Is rising income inequality a serious problem?

Lane Kenworthy

Fall 2011

Outline

Inequality rising

Public opinion

Should we worry?

- Economic growth
- Employment
- The safety net
- Incomes of the poor
- Middle-class living standards
- Educational attainment
- Family
- Health
- Safety
- Democracy

Inequality rising

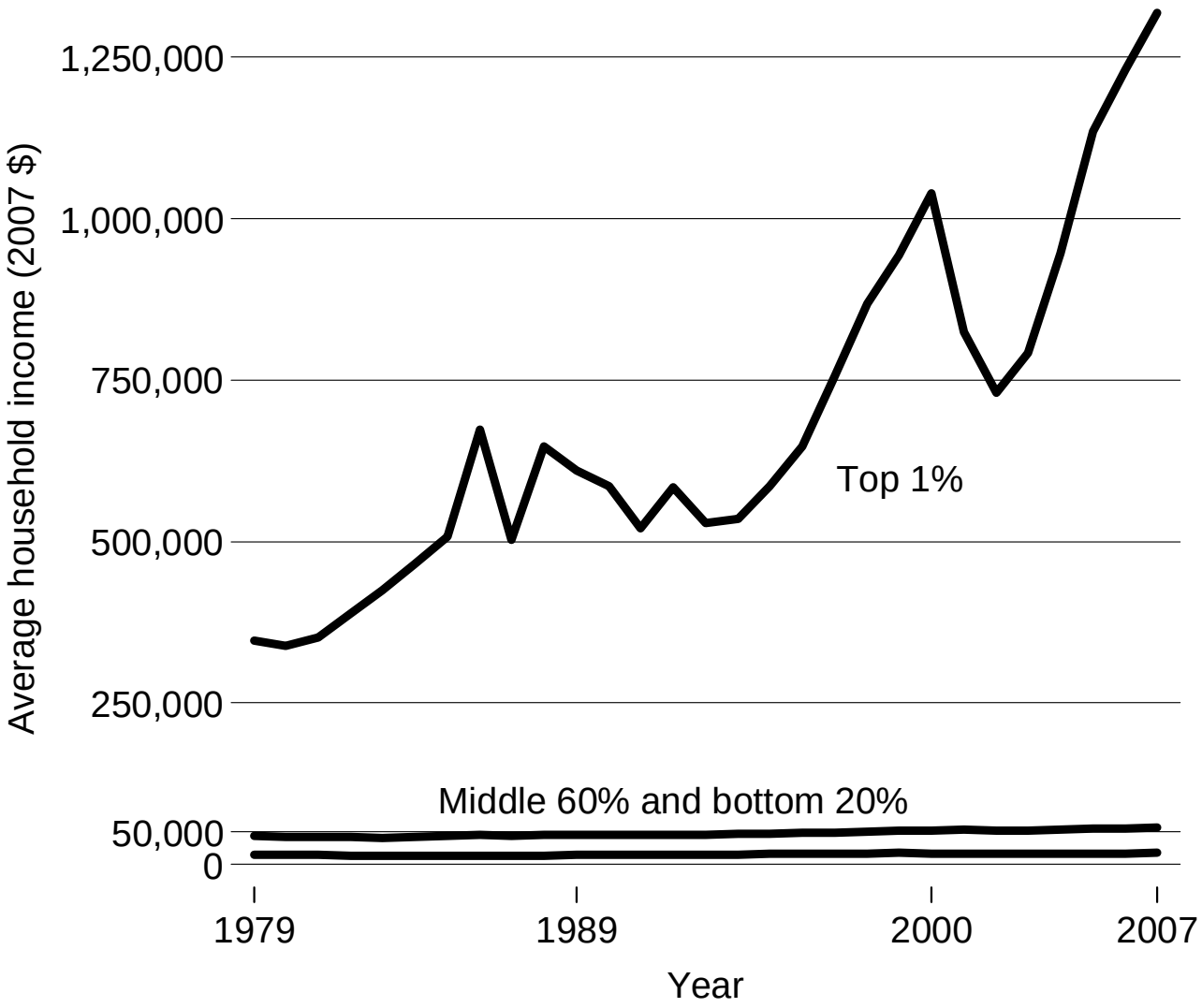
Inequality rising

From the mid-1940s to the mid-1970s, income inequality in the United States decreased a little

Since the mid-to-late 1970s, it has increased sharply

The rise has two components:

1. Slow income growth for the bottom two-thirds
2. Soaring incomes at the top



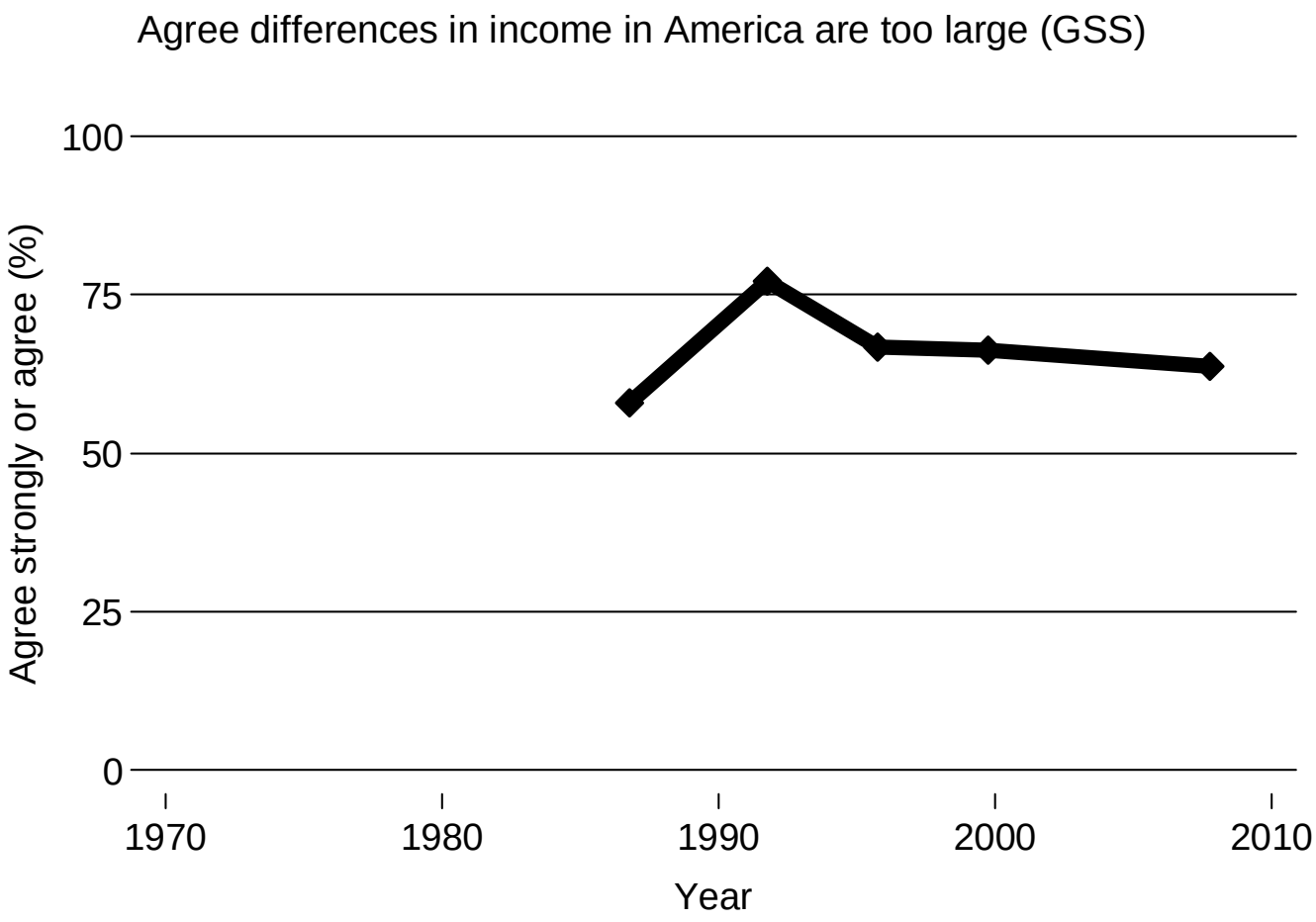
Household posttranster-posttax income. The data are averages within each group. Incomes in 1979 and 2007: $15,500 and $17,500 for the bottom 20%; $44,000 and $57,000 for the middle 60%; $350,000 and $1,300,000 for the top 1%. The top 1% includes 1.1 million households. The data are generated by merging survey (CPS) data with tax (IRS) records. Data source: Congressional Budget Office, www.cbo.gov/publications/collections/collections.cfm?collect=13.

Public opinion

Public opinion

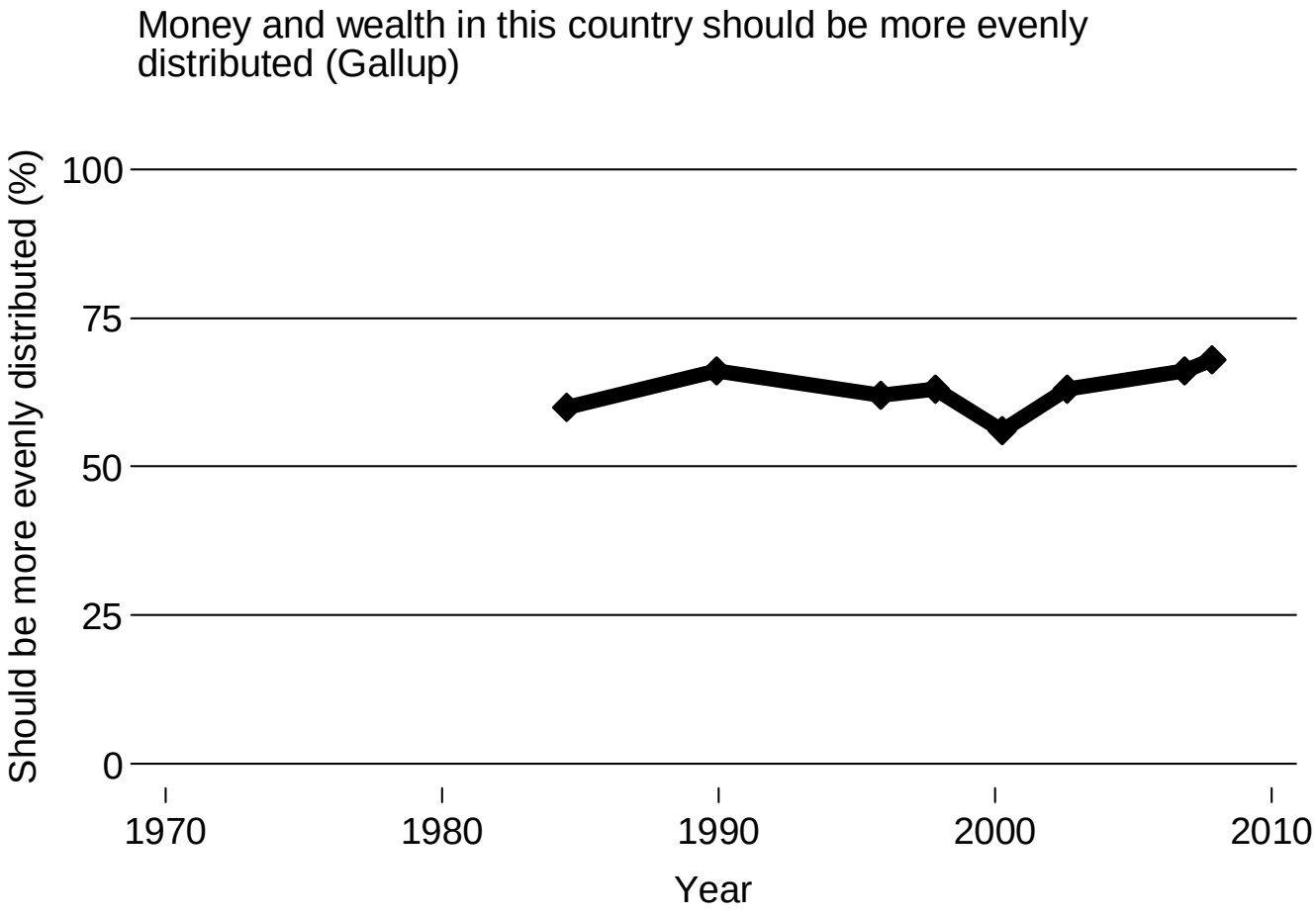
A majority of Americans think income inequality is too high

Public opinion



Other response choices: neither, disagree, disagree strongly. Data source: General Social Survey data, variable incgap, sda.berkeley.edu/ archive.htm.

Public opinion



Other response choices: distribution is fair, no opinion. Data source: Gallup.

Public opinion

But we don't have a good understanding of exactly why they'd prefer less income inequality

Should we worry?

Is rising income inequality bad for us?

