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Chuck Collins
United for a Fair Economy

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The Economic Context

Growing Disparities of Income and Wealth

Chuck Collins

In the last few years, poverty rates have remained constant in the New England states. The effort to reduce poverty in New England and the United States has been thwarted by trends of growing income and wealth inequality. Since the late 1970s, the real incomes for the majority of U.S. households have remained stagnant or fallen. During the same time, asset ownership has become dramatically more unequal, and the concentration of wealth in the hands of a few has increased. The causes of this accelerated inequality are complex, but underlying the picture are a series of rule changes, both public policies and private corporate practices. These include public policies governing taxation, global trade, labor rules, and government spending priorities. These rules have favored asset owners at the expense of wage earners.

The economic health of the United States could be summed up on a T-shirt spotted recently at a New England county fair: “I lived through ten years of unprecedented economic prosperity and all I got was this lousy T-shirt.”

“The reality is that the U.S. society is polarizing and its social arteries are hardening,” said Will Hutton, a British commentator on U.S. society. “The sumptuousness and bleakness of the respective lifestyle of the rich and poor represent a scale of difference in opportunity and wealth that is also medieval — and a standing offence to the American expectation that everyone has the opportunity for life, liberty, and happiness.”

In hearing Hutton, many of us might defensively respond that at least U.S. inequality is not as severe as that in countries like Brazil. Brazil, after all, is a society where a small, wealthy elite drives their bullet-proof Mercedes Benzes from their gated residential enclave to their walled shopping district enclave (or if they are very wealthy they take helicopters). Meanwhile the great mass of people are living in sprawling slums in severe deprivation.

Chuck Collins is the co-founder and Associate Director of United for a Fair Economy in Boston. He is co-author, with Bill Gates, Sr., of Wealth and Our Commonwealth: Why America Should Tax Accumulated Fortunes.

It is true that U.S. inequalities are not as extreme as Brazil's, but the signs of the times in our country should give us pause. The economic prosperity of the 1990s was remarkable in many regards — and the technologically driven increase in productivity made many people very wealthy. But the benefits of the 1990s “boom” were very uneven, and if we look at the whole picture, the last three decades have seen growing income and wealth inequality.

For individuals and families attempting to rise out of poverty, there have been a number of structural economic forces thwarting the climb. A “poverty framework,” looking solely at the experience of individuals in poverty, fails to take into account the changing U.S. and global economy and the trends of growing economic inequality. A large part of this story has to do with stagnant wages, the changing structure of work, and growing disparities of wealth.

Wages, Work, and Wealth: A Quarter Century of Growing Inequality

In the thirty years after World War II, the growth in wages was experienced all across the economic spectrum. Wage earners in the lowest-income quintile saw their real incomes rise 116 percent between 1947 and 1979. At the same time, the middle quintile and the top quintile saw their income's rise 111 percent and 99 percent respectively. Simply looking at family income, the “rising tide” really did lift all boats.¹

This contrasts sharply with the story of wages and income between 1979 and 2000, which could be characterized as a dramatic pulling apart. With the exception of a few good years at the end of the 1990s, when some of the gains of the 1990s economic boom were experienced more broadly, incomes for the bottom half of the population fell or remained stagnant over this period.

Between 1979 and 2000, the bottom quintile saw their real after-tax incomes grow 9 percent. The middle and top quintiles saw their real after-tax incomes rise 15 percent and 68 percent respectively. But if we break out the top quintiles into different segments, we see that the most dramatic pulling apart is at the very top of the economic ladder.

The highest 1 percent of income earners, those with incomes in 2003 exceeding \$337,000, saw their real incomes rise 201 percent between 1979 and 2000.² In 2000, according to the Center on Budget and Policy Priorities, this top 1 percent of the U.S. population took home a bigger slice of after tax income than at any time during the previous seventy years. The 1 million households at the top received more income than the forty million households at the bottom of the income spectrum.³

In Massachusetts, income inequality increased over the same period. The Commonwealth ranked as the fifth most unequal state in the country, as demonstrated by the richest fifth of income earners and the poorest fifth.⁴

Between the late 1980s and the late 1990s, the bottom 40 percent of income earners in Massachusetts saw their real incomes decline 7 percent, reflecting the unevenness of the economic boom in the state.⁵

Another indicator of U.S. inequality is the disparity between average worker pay and top management pay in America's largest corporations. In 1980, the ratio between the paychecks of the highest paid and average employee was 42 to 1. Today, according to the *Business Week's* annual survey, the ratio is over 400 to 1, a ten-fold increase in compensation inequality.⁶

Looking at the U.S. economy through the lens of wages and income, it would be accurate to characterize the three decades after World War II as a time of "growing together," whereas the last 25 years has been a time of "pulling apart."

