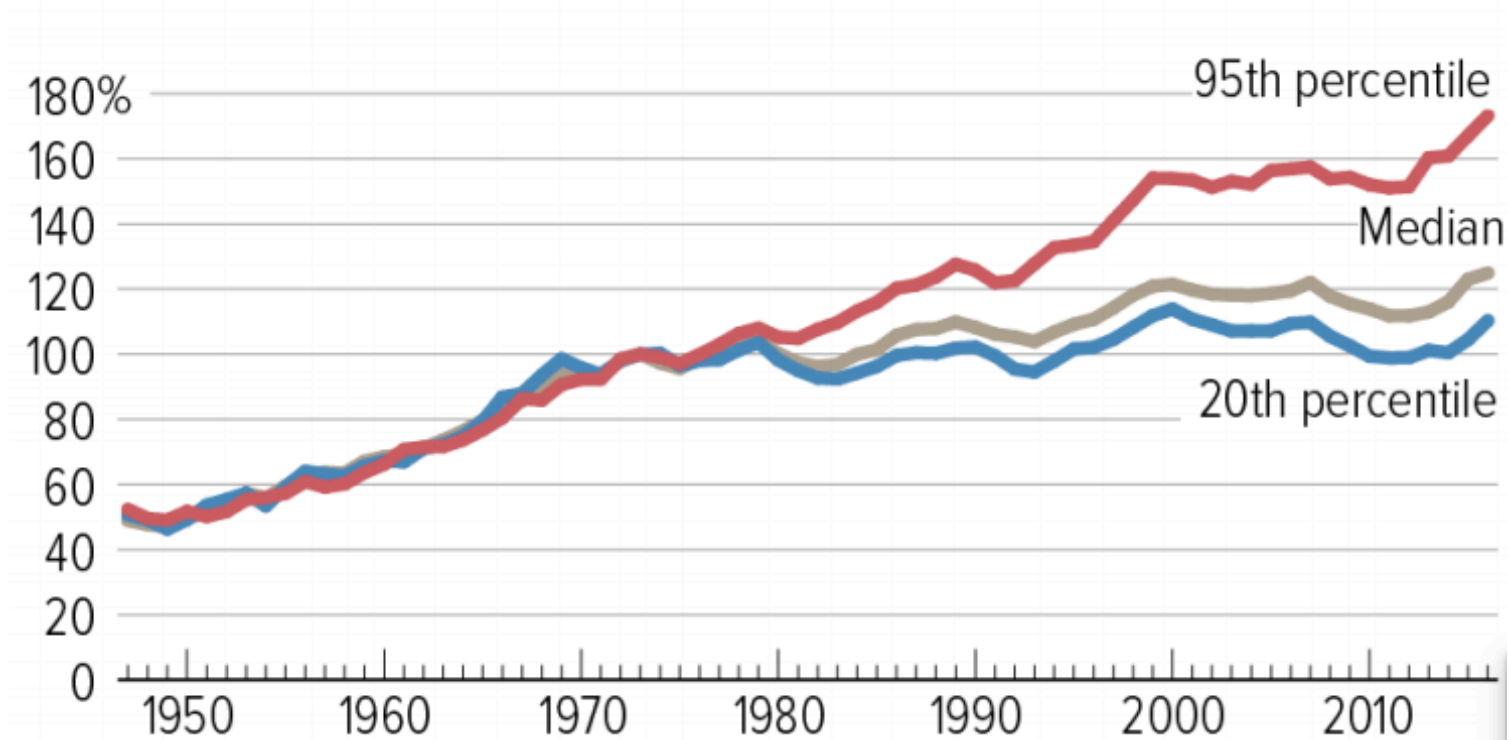
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The Abrupt Increase in Inequality (Before Taxes)

Real family income between 1947 and 2016, as a percentage of 1973 level

Source: Chad Stone, Danilo Trisi, Arloc Sherman, and Roderick Taylor, "A Guide to Statistics on Historical Trends in Income Inequality," Center on Budget and Policy Priorities, Policy Futures, May 15, 2018, page 10.

Most of the Action Is at the Very Top

Percent change in income after transfers and taxes since 1979

Legend:
- Top 1 percent
- Next 19 percent
- Middle 60 percent
- Bottom 20 percent

228%
73%
69%
42%

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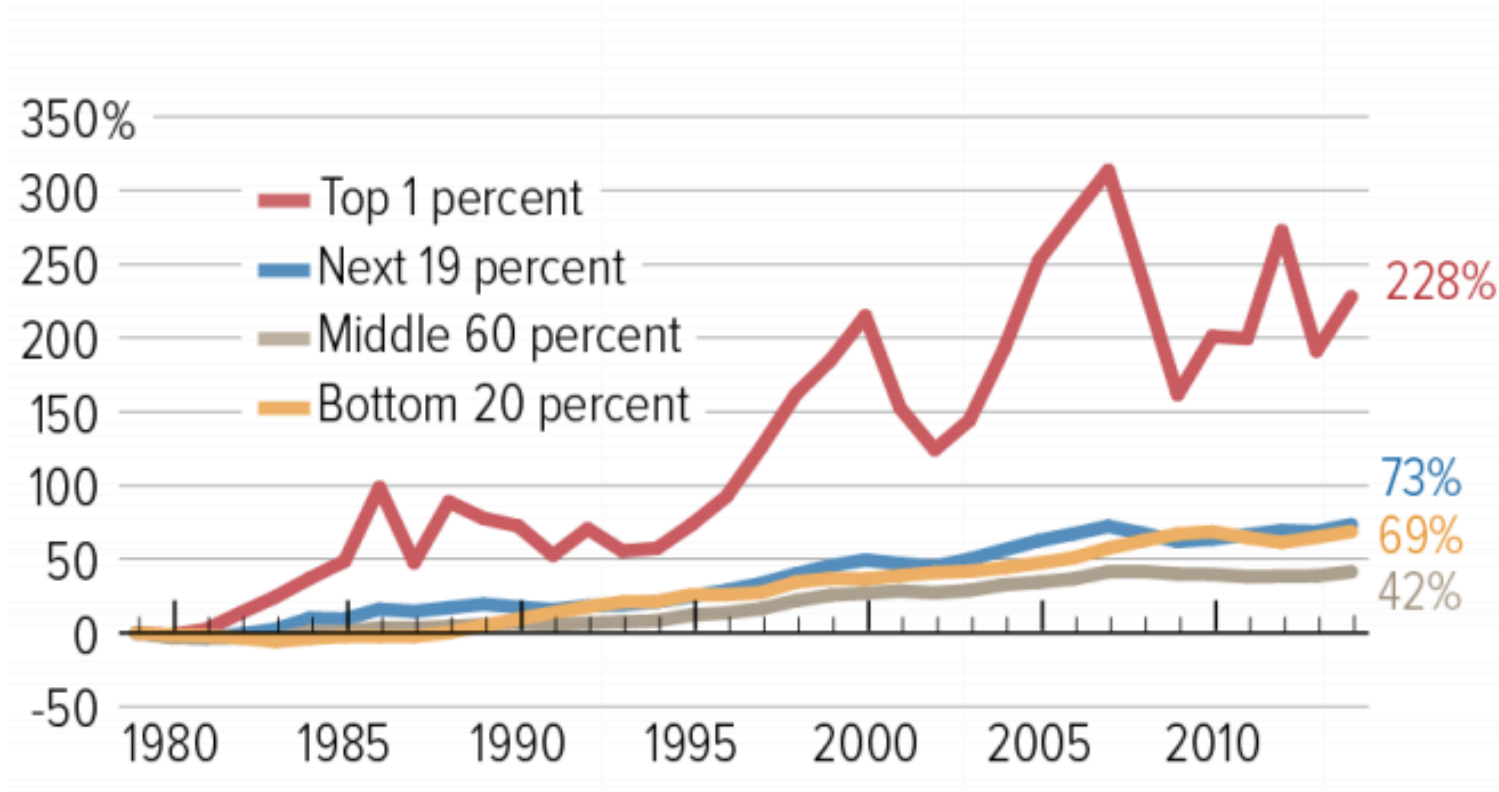
Income Changes from Growing Inequality