Rising income inequality could worsen

- Economic growth
- Employment
- The safety net
- Incomes of the poor
- Middle-class living standards
- Educational attainment
- Family
- Health
- Safety
- Democracy

WHY GREATER EQUALITY MAKES SOCIETIES STRONGER

THE SPIRIT LEVEL

RICHARD WILKINSON AND KATE PICKETT

How can we assess this hypothesis?

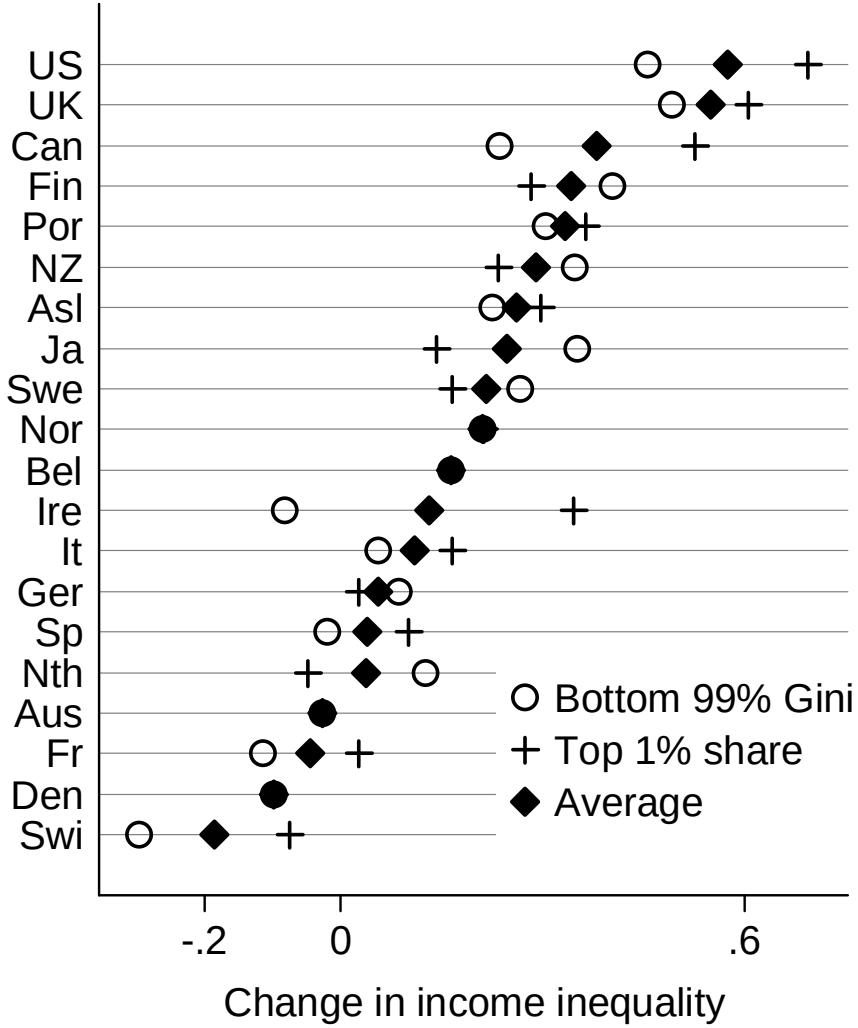
Compare

1. Within the United States over time
2. Across countries at a given point in time
3. Change over time across countries

The third strategy is the best. It's the closest we can get to an experiment

The question: Have outcomes worsened more (or improved less) in countries with bigger increases in income inequality?

Change in income inequality, 1979 to 2007



1. Bad for economic growth?

Rising income inequality might reduce economic growth by

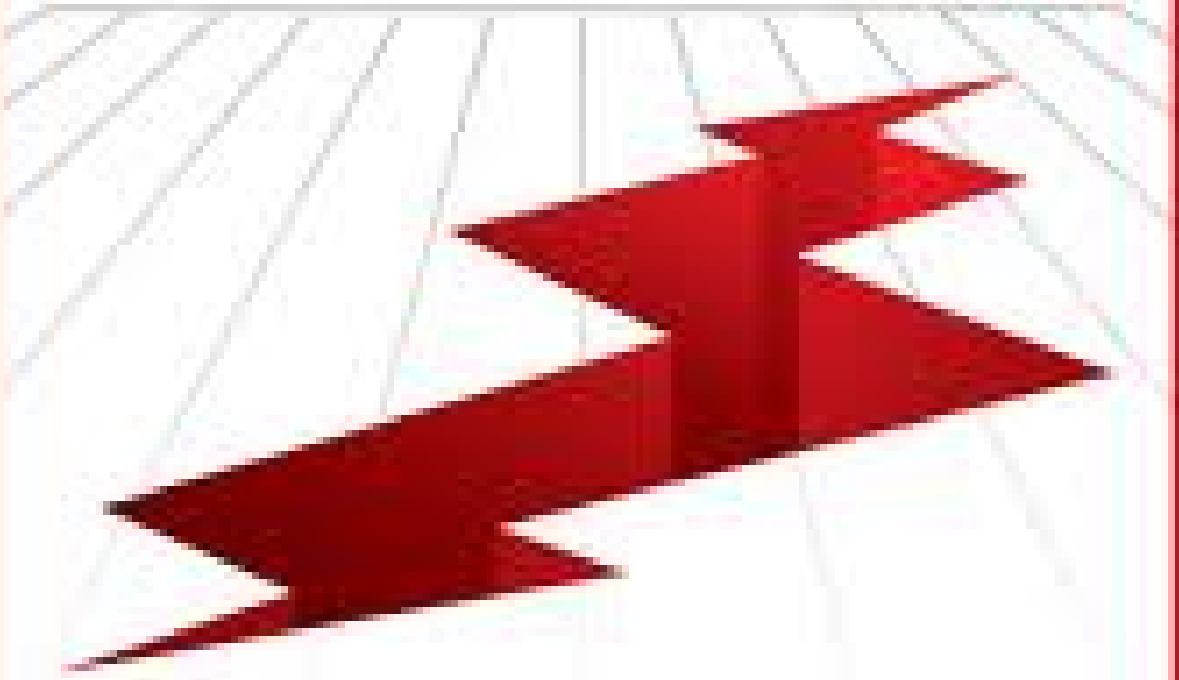
- Reducing consumption: the rich spend a smaller share of their income than the poor
- Reducing work effort: diminished sense of fairness

NATIONAL BESTSELLER

AFTERSHOCK

THE NEXT ECONOMY & AMERICA'S FUTURE

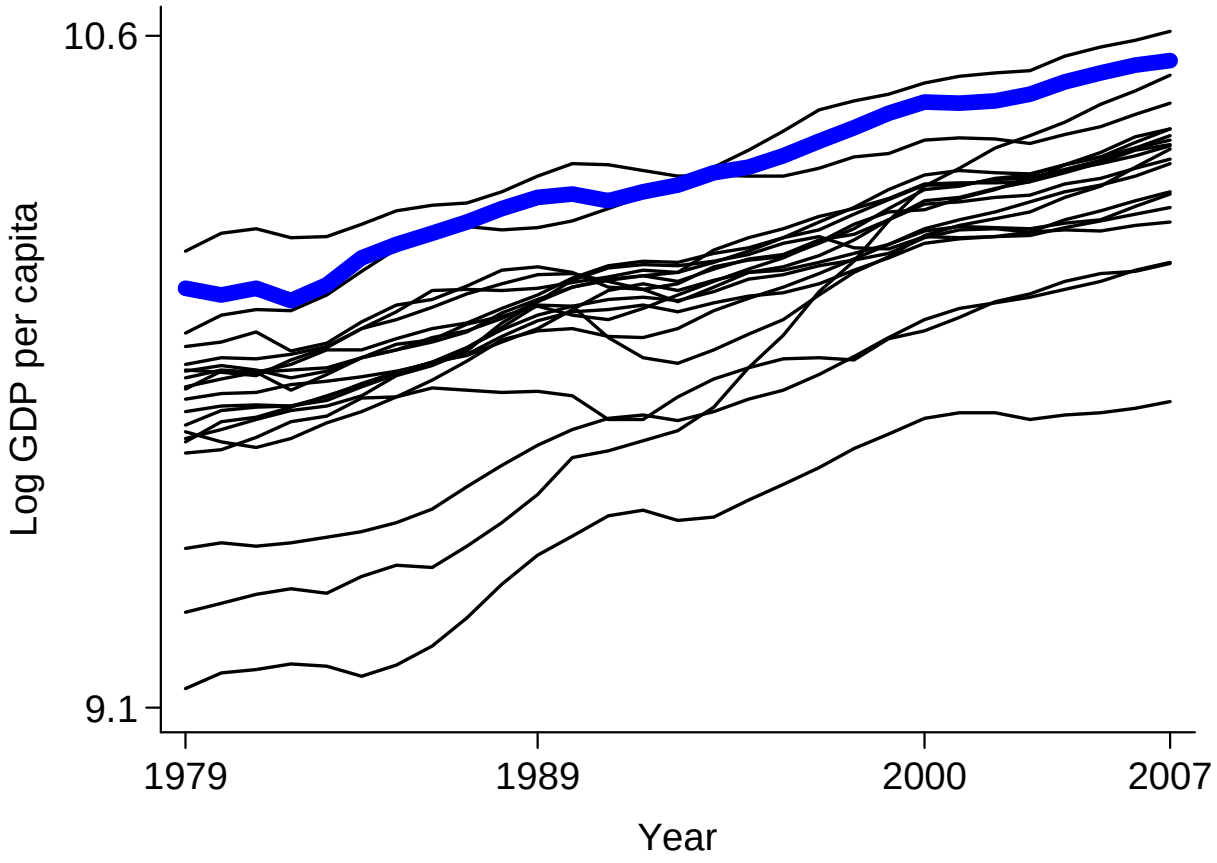
UPDATED



ROBERT B. REICH

"Important and well executed. . . . Reich is fluent and fearless."
—THE NEW YORK TIMES BOOK REVIEW

1. Bad for economic growth?



Source: Christopher Jencks and Lane Kenworthy, *Should We Worry About Inequality?* (forthcoming), using data from the OECD.

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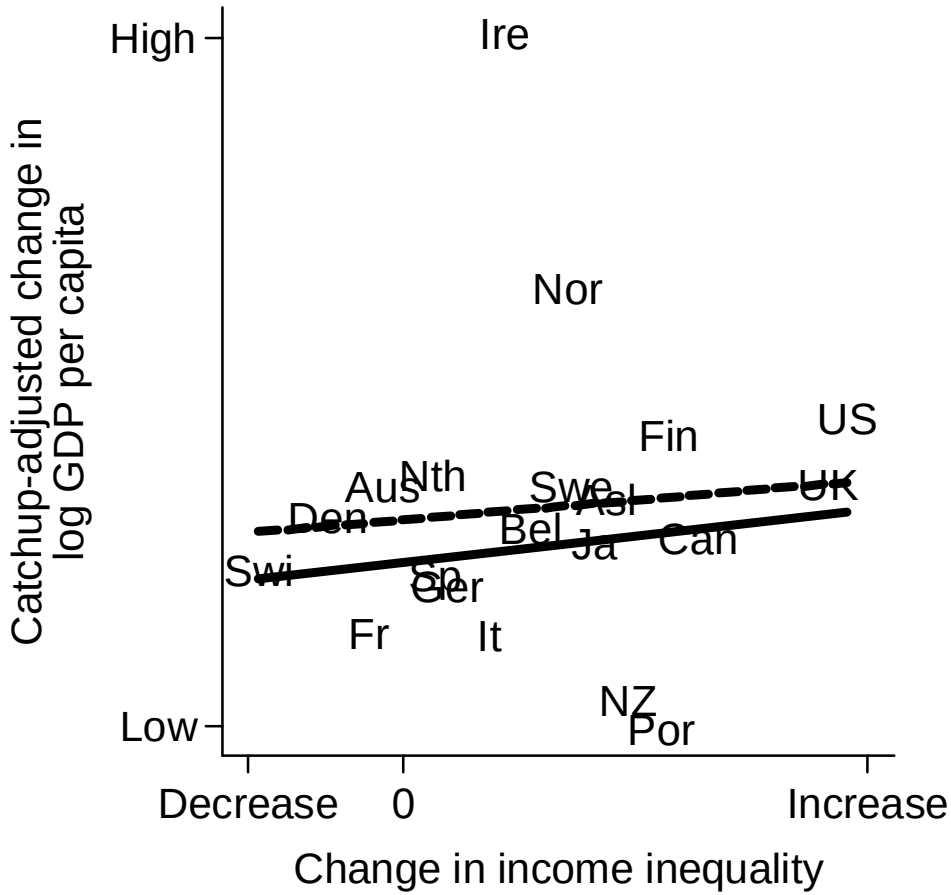


Source: Christopher Jencks and Lane Kenworthy, *Should We Worry About Inequality?* (forthcoming), using data from the Luxembourg Income Study Database, the World Top Incomes Database, and the OECD.