Work in the New Economy

Part of the explanation for growing wage disparities is because the nature of work itself has changed since the years after World War II. Employers in the post-war years shared more of the prosperity of those decades with their workers. Wages steadily rose and the percentage of jobs with health care coverage, employer-funded pensions and long-term security increased. Workers without college educations could still secure high paying jobs in U.S. manufacturing. And a single income could provide a family with a decent standard of living.

U.S. social policy contributed to a post-war middle class expansion with enormous public investments in higher education and low-interest mortgages for first-time homebuyers. Between 1945 and 1968, the percentage of American families living in owner-occupied dwellings rose from 44 percent to 63 percent.⁷

But since the mid-1970s there has been a steady shift in the nature of the job itself. The "new economy" job pays less, has little long-term security, and fewer benefits associated with the job. A higher percentage of jobs are in the temporary or "contingent" workforce without security. The "Walmartization" of the economy has seen a growing number of employers paying poverty wages with minimal benefits. In one cartoon a politician boasts at a black tie dinner, "My administration has created 8 million new jobs." The waiter at the banquet concurs: "I know. I have three of them." A household needs several of these "new economy" jobs to hold life together.

The Wealth Gap

Income and the changing nature of work provide one dimension of America's "apartheid economy." But an examination of wealth disparities reveals a more startling picture of inequality than income.

In the years after World War II, not only did incomes for all households double, there was an enormous broadening of wealth in the form of savings and homeownership. In 1976, after several decades of public policies aimed at broadening wealth, the top 1 percent of households owned 19 percent of all

private wealth. By 2001 the share of wealth owned by the top 1 percent of households was 33 percent. To join this richest 1 percent that year you needed to have at least \$3 million in net worth. The richest 5 percent of U.S. households controlled over 59 percent of the country's wealth; the richest 20 percent held 83 percent. At the same time, the bottom 80 percent of households had 17 percent of the wealth pie and the bottom 40 percent had just 0.3 percent.⁸

For the majority of Americans, their wealth is in the form of homeownership. Taking homeownership out of the picture and looking at "financial wealth," the picture is even more skewed. The wealthiest 1 percent own 42.1 percent of financial wealth, while the bottom 90 percent has 21.3%.⁹

The "dot com" technology bust deflated some of the paper wealth of this wealthiest group. But at the highest reaches of America's wealth ladder, recent wealth assessments indicate that there has been a resurgence of millionaires in the United States and worldwide. The number of individuals with at least \$1 million in financial or liquid assets jumped from 2 million to 2.27 million households between 2002 and 2003.¹⁰

Almost one fifth of the population, mostly located the bottom of the income ladder, have no wealth or savings. They may owe more than they own. Nearly 31 percent of black households and more than 13 percent of white households are "assetless," possessing zero or negative net worth.¹¹

The racial wealth divide is even more dramatic and underscores how the legacy of discrimination in lending practices, business ownership, and job opportunities has thwarted wealth opportunities for people of color. In 2001, the typical black household had a net worth of just \$19,000, including home equity, compared with \$121,000 for whites. Blacks had 16 percent of the median wealth of whites, up from 5 percent in 1989. This is progress, but at this rate it will take until 2099 to reach parity in median wealth.¹²

Many low- and middle-income households have seen their savings erode and wages stagnate. They've compensated for these changes by increasing the number of hours they work in the paid workforce and by taking on unprecedented levels of personal debt. While longer work hours and personal debt have masked inequality trends, they've come at enormous personal cost to individual families and are not sustainable.

These trends in wealth are troubling on their own, but they also have wider societal implications. Concentrations of wealth are also concentrations of social and political power. As wealth concentrates in fewer hands, so does the power to influence the rules that govern our society and the economy.

Why Has This Happened?

While the 1950s and 1960s were still times of economic inequality, prosperity was shared significantly better than during the last couple of decades. Why

was inequality declining in the 1950s and 1960s? Why has inequality grown so dramatically in the last two decades? There is no simple answer.