Bottom 90% of Households

INCOME GROUP	TOTAL LOSS/GAIN IN ANNUAL INCOME*	AVERAGE LOSS/GAIN PER HOUSEHOLD PER YEAR*
TOP 1%	$673 billion more	$597,241 more
96-99	$140 billion more	$29,895 more
91-95	$29 billion more	$4,912 more
81-90	$43 billion less	$3,733 less
61-80	$194 billion less	$8,598 less
41-60	$224 billion less	$10,100 less
21-40	$189 billion less	$8,582 less
BOTTOM 20%	$136 billion less	$5,623 less

* Compared to what incomes would have been had all income groups seen the same growth rate in 1979-2005 as they did during previous decades.
Source: Jacob Hacker, Yale University; Paul Pierson, UC-Berkeley

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Income and Wealth Inequality
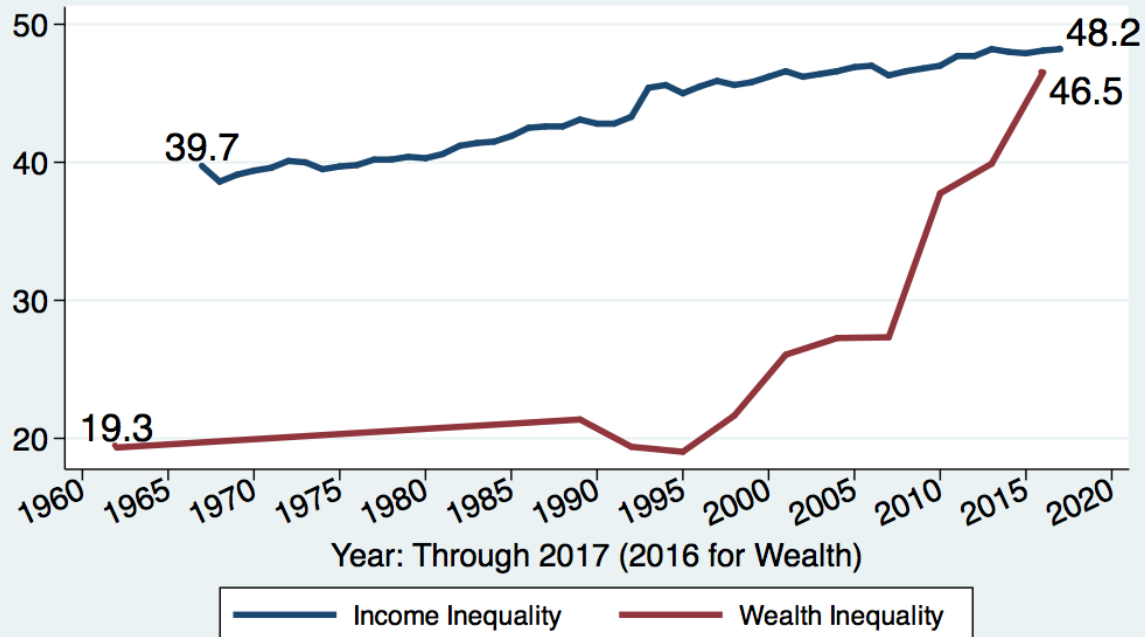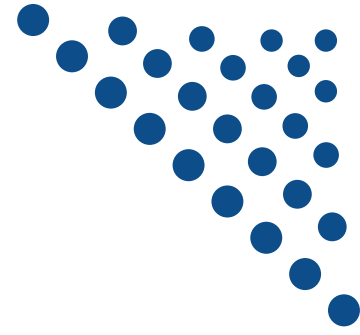
Income Inequality (Gini)

- US: 48.2%
- CA: 48.7%
- Marin: 51.5%

The chart shows values: 39.7 and 48.2 for Income Inequality (blue line), 19.3 and 46.5 for Wealth Inequality (red line), plotted from 1960 through 2020.

X-axis: Year: Through 2017 (2016 for Wealth)

Legend: Income Inequality | Wealth Inequality
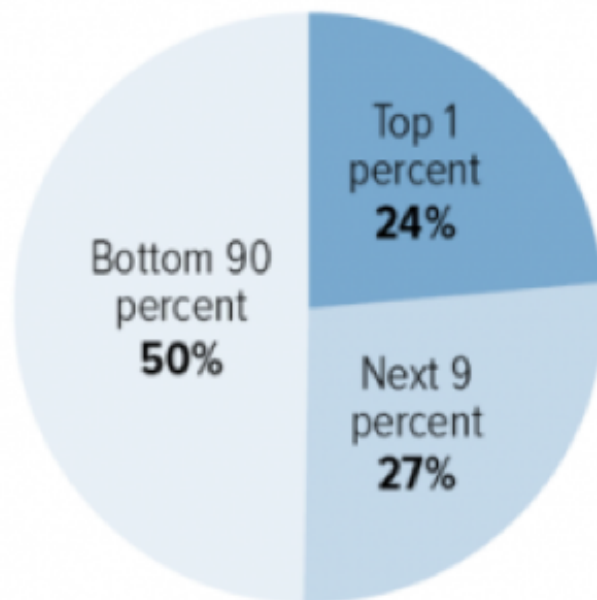
Source: U.S. Census Bureau and Board of Governors
INCOME INEQUALITY is measured by the Gini coefficient.
WEALTH INEQUALITY is the ratio of the mean wealth of the top decile to median overall wealth.
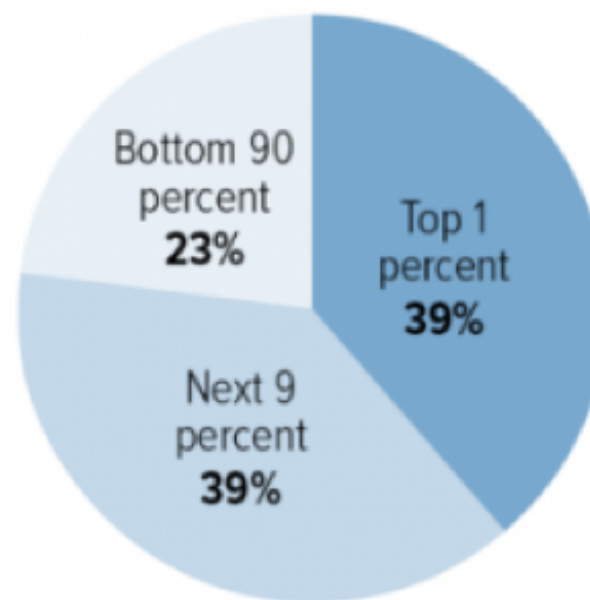Wealth data are only available for 1962, and at three year intervals beginning in 1989.

