



Cornell University
ILR School

Cornell University ILR School
DigitalCommons@ILR

Book Samples

ILR Press

2012

The State of Working America

Lawrence Mishel

Josh Bivens

Elise Gould

Heidi Shierholz

Follow this and additional works at: <https://digitalcommons.ilr.cornell.edu/books>

Thank you for downloading an article from DigitalCommons@ILR.

Support this valuable resource today!

This Article is brought to you for free and open access by the ILR Press at DigitalCommons@ILR. It has been accepted for inclusion in Book Samples by an authorized administrator of DigitalCommons@ILR. For more information, please contact catherwood-dig@cornell.edu.

If you have a disability and are having trouble accessing information on this website or need materials in an alternate format, contact web-accessibility@cornell.edu for assistance.

The State of Working America

Abstract

[Excerpt] Like its predecessors, this edition of *The State of Working America* digs deeply into a broad range of data to answer a basic question that headline numbers on gross domestic product, inflation, stock indices, productivity, and other metrics can't wholly answer: "How well has the American economy worked to provide acceptable growth in living standards for most households?"

According to the data, the short answer is, "not well at all." The past 10 years have been a "lost decade" of wage and income growth for most American families. A quarter century of wage stagnation and slow income growth preceded this lost decade, largely because rising wage, income, and wealth inequality funneled the rewards of economic growth to the top. The sweep of the research in this book shows that these trends are the result of inadequate, wrong, or absent policy responses. Ample economic growth in the past three-and-a-half decades provided the potential to substantially raise living standards across the board, but economic policies frequently served the interests of those with the most wealth, income, and political power and prevented broad-based prosperity.

Comments

The abstract, table of contents, and first twenty-five pages are published with permission from the Cornell University Press. For ordering information, please visit the [Cornell University Press](#).

The State of Working America

12th Edition

The State of Working America

12th Edition

LAWRENCE MISHEL

JOSH BIVENS

ELISE GOULD

HEIDI SHIERHOLZ



ILR Press

an imprint of Cornell University Press
Ithaca and London

Copyright © 2012 by Cornell University

All rights reserved. Except for brief quotations in a review, this book, or parts thereof, must not be reproduced in any form without permission in writing from the publisher.

For information, address Cornell University Press, Sage House, 512 East State Street, Ithaca, New York 14850.

First published 2012 by Cornell University Press
First printing, Cornell Paperbacks, 2012

ISBN 978-0-8014-5170-6 (cloth: alk. paper)

ISBN 978-0-8014-7855-0 (paper: alk. paper)

Printed in the United States of America

Recommended citation for this book is as follows: Mishel, Lawrence, Josh Bivens, Elise Gould, and Heidi Shierholz, *The State of Working America, 12th Edition*. An Economic Policy Institute Book. Ithaca, N.Y.: Cornell University Press, 2012

Cornell University Press strives to use environmentally responsible suppliers and materials to the fullest extent possible in the publishing of its books. Such materials include vegetable-based, low-VOC inks and acid-free papers that are recycled, totally chlorine-free, or partly composed of nonwood fibers. For further information, visit our website at www.cornellpress.cornell.edu.

Cloth printing 10 9 8 7 6 5 4 3 2 1
Paperback printing 10 9 8 7 6 5 4 3 2 1

For the newest generation in my family, grandson Oliver and great nephew Nathan, who won't hit the job market for two decades.

— LAWRENCE MISHEL

To Holley and Finn, as well as to my parents and in-laws, who sometimes must think that they're the only people in the world I'm not trying to flood with my views on how the economy is doing.

— JOSH BIVENS

To Alex for patience and understanding; Eli, Sarah, and Jess for inspiration and perspective; and mom and dad for everlasting support.

— ELISE GOULD

For my little sangha, Alan, Sal, and Iko.

— HEIDI SHIERHOLZ

Visit **StateofWorkingAmerica.org**

The StateofWorkingAmerica.org website presents up-to-date historical data series on incomes, wages, employment, poverty, and other topics. All data presented in this book can be viewed online or downloaded as spreadsheets.

Acknowledgments

The preparation of this publication requires the work of many people on EPI's staff as well as contributions from other researchers. At EPI, Nicholas Finio, Natalie Sabadish, and Hilary Wething provided valuable research assistance by collecting and organizing data and creating the tables and figures with diligence, dedication, and good humor. Jin Dai provided extensive and able computer programming and data analysis.

We thank all the co-authors of previous editions of *The State of Working America*—Sylvia Allegretto, Jared Bernstein, Heather Boushey, David Frankel, John Schmitt, and Jacqueline Simon—for their lasting contributions. Joe Procopio and Pat Watson, editors of previous editions of this volume, also deserve acknowledgment for their contributions.

We want to particularly recognize the contribution of Lora Engdahl, EPI's publications director. Lora directed the entire production process, coordinating with the authors, the publisher, the designer, and EPI staff to ensure the highest quality product possible. She spent many late nights and weekends editing every chapter, every table, and every endnote with intelligence, diligence, and precision, providing much-needed consistency throughout the chapters. The book is better for her efforts and we are grateful.