1. Bad for economic growth?

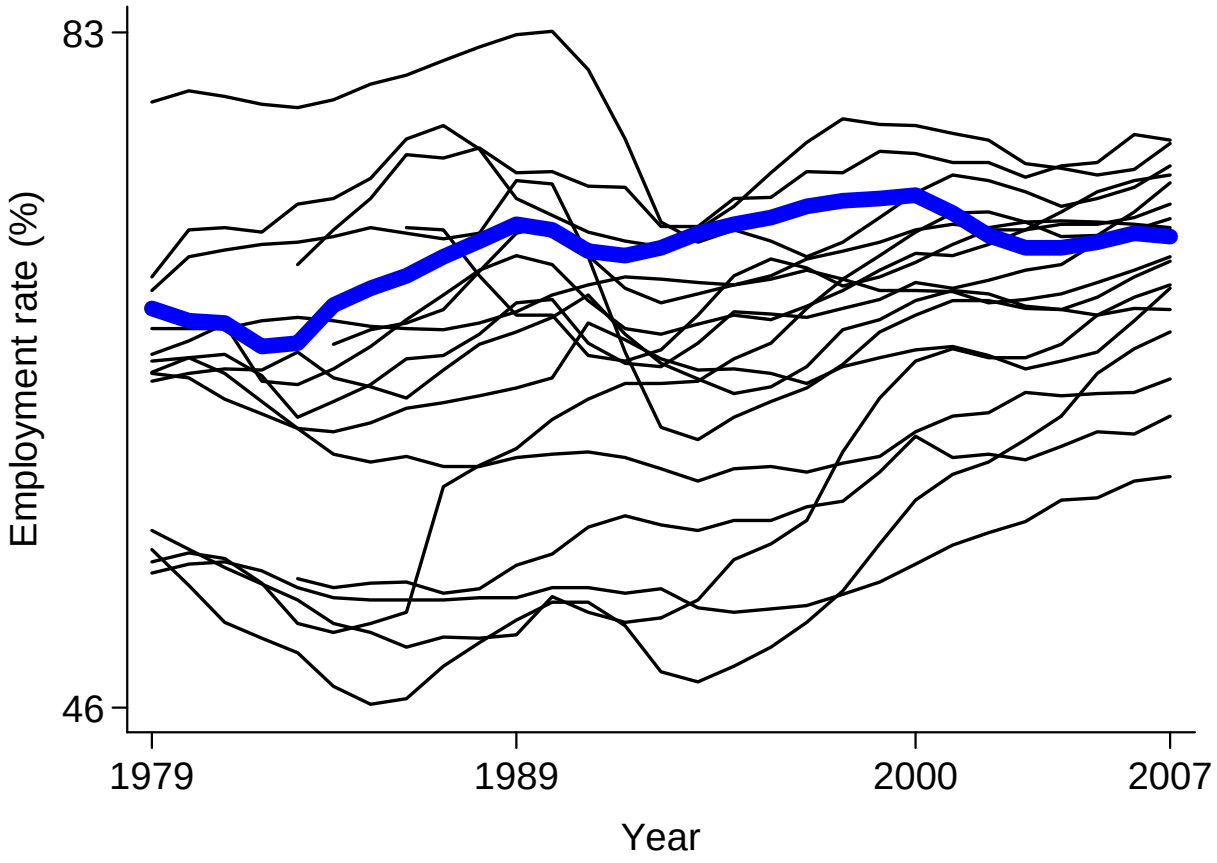
Probably not

2. Bad for employment?

Rising income inequality might hurt employment by

Reducing consumption (same as for economic growth)

2. Bad for employment?



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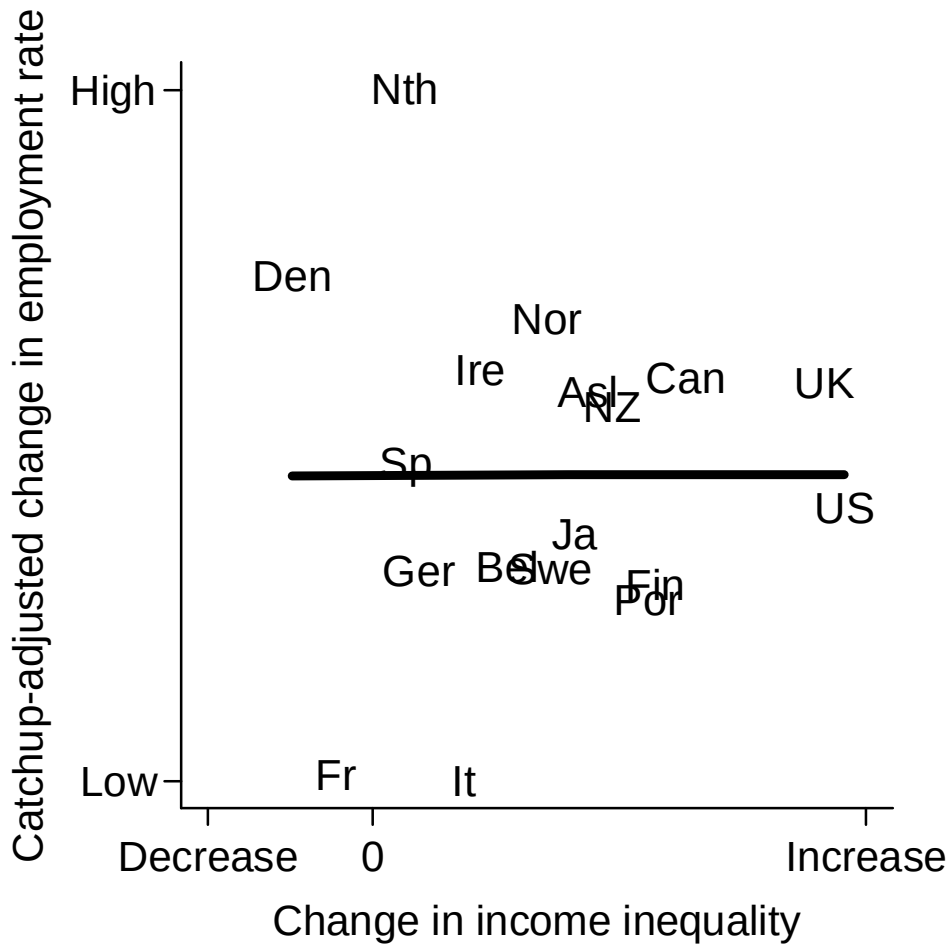

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2. Bad for employment?

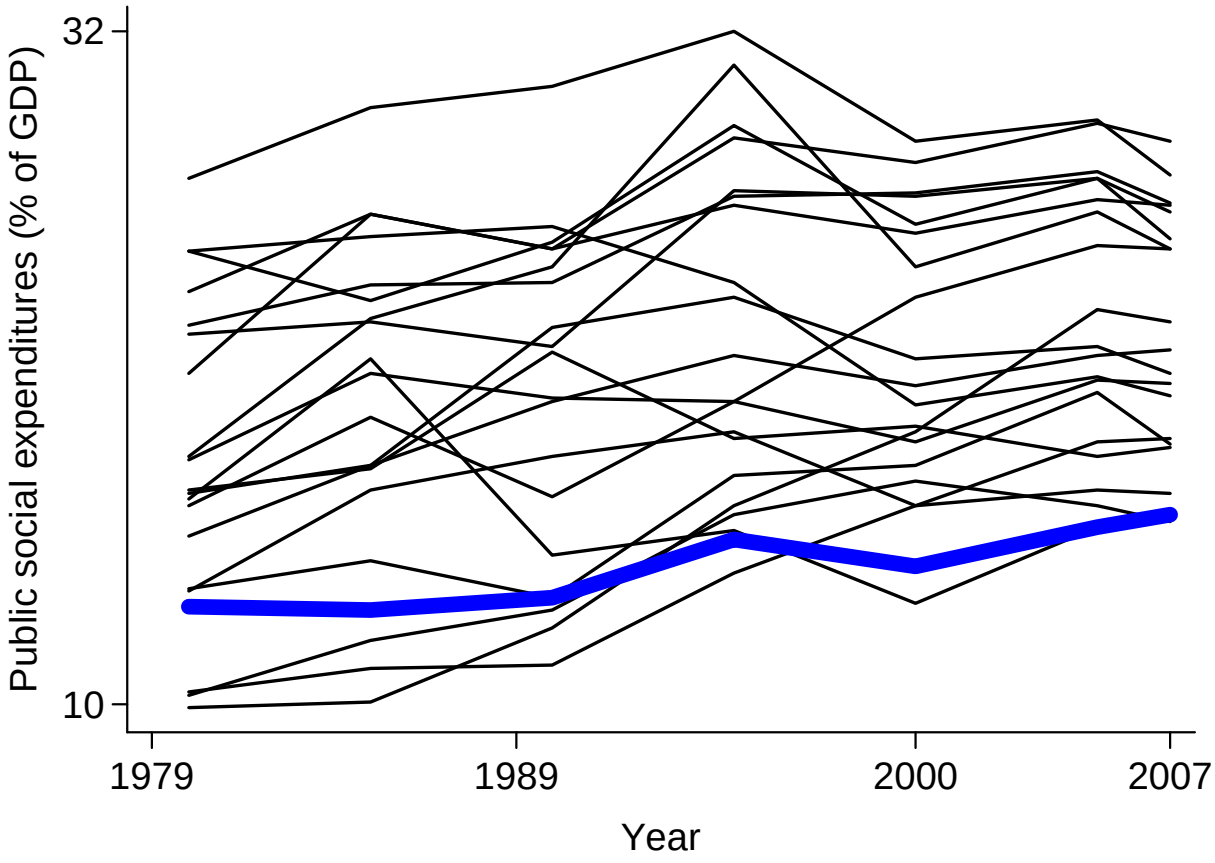
Probably not

3. Bad for the safety net?

Rising income inequality might weaken the public safety net (social programs) by

- Increasing the incentive and capacity of the rich to push for reduced taxation

3. Bad for the safety net?



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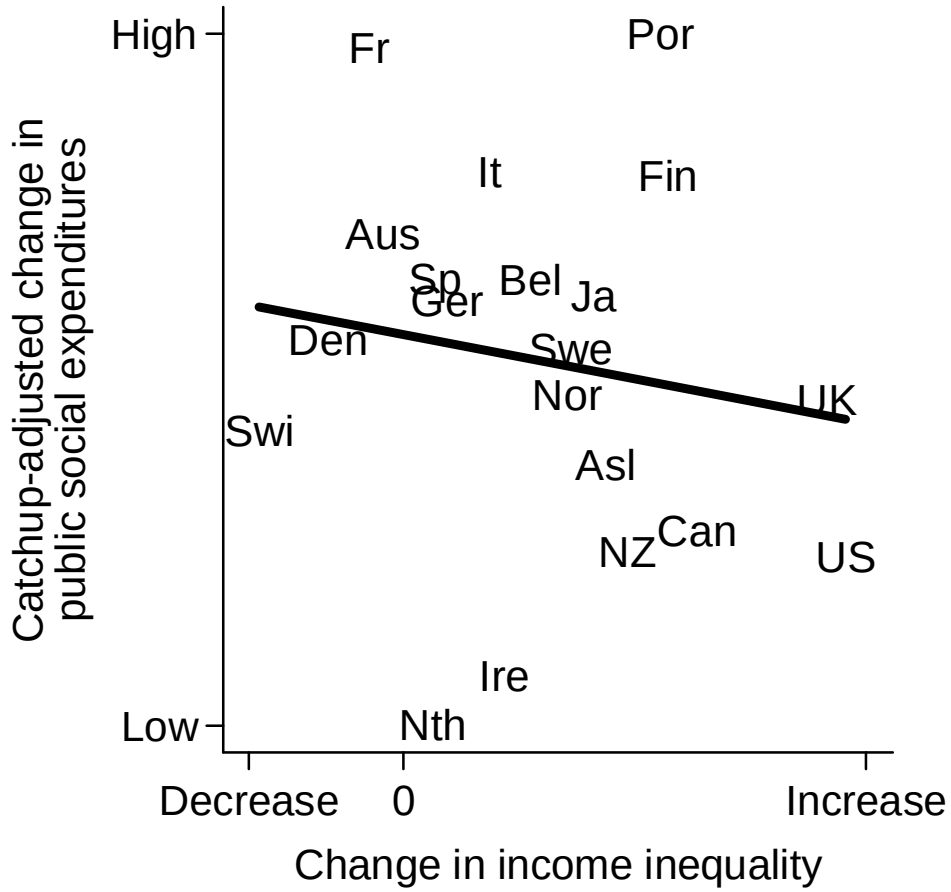

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3. Bad for the safety net?

