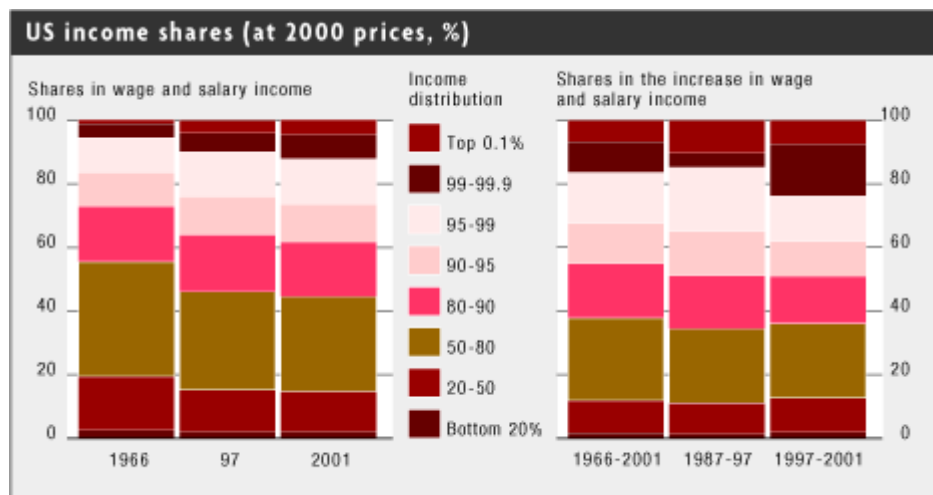


# A New Gilded Age

Martin Wolf, *Financial Times*, April 25, 2006

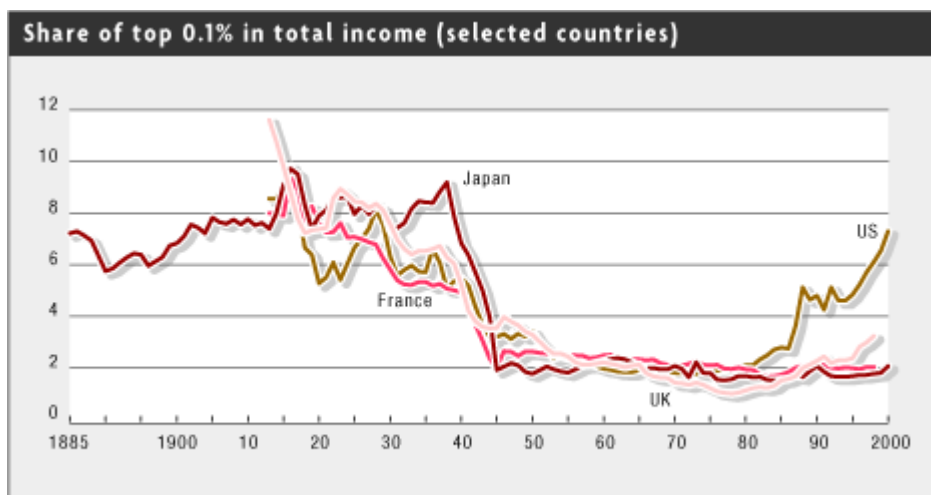
Between 1997 and 2001, the top 10 per cent of US earners received 49 per cent of the growth in aggregate real wages and salaries, while the top 1 per cent received an astonishing 24 per cent. Meanwhile, the bottom 50 per cent received less than 13 per cent. Why is this happening? And should non-egalitarians care? The data I have cited come from a remarkable paper from two economists at Northwestern University. The authors ask a simple, but telling, question: if the US economy is becoming more productive, why have most of its citizens not become better off?

The answer, it turns out, is that the normal link between productivity and real earnings is broken. Thus, between 1966 and 2001, real median earnings ... rose by only 11 per cent. Over the same period, the earnings of those at the 90th percentile ... rose by 58 per cent, of those at the 99th percentile by 121 per cent, of the top 0.1 per cent by 236 per cent and of the top 0.01 per cent by 617 per cent. ... The distribution of US earnings has, as a result, become significantly more unequal over the past four decades. ...



A paper published by the National Bureau of Economic Research shows that income inequality in the US is returning to where it was almost a century ago, after a steep decline in the mid-20th century (see chart). ... The greater part of the decline in the early part of the century was due to a collapse in income from capital. The greater part of the increase since 1971 is due to the rise in earned income.

In consequence, conclude the authors, "top wage earners have replaced capital income earners at the top of the income distribution". Moreover, this is also true of other English-speaking countries, though to a smaller extent, but not of Japan and continental European (see chart).



So why is this happening? The classic explanation is “skill-biased technical change”, reinforced by the impact of globalisation on incomes of the unskilled. Yet the pattern that emerges is hardly consistent with this...

More plausible answers are the “superstar” phenomenon in sports and entertainment and the ability of corporate bosses and investment bankers to extract vastly higher relative salaries than before. The authors from Northwestern university conclude that top corporate executives account for more than half of the incomes in the elite 0.01 per cent of the US income distribution.

So are they worth it? That is a controversial question. I, for one, doubt it. ... it is easy to find non-US CEOs whose performance has vastly outshone that of their US peers, without close to commensurate rewards. ...

This raises a bigger question: do these changes in the US distribution of incomes matter? I would suggest that they should do so even to non-egalitarians, for three reasons.

First, income mobility does not offset the rising inequality. As the two Northwestern university authors note, “not only are half the penthouse dwellers still there a decade later, but the differential opulence of the penthouse keeps increasing relative to the basement”. The chances of leaving the basement are low. ...

Second, the failure of an economy to generate rising incomes for a majority over decades causes frustration. US individualism may contain this reaction. Most cultures cannot.

Third, politics inevitably become more populist: the US “right” has become “pluto-populist” – an alliance of free-marketeers, nationalists and social conservatives – and the “left” is increasingly “protecto-populist” – an alliance of protectionists, dirigistes, social liberals and anti-nationalists. This endangers both intellectual coherence and sensible policymaking.

So long as the distribution of incremental incomes remains as skewed as it has been in recent decades, politics in the US are likely to remain at least as fractious as they are today. Moreover, so long as this trend continues, many other high-income countries will reject the US economic model. No simple solutions exist. But the return of the “gilded age” is a big event, for the US and the world.

[Note: The Dew-Becker and Gordon paper is [here](#). The Piketty and Saez paper is [here](#).]