For most economists, politicians, and media professionals, growing inequality is not even newsworthy. Of those who acknowledge this phenomenon, most attribute it to unnamed “market forces.” Most orthodox economists point to three primary reasons for growing inequality: changing technology, lack of education (resulting from technological change), and globalization.¹³ As James K. Galbraith writes in *Created Unequal: The Crisis in American Pay*, “To a predominant faction within the economics profession, the ‘why’ of rising inequality has been answered by a single, all-encompassing phrase: *skill-based technological change*.”¹⁴ This basic theory states that workers in our economy have not kept up with dramatic changes in technology, creating a shortage of highly skilled people who have made the leap into the new technological arena and whose services, by virtue of supply and demand, command high salaries. The labor of under-skilled workers, on the other hand, is less valued, so their wages plummet. The policy implications of this are, if anything, to invest in worker training and education and sit back and wait for the supply of skilled workers to catch up to demand.

Galbraith challenges this theory, arguing that rising wage inequality is neither “mysterious nor necessary nor the dark side of a good thing.” Rather, it is the result of recession, unemployment, slow economic growth, inflation, and a stagnant minimum wage. *It is the result of changes in the rules that govern the economy — at least two decades of public policies and private corporate practices — that have benefited asset owners at the expense of wage earners.* Tax policy, global trade policy, government spending, and regulation have all been tilted in favor of asset owners and large corporations.

Technological change and global competition *do* contribute to inequality. Yet even in these areas there are political decisions and rules that govern how we choose to evolve technologically and how we integrate into the global economy. Other nations have experienced technological change and global integration without the same dramatic increases in inequality.¹⁵ Inequality will be reduced through policies such as increasing employment, controlling the negative effects of globalization, and raising the minimum wage.

There have always been great inequalities of wealth and power, but the imbalance of power has accelerated in the last two decades as result of a power shift. Corporations, investors, and campaign donors gained power while main street businesses, wage earners, and voters have lost power. As political influence has shifted, the rules governing the economy have changed to benefit asset owners and large corporations at the expense of wage earners.

These rule changes are government actions and corporate practices that have worsened the wealth and income divide, putting a heavy thumb on the scale in favor of the rich and powerful. The federal government has changed

the rules governing taxes, trade, wages, spending priorities, and monetary policy. In each case, the government has acted on behalf of corporations and the rich to rig who wins and who loses in the economy.

One example of a rule change that has affected workers is their ability to join unions. As corporate power has increased, the power of workers, communities, consumers, and others has decreased. In the 1950s, when prosperity was shared relatively more equitably, 35 percent of the U.S. workforce was represented by a labor union. By 1983, that number had dropped to 20.1 percent. Today, less than 13.9 percent of the workforce is unionized and fewer than one in ten workers in the private workforce is in a union. In 1998, more than 100,000 people joined unions, but the number of new jobs in the economy grew even faster, so the percentage of workers in unions declined overall.¹⁶ This represents a tremendous loss in clout for the institutional voice of wage workers, a voice that continually asks “Hey, what about the workers?” whenever national economic policies were debated.

During the years after World War II, unions were a countervailing force to the power of domestic and transnational corporations. These unions enforced a “social contract” ensuring that the fruits of economic growth were shared. This sharing was not entirely equitable, as many unions excluded people of color and women from their ranks. But evidence is clear that unions raised the standard of living for most low- and moderate-income people, whether they joined unions or not.

Another example of rule changes that affect our lowest income neighbors relate to the weakening of the social safety net. Over the last two decades, we have witnessed a reversal in state and federal government programs that historically worked to narrow economic inequalities. Cuts in social spending increase Americans’ reliance on unequal personal income and savings and guarantee a growing divide between rich and poor.

For example, the restructuring of welfare and the elimination of federal college assistance have weakened the ladder of economic opportunity. Federal Pell Grants, created in 1972 to provide aid to working-class college students, are much less generous than they used to be. The maximum Pell Grant in 1975–76 covered 84 percent of the average cost of attending a four-year public institution, today it covers just 39 percent of that cost.

The situation will only worsen in the coming decade. The Bush administration’s proposed 2005 budget includes \$1 billion in cuts for Section 8 housing vouchers. These vouchers help 2 million poor, elderly and disabled Americans pay their rent. A \$1 billion cut would amount to 5.5 percent of the program’s total funding.

