THE CAUSES OF INCOME INEQUALITY

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I disagree with this paper, which concludes that education appears to be the predominant force behind the growth in both labor and capital income inequality in the United States.

I also looked at the census "Table P-16 Educational Attainment--People 25 Years Old and Over by Median Income and Sex 1991 to 2019" (male). All education level 2019 dollar incomes were fairly flat. High school down 6.09%, bachelors up 4.98%, masters up 11.52%, professional up 9.07%, and doctorate up 11.87%. Over the same period of time real GDP per capita was up 57%.

United States median incomes did go up with real GDP per capita between World War II and 1973. Since then median incomes have stagnated and, from the data I can find, none of the education levels were able to keep up with their share of economic growth. They are all victims of income inequality.

The Wikipedia article "Educational Attainment in the United States" has a graph titled "Percentage of the Population 25 years and Over Who Completed High School or College by Age Group: Selected Years 1940-2015" that shows education attainment has been going up since 1940. We have had more income inequality as the education level has gone up. Higher education attainment has not resulted in a higher median income. Education may affect the income distribution within the ever-shrinking slice of economic pie that the wage earners get, but it does not make that slice of pie bigger.

Education could not be the principal cause of income inequality.

There are many causes of income inequality. Over the last 47 years almost no stone has been left unturned in the drive to push America's wealth upward toward the top 0.1%. However, these are what I think are the primary causes of income inequality:

1. Wage Suppression

In 1973 Nixon's wage and price controls put an end to 40 years of strong wage growth and the 40 year decline in the poverty rate. This was a government program designed to stop wage growth, and it did.

After the wage and price controls officially ended in 1974, a "Council on Wage and Price Stability" was created and lasted until 1981 to provide guidance on wages.

Wage suppression continued to be the policy of the Federal Reserve Board. In "What's (not) up with inflation?" Janet Yellen discussed the use of the Phillips curve by the Federal Reserve to forecast inflation. The Phillips curve relates inflation to the unemployment rate. The idea is that low unemployment raises wages, in turn raising inflation.

The Federal Reserve Board has pursued a monetary policy that has kept unemployment high in order to hold inflation down. This policy has put millions of American out of work, suppressed wages, and kept millions of people in poverty.

Between 1948 and 1973 real median income grew by 2.5% per year. The average inflation rate during that time was 2.4%. Between 1974 and 1981 the average inflation rate was 9.2% and median incomes shrank 1.2% per year. This is the opposite of the "higher wages cause inflation" theory.

There does not seem to be a strong connection between real wage growth and inflation. The failure of Nixon's wage and price controls to stop inflation provides evidence that higher wages don't cause inflation.

The idea that "higher minimum wage costs jobs" has also been used for wage suppression. This idea has been disproven by recent minimum wage increases.

The Rand paper, "Trends in Income From 1975 to 2018", said "From 1975 to 2018, the difference between the aggregate taxable income for those below the 90th percentile and the equitable growth counterfactual totals $47 trillion." Wage suppression cost the bottom 90% a total of $47 trillion dollars in income. That has been a huge contributor to income inequality.

2. Tax cuts

Tax cuts since 1980 have delivered trillions of dollars to the top 1%, paid for with public debt. The top tax rate was over 90% from the mid 40's to the early 60's. That high tax rate effectively put a cap on top incomes, so that hardly anyone made more than $3 million per year in today's dollars. That is what made high wage growth possible.

Reagan's 1981 tax cut removed the income cap and allowed unlimited incomes. Since 1981 top incomes rose so fast there was no money left over for wage earners. This fantastic rise in top incomes could not have happened without wage suppression.

The purported rationale for the tax cuts was to increase economic growth, which would in turn create more jobs. This was based on the Laffer curve which says that if tax rates are high, a tax cut can increase tax revenue by increasing economic growth.

Unfortunately for that theory the chart of real GDP per capita in logarithms since 1870 shows that the long term trend line is straight, meaning that economic growth has been nearly constant despite significant changes in tax rates. There is no correlation between tax rates and economic growth.

3. Stock Repurchases

Stock repurchases were legalized in 1982. Since then corporations have spent trillions of dollars repurchasing their own stock. That is money that used to be spent on employee wages and benefits.

By removing the top income cap, tax cuts gave CEO's the incentive to redirect corporate profits away from the employees to themselves. The legalization of stock repurchases gave them the means to do it. Stock repurchases are used to goose the share price when the CEO's stock options vest. In 1965 CEO income was about 20 time the average worker salary. By 2006 it was 400 times. That is income inequality.

Conclusion

Income inequality, which could also be called wealth concentration or upward wealth redistribution, was a two-step process. First, wage suppression under the guise of controlling inflation. Then tax cuts under the guise of creating economic growth. Both were rationalized with highly questionable curves, the Phillips curve and the Laffer curve. Income inequality is baked into government policy.