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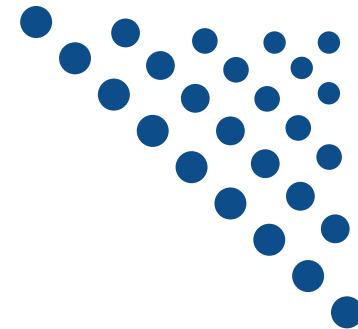
Wealth Inequality Exceeds Income Inequality

Distribution of before-tax income, 2016

Top 1 percent **24%**

Next 9 percent **27%**

Bottom 90 percent **50%**

Distribution of wealth, 2016

Top 1 percent **39%**

Next 9 percent **39%**

Bottom 90 percent **23%**

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Source: Chad Stone, Danilo Trisi, Arloc Sherman, and Roderick Taylor, "A Guide to Statistics on Historical Trends in Income Inequality," Center on Budget and Policy Priorities, Policy Futures, May 15, 2018, page 15, Figure 4.

Where Does Inequality Come From?

- **Labor Characteristics**
  - Demographics
    - Age distribution
  - Personal Choices
    - Educational attainment
    - Effort
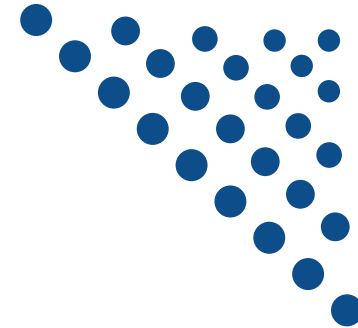   - Priorities
    - Household composition
  - Immigration

- **Market Forces**
  - Technology
  - Changing demand patterns
  - Competition for labor

- **Government Policy**
  - Market influence
  - Redistribution
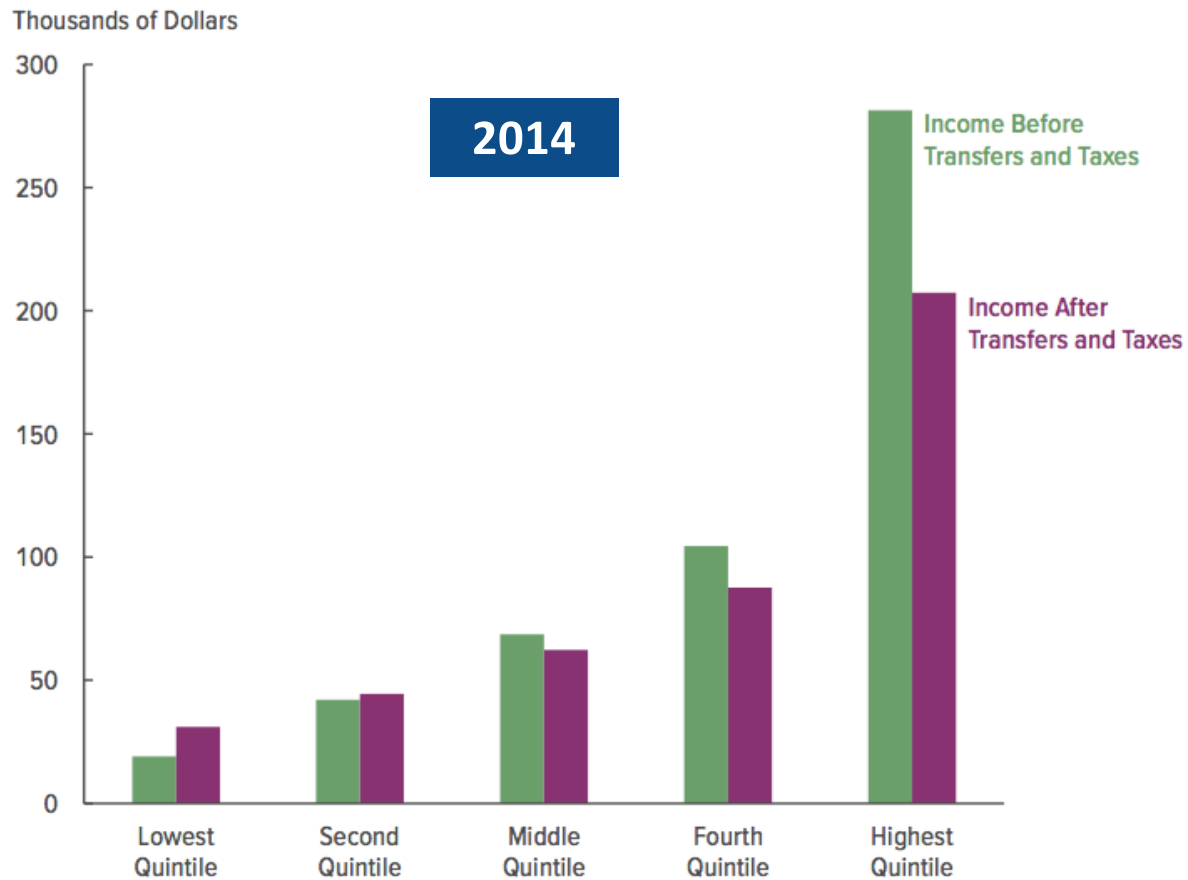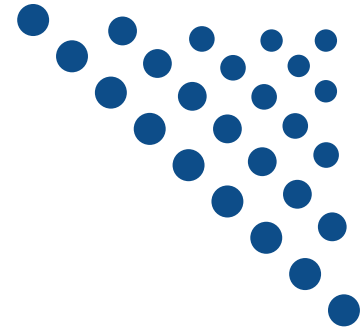
Government Policy and Inequality

