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Reflections on American Wealth Concentration – and What To Do About It

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Just over one year ago, the Center on Capital & Social Equity (CCSE) began exploring the phenomenon of growing wealth concentration and inequality, while advocating for a more inclusive form of capitalism. Following are some general observations.

Over the past year, the issue of economic inequality in the United States has moved from the backburner to center stage. Much credit for this goes to Sen. Bernie Sanders' attack on the "top one percent" in his run for the Democratic nomination. While there is ample reason to question many details of his proposals, Sanders' call for an increased role for government in providing opportunity and essential services resonated with many Americans who feel they have been left out of the economic mainstream. Yet the problems posed by rising economic inequality are deeply rooted and go well beyond the disproportional gains of the top one percent. They will be harder to address than portrayed in election rhetoric and require judicious use of public resources.

Three observations can be made about economic inequality in the United States. First, income and wealth inequality have grown steadily since the 1980s, suggesting that some of the causes are structural in nature. Second, high levels of inequality increase the risk of political and economic instability. Finally, moving toward an economy that is less unequal and offers opportunity to more Americans will require major changes in public policy and shifts in spending.

<u>Wealth concentration is embedded in the economic and political system</u>. In most Western countries including the United States, economic and political systems create a tendency for wealth to concentrate at the top. This dynamic has been driven by a number of factors including the loss of jobs due to expanded global trade; rapid technology development that has reduced the role and leverage of labor; decisions on public policy and taxation; and the political power of the wealthy and corporate interests. The United States now has the highest level on income inequality in the world. The U.S. could soon have the highest level of wealth inequality, in part because those with the highest incomes also tend to have the highest levels of invested capital.

Analyzing how wealth is concentrating is tricky. A lot depends on how one defines economic classes. The Pew Research Center released a report in December 2015 showing that that the American middle class has shrunk since 1970 and that “the nation’s aggregate household income has substantially shifted from middle-income to upper-income households, driven by the growing size of the upper-income tier and more rapid gains in income at the top.” According to the report: “Fully 49 percent of U.S. aggregate income went to upper-income households in 2014, up from 29 percent in 1970. The share accruing to middle-income households was 43 percent in 2014, down substantially from 62 percent in 1970.”

An Urban Institute report published in June 2016 found that the percentage of wealthy and upper-middle-class Americans has grown dramatically since 1979, while middle- and lower-middle income tiers have become smaller. The study found that the proportion of the population in the upper middle class went from under 13 percent in 1979 to over 29 percent in 2014. The study divides the population into five tiers. The poor and the near-poor had annual incomes from $0 to $29,999; the lower middle class, from $30,000 to $49,999; the middle class, from $50,000 to $99,999; the upper middle class, from $100,000 to $349,999; and the rich, $350,000 and up.

The Urban Institute report also documents a major shift in the distribution of income: "In 1979, the bottom three income groups controlled 70 percent of all incomes, and the upper middle class and rich controlled 30 percent. By 2014, this distribution shifted to 37 percent for the bottom three groups and 63 percent for the upper middle class and rich groups. The middle class alone saw its share of income decline from 46 percent in 1979 to 26 percent in 2014."

A recent analysis by an International Monetary Fund economist also found increased income polarization in the U.S., and the number of middle-income households shrinking as a percent of total from 58 percent in 1970 to 47 percent in 2014. He defined middle-income households as those whose real incomes are within 50 to 150 percent of the median income. Households with incomes below this range were viewed as low-income and above it, high-income.

The global inequality picture is more complex, as economic growth in has led to a larger middle class in many countries such as China, which has closed the income gap somewhat if viewed across countries. (For more information on forces driving wealth and income inequality, see the "Economics of Inequality" section of the CCSE website.)