EPI's communications team, led by Jody Franklin, worked diligently, creatively, and around-the-clock to produce this publication, to make its information available on the Web, and to disseminate it to the media and many other audiences. We thank editors Michael McCarthy and Pat Watson. We thank the Web and design team led by Eric Shansby, our online and creative director, who devised a new, more efficient Web-based system for producing the tables and figures. Dan Essrow, EPI's graphic designer, designed the book cover as well as many collateral pieces associated with this project. Communications team members Arin Karimian and Yesica Zuniga also helped get text and figure files ready for the design firm Winking Fish, led by Kieran Daly, which once again laid out the entire book with dedication and great patience. EPI's media relations team—led by Phoebe Silag and including Karen Conner and Donté Donald—provided very creative work to communicate our findings to the media, in all its many incarnations, traditional, social, and new. We acknowledge the dedicated work of Karen Conner, who has recently left EPI—this is the sixth edition of *The State of Working America* she has been an integral part of, and we will miss her expertise the next time around.

Many experts were helpful in providing data or their research papers for our use. We are particularly grateful for the assistance of Ed Wolff, who provided special tabulations. Others who provided data, advice, or their analysis include David Autor, Jon Bakija, Michael Chernousov, Miles Corak, Dirk Jenter, Janelle Jones, Brooks Pierce, and John Schmitt. Colleagues at the Economic Policy Institute,

particularly David Cooper and Monique Morrissey, provided guidance and data for particular sections of the book. Christian Dorsey was responsible for generating the fact sheets that make this information accessible to a broader audience who (though we can't imagine why) might not want to read the entire book.

We extend our gratitude to the many dedicated public servants who collect and produce economic data for the U.S. government, including those at the Bureau of Labor Statistics, the Census Bureau, the Bureau of Economic Analysis, the Congressional Budget Office, and the Federal Reserve. Without their work, we could not have written this book.

Last, we wish to thank the following funders for their support of the Economic Policy Institute: The Annie E. Casey Foundation; The Atlantic Philanthropies; The Bauman Foundation; Ford Foundation; W.K. Kellogg Foundation; Open Society Foundations; Public Welfare Foundation; The Rockefeller Foundation; and Anonymous.

—The authors

Table of contents

Documentation and methodology	1
--	----------

Chapter 1

Overview: Policy-driven inequality blocks living-standards growth

for low- and middle-income Americans.....	5
--	----------

America's vast middle class has suffered a 'lost decade' and faces the threat of another.....	5
Income and wage inequality have risen sharply over the last three-and-a-half decades.....	6
Rising inequality is the major cause of wage stagnation for workers and of the failure of low- and middle-income families to appropriately benefit from growth.....	6
Economic policies caused increased inequality of wages and incomes	7
Claims that growing inequality has not hurt middle-income families are flawed.....	8
Growing income inequality has not been offset by increased mobility	9
Inequalities persist by race and gender	9

Economic history and policy as seen from below the top rungs of the wage and income ladder.....	10
--	-----------

The Great Recession: Causes and consequences.....	11
--	-----------

A very condensed macroeconomic history of the Great Recession and its aftermath.....	12
--	----

Economic 'lost decades': Weak growth for most Americans' wages and incomes before and likely after the Great Recession	15
---	-----------

Weak labor demand at the heart of the lost decade	16
Weak labor demand devastates key living standards	18
Dim growth prospects forecast another lost decade.....	20
Two key lessons from the lost decade	22

Extraordinarily unequal growth <i>before</i> the lost decade: Rising inequality blocks income and wage growth from 1979 to 2007	23
--	-----------

Income inequality and stagnating living standards.....	23
Wage inequality and the break between wages and productivity.....	28
Strong income and wage growth in the atypical last half of the 1990s.....	31
Economic mobility has neither caused nor cured the damage done by rising inequality.....	33

Today's private economy: Not performing for middle-income Americans.....	35
---	-----------

Middle-income growth lags average income growth and historical income growth rates.....	35
Social insurance programs, not private sources, account for the majority of middle-fifth income growth.....	36
Growing shares of income are dedicated to holding families harmless against rising medical costs.....	36
Households have to work more to achieve income gains	37
Assessing what the private economy is really delivering to middle-income Americans.....	38

Today's economy: Different outcomes by race and gender	39
---	-----------

Many more than just two Americas.....	39
Male and female America	41
No one 'American economy'.....	43

Conclusion: The struggling state of working America is policy-driven43
 The policy good for everybody in the fractured U.S. economy: Ensuring rapid recovery
 to full employment.....46
Table and figure notes48

Chapter 2

Income: Already a ‘lost decade’..... 53
The basic contours of American incomes.....57
 Family and household money income 58
 Median family income as a metric of economic performance..... 65
 A look at income by income fifths..... 67
 Median family income by race, ethnicity, and nativity..... 68
The Great Recession and American incomes71
 Impact by income group..... 71
 Impact by race and ethnicity 74
 Income losses projected for years to come 74
Rising inequality of American incomes.....76
 Family income inequality 76
 Unequal growth of comprehensive household incomes suggests diverging well-being 79
 Sharp rise in income inequality apparent in every major data source 80
 The limited impact of taxes and transfers relative to market income 84
 Factors behind the large rise in inequality of market incomes..... 94
**How much did middle-income living standards actually rise
 between 1979 and 2007? 106**
 Measuring living standards at the middle 107
 Sources of income for the middle fifth 109
 Income growth for the middle fifth has been driven largely by elderly households’
 pension and transfer income 112
 Adjusting income for the truer contribution of health care transfers 112
 Disproportionate growth of transfers directed toward elderly households 114
 The role of hours worked and educational upgrading in wage growth 120
 Little of the growth of middle incomes can be attributed to a well-functioning economy..... 127
Conclusion 128
Table and figure notes 130