- **Market Influence: PRE-distribution**
  - Characteristics of labor
    - o Access to education
  - Effects on labor demand
    - o Market regulation
      - Competition policy
    - o Labor regulations
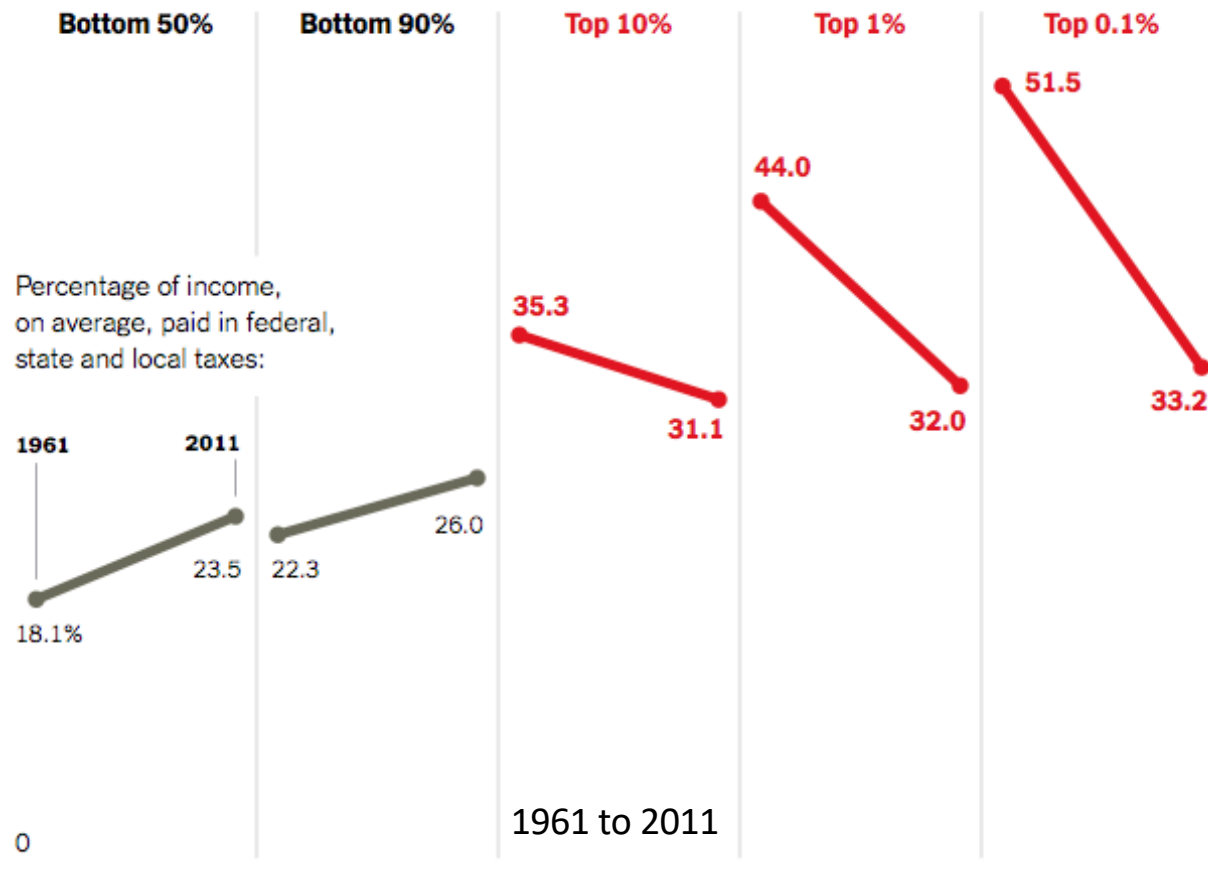   - Minimum wage, overtime, health insurance, etc.

- **RE-distribution**
  - Tax Rates
  - Income support
    - o Direct aid
    - o Food stamps

Tax and Transfer Programs and Inequality

Thousands of Dollars

2014

Income Before Transfers and Taxes

Income After Transfers and Taxes

Lowest Quintile · Second Quintile · Middle Quintile · Fourth Quintile · Highest Quintile

Source: U.S. Congressional Budget Office, "The Distribution of Household Income, 2014", Average Income Before and After Means-Tested Transfers and Federal Taxes, by Income Group, 2014.

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Dramatically Less Progressivity in the Tax Code

Bottom 50%   Bottom 90%   Top 10%   Top 1%   Top 0.1%

Percentage of income, on average, paid in federal, state and local taxes:

1961   2011

18.1%   23.5   22.3   26.0   35.3   31.1   44.0   32.0   51.5   33.2

1961 to 2011

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Market Forces and Inequality

- **Changing demand patterns**
  - Technology
  - Globalization
  - Industry composition
    - PCs instead of typewriters
    - Services instead of goods
    - Professional services instead of personal services

- **Competition in labor markets**
  - Unionization
  - Market concentration

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Where Does Inequality Come From? Summary

- **Labor characteristics**
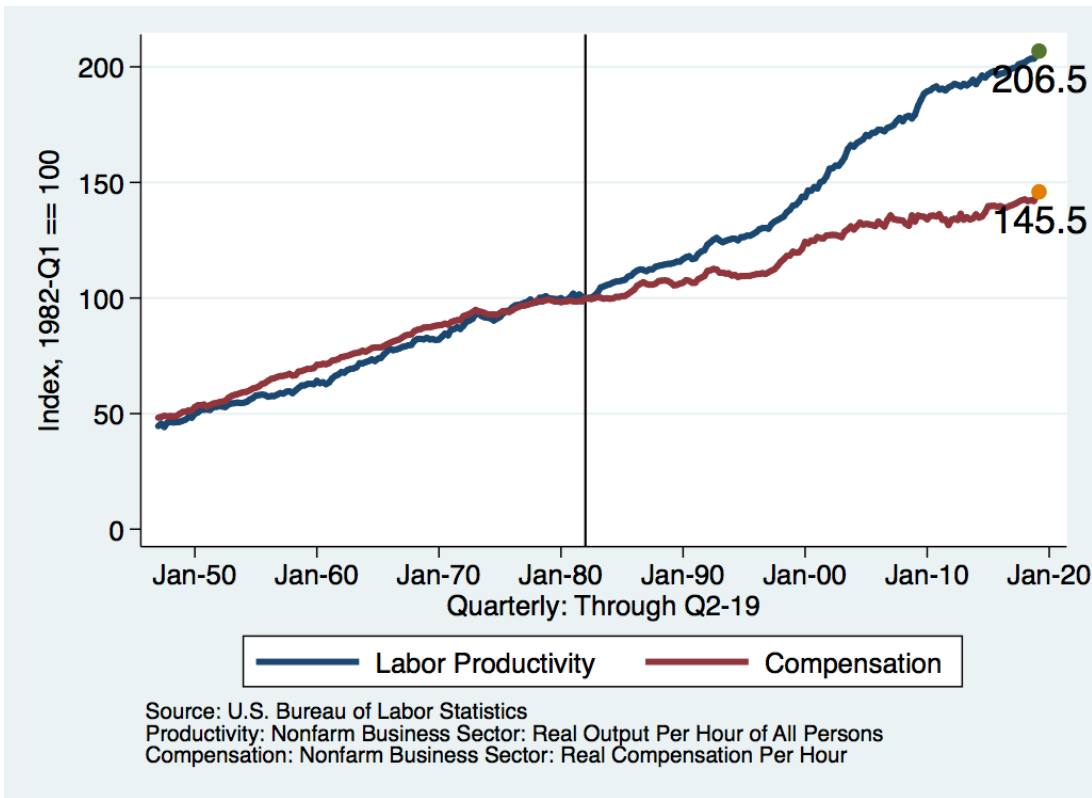 - What do workers bring to the market?