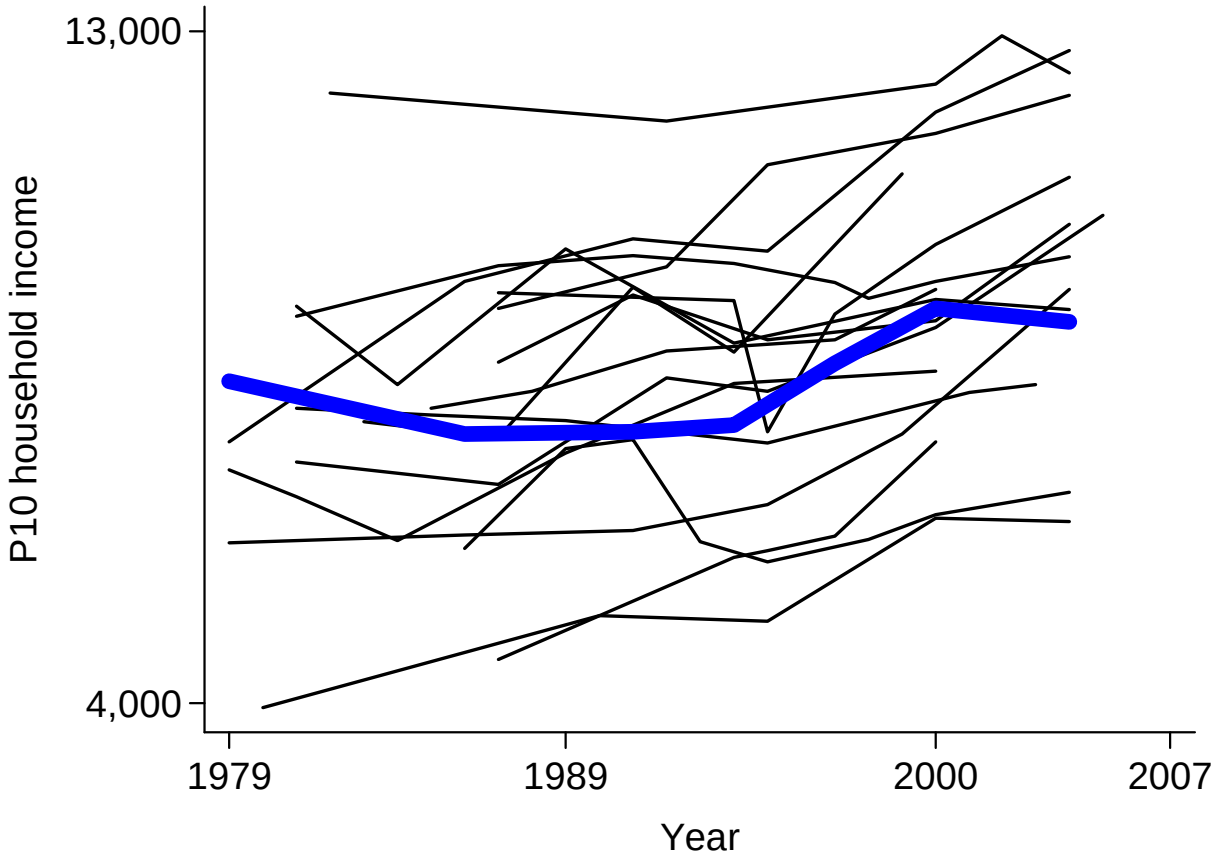
Probably not

4. Bad for incomes of the poor?

Rising income inequality might reduce income growth for low-end households by

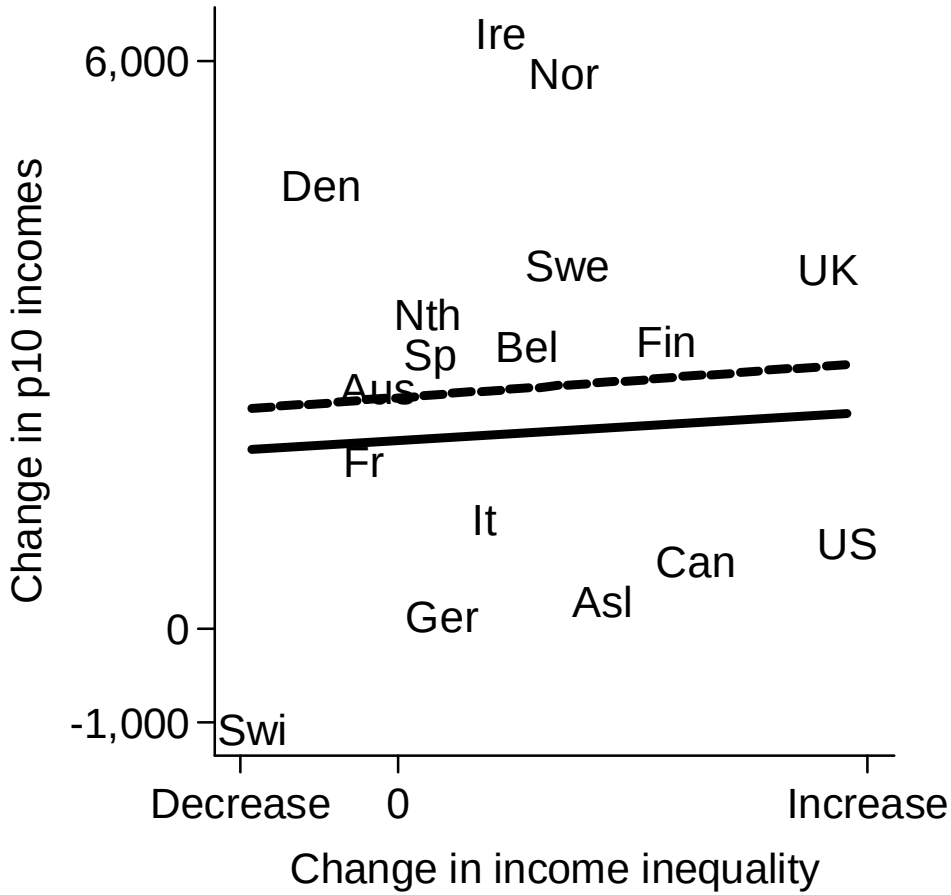
- Reducing the share of economic growth that trickles down to the bottom

4. Bad for incomes of the poor?



The dollar amounts on the vertical axis refer to a household with one person; for a household with four persons, multiply by two. Source: Christopher Jencks and Lane Kenworthy, *Should We Worry About Inequality?* (forthcoming), using data from the Luxembourg Income Study Database.

4. Bad for incomes of the poor?



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4. Bad for incomes of the poor?

Probably not

4. Bad for incomes of the poor?

Why not?

Where low-end incomes have increased, that typically has been a result of increases in net government transfers (transfers received minus taxes paid)

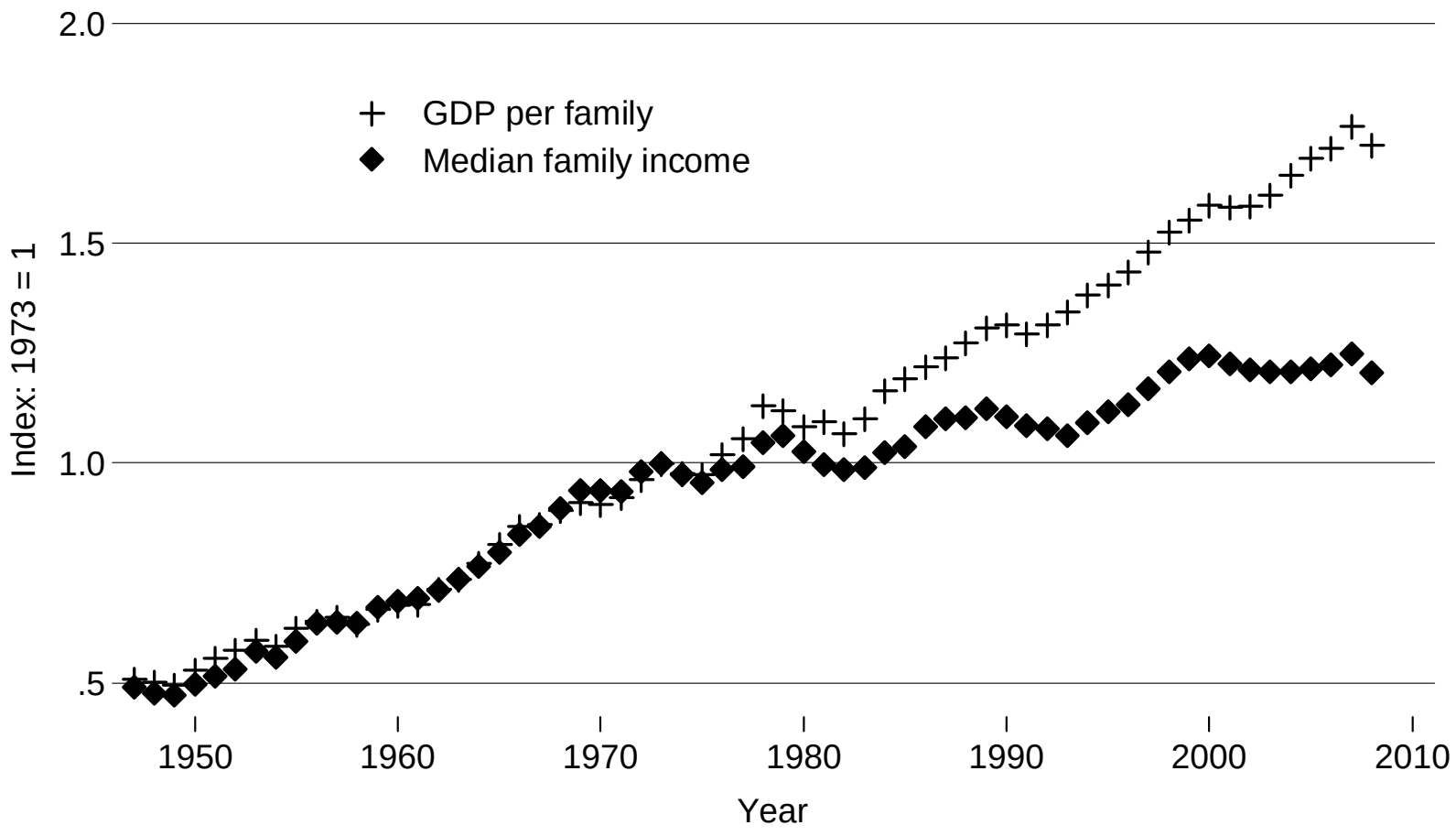
- Government transfers to the poor have increased in some rapidly-rising-inequality countries but not in others
- Government transfers to the poor have increased in some no-rise-in-inequality countries but not in others

5. Bad for middle-class incomes?

Rising income inequality might reduce income growth for middle-class households by

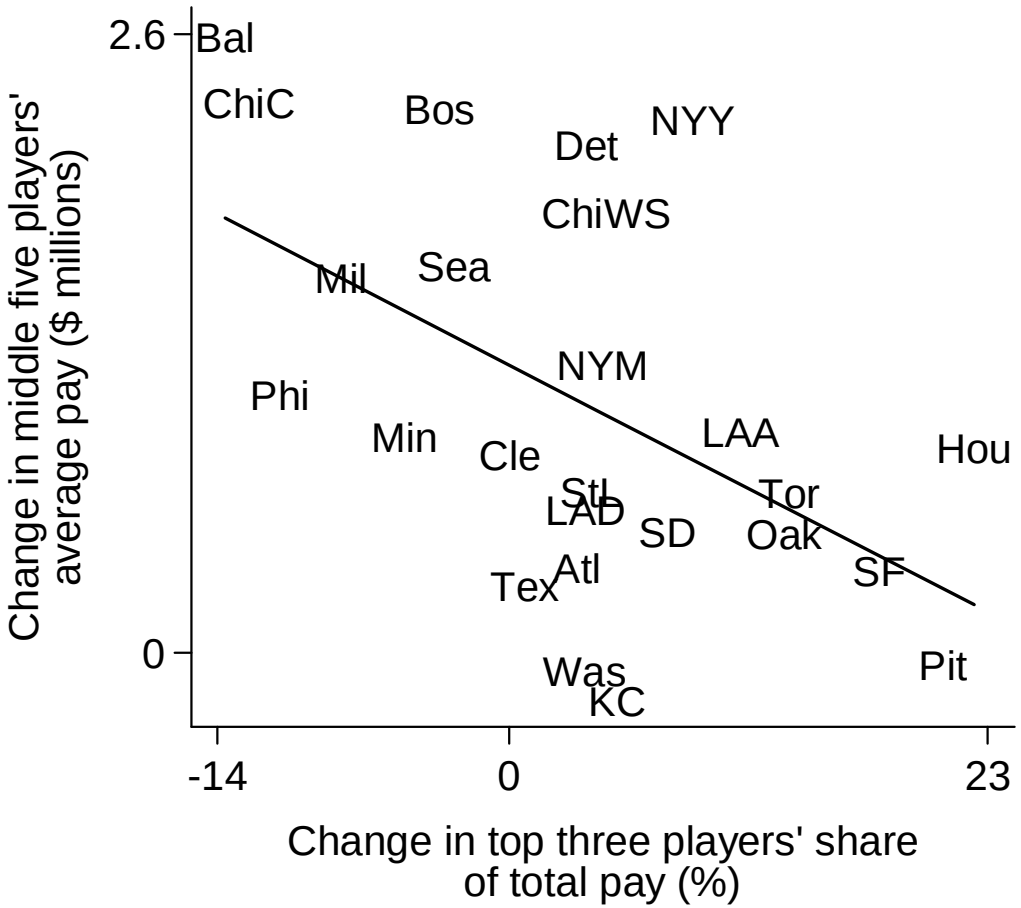
- Reducing the share of economic growth that trickles down to the middle