The Bush tax cuts of 2001 and 2003, which the administration’s 2005 budget proposes to make permanent, guarantee further cuts to social spending. The 2001 tax cut was the largest income tax rollback in two decades, and the

2003 cut reduced dividend and capital gains taxes while accelerating the 2001 rate cut for the top income brackets. These tax cuts, which mainly benefit the rich, will cost at least \$824.1 billion between 2001 and 2010. If extended, they will cost \$5.9 trillion over the next seventy-five years. Revenue losses of this magnitude can only be sustained by cutting social programs.

Wanted: A Real Opportunity Society

It has not always been like this. Throughout U.S. history are multiple examples of ways that our government has helped to level the playing field and expand the wealth and security of many of its citizens. After the Civil War, the government gave millions of acres of land to homesteaders. In the two decades after World War II, the white middle class was greatly expanded thanks to massive government scholarships for higher education and subsidies for affordable housing and small business development. Our government provided low-interest mortgages to homebuyers, enabling millions of people to get on board the wealth-building train. In both historical periods, however, people of color were left standing at the train station because of discrimination in these programs. The Economic Opportunity Act and fair housing laws were attempts to address persistent poverty and discrimination and ensure greater opportunity.

We must work to overcome the perpetuation of income and wealth inequality and the barriers they present to equality of opportunity. The accumulated advantages and disadvantages of inequality are like sediment. The accumulated opportunities for those with wealth build up, layer upon layer, from the previous generation's wealth, education, and opportunity. And the accumulated disadvantages of inadequate income and no wealth and savings deepen the hole of discrimination, poverty, debt, and unequal opportunity. We will not be able to adequately address poverty without challenging the structural changes in the economy that fuel a growing income and wealth inequality. ❁

Notes

1. Analysis of U.S. Census Bureau data in Economic Policy Institute, *The State of Working America 2002-2003* (M.E. Sharpe: 2003), 37, and U.S. Census Bureau, Historical Income Tables, Table F-3.
2. Center on Budget and Policy Priorities, "The New, Definitive CBO Data on Income and Tax Trends," September 23, 2003.
3. Center on Budget and Policy Priorities, September 23, 2003.
4. Economic Policy Institute/Center on Budget and Policy Priorities, *Pulling Apart: A State-By-State Analysis of Income Trends*, April 2002.
5. Ibid.
6. *Business Week* conducts an annual survey of executive compensation. In 2000, the ratio went up to 531 to one, but has since dropped. The most recent survey was April 19, 2004.

7. Kenneth Jackson, *Crabgrass Frontier: The Suburbanization of the United States* (New York: Oxford University Press, 1985), 205.
8. Edward N. Wolff, "Changes in Household Wealth in the 1980s and 1990s in the U.S.," April 27, 2004 draft, in Edward N. Wolff, Editor, *International Perspectives on Household Wealth* (Cheltenham, UK: Elgar Publishing Ltd., forthcoming).
9. Edward Wolff, "Recent Trends in Wealth Ownership 1983-1998," April 2000, Table 6. <<http://www.levy.org/docs/wrkpap/papers/300.html>>
10. Merrill Lynch/Capge mini report, as reported in Robert Frank, "U.S. Led a Resurgence Last Year Among Millionaires World Wide," *Wall Street Journal*, (June 15, 2004).
11. All data from "Recent Changes in U.S. Family Finances: Evidence from the 1998 and 2001 Survey of Consumer Finances," Ana M. Aizcorbe, Arthur B. Kennickell, and Kevin B. Moore *Federal Reserve Bulletin*, 89 (January 2003): 1–32. <<http://www.federalreserve.gov/pubs/oss/oss2/2001/scf2001home.html>>
12. Dedrick Muhammad, Allieno Davis, Betsy Leonar-Wright, and Meizhu Lui, *State of the Dream 2004*, (Boston: United for a Fair Economy, 2004).
13. Some of these arguments are made in Richard Alma and Michael Cox, *Myths of Rich and Poor: Why We're Better Off Than We Think* (New York: Basic Books, 1999).
14. James K. Galbreath, *Created Unequal: The Crisis in American Pay* (New York: Twentieth Century Fund and the Free Press, 1998), 5.
15. See Economic Policy Institute, *The State of Working America, 1997-98*.
16. Bureau of Labor Statistics, February 1999.