- **Market forces**
  - How does the market value the labor characteristics?

- **Government policies**
  - PRE-distribution – affecting markets
  - Redistribution – affecting incomes

Labor Income is Unhinged from Productivity

Source: U.S. Bureau of Labor Statistics
Productivity: Nonfarm Business Sector: Real Output Per Hour of All Persons
Compensation: Nonfarm Business Sector: Real Compensation Per Hour

Why?

- Declining unionization
- Globalization
- Immigration
- Competition policy
- Cheap technology

Declining Unionization

Percent

- Top 10 Percent Share of Income — 2014
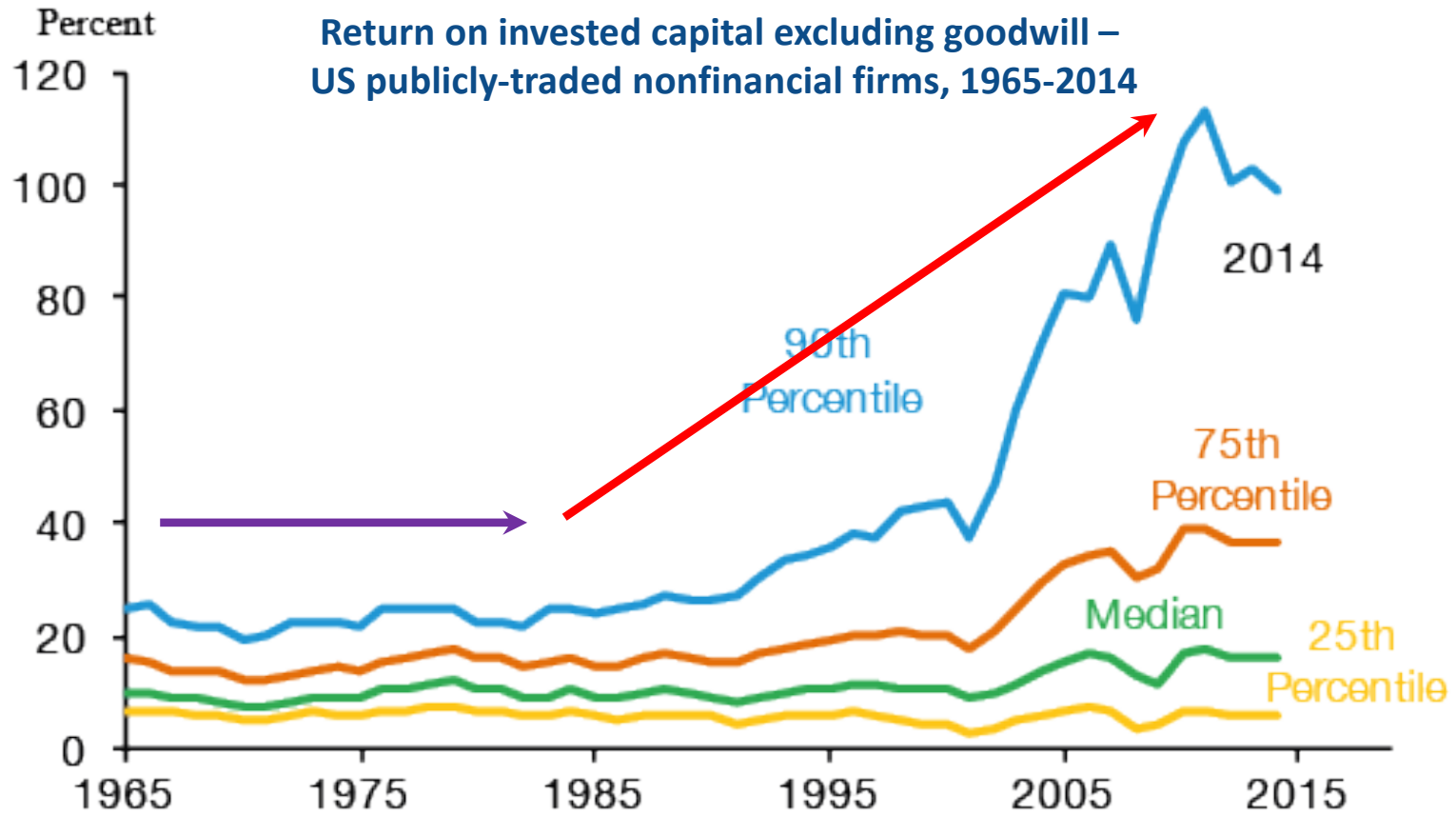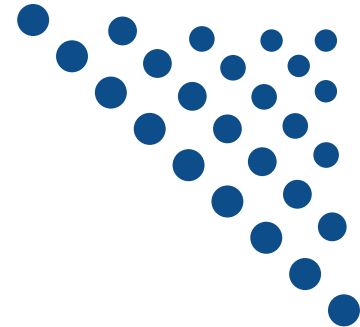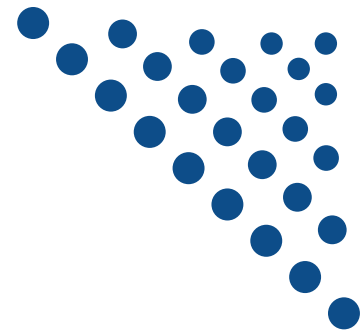- Troy and Sheflin (1985)
- CPS: Membership — 2015
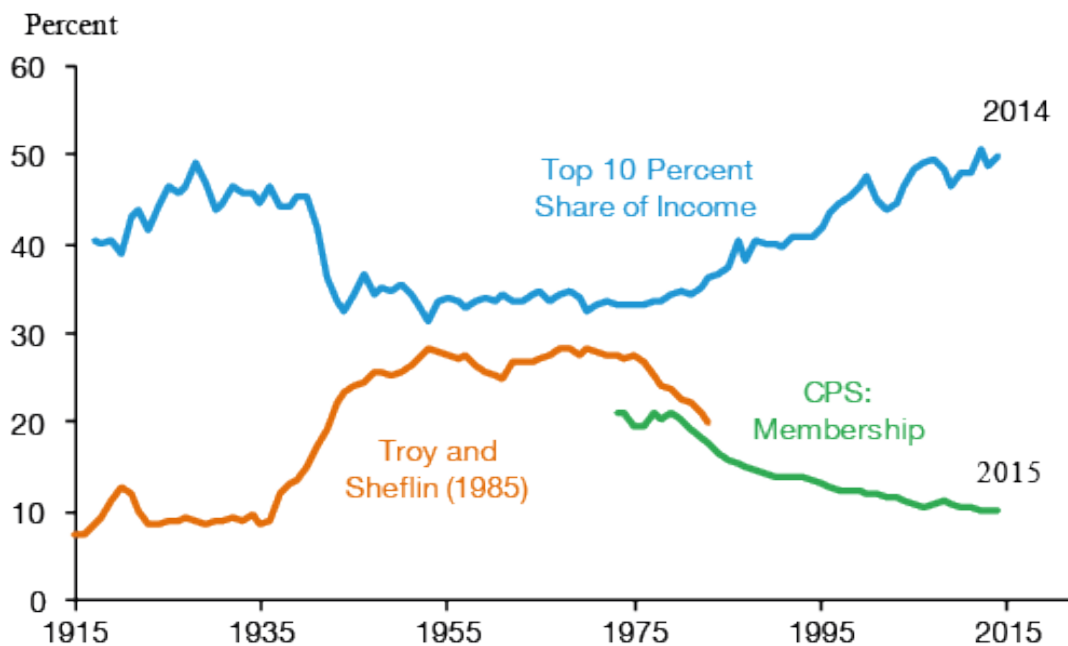
Unionization Rates
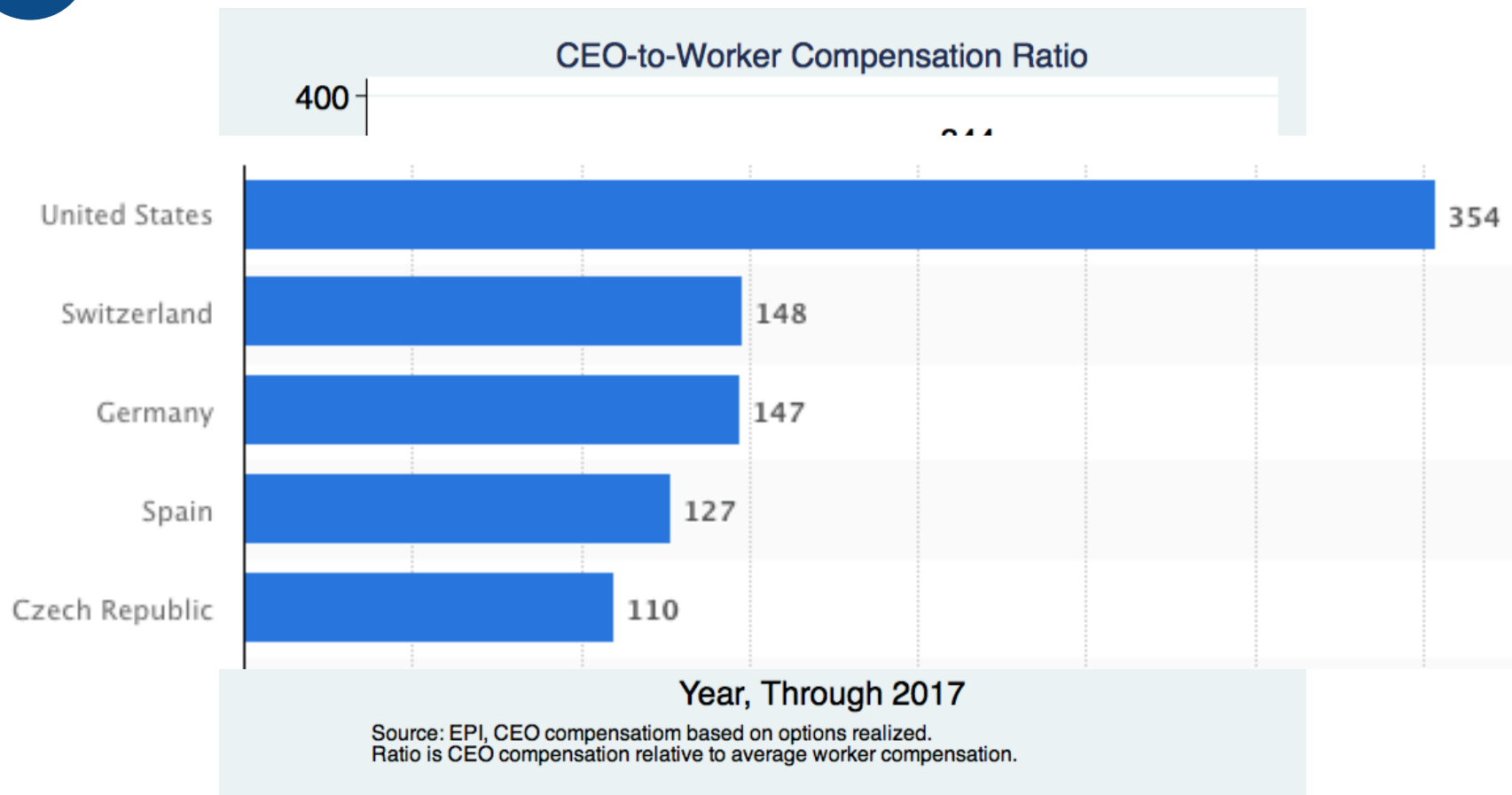- **1983:** 20.1%
- **2018:** 10.5%

Unionization Rates
- **Public:** 33.9%
- **Private:** 6.4%

Source: Jason Furman, "Forms and sources of inequality in the United States", VOX, March 17, 2016, Figure 4.

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Competition in the Economy

**Return on invested capital excluding goodwill –
US publicly-traded nonfinancial firms, 1965-2014**

Percent

90th Percentile

75th Percentile

Median

25th Percentile

2014

Source: Jason Furman, "Forms and sources of inequality in the United States", VOX, March 17, 2016, Figure 6.

CEO Pay Has Been Growing Rapidly

CEO-to-Worker Compensation Ratio

400

Country	Ratio
United States	354
Switzerland	148
Germany	147
Spain	127
Czech Republic	110

Year, Through 2017

Source: EPI, CEO compensatiom based on options realized.
Ratio is CEO compensation relative to average worker compensation.

