

Lecture 14(iii)

Announcements

- Final OneStop page at the bottom of our Canvas site

Lecture

1. Trends in Inequality
1% and 99%
2. Policies that address inequality
3. Labor market discrimination

The 99% and the 1% (or 99.99 and .01%)

Next look at increasing inequality even within the upper range of the income distribution. The “haves” starting to complain about the “have mores”

Let's look at recent research from Piketty and Saez
(“World Top Incomes Data Base”) <http://wid.world/>

Use tax return data to estimate the distribution of income at the very top. Strong evidence that “have mores” rising relative to the “haves”

Start with the top 10 percent

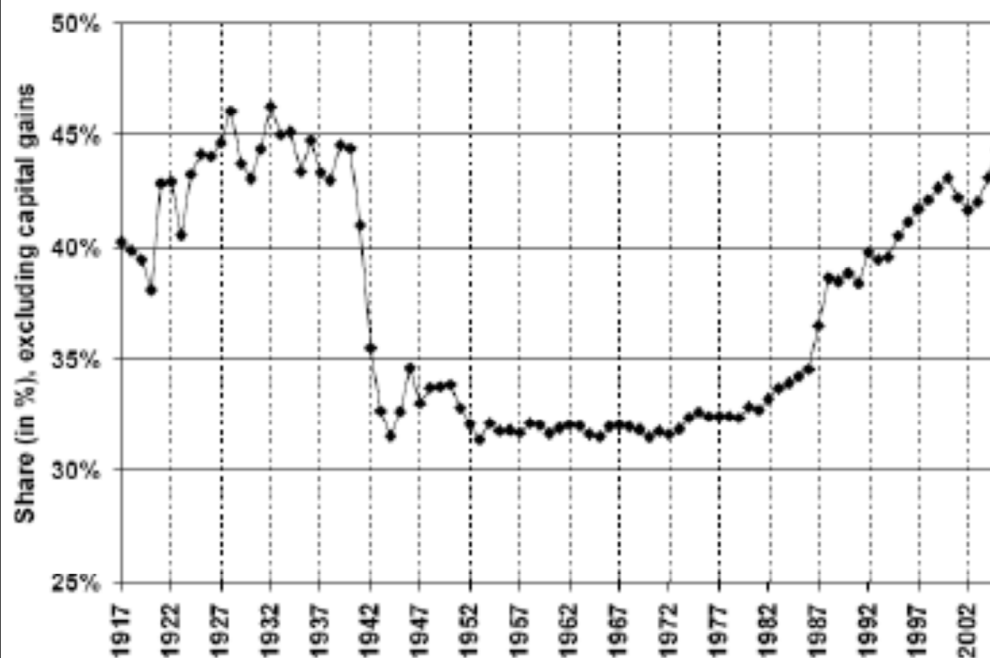


FIGURE 1
The Top Decile Income Share, 1917-2005

Top 10 percent

Year	Share of Total Income	Income Relative to Average
1917	40%	4.0
1972	32%	3.2
2012	48%	4.8

So a nice relative raise for “**haves**” between 1972 to 2012:
 3.2 times average income to 4.8 times average income.
 Next look at the “have mores,” the top .1% income share