Chapter 3

Mobility: Not offsetting growing inequality..... 139
Intragenerational mobility 142
 Lifetime mobility against the backdrop of generational stagnation 142
 Family and individual mobility trends 143
 Factors associated with intragenerational mobility 147
Intergenerational mobility 150
 Cross-country comparisons 151

The impact of race, wealth, and education on mobility.....	154
Race.....	155
Wealth.....	156
Education.....	157
Income inequality and mobility.....	161
Has the American Dream become more or less attainable over time?.....	163
Conclusion	168
Figure notes.....	169

Chapter 4

Wages: The top, and very top, outpace the rest	173
Describing wage trends	177
The decade of lost wage growth.....	177
Contrasting work hours and hourly wage growth	179
Contrasting compensation and wage growth	180
Wages of production and nonsupervisory workers	183
Wage trends by wage level	185
Shifts in low-wage jobs.....	192
Trends among very high earners fuel growing wage inequality.....	194
Trends in benefit growth and inequality	198
Dimensions of wage inequality	206
Gaps between higher- and lower-wage workers.....	208
Gaps between workers with different education and experience levels.....	211
The gap between workers with comparable education and experience	213
Rising education/wage differentials.....	214
Young workers' wages.....	222
The growth of within-group wage inequality.....	228
Wage inequality by race/ethnicity and gender.....	232
Productivity and the compensation/productivity gap.....	235
Factors driving wage inequality	241
Unemployment	242
The shift to low-paying industries	247
Employer health care costs	248
Trade and wages.....	253
Immigration	265
Unionization	268
The decline in the real value of the minimum wage	279
Executive and finance-sector pay.....	286
Explaining wage inequality: Bringing the factors together	292
Technology and skill mismatches.....	294
What is the appeal of the technology story?	295
Education gaps and wage inequality	296
The slowdown in the growth of demand for college graduates	299
Within-group wage inequality	301
The labor market difficulties of college graduates	302

Jobs of the future	305
Conclusion	309
Table and figure notes	310

Chapter 5

Jobs: A function of demand	321
Job creation is a macroeconomic outcome	323
Zero is not the baseline for job growth	325
What are today's jobs like?	327
Industries	327
Firm size	329
Occupations	330
Job quality	333
Unemployment	334
Unemployment and age	336
Unemployment and race/ethnicity, gender, and education	339
Unemployment rates of foreign- and native-born workers	342
Unemployment insurance benefits	343
Labor force participation: Structural and cyclical changes	345
Beyond the unemployment rate: Other measures of labor market slack	348
Employment-to-population ratio	349
Underemployment	350
Long-term unemployment	351
Over-the-year unemployment	354
Job-seekers ratio	355
Voluntary quits	356
Recovering from the Great Recession	357
Comparing the Great Recession and its aftermath with earlier recessions and recoveries	358
Job loss and gender in the Great Recession	360
Unemployment in the aftermath of the Great Recession: Structural or cyclical?	363
The consequences of job loss and unemployment for workers and their families	367
Conclusion	370
Table and figure notes	371

Chapter 6

Wealth: Unrelenting disparities	375
Net worth	377
The racial divide in net worth	385
Assets	386
Stocks	391
Housing	393
Retirement insecurity	398
Liabilities	400
Student loan debt	403

Debt relative to disposable personal income.....	404
Debt service.....	404
Hardship.....	408
Bankruptcy.....	409
Wealth of U.S. citizens compared with citizens' wealth in peer countries	411
Conclusion	413
Table and figure notes	414
Chapter 7	
Poverty: The Great Recession adds injury to insult.....	419
Poverty measurement	421
Official poverty line.....	421
Supplemental Poverty Measure.....	428
Relative poverty.....	431
The working poor	432
Poverty-level wages.....	432
Job quality.....	434
Work hours.....	435
Determinants of low incomes.....	437
The macro economy and poverty	437
The impact of economic, demographic, and education changes on poverty rates.....	440
Resources for low-income Americans.....	444
International comparisons	447
Poverty and the earnings distribution	448
Resource allocation.....	452
Conclusion	454
Table and figure notes	455
Appendix A: CPS income measurement	461
Appendix B : Wage measurement	465
Bibliography	475
Index	489
About EPI.....	504
About the authors	505

Documentation and methodology

Documentation

This book's comprehensive portrait of changes over time in incomes, taxes, wages, employment, wealth, poverty, and other indicators of economic performance and well-being relies almost exclusively on data in the tables and figures. Each table and figure has an abbreviated source notation that corresponds with a full citation in the bibliography at the end of the book. More detailed documentation (as well as information on methodology) is contained in the table and figure notes found at the end of each chapter. This system of documentation allows us to omit distracting footnotes and long citations within the text and tables.

In instances where we directly reproduce other people's work, table and figure source lines provide an "author/year" reference to the bibliography. Where we present our own computations based on other people's work, the source line reads "Authors' analysis of (source)." In these instances we have made computations that do not appear in the original work and are thus responsible for our analyses and interpretations. We also use this source notation when presenting descriptive trends from government income, employment, or other data, since we have made judgments about the appropriate time periods or other matters for the analysis that the source agencies have not made. When we present our own analysis of survey data we list the name of the survey and cite as a source "Authors' analysis of [name of Survey]." The table or figure notes provide information on the data analysis.

Time periods

Economic indicators fluctuate considerably with short-term swings in the business cycle. For example, incomes tend to fall in recessions and rise during expansions. Therefore, economists usually compare business cycle peaks with other peaks and compare troughs with other troughs so as not to mix apples and oranges. In this book, we examine changes between business cycle peaks. The initial year for some tables is 1947, with intermediate years of 1967, 1973, 1979, 1989, 2000, and 2007, all of which were business cycle peaks (at least in terms of having low unemployment). We also present data for the latest full year for which data are available (2010 or 2011 when available). Whenever figures show recessionary periods we base these on the National Bureau of Economic Research dating of cycles (NBER 2010).

