

TRENDS IN ECONOMIC INEQUALITY IN THE U.S. SINCE WORLD WAR II: A CONFERENCE

by
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. . . given the inadequacies of the data available, the true postwar trend in the distribution of income is a mystery. This is the only strong consensus emerging from a national conference on the subject held last week at the Institute for Research on Poverty. . . .

The New York Times, Saturday, November 6, 1976

According to the official statistics, income inequality among households has remained stable throughout the post-World War II period. In spite of this, however, conflicting assessments of the trend in income inequality abound among economists:

Trends in Inequality of Well-Offness in the United States since World War II, background paper by Michael K. Taussig and Conference Overview by Sheldon Danziger, Institute for Research on Poverty, Special Report no. SR11. Forthcoming, January 1977.

SELECTED PAPERS

Sheldon Danziger, "Some Effects of the 1974-1975 Recession on the Level and Distribution of Income," Institute for Research on Poverty Discussion Paper no. 368-76.

Sheldon Danziger and Robert Plotnick, "Demographic Change, Government Transfers, and the Distribution of Income," Institute for Research on Poverty Discussion Paper no. 274-75.

Morgan Reynolds and Eugene Smolensky, "Why Changing the Size Distribution of Income through the Fisc is Now More Difficult," Institute for Research on Poverty Discussion Paper no. 356-76.

Morgan Reynolds and Eugene Smolensky, "Post-Fisc Distribution of Income: 1950, 1961, and 1970," Institute for Research on Poverty Discussion Paper no. 270-75.

FORTHCOMING MONOGRAPH

Morgan Reynolds and Eugene Smolensky, *Public Expenditure, Taxes, and the Distribution of Income: the U.S., 1950, 1961, 1970*. Institute for Research on Poverty Monograph Series (New York: Academic Press). Expected publication date, June 1977.

Edgar Browning: *The share of net income accruing to the lowest quintile is estimated to be 62 percent higher in 1972 than in 1952.*¹

Morgan Reynolds and Eugene Smolensky: *The distributions of net income were about the same in 1970 as they were in 1950.*²

Morton Paglin: *The trend of inequality from 1947-1972 has declined by 23 percent.*³

Sheldon Danziger, Robert Haveman, and Eugene Smolensky: *We reject the new measure of inequality proposed by Paglin, and with it the reliability of his conclusion.*⁴

The extent of the disagreement about the trend in inequality, combined with the enormous emotional charge it carries, led the Institute for Research on Poverty to hold a small conference of experts, both from academia and from government, to analyze the uncertainties, discuss needed research in the area, and relate the whole to public policy.

The focus of the conference was provided by Michael K. Taussig of Rutgers University, who was commissioned by the Institute to prepare a background paper surveying the literature and laying out the issues.

The Inadequacies of Existing Data

Although there was no strong consensus as to what appropriate data would show with regard to the trend in economic inequality, there was wide agreement that the official source of data on income—the Current Population Survey (CPS)—is so deficient that it cannot enlighten us.

First, and most straightforward, the CPS income series is designed to count current cash income.⁵ Even if this were the appropriate income concept—and most economists agree that it is not—the CPS does not provide a good measure of it. There is substantial underreporting, the estimates of which range from 10 to 30 percent depending on the kinds of income. In addition, the income measured is *before* taxes. Since the tax burden falls unequally on different income classes, this omission distorts the picture of their actual command over resources. Finally, realized capital gains and losses are also ignored, producing a further distortion.

The second major criticism is that even if current money income were measured accurately it is not the appropriate concept with which to measure economic inequality. The argument is that there are many factors (in addition to cash receipts) that make significant contributions to economic well-offness and are not distributed uniformly across income classes. In-kind transfers from government constitute an obvious example (Food Stamps, Medicaid,

Medicare are all ignored). Another example is the holding of wealth. Wealth is ignored, although few would argue that two people with the same money income but vastly different wealth holdings are really equally well-off. An additional example emphasized at the conference was the increasing importance of job perquisites (such as pension rights, free time on the job, and business expenses) which are distributed very unequally among the population and are omitted from the CPS.

A third set of factors, difficult even to specify, is nonetheless relevant to any serious effort to compare well-being.

One example is the valuation of leisure time. Suppose two individuals earn the same wages, but one works sixty hours per week, while the second works only forty. The CPS considers each individual to be equally well-off, while a "complete" definition of well-being would consider the earner with more leisure (that is, fewer hours worked) to be better off.

A related behavioral issue concerns the effect of government transfers, both cash and in-kind. These transfers not only add to current income (remember that the CPS measures cash but not in-kind transfers), but also may induce changes in behavior. Some people may reduce the amount they work in order to become eligible. Others (particularly the old and women) may be encouraged by the transfers to form separate living units.

For example, aged parents who move out of their children's houses because of the additional income they might receive from Social Security, Supplemental Security Income (SSI), or Food Stamps add to the count of poor units if their current incomes as defined by the CPS are below the official poverty line. This increase in the poverty count also increases measured income inequality even though the combined resources of the aged parents and their children have increased.

This problem leads to the next measurement issue: What is the appropriate income-receiving unit for economic inequality comparisons? The CPS measures the income of individuals and families (that is, relatives living together). Conference participants made the point that neither of these is necessarily the appropriate unit to use. The concept we need is the resources individuals really have command over *in the context of the consuming unit within which they pool their incomes.*

What is the "Real" Trend in Inequality?