5. Bad for middle-class incomes?



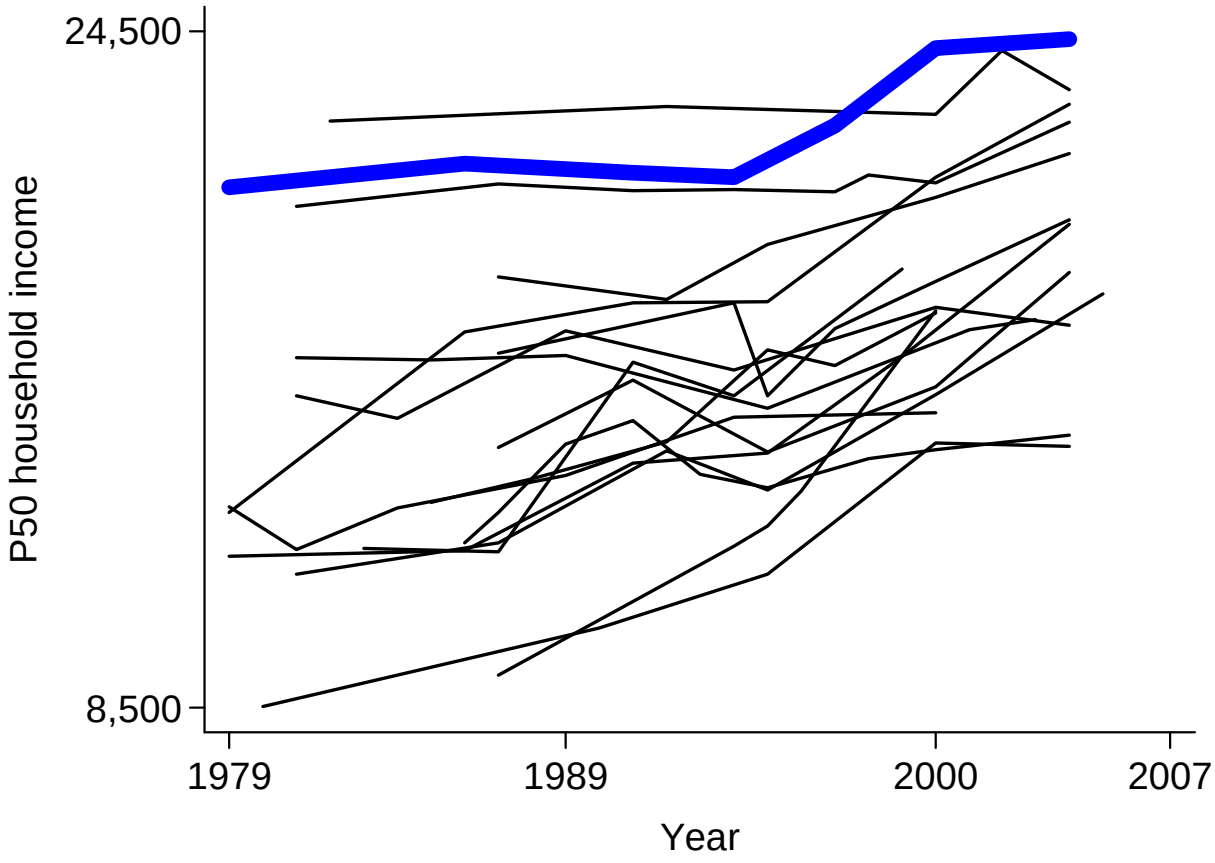
Inflation adjustment for both GDP and family incomes is via the CPI-U-RS. Data source: Bureau of Economic Analysis and Census Bureau.

5. Bad for middle-class incomes?



Major league baseball teams. The period covered is 1989 to 2007. Pay is in 2007 dollars. Data source: baseball-almanac.com.

5. Bad for middle-class incomes?



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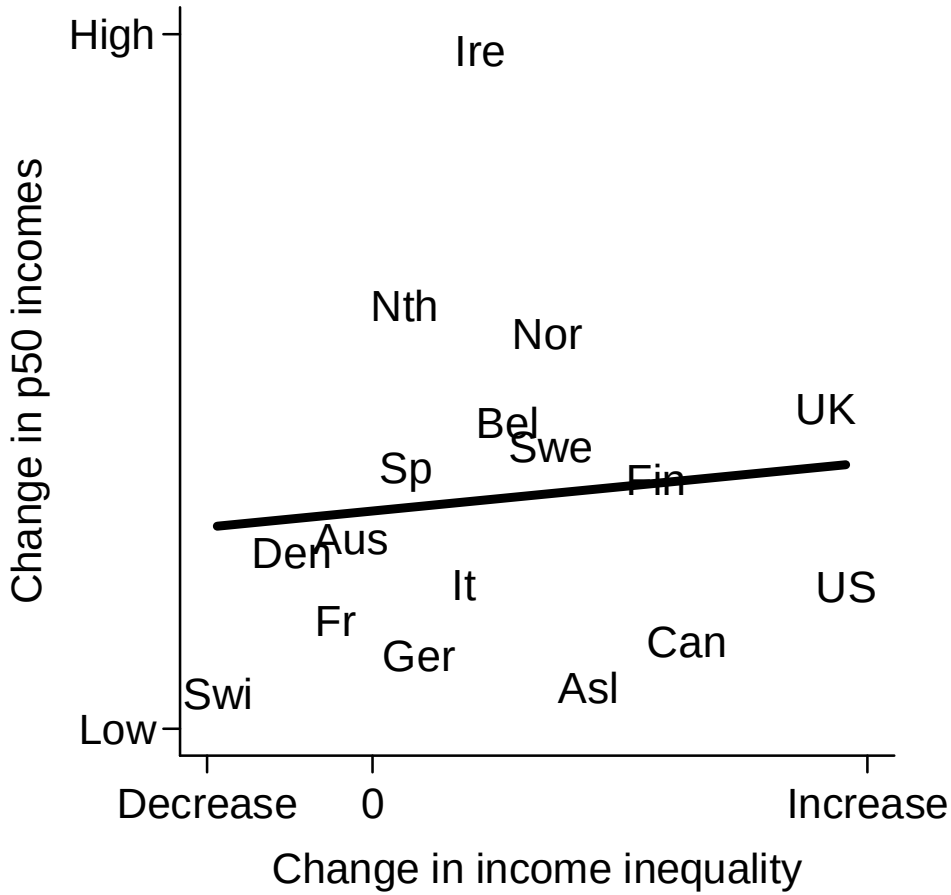

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5. Bad for middle-class incomes?

Probably not

5. Bad for middle-class debt?

Rising income inequality might increase middle-class debt because

- The rich have more money to spend. They build bigger, fancier houses
- Middle-class families try to keep up. To do so, they have to take on more debt

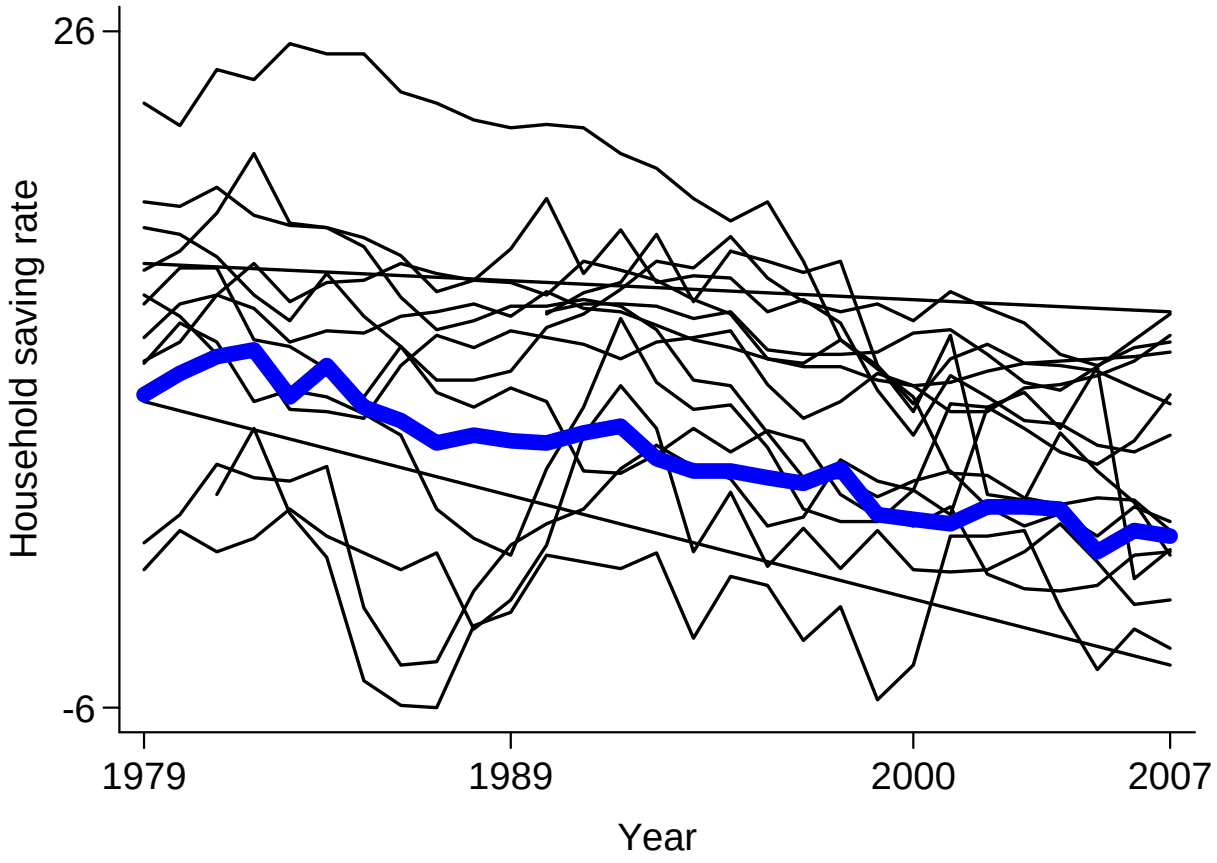
FALLING BEHIND

ROBERT H. FRANK

"Lucid. Explains exactly how and why an unequal society leaves almost all of its members worse off." **James Fallows**

How Rising Inequality Harms the Middle Class

5. Bad for middle-class debt?



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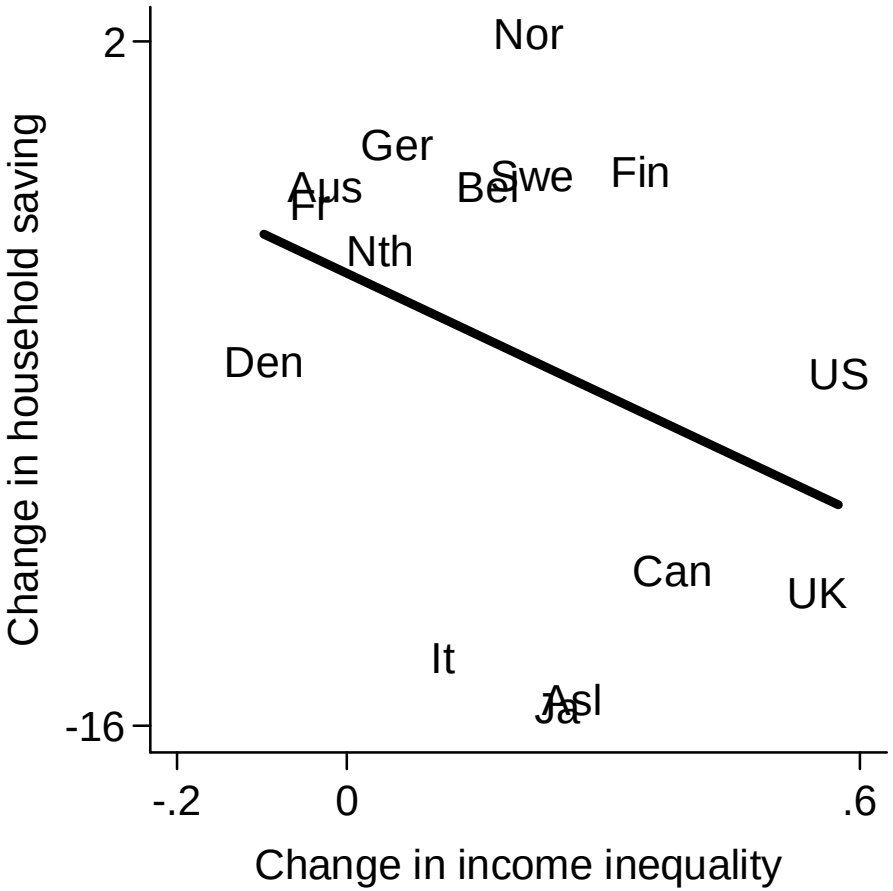

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5. Bad for middle-class debt?