In some tables, we also separately present trends for the 1995–2000 period (referred to as the late 1990s) in order to highlight the differences between those years and those of the early 1990s (or, more precisely, 1989–1995) and the business cycle of 2000–2007. This departs from the convention of presenting only business cycle comparisons (e.g., comparing 1979–1989 with 1989–2000 trends) or comparisons of recoveries. We depart from the convention because there was a marked shift in a wide variety of trends after 1995, and it is important to understand and explain these trends. We frequently refer to the 1979–2007 period because it represents the long period of growing inequality that predated the recession that began at the end of 2007.

Growth rates and rounding

Since business cycles differ in length, to facilitate comparisons we often present the average annual growth rates in each period rather than the total growth. In some circumstances, as noted in the particular tables, we have used log annual growth rates. This is done to permit decompositions.

In presenting the data, we round the numbers, usually to one decimal place, but we use unrounded data to compute growth rates, percentage shares, and so on. Therefore, it is not always possible to exactly replicate our calculations by using the data in the table. In some circumstances, this leads to an appearance of errors in the tables. For instance, we frequently present shares of the population (or families) at different points in time and compute changes in these shares. Because our computations are based on the “unrounded” data, the change in shares presented in a table may not exactly match the difference in the actual shares. Such rounding discrepancies are always small, however, and never change the conclusions of the analysis.

Adjusting for inflation

In most popular discussions, the Consumer Price Index for All Urban Consumers (CPI-U), often called the consumer price index, is used to adjust dollar values for inflation. However, some analysts hold that the CPI-U overstated inflation in the late 1970s and early 1980s by measuring housing costs inappropriately. The methodology for the CPI-U from 1983 onward was revised to address these objections. Other changes were introduced into the CPI-U in the mid-1990s but not incorporated into the historical series. Not all agree that these revisions are appropriate. We choose not to use the CPI-U to avoid any impression that this book's analyses overstate the decline in wages and understate the growth in family incomes over the last few decades.

Instead of the CPI-U, we adjust dollar values for inflation using the Consumer Price Index Research Series Using Current Methods (CPI-U-RS). This index uses the post-1983 methodology for housing inflation over the entire 1967–2007 period and incorporates the 1990s changes into the historical series (though not before 1978, as doing so would make economic performance in the years after 1978 falsely look better than the earlier years). The CPI-U-RS is now used by the Census Bureau in its presentations of real income data. Because it is not available for years before 1978, we extrapolate the CPI-U-RS back to earlier years based on inflation as measured by the CPI-U.

In our analysis of poverty in Chapter 7, however, we generally use the CPI-U rather than the CPI-U-RS, since the chapter draws heavily from Census Bureau publications that use the CPI-U. Moreover, the net effect of all of the criticisms of the measurement of poverty is that current methods understate poverty. Switching to the CPI-U-RS without incorporating other revisions (i.e., revising the actual poverty standard) would lead to an even greater understatement and would be a very selective intervention to improve the poverty measurement. (A fuller discussion of these issues appears in Chapter 7.)

The Current Population Survey

Many tables and figures in the book are based on original analyses of survey data generated by the monthly Current Population Survey (CPS), which is best known for producing the monthly unemployment rate and for the annual data on poverty and incomes. There are three separate CPS sources of data employed in our analyses: the Annual Social and Economic Supplement (the ASEC, commonly referred to as the March Supplement), the full monthly public data series, and the Outgoing Rotation Group. We examine trends in annual household or family income and poverty, as well as employer-provided benefits (health and pension) and annual wages, using the March Supplement. The formal name for these data and the way the data are referred to in source notes is the “Current Population Survey Annual Social and Economic Supplement microdata” or “Current Popula-

tion Survey Annual Social and Economic Supplement *Historical Income Tables*.” Details of our use of the March microdata are presented in Appendix A. We employ the full samples of the monthly CPS in analyses of employment/unemployment trends, and this is referred to in source notes as “basic monthly Current Population Survey microdata.” The CPS Outgoing Rotation Group (CPS-ORG) provides information on the wages of workers for one-fourth of each month’s sample, and we use these data for analyses of wage trends. These data are referred to in source notes as “Current Population Survey Outgoing Rotation Group microdata.” Details of our use of these wage data are provided in Appendix B.

Household heads and families

We often categorize families by the age or the racial/ethnic group of the “household head,” that is, the person in whose name the home is owned or rented. If the home is owned jointly by a married couple, either spouse may be designated the household head. Every family has a single household head. A “household head” may sometimes be referred to as the “householder.”

Black, Hispanic, and white designations

Unless otherwise noted, races/ethnicities are presented in the following mutually exclusive categories: White refers to non-Hispanic whites, black refers to non-Hispanic blacks, and Hispanic refers to Hispanics of any race.

However, we sometimes use data from published sources that employ the U.S. Census Bureau’s convention of including Hispanics in racial counts (e.g., with blacks and whites) as well as in a separate category. For instance, in Table 2.5 a white person of Hispanic origin is included both in counts of whites and in counts of Hispanics. In these cases, we alert readers to the exception.

Overview

Policy-driven inequality blocks living-standards growth for low- and middle-income Americans

Like its predecessors, this edition of *The State of Working America* digs deeply into a broad range of data to answer a basic question that headline numbers on gross domestic product, inflation, stock indices, productivity, and other metrics can't wholly answer: "How well has the American economy worked to provide acceptable growth in living standards for most households?"

