OECD (2011), *Divided We Stand: Why Inequality Keeps Rising*

www.oecd.org/els/social/inequality

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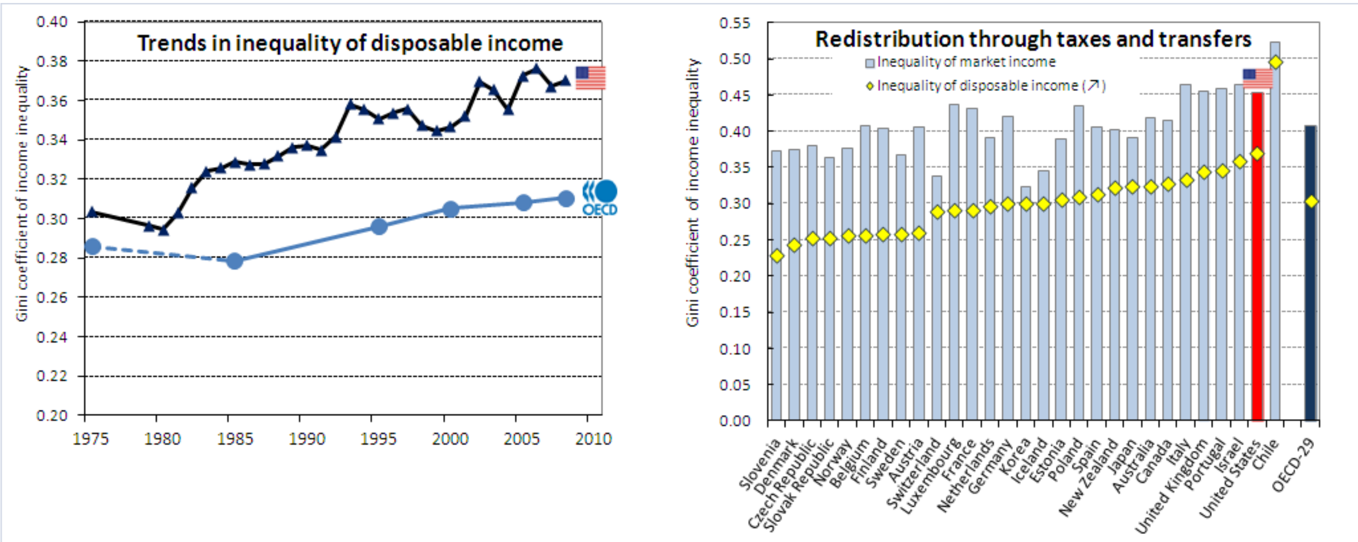
COUNTRY NOTE: UNITED STATES

The United States has the fourth-highest inequality level in the OECD, after Chile, Mexico and Turkey. Inequality among working-age people has risen steadily since 1980, in total by 25%. In 2008, the average income of the top 10% of Americans was 114 000 USD, nearly 15 times higher than that of the bottom 10%, who had an average income of 7 800 USD. This is up from 12 to 1 in the mid 1990s, and 10 to 1 in the mid 1980s.

Income taxes and cash benefits play a small role in redistributing income in the United States, reducing inequality by less than a fifth – in a typical OECD country, it is a quarter. Only in Korea, Chile and Switzerland is the effect still smaller. [Figure6.1]



Notes: The Gini coefficient ranges from 0 (when all people have identical incomes) to 1 (when the richest person has all the income). Market incomes are labor earnings, capital incomes and savings. Disposable income is market income plus social transfers less income taxes. Incomes are adjusted for household size. Data refer to the working-age population. Information on data for Israel: http://dx.doi.org/10.1787/888932315602.

Key findings:

- The wealthiest Americans have collected the bulk of the past three decades' income gains. The share of national income of the richest 1% more than doubled between 1980 and 2008: from 8% to 18% [Table9.1]. The richest 1% now makes an average US$1.3 million of after-tax income (compared to US$17,700 for the poorest 20% of US citizens). During the same time, the top marginal income tax rate dropped from 70% in 1981 to 35% in 2010.
- The rising incomes of executives and finance professionals account for much of the rising share of top income recipients. Moreover, people who achieve such a high income status tend to stay there: only 25% drop out of the richest 1% in the US, compared to some 40% in Australia and Norway, for instance.
- The main reason for widening inequality in the US is the widening wage gap. The gap between the richest and poorest 10% of full-time workers has increased by almost one third, more than in most other OECD countries.
- Contrary to the OECD trend, annual hours among lower-wage workers in the US *increased* by more than 20% over the past decades [Table4.A1.2] – probably linked to incentive policies such as the Earned Income Tax Credit (EITC) but also the relatively low level of the minimum wage. This trend partially offset the rising wage gap and led to a more moderate increase in overall annual earnings inequality.

- Societal change — more single and single-parent households, more people with a partner in the same earning group — accounts for much less of the increase in household earnings inequality (about 13%) than the widening dispersion of men's earnings (about 46%). At the same time, increase in employment, both among women and men, countered the increase toward higher inequality.
- Redistribution of income by taxes and benefits is limited. Over the long run, these offset less than 10% of the increase in inequality of market incomes – gross earnings, savings and capital taken together.
- The limited redistributive effect in the United States is to be found on the benefit side rather than the tax side: benefits represent just 6% of household income, while the OECD average is about 16%. Income support for the unemployed has become less generous over time prior to the 2008-09 financial crisis. The gap between in-work and out of work income has increased for lone parent families and couples with children particularly. The income of a lone mother with 2 kids, who had full unemployment insurance and earned around the average wage, is less than 40% of her former take-home pay – in 1995, this was over 50%.
- On the other hand, the US invests relatively more in public expenditures in in-kind services [Figure8.1], and those help reducing inequality by roughly 18%.

Key policy recommendations for OECD countries from Divided We Stand

- Employment is the most promising way of tackling inequality. The biggest challenge is creating more and better jobs that offer good career prospects and a real chance to people to escape poverty.
- Investing in human capital is key. This must begin from early childhood and be sustained through compulsory education. Once the transition from school to work has been accomplished, there must be sufficient incentives for workers and employers to invest in skills throughout the working life.
- Reforming tax and benefit policies is the most direct instrument for increasing redistributive effects. Large and persistent losses in low-income groups following recessions underline the importance of government transfers and well-conceived income-support policies.
- The growing share of income going to top earners means that this group now has a greater capacity to pay taxes. In this context governments may re-examine the redistributive role of taxation to ensure that wealthier individuals contribute their fair share of the tax burden.
- The provision of freely accessible and high-quality public services, such as education, health, and family care, is important.

The roles of globalisation, technological progress and regulatory reforms

Divided we Stand also looks into the impact of global developments on rising wage dispersion and employment trends over the past quarter century up to the 2008-09 financial crisis. For the OECD area as a whole, the following key findings emerge:

- Globalisation, i.e. the rapid trade and foreign direct investment integration that occurred in all OECD countries over the past quarter century did not – per se- play a major role in driving growing wage dispersion. However, globalisation pressure affected domestic policy and institutional reforms (see below).
- Technological progress led to higher wage differentials: advances in information and communication technologies in particular have been more beneficial for workers with higher skills.
- Regulatory reforms and changes in labor market institutions increased employment opportunities but also contributed to greater wage inequality. More people, and in particular many low-paid workers, were brought into employment. But one of the consequences of more low-paid people in work is a widening distribution of wages.
- The rise in the supply of skilled workers provided a sizeable counterweight to offset the increase in wage inequality resulting from technological progress, regulatory reforms and institutional changes. The upskilling of the labor force also had a significant positive impact on employment growth.