Yes, possibly

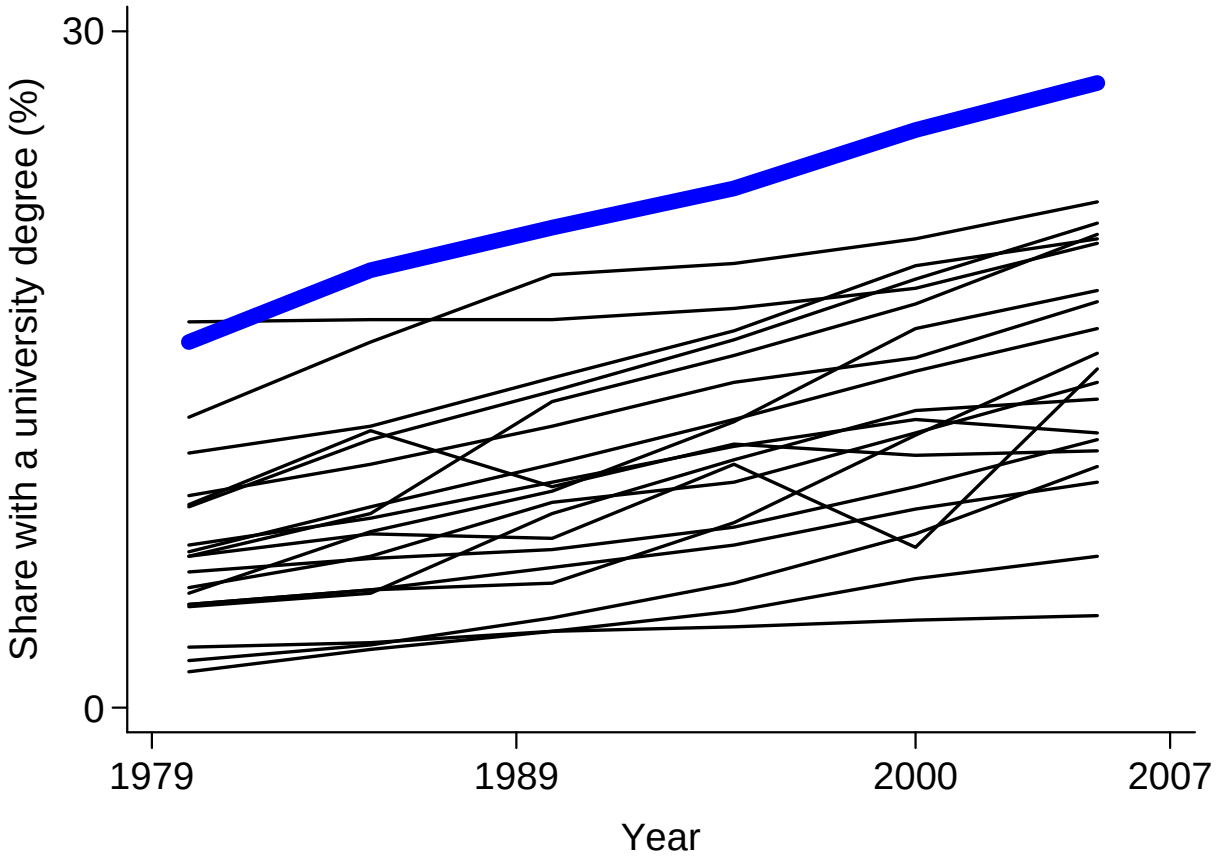
We're trying to figure out whether big reductions in the saving rate correlate with big increases in house prices, as Robert Frank hypothesizes

6. Bad for educational attainment?

Rising income inequality might reduce college completion by

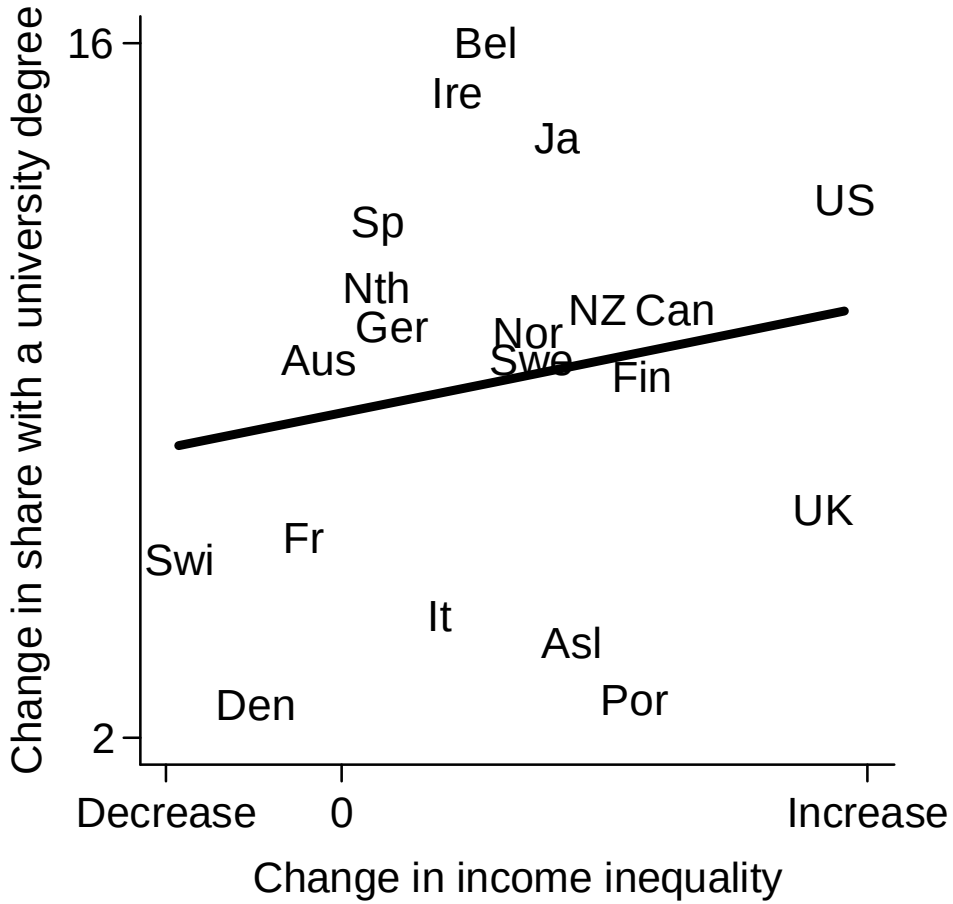
- Enabling the rich to bid up tuition prices, making college unaffordable for more middle-class and poor kids

6. Bad for educational attainment?



Source: Christopher Jencks and Lane Kenworthy, *Should We Worry About Inequality?* (forthcoming), using data from the Barro-Lee education database.

6. Bad for educational attainment?



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6. Bad for educational attainment?

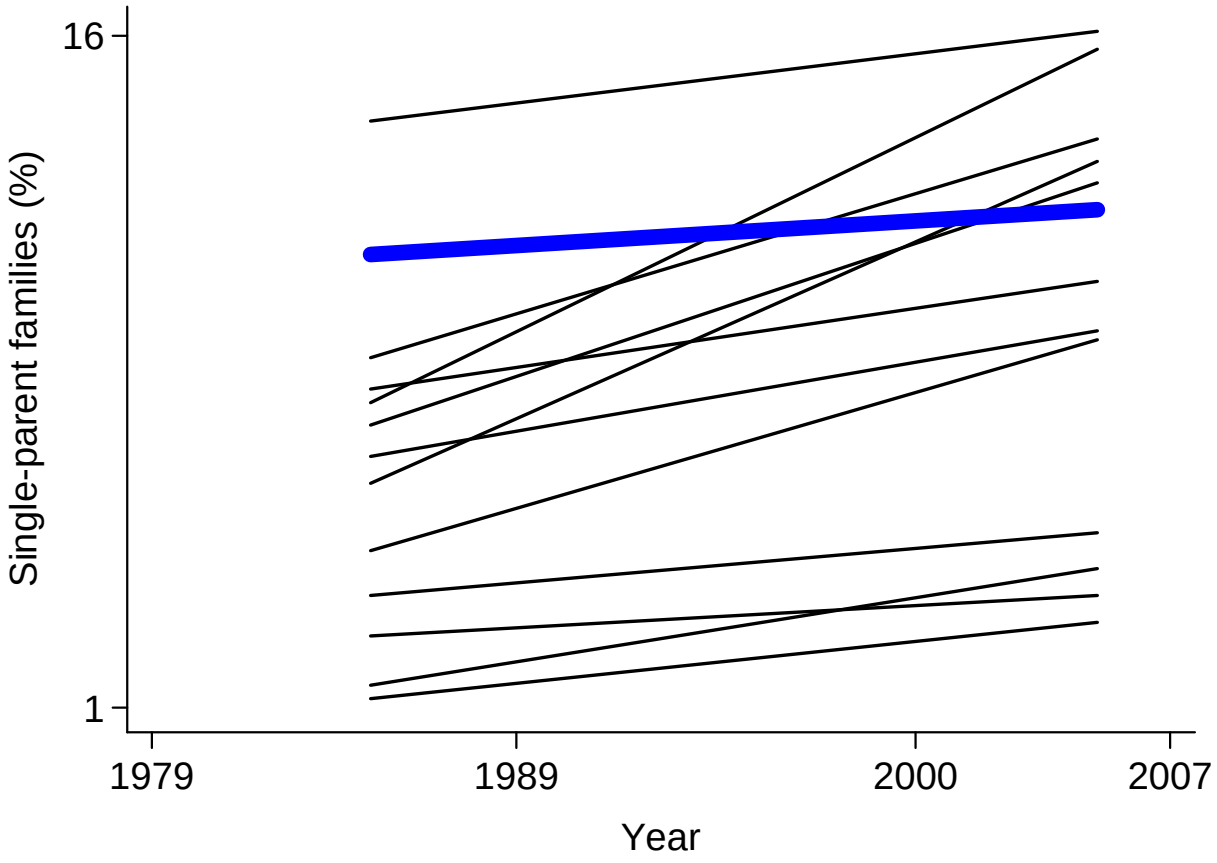
Probably not

7. Bad for family?

Rising income inequality may increase family breakdown by

Increasing stress due to status competition

7. Bad for family?



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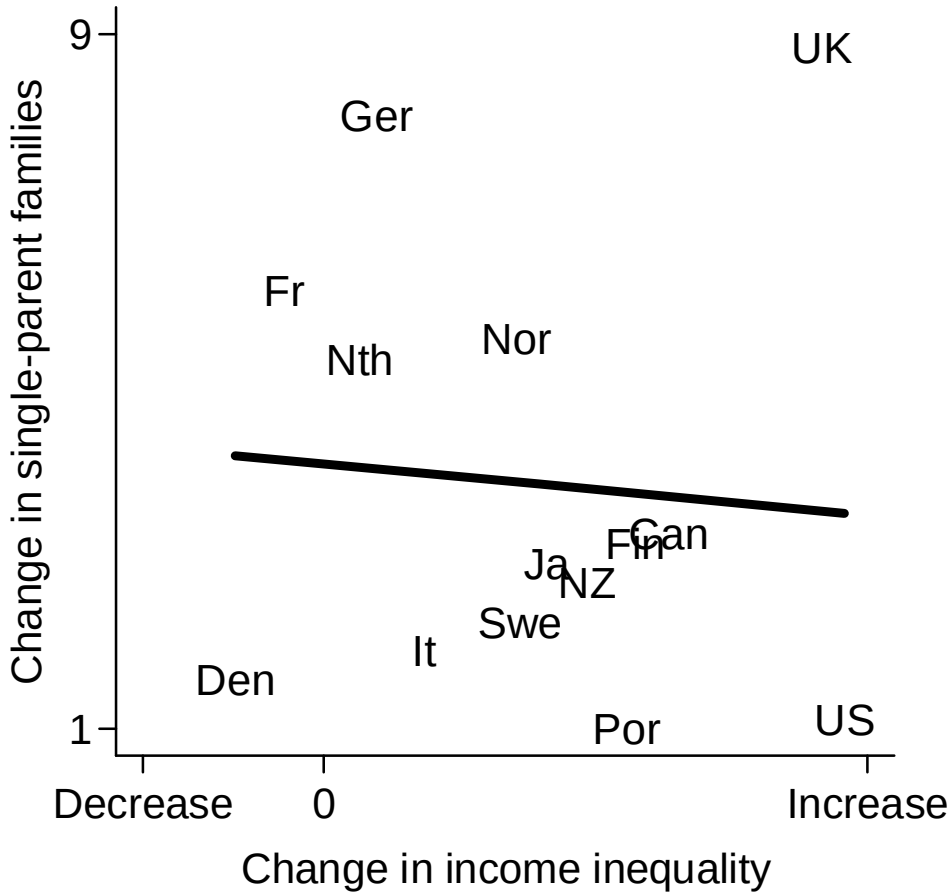

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7. Bad for family?