According to the data, the short answer is, "not well at all." The past 10 years have been a "lost decade" of wage and income growth for most American families. A quarter century of wage stagnation and slow income growth preceded this lost decade, largely because rising wage, income, and wealth inequality funneled the rewards of economic growth to the top. The sweep of the research in this book shows that these trends are the result of inadequate, wrong, or absent policy responses. Ample economic growth in the past three-and-a-half decades provided the potential to substantially raise living standards across the board, but economic policies frequently served the interests of those with the most wealth, income, and political power and prevented broad-based prosperity.

America's vast middle class has suffered a 'lost decade' and faces the threat of another

Wages and incomes of typical Americans are lower today than in over a decade. This lost decade of no wage and income growth began well before the Great Recession battered wages and incomes. In the historically weak expansion following the 2001 recession, hourly wages and compensation failed to grow for either

high school– or college-educated workers and, consequently, the median income of working-age families had not regained pre-2001 levels by the time the Great Recession hit in December 2007. Incomes failed to grow over the 2000–2007 business cycle despite substantial productivity growth during that period.

Although economic indicators as of mid-2012 are stronger than they were two or three years ago, protracted high unemployment in the wake of the Great Recession has left millions of Americans with lower incomes and in economic distress. This problem is actually quite solvable: Tackle the source of the problem—insufficient demand—with known levers of macroeconomic policy to generate demand. Unfortunately, the problem is not being solved.

Consensus forecasts predict that unemployment will remain high for many more years, suggesting that typical Americans are in for another lost decade of living standards growth as measured by key benchmarks such as median wages and incomes. For example, as a result of persistent high unemployment, we expect that the incomes of families in the middle fifth of the income distribution in 2018 will still be below their 2007 and 2000 levels.

Income and wage inequality have risen sharply over the last three-and-a-half decades

Income inequality in the United States has grown sharply over the last few decades. This is evident in nearly every data measure and is universally recognized by researchers. For example, if we look at cash “market-based incomes,” which exclude the effects of taxes and transfers (benefits received through government programs such as Social Security) and employer-provided in-kind benefits such as health insurance, the top 1 percent of tax units claimed more than six times as much of the total income growth between 1979 and 2007 as the bottom 90 percent—59.8 percent to 8.6 percent. Similarly, there has been a tremendous disparity in the growth of wages earned by individual workers. Wages for the top 1 percent grew about 156 percent between 1979 and 2007, whereas wages for the bottom 90 percent rose by less than 17 percent.

Rising inequality is the major cause of wage stagnation for workers and of the failure of low- and middle-income families to appropriately benefit from growth

There has been sufficient economic growth since 1979 to provide a substantial across-the-board increase in living standards. However, because wage earners and households at the top reaped most of the benefits of this growth, wages were relatively stagnant for low- and middle-wage workers from 1979 to 2007 (except in the late 1990s), and incomes of lower- and middle-class households grew slowly. This pattern of income growth contrasts sharply with that of the postwar period up through the 1970s, when income growth was broadly shared.

The economy's failure to ensure that typical workers benefit from growth is evident in the widening gap between productivity and median wages. In the first few decades after World War II, productivity and median wages grew in tandem. But between 1979 and 2011, productivity—the ability to produce more goods and services per hour worked—grew 69.2 percent, while median hourly compensation (wages and benefits) grew just 7.0 percent.

Economic policies caused increased inequality of wages and incomes

Since the late 1970s, economic policy has increasingly served the interests of those with the most wealth, income, and political power and effectively shifted economic returns from typical American families to the already well-off. A range of economic policy choices—both actions and failures to act—in the last three decades have had the completely predictable effect of increasing income inequality. These choices include letting inflation consistently erode the purchasing power of the minimum wage, and allowing employer practices hostile to unionization efforts to tilt the playing field against workers. U.S. policies have also hastened integration of the U.S. economy and the much poorer global economy on terms harmful to U.S. workers, refused to manage clearly destructive international trade imbalances, and targeted rates of unemployment too high to provide reliably tight labor markets for low- and middle-wage workers.

Industry deregulation (of trucking, communications, airlines, and so on) and privatization have also put downward pressure on wages of middle-class workers. Meanwhile, deregulation of the financial sector—without a withdrawal of the government guarantees that allow private interests to take excessive risks—has provided the opportunity for well-placed economic actors to claim an ever-larger share of economic growth. An increasingly well-paid financial sector and policies regarding executive compensation fueled wage growth at the top and the rise of the top 1 percent's incomes. Large reductions in tax rates provided a motive for well-placed actors to take these risks and also fueled the after-tax income growth at the top.

Although these post-1979 economic policies predictably redistributed wages, income, and wealth upward, there was no corresponding benefit in the form of faster overall economic growth. In fact, economic growth from the 1970s onward was slower than the economic growth in the prior 30 years. Besides resulting in slower growth, economic policy decisions also contributed to the fragility of the U.S. economy in the run-up to the Great Recession. For example, otherwise-anemic economic growth in the mid-2000s was driven by a housing bubble made possible largely through a deregulated financial sector that was hiding, not managing, the growing risk that home prices would fall. This economic fragility proved catastrophic when confronted with the shock of plummeting

demand after the housing bubble burst and destroyed families' housing wealth. More equitable and stable economic growth can only occur if there is a marked change in the direction of U.S. economic policy.