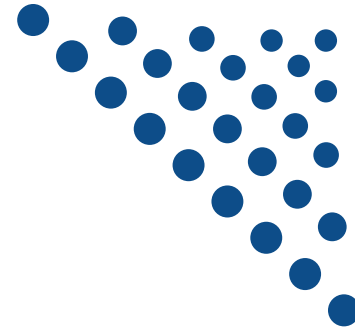# Technology can Hurt Low Income Workers
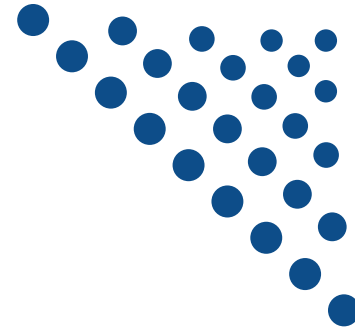
Early on, technology was good to low income workers

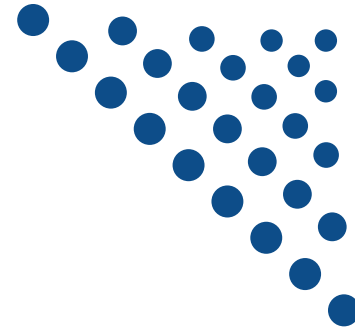Until it was bad for them....

Globalization

- **What is globalization?**
  - Flow of goods, services, capital, and labor across international borders

- **How does it affect inequality?**
  - Through a differential impact on low-skilled workers and hence their wages

  - For the United States, globalization is thought to lower the wages of low skilled and hence low-wage workers relative to those of high-skilled workers

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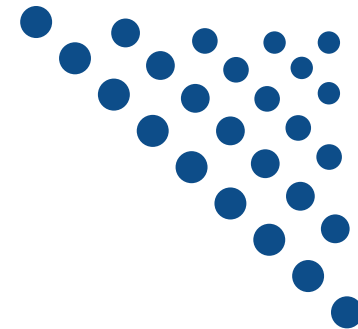# What is driving increasing inequality?

- **Primary drivers:**
  - Technology
  - Globalization
  - Institutions

- **These drivers can also influence personal choices in ways that affect measured income inequality.**
  - For example, educational choices or labor force participation

Why Does Inequality Matter?

- **Too little inequality can:**
  - Reduce individual motivation
  - Slow economic growth
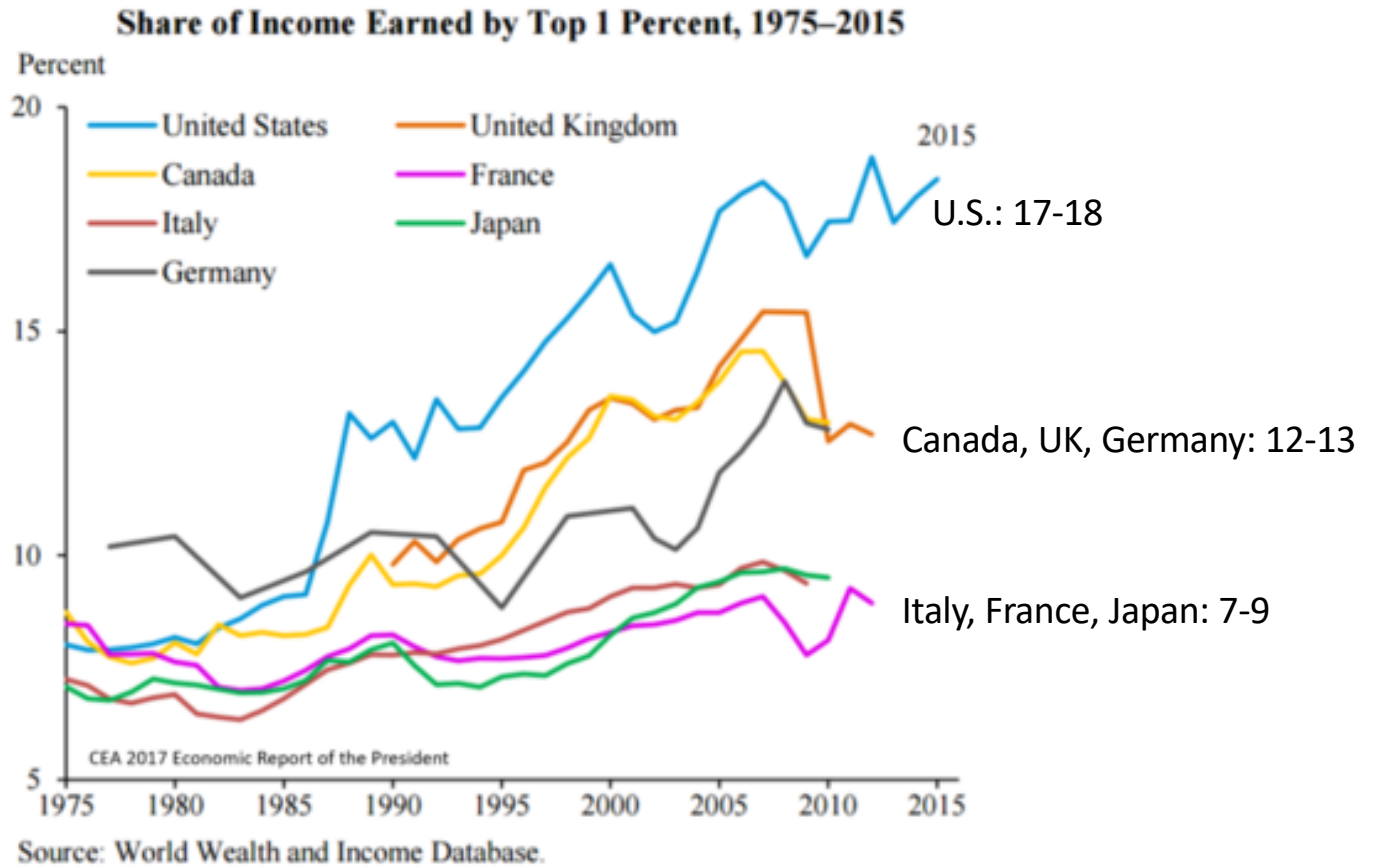
- **Too much inequality can:**
  - Reduce individual motivation
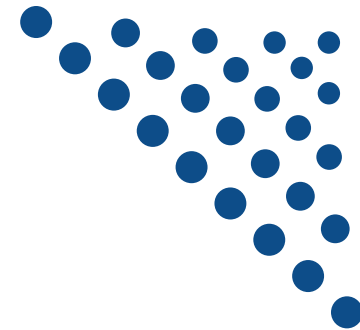 - Slow economic growth

- **Too much inequality may also:**

  - Divide society
  - Distort political environment
  - Reduce political participation

  - Reduce investments in public goods
    - Education
    - Environmental protection

An International Perspective: Comparables

Share of Income Earned by Top 1 Percent, 1975–2015

Percent

- United States
- United Kingdom
- Canada
- France
- Italy
- Japan
- Germany

2015

U.S.: 17-18

Canada, UK, Germany: 12-13

Italy, France, Japan: 7-9

CEA 2017 Economic Report of the President

Source: World Wealth and Income Database.