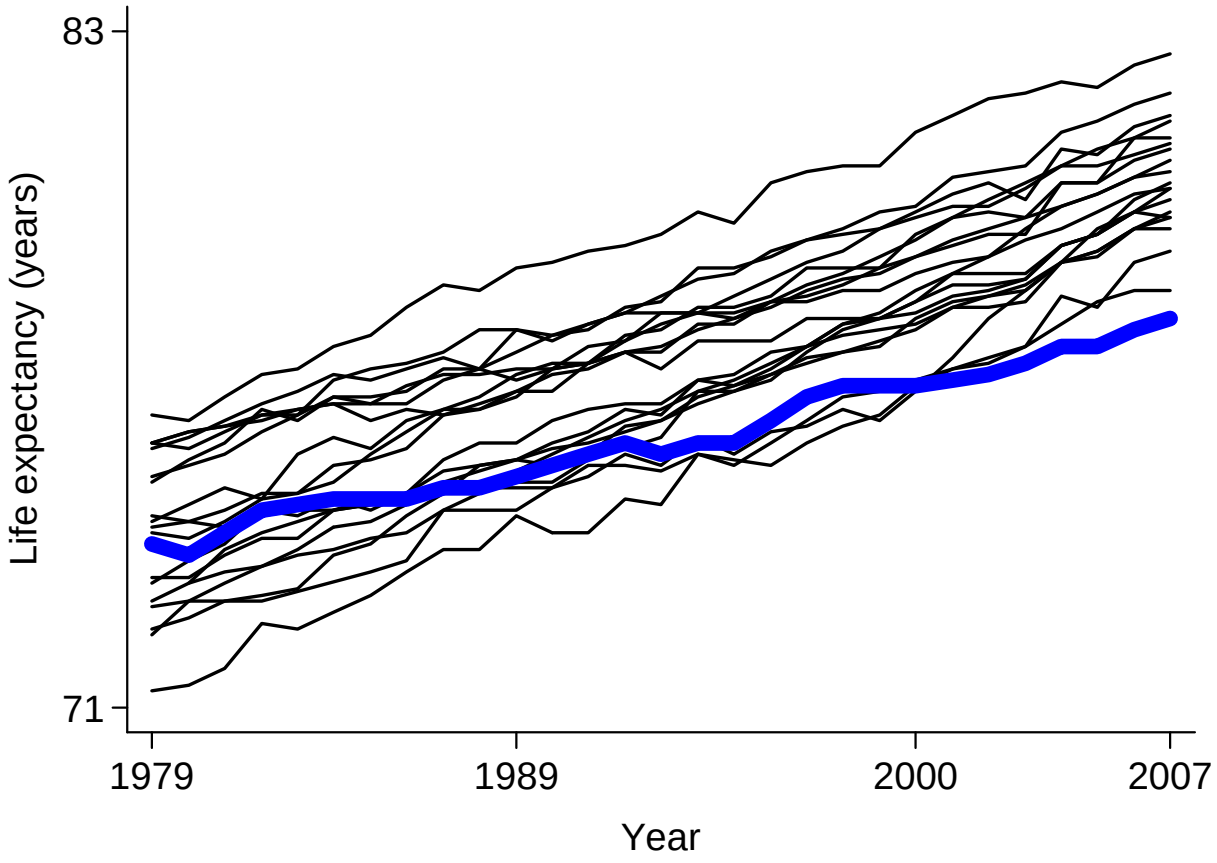
Probably not

8. Bad for health?

Rising income inequality might reduce health by

Increasing stress due to status competition

8. Bad for health?



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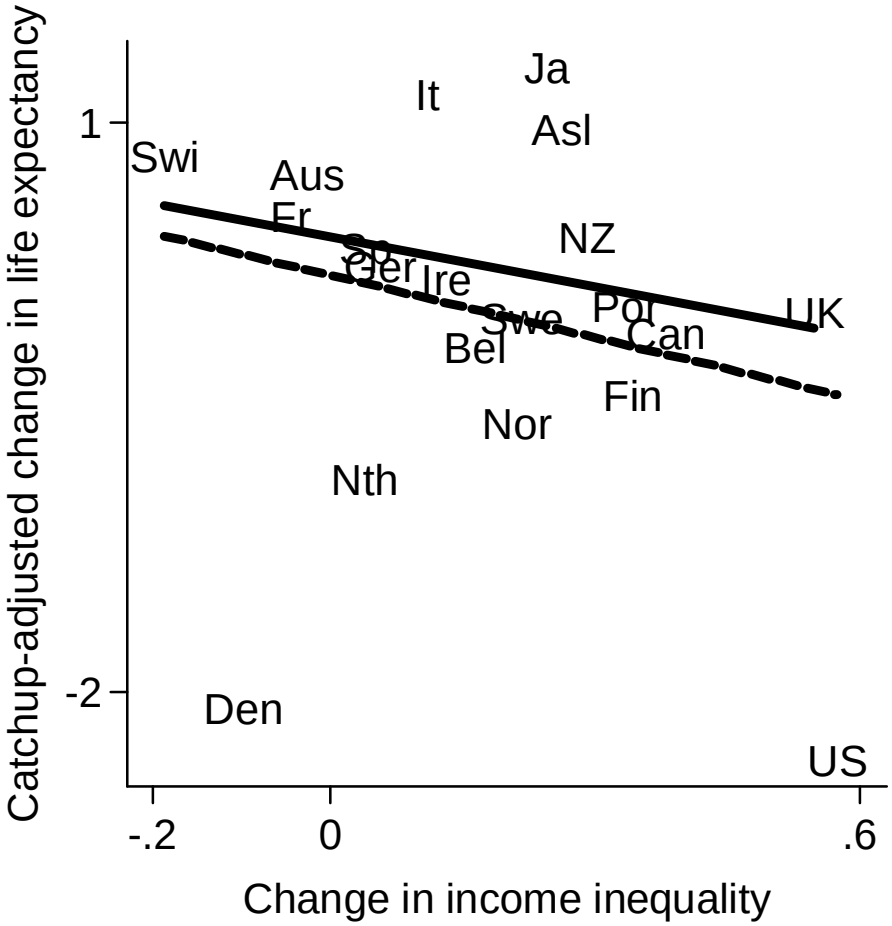

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8. Bad for health?

Here we do see some indication of an adverse effect of rising income inequality

But it's small

> An increase in income inequality the size of the U.S.'s is estimated to reduce life expectancy by about half a year
>
> The average change in life expectancy in these countries between 1979 and 2007 was +6 years

8. Bad for health?

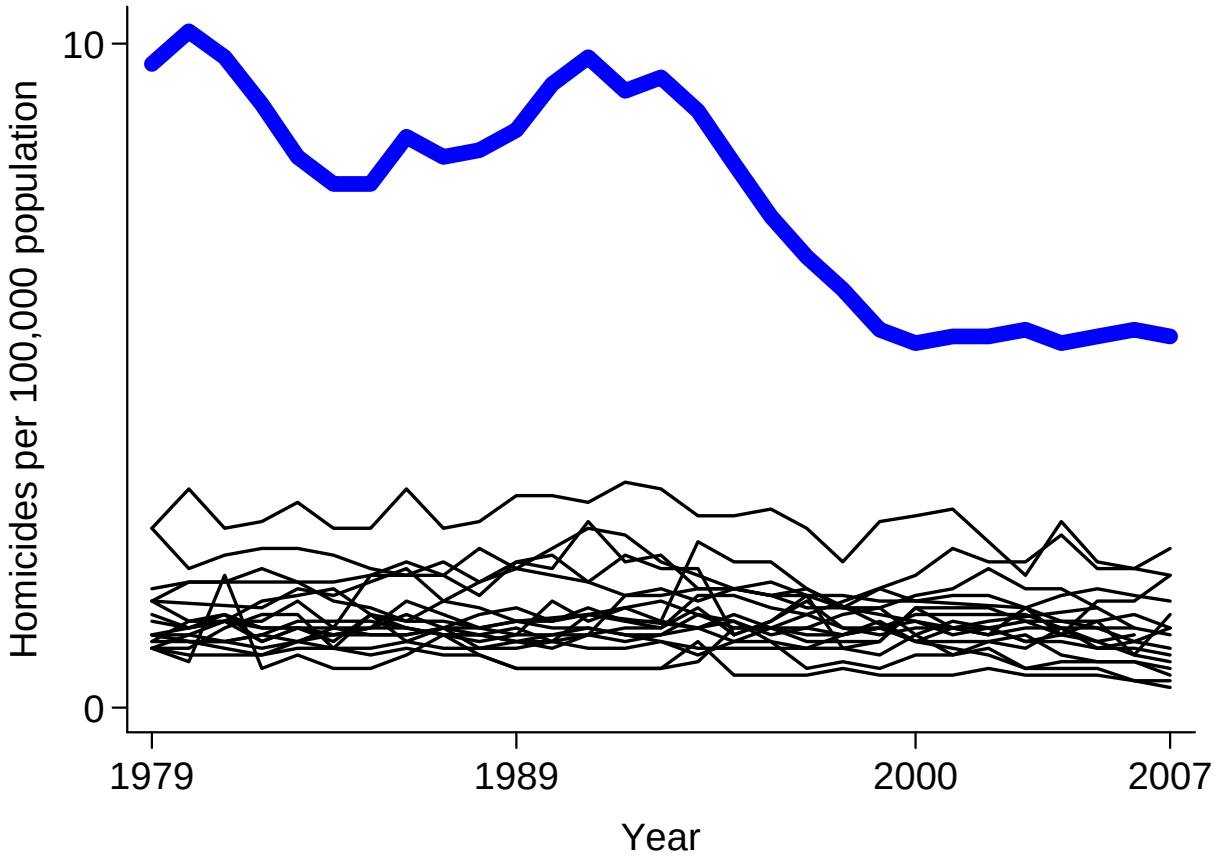
The same is true for infant mortality

9. Bad for safety?

Rising income inequality may increase violent crime by increasing people's sense of relative deprivation, which

- Encourages those at the low end of the distribution to engage in illicit activities, where the pay may be greater but there's greater likelihood of violence
- Increases frustration

9. Bad for safety?



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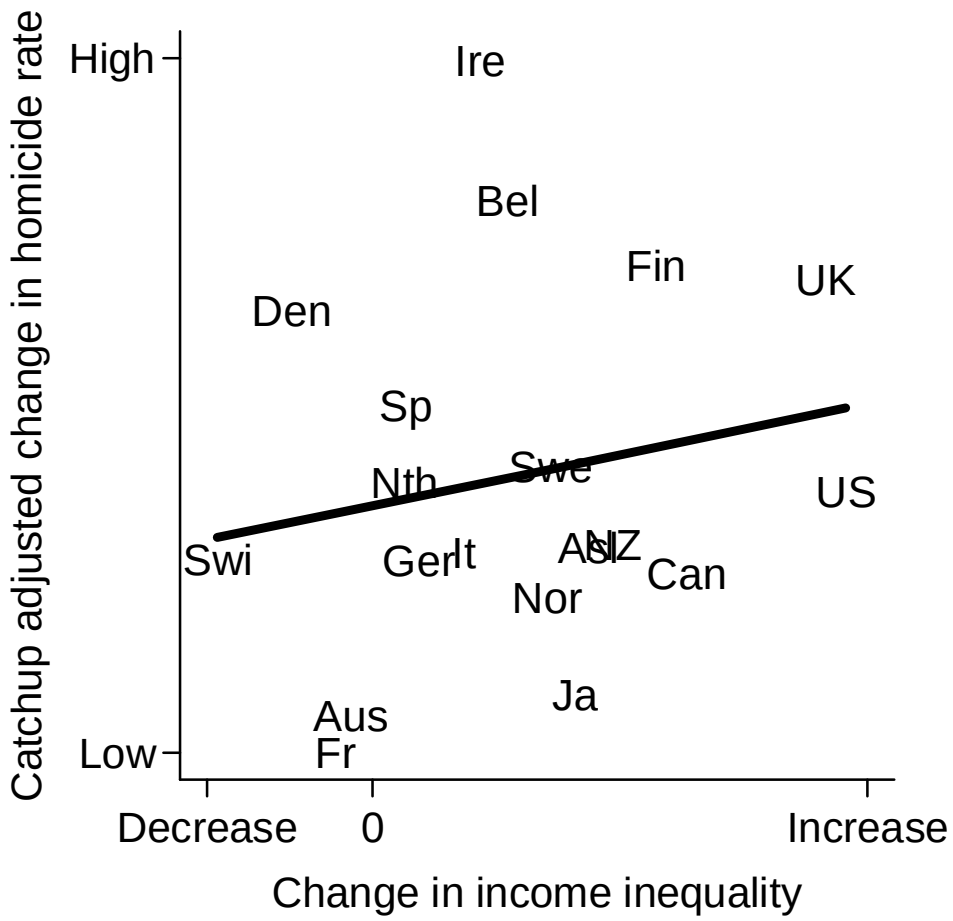

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9. Bad for safety?