Claims that growing inequality has not hurt middle-income families are flawed

Despite the near-universal acknowledgement of growing income inequality as a fact of recent American economic history, a number of studies have claimed that it has not prevented middle-income families from achieving acceptable income growth since 1979. These studies argue that under a comprehensive measure of income that includes benefits from employers and government transfers, incomes of the middle fifth of households in the income distribution grew by 19.1 percent between 1979 and 2007. But this 19.1 percent cumulative (0.6 percent annual) growth rate does not mean that the private sector of the American economy is performing well for middle-income families. First, had the middle fifth's incomes grown at the same 51.4 percent cumulative rate as overall average incomes (i.e., had there been no growth in income disparities), their annual income in 2007 would have been far greater—\$18,897 higher. Second, this 0.6 percent annual growth rate does not come close to the income growth between 1947 and 1979, when middle-fifth family income grew 2.4 percent annually.

Third, the large share of this 1979–2007 income growth coming from government transfers (53.6 percent) reflects the strength of American social insurance programs (Social Security, Medicare, and Medicaid) and is not evidence that the private U.S. economy is being managed effectively or fairly. Given the unnecessary push to cut these programs going forward, it is unlikely that this source of middle-class income growth can be relied on in future decades. Fourth, higher household labor earnings contributed a modest 6.1 percent to this middle-fifth income growth, and the impressive ability of American households to steadily increase their work hours over this period, in part by increasing the number of household members employed, will not be replicable in the years ahead.

Last, the data on comprehensive incomes are technically flawed because they count, as income, rapidly rising health expenditures made on behalf of households by employers and the government without accounting for the excessive health care inflation that has absorbed large portions of the increase in this particular source of income. If rising health care costs are properly accounted for, the 19.1 percent growth in comprehensive middle-fifth incomes is lowered by a third. If we strip out health care inflation, government transfers, and additional hours worked—elements that add to measured income growth but cannot be attributed to a well-performing private economy—middle-class incomes grew just 4.9 percent across the 28 years from 1979 to 2007, with most of that growth occurring just in the late 1990s.

Growing income inequality has not been offset by increased mobility

Growing income inequality in the United States is a trend made more disturbing by static, and perhaps declining, economic mobility. Despite the image of the nation as a place where people with initiative and skills can vault class barriers, America today is not a highly mobile society, compared with our international peers. In one study of 17 Organisation for Economic Co-Operation and Development (OECD) countries, the United States ranked 13th on a measure of mobility, ahead only of Slovenia, Chile, Italy, and the United Kingdom, and far behind Denmark, Norway, Finland, and Canada.

Americans largely end up where they started out on the economic ladder, and the same is true for their children. For example, one study showed that two-thirds (66.7 percent) of sons of low-earning fathers (in the bottom fifth of the earnings distribution) end up in the bottom two-fifths as adults, while only 18.1 percent make it to the top two-fifths. There is no evidence that mobility has increased to offset rising inequality, and in fact some research shows a decline.

Inequalities persist by race and gender

As this book, and our research in general, shows, there is actually no single economic “state of America” but rather an America that is experienced differently, and often unequally—not only by class, as discussed, but by race and gender. For example, a review of employment rates from 1979 to 2011 shows that black and Hispanic unemployment always far exceeded white unemployment. As this book was nearing completion in July 2012, the overall unemployment rate was 8.3 percent—roughly the same as the African American unemployment rate during all of 2007, the last year of economic expansion before the Great Recession.

Further, even in 1992, the peak of black/white equality in wealth holdings, median black household wealth was just 16.8 percent of median white household wealth. By 2010—after the housing bubble had burst and destroyed \$7 trillion in equity in residential real estate (the most widely held type of wealth)—median African American wealth was just 5.0 percent of median white wealth.

And while gaps between labor market outcomes of men and women have closed in recent decades, progress has occurred not just because women gained ground, but also because men lost ground. Gaps in employer-provided pension coverage rates between men and women, for example, have rapidly closed in recent decades, but only because men’s coverage rates have fallen while women’s have stagnated.

Economic history and policy as seen from below the top rungs of the wage and income ladder

This chapter assesses U.S. economic performance over the last 30 years through the lens of this failure of the economy to deliver appropriate gains to the broad middle class and fuel greater social mobility. One could label this policy regime a “failure,” but one could also say this was a “failure by design”—the policies worked as intended to boost the economic standing of those who already had the most income and wealth. Our discussion in this chapter begins with the Great Recession and its aftermath, moves to the lost decade period commencing with the 2001 recession, and concludes with the years between 1979 and the beginning of the Great Recession.

The Great Recession: The shock to demand and the need for continued stimulus. The key lesson to be learned from our current crisis is that full and meaningful recovery from the Great Recession that officially ended in June 2009 has not yet happened and is assuredly not guaranteed. As this book is being written in mid-2012, things are indeed better than they were two and three years ago, but the American economy remains far from healthy, and there is danger in prematurely declaring “mission accomplished.” There is a clear continued need for fiscal stimulus such as aid to the states, infrastructure investments, and safety net supports such as unemployment insurance and food stamps, as well as expansionary monetary policy. But, just as patients prescribed antibiotics should not stop taking them as soon as their immediate symptoms fade, we must not remove economic supports before full economic health has been genuinely restored; doing so could come back to hurt us.