It proved simple enough for conference participants to draw up a list of inadequacies in the CPS measure. But the ultimate question was harder to answer: Is economic inequality decreasing or increasing?

A majority of participants would probably agree on their "best guess" as to what a perfect set of data would reveal—greater equality in any one year than shown by the CPS, and a slightly greater trend toward equality over time.

The trend would be only "slightly" affected not because each of the inadequacies noted makes little difference but because the differences offset each other. These are the directions in which conference participants estimated the various factors would alter the trend:

1. *Inclusion of in-kind transfers* would influence the trend toward greater equality.

2. *Inclusion of work-related perquisites* would influence the trend toward greater inequality because they are becoming more important and are concentrated in the top half of the earnings distribution.

3. *Inclusion of realized capital gains and losses*, it was generally agreed, would increase measured inequality, but there was no consensus on the influence they would have on the trend over time.

5. *Taking account of behavioral responses to government transfers* (family splitting and changes in work effort, for example) would influence the trend in the direction of greater equality as well as reducing inequality in any year.

6. *Inclusion of taxes* would show greater equality within any given year, because the overall tax system is progressive. But, the tax system has become less progressive over time (despite recent efforts to offset it), especially because the progressive effect of exemptions has been eroded by economic growth and inflation. The influence of the tax system on the trend, therefore, is probably toward greater inequality.

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whites—but the worth of schooling for blacks had increased to such an extent that this was now one and one-half times as much as it was worth for blacks.

The relative influence of schooling on black–white differences deserves a closer look. The racial difference narrowed—in years of school completed—to imply an occupational status differential of only 2.5 units in 1973, compared to nearly 8 units a decade earlier. The large gap in occupational status between black and white men who did have the same schooling and social background, in contrast, has remained unchanged. In both 1962 and 1973 the occupational standing of black and white men was separated by about 6 units when they shared the same levels of schooling and social background.

Most of the effects of social background on occupational standing are due to the facts that men with advantaged backgrounds stay in school longer and men with more schooling gain higher status jobs. The recent equalizing trends in schooling and in its effects on occupations have enabled black men to begin to experience the intergenerational gains in social standing that had earlier been largely restricted to whites. If these trends continue, the passage of time may one day eliminate the contribution of social background and schooling to the black–white status gap.

There is no such optimistic outlook for the effects of discrimination (that is, effects beyond background and schooling), however. The persistence of the black–white gap between men who did have the same schooling and social background means that time is *not* narrowing the status difference between blacks and whites that is due to the effect of race *per se*.

¹Seed money for the project came from the Institute for Research on Poverty. The major funding for the survey itself came from the RANN program of the National Science Foundation.

²In both samples, unfortunately, women were represented only through their husbands. But Featherman and Hauser have been able to make some comparisons of the socioeconomic opportunities of married men and women. See David L. Featherman and Robert M. Hauser, "Sexual Inequalities and Socioeconomic Achievement in the U.S., 1962–1973." *American Sociological Review* 41 (June 1976):462–483. Institute for Research on Poverty Reprint no. 202.

Note: FOCUS/Institute for Research on Poverty Newsletter should be distinguished from *Sociological Focus* (and from the Focus on Policy Series within it), information about which can be obtained from Margaret M. Poloma, Co–editor, Department of Sociology, The University of Akron, Akron, Ohio 44325. We apologize that this distinction was not noted in our first issue.

Trends in economic inequality (continued from page 6)

Income Inequality and Social Policy

The final session of the conference was devoted to the importance (or lack of it) of the income inequality issue for domestic social policy. It was pointed out that Americans have never made the lessening of income inequality an explicit policy goal. Whatever economists may conclude about the income trends, the public seems relatively satisfied on that score.

Policy goals that are related to the issue have certainly been articulated: among them full employment, the alleviation of income poverty, and the elimination of race and sex discrimination. Some of these, it was realized, might conflict with the goal of reducing income inequality as such. An end to discrimination against women was cited as a prime example of a social policy goal that, as it becomes increasingly realized, creates greater income inequality. More women are finding jobs and, since the social norm in this country is for highly educated people to marry each other, increased work among women will disproportionately increase the earnings of high income families.

No ranking of social objectives was attempted at the conference. But it was generally agreed that evidence of a pronounced trend in inequality would alter perceptions of the performance of both the public and private sectors. This, in turn, would be likely to affect substantially any ranking of public policy goals.

¹Edgar Browning. "The Trend Toward Equality in the Distribution of Net Income." *Southern Economics Journal*, July 1976.

²Morgan Reynolds and Eugene Smolensky. "Why Changing the Size Distribution of Income Through the Fisc is Now More Difficult." Institute for Research on Poverty Discussion Paper no. 356–76.

³Morton Paglin. "The Measurement and Trend of Inequality: A Basic Revision." *American Economic Review*, September 1975.

⁴Sheldon Danziger, Robert Haveman, and Eugene Smolensky. "The Measurement and Trend of Inequality: A Basic Revision: Comment." *American Economic Review*, March 1977 (in press).

⁵The income series includes money wages and salaries; net income from self-employment; income other than earnings (such as dividends, interest, and rent); public cash transfers (such as Social Security, welfare payments, and Unemployment Compensation); and regular private cash transfers (such as annuities, alimony, and private pensions).