Probably not

10. Bad for democracy?

Rising income inequality may weaken democracy by

- Enhancing the influence of the rich on policy decisions, via lobbying and campaign contributions

LARRY M. BARTELS

unequal democracy

★★★★★★★

The Political Economy of the New Gilded Age

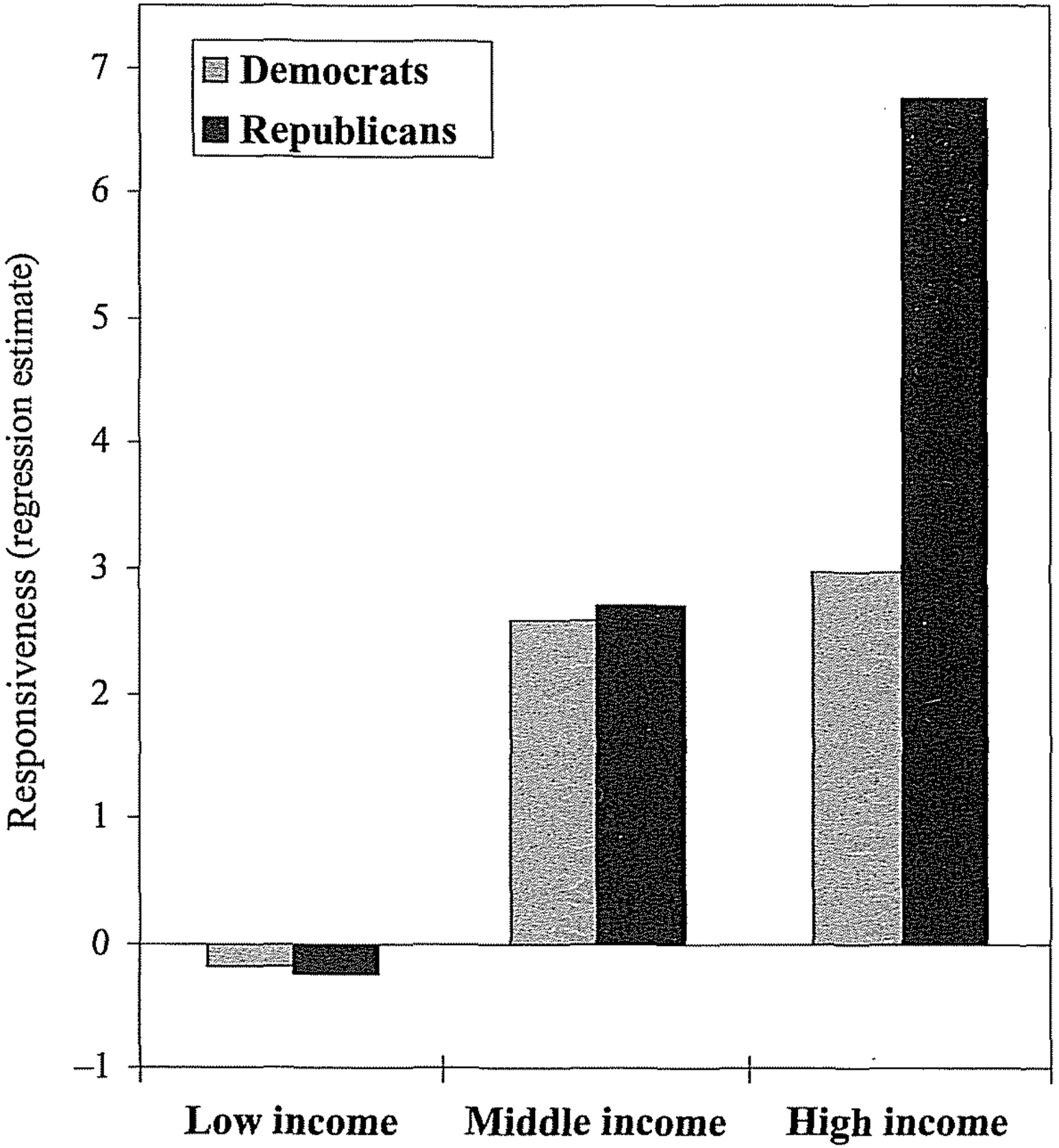


Figure 9.3 Democratic and Republican Senators' Responsiveness to Income Groups

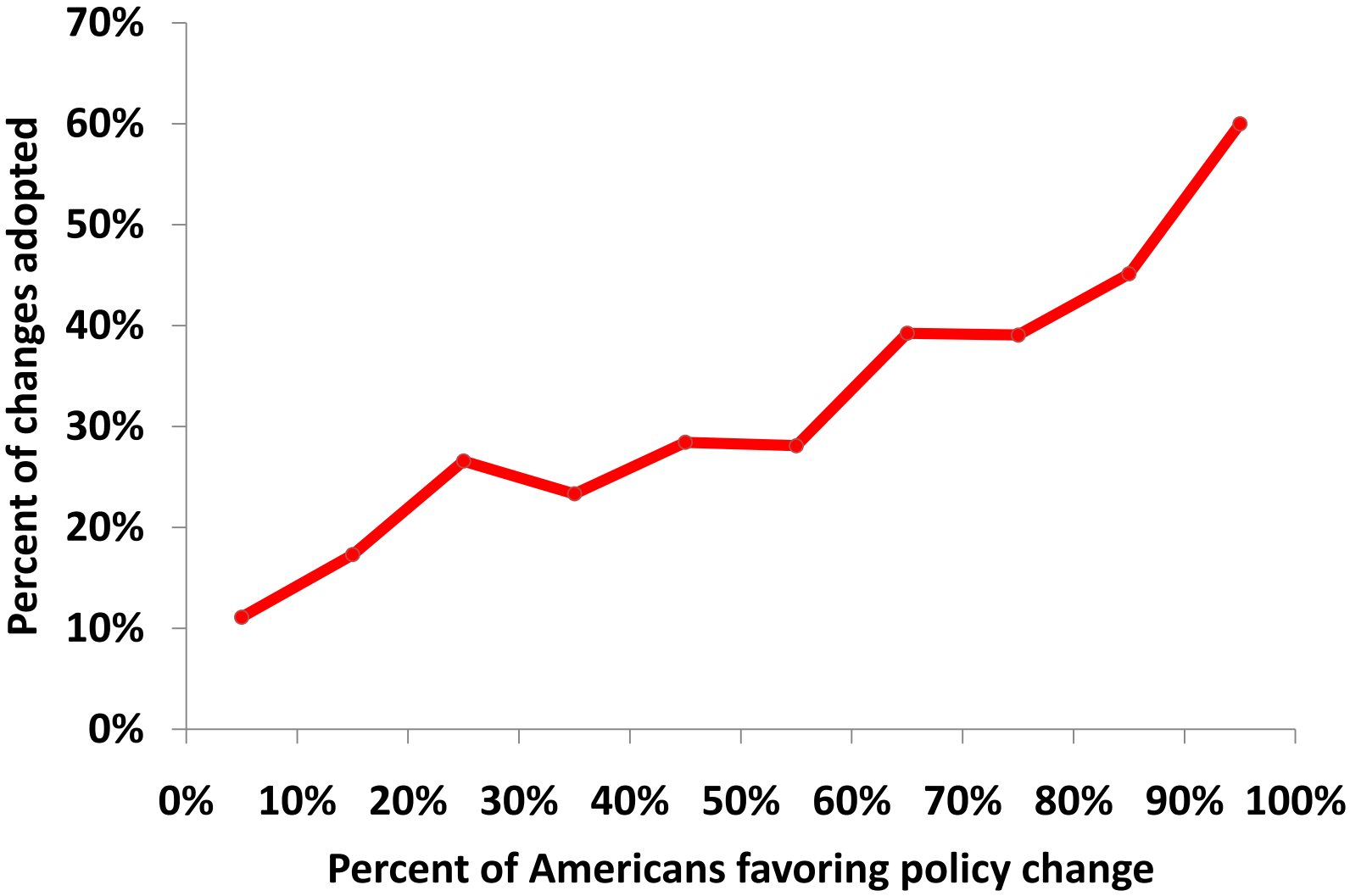
Affluence & Influence

Economic Inequality and Political Power in America

Martin Gilens

Department of Politics

Princeton University


70%
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Percent of changes adopted
0%
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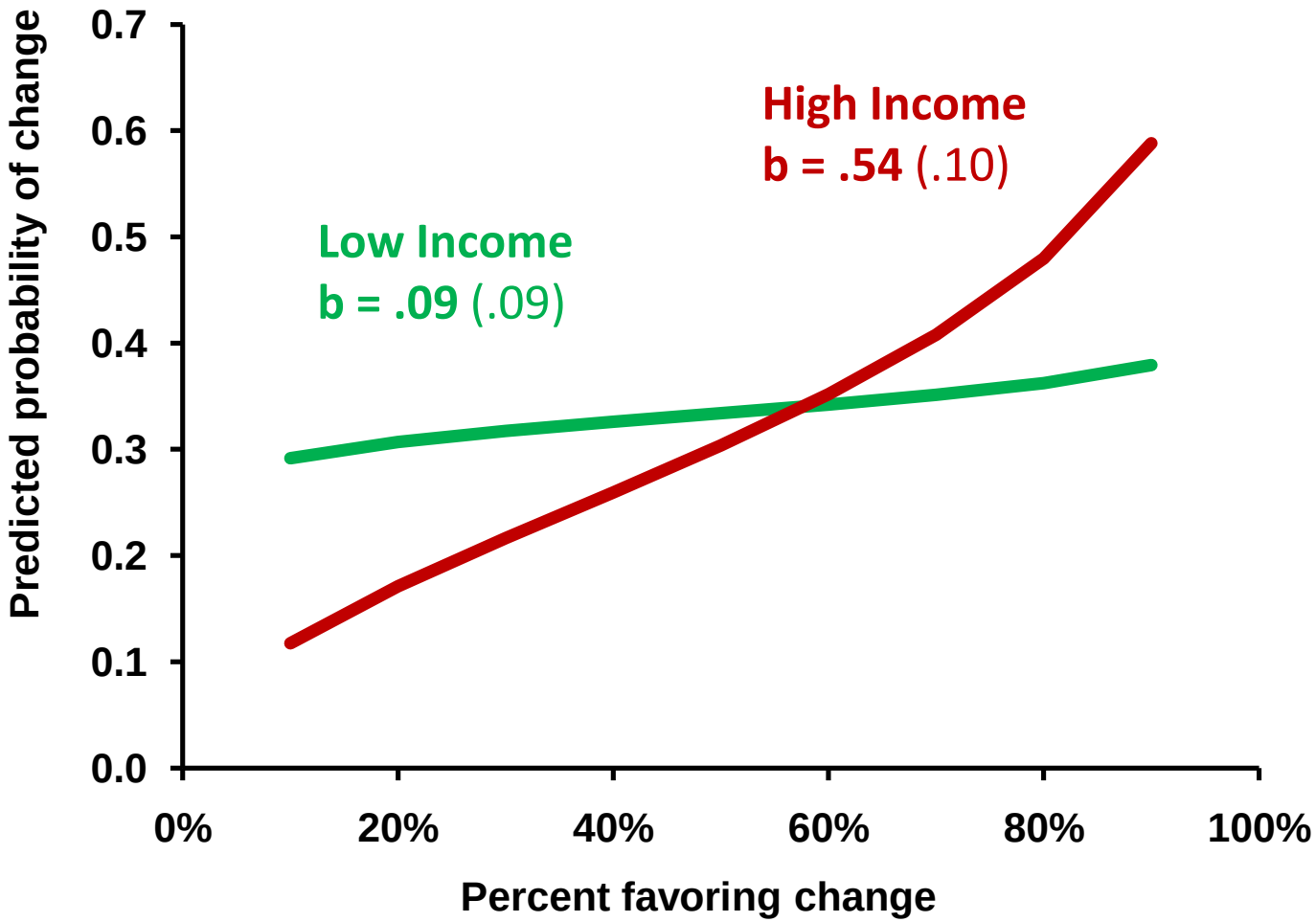
80%
90%
100%
Percent of Americans favoring policy change

When Low vs. High Income Preferences Diverge



10. Bad for democracy?

In the United States, the rich clearly do have more influence on policy than do the middle class or poor

But we don't know whether, and how much, that's increased as a result of rising income inequality

Summary

Summary

Is rising income inequality bad for us?

- For most of the outcomes we've looked at, our preliminary answer is "no" or "not much"
- Democracy may be an important exception

Even so, I consider rising income inequality a serious problem

- on normative grounds (importance of luck)
- because it increases inequality of health, happiness, etc.