Addressing Inequality: Is It a Problem?

- **Why it might be a problem.**
  - Economic issues (*Efficiency*)
    - o There is evidence that at some level, increased inequality slows economic growth.
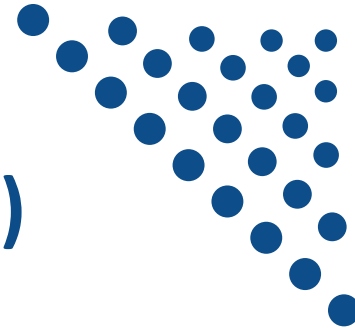   - o Or, inequality concentrates resources among investors.
  - Noneconomic issues (*Equity*)
    - o Values, ethics and morals will drive individual evaluations of the level of inequality.
      - E.g., inequality is primarily a function of market outcomes, so should be left alone.
      - Or, a solid middle class is important for maintaining a civil society, which runs contrary to a high degree of inequality.

- **Suppose you think it's a problem. How might it be addressed?**

Addressing Inequality:
# Immediately Available Policy Solutions (1/2)

- **RE-distribution**
  - Tax and transfer programs

- **PRE-distribution**
  - Strengthen labor unions
  - Minimum wages
  - Collective bargaining
  - Other policies that favor labor over business owners

Addressing Inequality:
Immediately Available Policy Solutions (2/2)

- **Other**
  - Reverse trends in market power

- **Locally**
  - Employment services: job training, interview skills, or assistance with day-to-day issues, such as child care
  - Cognizance of the potential for technologies to affect worker/employer power dynamics
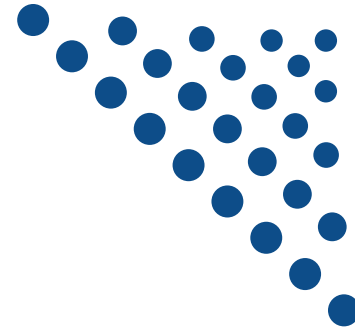   - Uber, Lyft, etc.

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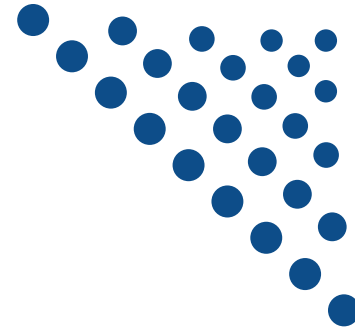# Addressing Inequality: Long Term
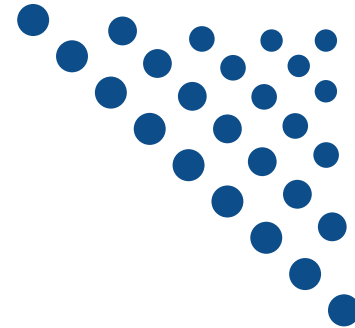
- **It's all about access to resources:**
  - Education, in particular
    - Improve public education
    - Reduce disparities in quality of public education
    - Improve counseling in low-income schools
      - With respect to college – paths to success and funding
  - Investments are needed in early education, not later
    - Universal pre-K
    - Upgrade quality of elementary schools in low-income areas

What to do About Inequality?

- **Nothing?**

- **Redistribution?**

- **PRE-distribution?**

- **Access to resources?**

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Tension in Policy Solutions

- **Is it possible to increase growth at the same time that you reduce income inequality?**
  - Common refrain among some that government intervention in the economy is always and everywhere bad for growth.

- **Possibly: expanding equality of access promotes the full utilization of resources.**
  - Expanding equality of access requires resources likely from the well-to-do.

Most Prominent Policy Proposals
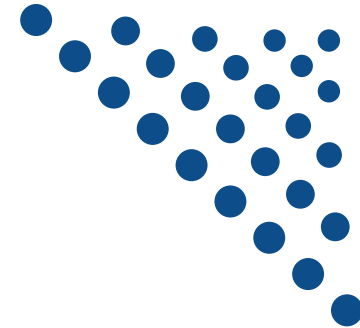
- **Redistributions:**
  - Raising the top marginal tax rate to 70%.
  - 2% annual tax on wealth.

- **Other:**
  - Minimum wage

- **Primary concern:**
  - How does it distort market decisions?
   - o Investments
    - o Labor supply

Summary

- **Income inequality is clearly increasing.**
  - The economy is clearly favoring owners of productive resources over labor.

- **The causes appear to be largely driven by:**
  - The market – technology, competition, and trade
  - Changing institutions.

- **Open questions are:**
  - To act or not to act?
  - If so, how?

- **The level of income inequality is a policy choice.**
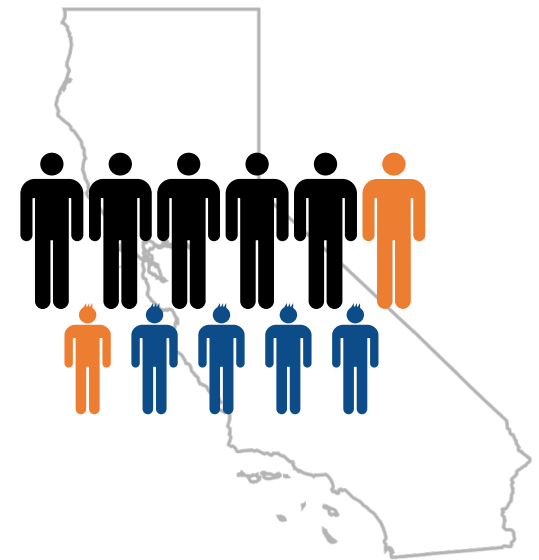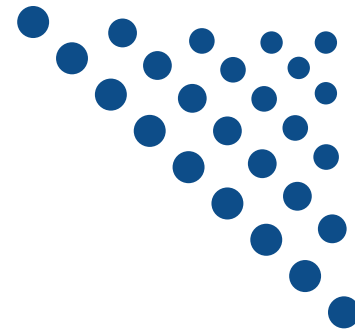
Thank you!

Any Questions?
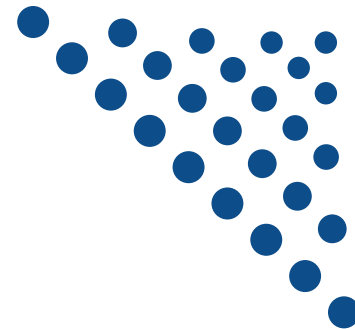
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