High levels of wealth concentration can undermine economic growth and stability, and corrode democratic forms of governance. Increasing wealth concentration has led to a smaller middle class and could lead to a growing number of low-income people in the United States and many other advanced countries. The "hollowing out" of the middle class dampens the growth of demand of goods and services, making it more difficult for the economy to grow. Ironically, as higher levels of inequality have muted growth of the tax base, policymakers face growing pressure to increase government spending to help people with low incomes. The sudden emergence of Sen. Sanders and Donald Trump in the U.S. presidential election is evidence that large numbers of people sense they are facing economic hardship. When people realize they are being left out of the economic mainstream, they are more likely to support radical political change.

Reducing the level of wealth concentration will require major changes in public policy. Policies that can reduce inequality include: 1) ensuring a basic standard of living for the poor; 2) enforcing minimum standards for wages and working conditions; 3) providing health care and retirement security through social insurance; and 4) ensuring that all citizens have economic opportunity and can benefit from growth of the economy. Policymakers should make use of all these tools, particularly those that broaden economic opportunity and inclusion:

- **Protecting the government safety net for the poor**. Current federal programs such as food assistance, Medicaid, and the earned income tax credit need to be maintained and expanded in accordance with the people's needs;
- **Ensuring fair wages and working conditions. T**he minimum wage should be increased to a level that allows people to cover the cost of living. Most important, the minimum wage should be indexed to inflation. All workers should have basic protections such as a minimum amount of sick leave;
- **Protecting and bolstering social insurance programs.** Social Security and Medicare, the most prominent and popular forms of social insurance in the U.S., should be protected, and benefits should be adjusted to meet the needs of the lower- and middle-income people; and
- **Fostering economic opportunity and inclusion.** Creating and funding institutions, such as a universal retirement savings system, that include all citizens in the capitalist system is one of the most effective ways to moderate economic inequality. Helping young people finance their education also is one of the most important ways to create greater opportunity and economic inclusion. And, of course, people need jobs.

Recognizing that many in the U.S. have very little or no retirement savings, President Obama said recently that the time has come to consider increasing future Social Security benefits. He is not alone in this regard. At least two policy think tanks with moderate to conservative leanings this year have proposed raising Social Security benefits for the lowest earners. The Bipartisan Policy Center's plan not only suggests increasing Social Security benefits for the lower-income, it also proposes a number of changes to keep the program solvent, including higher payrolls taxes, as well as developing a near-universal retirement savings system.

There is still great resistance among Republicans to maintaining many programs providing support to the poor at current levels. For example, the majority party in Congress continues to insist on repealing the Affordable Care Act (ACA), which has increased access to health insurance for millions of Americans. After six years of calling for repeal without offering an alternative, House Republicans on June 22 rolled out an outline of plan that would cover far fewer Americans than under the ACA. The House policy blueprint also would place caps on Medicaid spending and shift risk of medical inflation to Medicare beneficiaries. Instead of rolling the ACA's coverage expansion back and capping Medicaid, Congress should make health coverage universal by expanding Medicare to include all Americans (with a carve out for employers to run their own plans if they choose) and creating a national marketplace offering all qualified health plans to all citizens with premium subsidies for those that need them. Such a strategy could combine the best aspects of social insurance and marketplace efficiency.

One of the most important policies that could moderate the tendency of wealth to concentrate would be creation of a universal retirement savings system in which all citizens would have the ability to invest on a long-term basis with guidance of fiduciaries. The federal government already subsidizes voluntary retirement savings through tax incentives reaped primarily by the higher income, but about half of workers have little or no retirement savings. Shifting some government subsidies from higher to lower earners, where they are more needed, and helping people of modest means to invest in a way that provides comparable returns on investment to higher income people in the long run would help ensure their financial security and reduce wealth inequality. The CCSE web site presents a proposal for a universal retirement savings program and steps needed to implement it. While such a proposal might have seemed far-fetched in recent years, the Bipartisan Policy Center commission' report this month proposed a "near universal" retirement savings system, as noted above. As the U.S. begins exploring policy options in this area, many countries including Great Britain and Australia already have established universal retirement savings systems.