Economic lost decades: The threat of continued disappointing wage and income growth. Our examination of a broad range of living standards benchmarks argues strongly that recovery to the economic conditions that prevailed in 2007, immediately prior to the Great Recession, is too modest a goal. The 2000s expansion was the weakest on record and provided very little in terms of lasting gains for American families. As a result, we have had a lost decade where wages and benefits failed to grow for the vast majority of the workforce, including college-educated workers as well as the two-thirds of the workforce who lack a college degree. The typical working-age family had lower income in 2007 than before the early 2000s recession, and incomes fell further in the Great Recession. Using current projections of unemployment in coming years, we estimate that the average income of households in the middle fifth of the income distribution will remain below its 2000 level until at least 2018. This would lead to another lost decade for far too many American workers and the households and families they support.

Stagnating living standards before the lost decade: Rising inequality from 1979 to 2007 halts income and wage growth for most Americans. The stagnation of wages and incomes for low- and middle-income households during the 2000s was merely a continuation of longer-term trends. For most of the years between 1979 and 2007, living standards growth for most American households lagged far behind overall average growth because the vast majority of growth was claimed by a select sliver at the top of the income ladder. Without a brief period of strong across-the-board wage and income growth in the late 1990s, virtually the *entire* 28-year period before the Great Recession may well have been an era of lost growth for low- and middle-income families. The key to understanding the growing inequality of wages and benefits is the continued divergence between the growth of productivity and the hourly wages and benefits of a typical worker. Explaining this divergence is essential for understanding the failure of the U.S. economy to deliver for most Americans and their families.

Table notes and figure notes at the end of this chapter provide documentation for the data, as well as information on methodology, used in the tables and figures that follow.

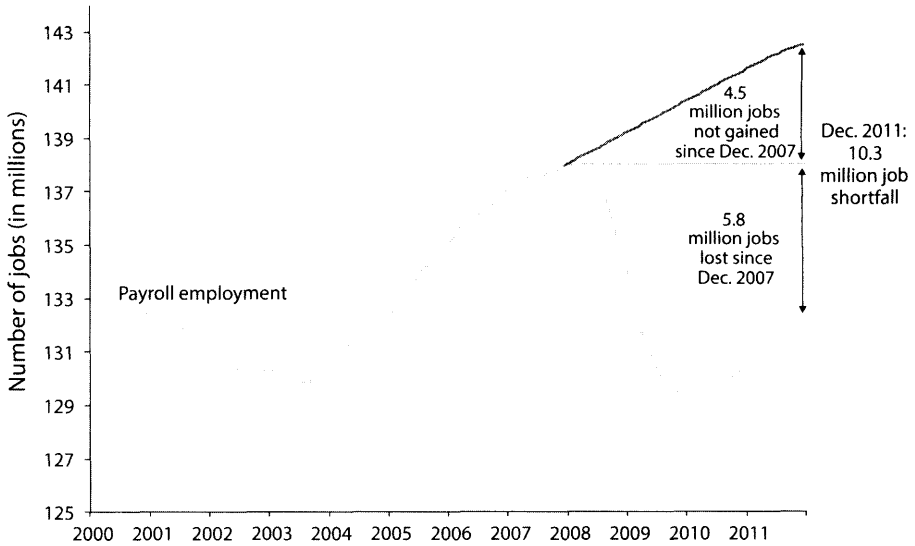
The Great Recession: Causes and consequences

The State of Working America's analysis of economic data extends from the 1940s through 2011. In the context of recent history, there was good news for the American economy at the end of 2011: After peaking at 10.0 percent in October 2009, the unemployment rate had fallen by 1.5 percentage points, fully 1.3 of which had been shaved off just in the preceding 13 months.

Unfortunately, this decline in the unemployment rate from October 2009 to December 2011 was not driven primarily by a jobs boom. Rather, essentially all of the reduction was spurred by a sharp decrease in the labor force participation rate (the share of working-age people who are either employed or unemployed, i.e., jobless but actively seeking work), which dropped by a full percentage point. Most of this decline in labor force participation was due to the sluggish economy itself, rather than any long-term demographic trend (as demonstrated in Table 5.5 later in this book).

Even worse, the unemployment rate at the end of 2011 was 8.5 percent—higher than it had been since 1983 (except since the onset of the Great Recession). Further, there remained a huge gap between labor-market health at the end of 2011 and even that which prevailed in December 2007, which was hardly a high-water mark (as will be discussed later). The size of this gap in labor-market health is depicted in **Figure 1A**: In December 2011, the American economy needed roughly 10.3 million jobs to return to the unemployment and labor force participation rates of December 2007—5.8 million jobs to replace those still lost from

Figure 1A Payroll employment and the number of jobs needed to keep up with the growth in the potential labor force, Jan. 2000–Dec. 2011



Source: Authors' analysis of Bureau of Labor Statistics Current Employment Statistics and Congressional Budget Office (2012)

the recession and 4.5 million new jobs to absorb the growth in the working-age population.

The source of this labor market distress is clear: the Great Recession, brought on at the end of 2007 by the bursting of the housing bubble that had provided the only real boost to the otherwise-anemic recovery from the 2001 recession.

