# WORKING GROUP ON GLOBAL MARKETS
Hoover Institution, Stanford University

**9th Meeting – June 3, 2008 – 12:00pm**
**"Has Income Distribution in the United States Widened, and If So, Why?"**
**Annenberg Conference Room**

## PARTICIPANTS

Guest speakers Emmanuel Saez (Berkeley) and Kevin Murphy (Chicago) met with Working Group members including John Taylor, Michael Boskin, John Cogan, Joe Grundfest, and John Shoven. A number of Hoover Institution officials and friends of Hoover also attended, including Marc Abramowitz, Martin Anderson, John & Jean DeNault, Sam Ginn, Deke Jackson, Pitch & Cathie Johnson, David Jorgensen, Al Lauer, Howard Leach, Bob McLalan, Bob Oster, and Dave Traitel.

## KEY ISSUES DISCUSSED

- **Changes in the U.S. Income Distribution.** Saez and Murphy agreed that wage and income disparities have grown in the United States over the past few decades, particularly in the upper income brackets. Saez showed that individuals in the top 10% have accounted for a rising share of total earnings since the 1970s (Fig.1), and higher incomes for the top 1% have largely driven that trend (Fig. 2).

**Fig. 1 – Share of U.S. Income for the Top 10%**

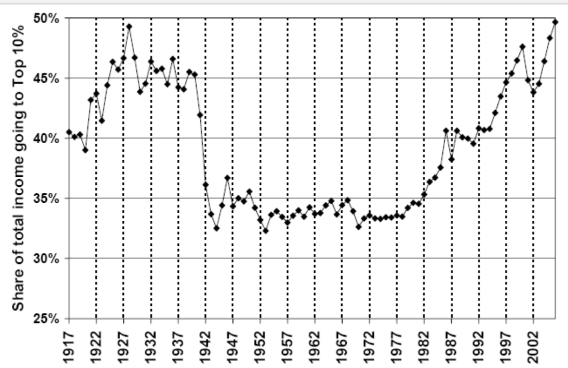
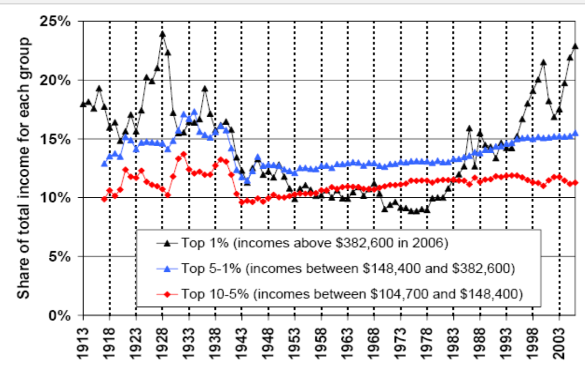



**Fig. 2 – Breaking Down the Top 10%**




*From Emmanuel Saez, June 2008*

- **Explaining the Trend.** Participants discussed a number of possible contributors to this phenomenon, including returns to capital gains, high rewards for entrepreneurship, and changes in how individuals report their earnings for tax reasons. A number of participants also cited the importance of considering income mobility, the growing size of fringe benefits in relation to income, and the consumption distribution after correcting for the relative reduction in prices of many basic goods and services. Saez argued that even after such factors are taken into account, there remains a significant trend toward income disparity, both in relation to prior U.S. periods and other advanced industrial economies. He reviewed some common explanations—including technological change, management entrenchment, and tax changes—but concluded that reductions in institutional constraints to top executive pay have also contributed.

- **Importance of the Phenomenon.** Saez contended that changes in U.S. income distribution matter, because they show that much of the recent growth in national income has been concentrated at the top. For example, U.S. GDP grew by 1.9% annually between 1993 and 2006, but that figure drops to 1.1% if one excludes the top percentile of income earners. Participants then discussed economic and social consequences of the trend.

- **Wage Disparities.** Murphy focused on wage disparities, discussing changes in the returns to education and more general trends in relative wages. He argued that technology, trade, and other factors have contributed to a rising "education premium" for highly skilled workers across races and sexes (Fig. 3). He also showed that wage inequality has risen, but particularly toward the top of the income distribution, by examining wage growth over the past few decades for workers from the 5th to 95th percentile on the wage spectrum (Fig. 4).

**Fig. 3 – The Education Premium**

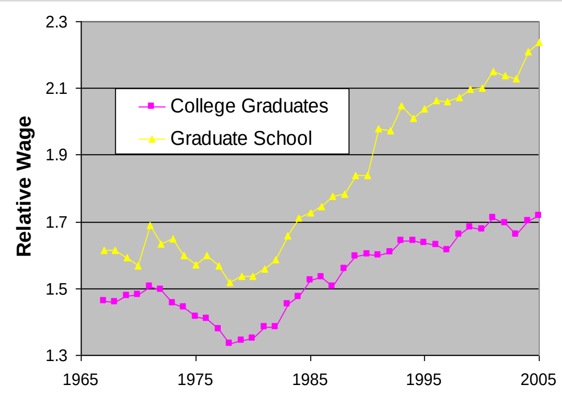
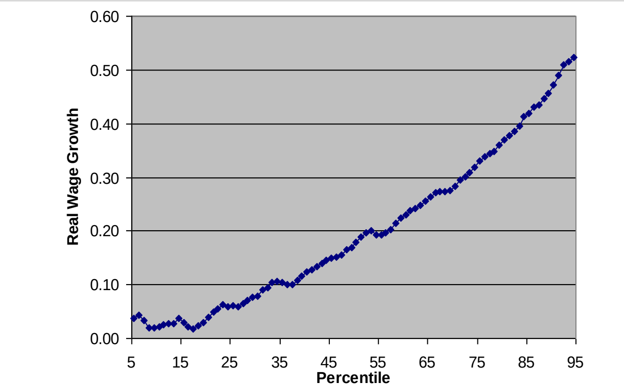



**Fig. 4 – Relative Wage Growth, 1968-2004**




*From Kevin Murphy, June 2008*

- **Explanations and Possible Policy Responses**. Murphy presented the Katz-Murphy Model, which explains wage inequality as a function of the supply and demand of skilled workers. Cheaper capital goods, overseas competition for low-skill jobs, and a shift toward services all raise the demand for skilled workers. Murphy argued that in the United States, supply of highly skilled workers has not kept pace with demand, resulting in much higher relative wages for skilled employees. He ended by stressing the importance of education in preparing U.S. workers to seize today's economic opportunities and realize the efficiency gains of increasing returns to human capital. Participants discussed policies that would help workers take advantage of the rising education premium.