Many U.S. government agencies now make it a practice to analyze trends in economic inequality. In early June, the Congressional Budget Office (CBO) published a report documenting the growth of income inequality over past several decades and how government programs ("transfers") and taxes tend to reduce inequality. It is interesting that, even though government transfers and taxes, in aggregate, tend to reduce inequality, CBO found that the government is transferring more to the wealthiest fifth of the population than to the poorest fifth. As shown on the chart below, in 2013 federal government transferred $9,600 to the average household in the lowest fifth (quintile) by income, while federal transfers to the highest fifth were $12,000. Transfers to the middle three fifths of the populations were significantly higher than either for the poorest or richest. One could conclude that the relative size of government transfers reflects differences in the political power of Americans at different income levels far more than mirroring their need for assistance. The variation in transfers also shows that there is plenty of room for the country to do more for its poorest citizens.

Average Household Income, Transfers, and Taxes, by Before-Tax Income Group, 2013

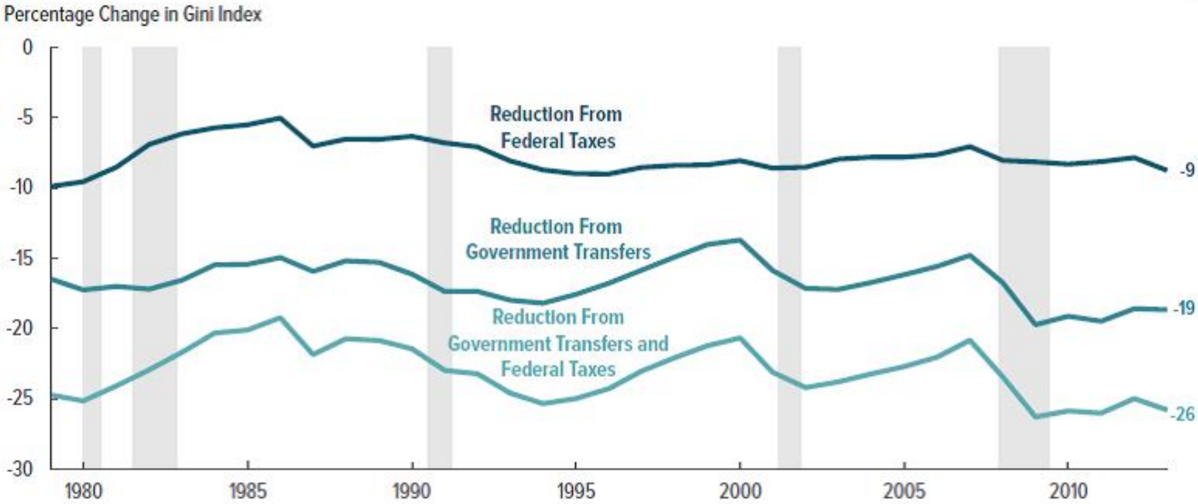
Dollars

	Lowest Quintile	Second Quintile	Middle Quintile	Fourth Quintile	Highest Quintile	All Households
Market Income	15,800	31,300	53,000	88,700	253,000	86,400
Government Transfers	9,600	16,200	16,700	15,000	12,000	13,900
Before-Tax Income	25,400	47,400	69,700	103,700	265,000	100,200
Federal Taxes	800	4,000	8,900	17,600	69,700	20,100
After-Tax Income	24,500	43,400	60,800	86,100	195,300	80,100

Source: "The Distribution of Household Income and Federal Taxes, 2013," Congressional Budget Office, June 8, 2016. See: https://www.cbo.gov/publication/51361

Figure 15.

Reduction in Income Inequality From Government Transfers and Federal Taxes, 1979 to 2013



Source: Congressional Budget Office.

The Gini index is a measure of income inequality that ranges from zero (the most equal distribution) to one (the least equal distribution). Gini indexes are calculated using income measures adjusted for household size.

Government transfers are cash payments and in-kind benefits from social insurance and other government assistance programs. Those transfers include payments and benefits from federal, state, and local governments.

Federal taxes include individual income taxes, payroll taxes, corporate income taxes, and excise taxes.