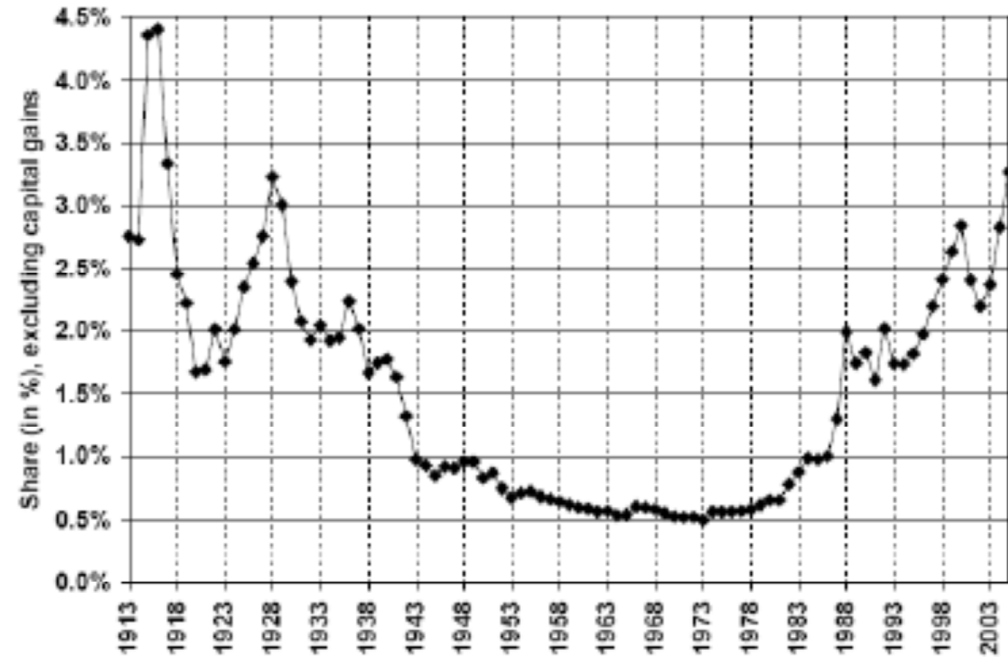


FIGURE 3
 The Top 0.01% Income Share, 1913-2004

Next look at the top 1% of income

Year	Share of Total Income	Income Relative to Average
1913	18.0%	18.0
1972	7.8%	7.8
2012	19.3%	19.3

So “**have mores**” get an even better wage.

To get the best raise, need to look at top .01% of income! “**have lots more**”

Year	Share of Total Income	Income Relative to Average
1913	2.7%	270
1972	0.5%	50
2012	4.0%	400

So a fantastic relative raise going from 1972 to 2012, going from 50 times average income to 400 times average income.

Explanations of Increase in returns at the very top:

1. (Supply and Demand)
“**Extreme skill-biased technical change**”
(benefiting workers way out a the extreme of the talent distribution.)
Return to very special talent has gone up, economics of superstars (easier to leverage up talent)
2. Return to special talent always there, but social norms limited pay differences.
3. **Looting**. The .01% have figured out a new way to work the system to redistribute the economic social pie to themselves, including busting unions. (Occupy Wall Street explanation.)

Let's have a look a baseball salaries.

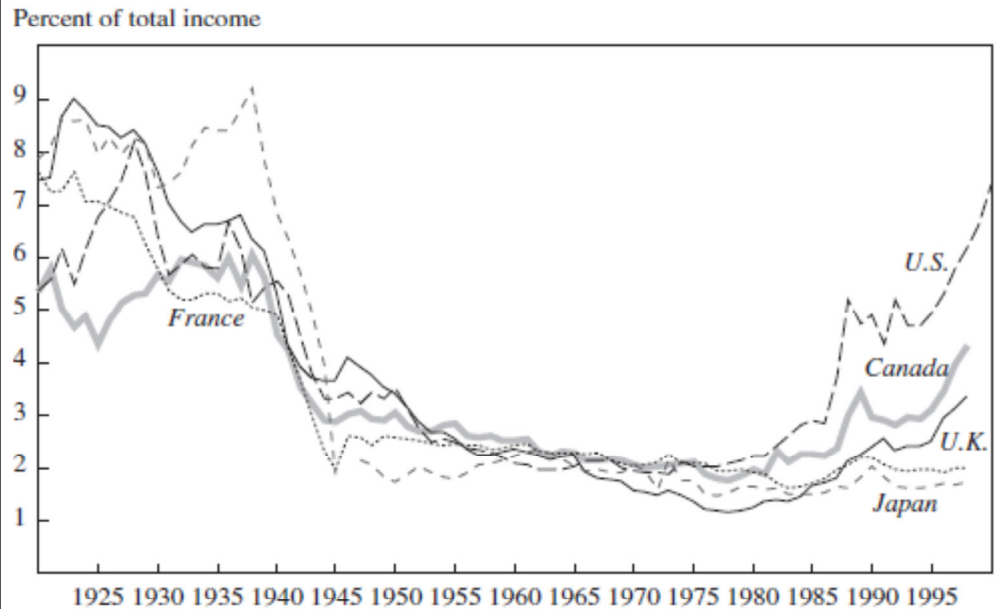
Pretty clear increase in the value of the marginal product. (Globalization, cable TV revenue, etc.)