A very condensed macroeconomic history of the Great Recession and its aftermath

Between June 2006 and June 2009, housing prices fell roughly 30 percent, which erased roughly \$7 trillion in U.S. household wealth. According to extensive research literature on the housing “wealth effect,” each \$1 in housing wealth generates roughly 6 to 8 cents of annual consumer spending. Thus the \$7 trillion in lost housing wealth led to a roughly \$500 billion contraction in consumer spending. On top of this, as housing prices fell, activity in the overbuilt residential real estate construction sector (i.e., building new homes and buildings) collapsed, leading to roughly another \$400 billion in lost demand. Then, the direct shock to demand from this drop in consumer spending and residential construction quickly rippled outward. As the supply of customers dried up, firms stopped investing in new

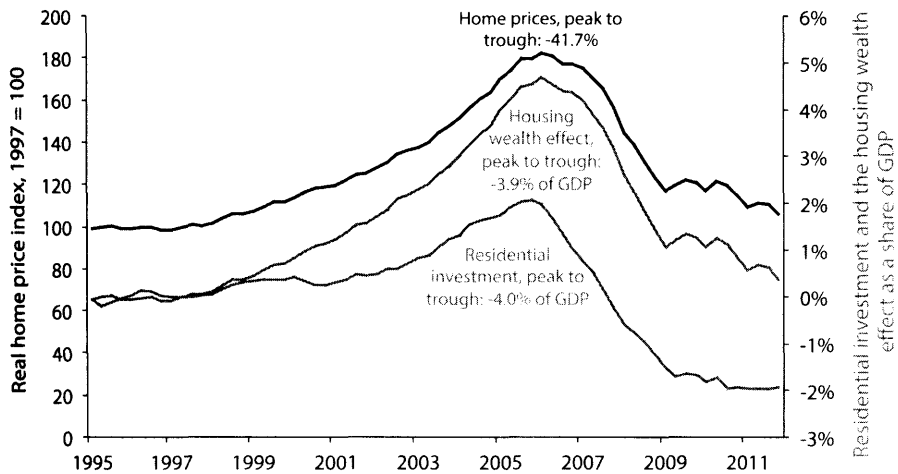
plants and equipment, depressing overall business investment. As tax revenues fell and social safety net expenditures increased, state and local governments reduced programs, cut jobs, and increased revenues, which further reduced overall demand for goods and services and exacerbated the recession. The relationships between home prices and wealth effects and residential investment are shown in **Figure 1B**.

In short, the Great Recession was a classic “Keynesian” downturn (one driven by deficient aggregate demand) that required, and still requires, Keynesian solutions (policy measures to restore this demand). The negative shock to private spending and demand that led to the Great Recession was enormous—greater in most estimates than the one that caused the Great Depression. Without sufficient spending to maintain demand for goods and services, the demand for labor fell, leading to massive job losses and a sharp rise in unemployment.

The proper policy response to this collapse in demand was analytically easy to design if daunting to implement: Use all the levers of macroeconomic policy that can spur spending in the near-term to restore the demand that was lost in the wake of housing price declines. Unfortunately, too many in the macroeconomic policymaking realm had grown accustomed to thinking that just one lever

WELLS FARGO

Figure 1B Home prices and their impact on residential investment and housing wealth, 1995–2011



Note: The housing wealth effect is obtained by multiplying the change in housing wealth from its 1997 average by \$.06 (the low-end estimate of annual consumer spending generated by each dollar in housing wealth) and expressing the resulting product as a share of overall GDP. Data are quarterly.

Source: Authors' analysis of Case, Quigley, and Shiller (2005); Shiller (2012); Bureau of Economic Analysis National Income and Product Accounts (Table 1.1.5); and Federal Reserve Board Flow of Funds Accounts

was ever needed to fight recessions. Specifically, a decades-in-the-making conventional wisdom argued that the U.S. economy could be revived simply by having the Federal Reserve lower short-term “policy” interest rates, putting downward pressure on the longer-term interest rates of housing and industrial loans. This, it was assumed, would spur households and businesses to sufficiently boost their borrowing and spending to buy new homes and new capital equipment. But in late 2008, these policy interest rates were buried at zero, even as job losses were reaching historic proportions, with roughly 740,000 jobs on average lost *each month* in the six months between November 2008 and April 2009.

This hemorrhaging of jobs was radically slowed and finally halted by the large boost to economic activity from the 2009 American Recovery and Reinvestment Act (ARRA), as well as by the federal budget’s “automatic stabilizers”—progressive taxes and safety net programs that kept households’ disposable incomes from falling as fast as market incomes fell.

However, as ARRA’s support began fading in the second half of 2010, economic growth decelerated markedly. The policy response to the Great Recession had indeed arrested the outright economic contraction, but had not gone far enough to bring the economy back to full health. At the end of 2011, the unemployment rate remained at 8.5 percent and had matched or exceeded the highest rates of the recessions of the early 1990s and early 2000s for a full three years. As this book went to press, policymakers were *talking* about the need to reduce unemployment but were effectively blocking precisely those efforts that would provide more support to the flagging economy.

We should be very clear about the danger of this complacency in the face of elevated unemployment. It’s not simply that full recovery to pre-recession health will come too slowly—though this delay alone does indeed inflict a considerable cost. Instead, the danger is that full recovery *does not come at all*. Nations have thrown away decades of growth because policymakers failed to ensure complete recovery. Japan has been forfeiting potential output—trillions of dollars’ worth, cumulatively—for most of the past 20 years. Recent research (Schettkat and Sun 2008) has suggested that the German economy operated below potential in 23 of 30 years between 1973 and 2002 because monetary policymakers were excessively inflation-averse. Lastly, U.S. economic history provides the exemplar of what can happen to a depressed economy when policymakers fail to respond correctly: The level of industrial production in the United States was the same in 1940 as it was 11 years before.

While we cannot *guarantee* that the current policy path leads inevitably to stagnation, it is unwise to flirt with this possibility when there are clear solutions to our current unemployment crisis. It is in fact by far the most immediately solvable of the economic problems confronting the United States. Experts widely agree on the source of the problem (insufficient demand) and the levers