Highest Paid ball players

		
	Hank Aaron 1972	Clayton Kershaw 2015
Salary (\$)	\$200,000	\$31 million
GDP per capita (\$)	\$6,000	\$53,000
Ratio	33	585

What is going on with top ball players fits the more general pattern

Figure 3. Share of the Top 1 Percent in Total Income in Selected Industrial Countries, 1920–2000^a



Source: Piketty and Saez (2006b).

a. Total income includes labor, business, and capital income but excludes capital gains.

As cited in Gordon and Dew-Becker, “Selected Issues in the Rise of Income Inequality

We see hear a similar picture as we saw for U.S. only, only now additional countries are added. This is a very interesting graph.

In terms of past several decades

“Anglo countries”
Canada is “US light”
UK is “US lighter”

Japan and France completely
different.

If this is all **Skill-Biased Technical
Change**, why are the Anglo
countries different?

One possible explanation: France
not paying market wages.

Interesting New York Times article
about “brain drain” of academics to
the United States

<http://www.nytimes.com/2010/11/22/world/europe/22france.html>

Percent of French émigrés to U.S
that were academics

1971-1981: 8 percent

1996-2006: 27 percent

Many reasons for this, one is pay.
A French biologist who moved
back to France had to take a 2/3
pay cut.

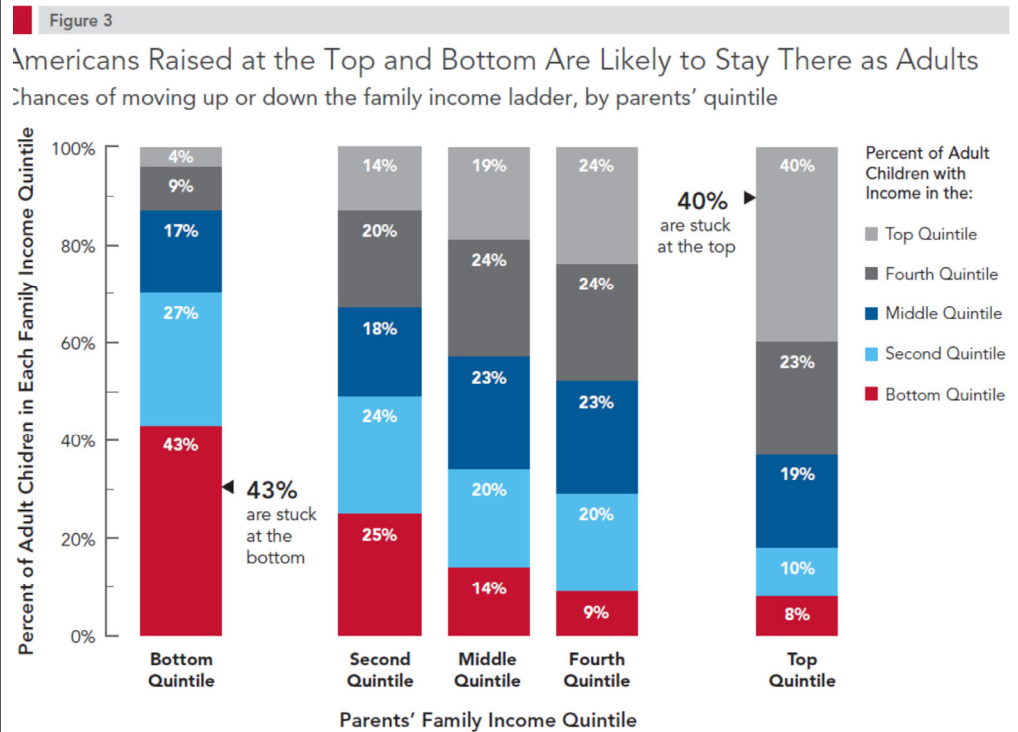
Next is issue of economic mobility

US society was clearly very mobile coming out of WWII.

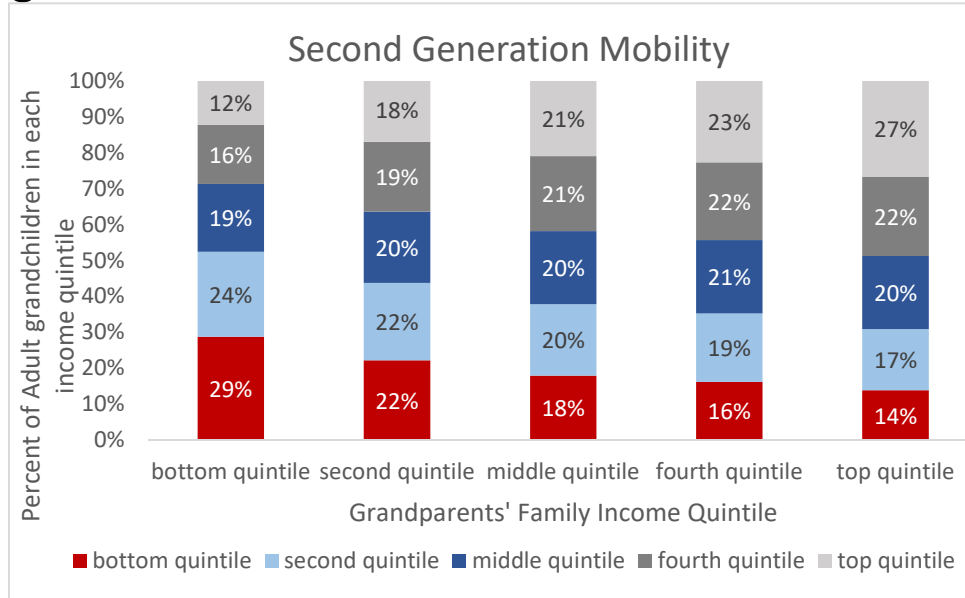
Many high-rolling Wall Street types today have grandparents who were dirt poor during the depression.

Income mobility is down.

Here is current mobility numbers in the US from 2012 Pew Report (Pursuing the American Dream):



But more mobility after another generation:



2. Proposed Policies to Change Income Distribution

1). Minimum wage
Minneapolis: currently \$10.00 goes to \$11.25 July 1, then a dollar a year.

Go back to our earlier analysis of price floors. This is a price floor.

A lot of arguments debate about who will benefit and how much it will cost business, and how much will costs be passed along to workers.

These are arguments about elasticities.

2) Using tax system to redistribute income.

More debates about elasticity.
Also, how high income people may flee (particularly need to worry about this at the state level compared to federal.)

Negative income tax:
People at the bottom of the income scale get money back.
Have something like this because:
1) earned income tax credit
2) some in-kind benefits.

3) Human capital
(Give a man a fish...vs. teach a man to fish)

(a) early childhood education
A big focus of recent economics literature

(b) investment in public schools

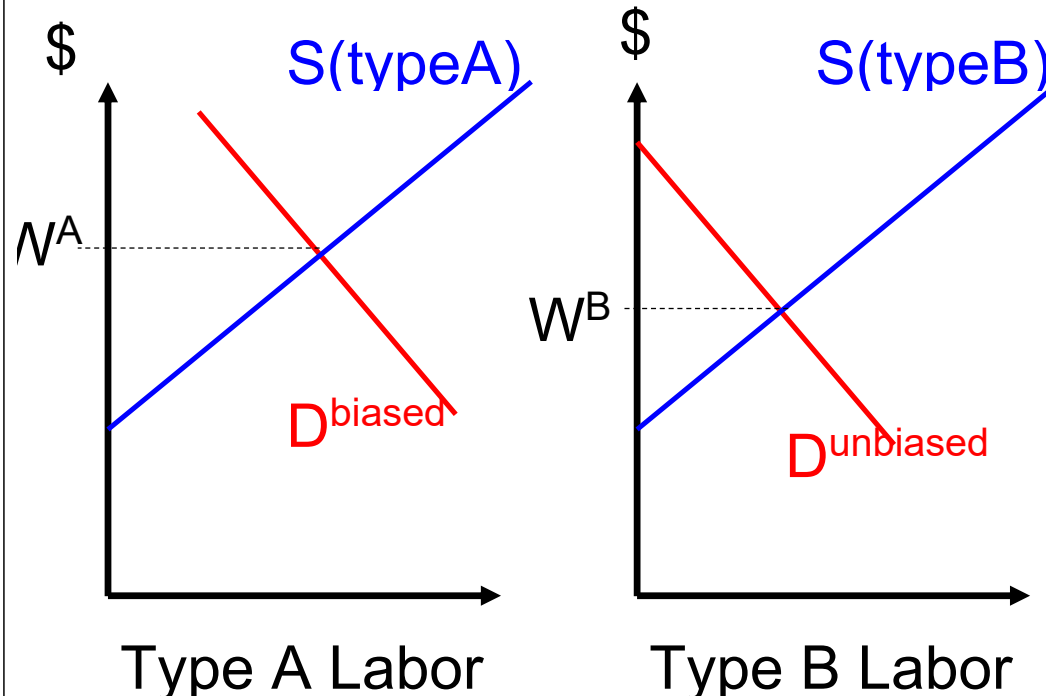
(c) public investment in higher education
student loan policy

3. Labor Market Discrimination

Suppose there are two kinds of workers, type A and type B, and they have equal ability.

- Suppose there are two kinds of firms, biased and unbiased.
 - Biased firms refuse to hire type B
 - Unbiased firms don't care, will hire whichever type is cheapest.

So equilibrium in the labor market might look like this



We see that in equilibrium $W^B < W^A$.

How can this be? Biased firms know they can pay less for type B workers, but they refuse to hire them. The wage W^A is where the demand for type A workers by biased firm equals all of the supply.

Since $W^B < W^A$, unbiased firms won't hire any type A workers, since they are too expensive. (Or rather then say they won't hire type A workers, they will offer W^B to both kinds of workers. But only type B workers will accept these wages. So W^B is where the supply of type B workers

equals the demand from unbiased firms.

Could we draw things differently and have an equilibrium where $W^B > W^A$?

Because.....

Bottom line: If some firms are biased, we can have an equilibrium where $W^B < W^A$.

But now think about the long run. Since biased firms pay higher wages for the same quality labor, biased firms will have higher average cost than unbiased firms. In the long run, low cost firms will tend to drive high cost firms out of the market.

We conclude: If discrimination is due to preferences by firms, we expect market forces to work towards driving the discrimination out of the market.

But what if firms don't care about the type of workers, but the firms' customers do? Suppose customers are biased and they don't like buying

from a firm that employs type B workers. Then these firms will be able to charge higher prices, and so they won't go out of business.

We conclude: If discrimination is due to preferences by consumers about the kind of workers that get hired, we **do not** expect market forces to work towards driving the discrimination out of the market.