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Causes of Income Inequality among the Social Classes in the U.S. Since The Great Recession 2008

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Abstract:
Background: *Shiller (2013), Nobel-winning economist, has stated that rising inequality in the United States and elsewhere is among the most important problems that Americans have to deal with today. In reality, the onward trend towards unequal income distribution has existed in the U.S. for a long time; however, after the Great Recession 2008, the issue has become significant when income gap among the classes, especially the gap between the top 1 percent and the bottom 99 percent, was at the highest level. The study aims to answer the question: What are the causes of severe income inequality among American social classes?*
Materials and Methods*: To conduct the study content analysis research method is adopted to employ statistics, articles, reports and studies.*
Results*: Study's findings have shown that the change in technology, resulting in "skill-biased technological change" which prefers skilled workers in production process and larger profits for the owners, is considered one of the driving causes of the U.S. income gap. In addition, government's policies, specifically tax cuts under Reagan's and Bush's years, are contributing factors to worsen income gap.*
Conclusion:
Technological changes, globalization and tax cuts policies are three main causes leading to in come inequality in the United States.
Key words: Great Recession 2008, income, inequality, issue, gap

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I. Introduction

The United States of America always is the centre of the attention of the world due to its impregnable position and extending sphere of influence in the world. The influence of the U.S. is huge in such a way that "the rest of the world sneezes when the U.S. catches a cold" (Verick and Islam, 2010, p.3). However, it does not mean that the U.S. does not have its Achilles heel. Entering the early years of the 21st century, to maintain the foothold as the number-one superpower, the U.S. has handled a number of challenges from both internal and external factors. One of the most striking instances that have devastating impacts on the U.S. is the Great Recession 2008. The Great Recession, also known as the financial crisis, occurred in December 2007 to June 2009 and became the global crisis in 2009, is considered "the worst recession that the world has witnessed for over six decades" (Verick and Islam, 2010, p.2). Not only has the Great Recession influenced the U.S. comprehensively but also shown that there have remained a variety of problems existing in the U.S. intrinsically, in which income inequality is the long-standing issue. However, never ever has unequal income distribution fueled contentious topic as such since the Great Recession 2008, especially when income disparity soared at the highest record in the history of the U.S in 2012. The issue of income disparity has caught concern of the U.S. society, including economists, scholars and publicity. It is inevitable that the ever-widening income gap among the social classes has enormous multifaceted impacts on the U.S. Although income disparity has prompted strong criticisms and mass movements of which the Occupy Wall Street (2011) is the most noticeable event as response of publicity to this problem in evidence, it has remained the issue on debate. Some hold the belief that unequal income distribution benefits the U.S. as a whole, but some dissent. Admittedly, it has posed a challenging question which needs to be settled for the U.S. authorities about how to narrow income disparity among classes. Similar to the impacts of income gap, the answer for the question about the root causes of income inequality has maintained the thought-provoking issue on the table.

In reality, inequality issues, including unequal income distribution, have remained one of the most outstanding problems for those who want to explore the contemporary United States. Furthermore, this issue is of personal interest of many people. These are the reasons why the study on "Causes of Income inequality

among the social classes in the U.S. since the Great Recession 2008" is carried out to answer following research question:
What are the causes of severe income inequality among American social classes?

II. Materials and Methods

Content analysis is denoted in different ways. As cited in *Content Analysis: A method in Social Science Research* (Prasad, 2008, p.2), A. Nachmias (1976) defined that "broadly, content analysis may be seen as a method where the content of the message forms the basis for drawing inferences and conclusions about the content".

"Content analysis is any research technique for making inferences by systematically and objectively indentifying specified characteristics within the text" (Stone et al, 1996, p.5) as cited in *The Content Analysis Guidebook* (Neuendorf, 2001, p.10). To be clearer, instead of analyzing numbers, this method gives focus on the text "in order to represent its content" (Millet and Brewer, 2003, p.43). As mentioned above, content analysis is used for interpreting information and making inferences on the basis of text-based sources.

With the aim of explaining American opinions on income disparity and finding out the causes of income inequality, sources for the research cannot base on only numbers but also are collected from different types of sources ranging from legal documents of governmental offices, reports of organizations to studies of scholars at different universities, opinions and quotations of policy-makers, economists and researchers. Besides number-related figures employed by applying data analysis, content of studies and articles are analyzed via content analysis. Firstly, content analysis is used to analyze the responses of all the American classes to the upward trend of the income inequality, especially the huge income gap between the richest 1 percent and the bottom 99 percent. More importantly, this method is applied to find the answer for the second research question about the causes of income disparity. For that reason, in the next stage, content analysis is used to focus and compare evidence from previous studies to analyze three main causes of unequal income distribution: technological changes, globalization and government tax policies. These factors are mentioned, quoted, analyzed, compared and generated to show why they are major causes of inequality in income distribution. Furthermore, based on detailed interpretation of collected information, assessments will be offered and supported with clear evidences.

In short, the thesis adopts content analysis as the main research method. This method is used for analyzing American reactions to the issue and giving focus on the causes of this matter.

III. Results

This section focuses on three reasons leading to growing income disparity in the U.S., including technological changes, globalization and tax cuts. Firstly, technological achievements have induced "skill bias" which high skill employees outweigh low skill staff. Moreover, technology-based production has displaced manual tasks, which increases productivity but reduces jobs. As a consequence, income of the owners boosts up while income of those who work for them declines. Secondly, international trade openness and immigration are the products of globalization making contribution to growing trend of income gap because the rich group finds more opportunities to reduce production costs and gain more profits while the middle and the low wage group have lost jobs to immigrants. Finally, tax cuts policies under Reagan's and Bush's administration benefit the rich class but impoverish the middle and the low-income class.

3.1. Technological changes

According to studies conducted on the roots of income inequality in the U.S., technology, especially high-tech equipment, applied in production is among the main drive forces for two reasons. Firstly, technological innovation resulted in "skill-biased technological change" which prefers skilled to unskilled workers. As a result, income increases in high skill labor but declines in low skill staff. Secondly, technological achievements have contributed to increasing productivity and decreasing costs in production, which benefit the owners only.

Due to technological advancement, manual works have been rapidly replaced by technology-based tasks. Go along with decrease in manual works, there has appeared demand for skilled workers and "skill-based technological change hypothesis" (Card and Dinardo, 2002, p.734) because skilled human capital is more adaptable to control and make full use of technology in production line. It is clear that when making comparison in productivity within a certain amount of time between skilled and unskilled workers, the former definitely can get higher results. As a result, there has had a transfer of labor market from blue-collar workers to white-collar labors. For that reason, demand for skilled workers has been growing in contrast to declining occupations for unskilled labors. Furthermore, a technology revolution led by computer, micro-chip and the internet has caused faster demand for skilled workers in the last thirty years. Katz (1999), as cited in Card and Dinardo (2002, p.734), has shown the evidence that "computer technology is timing: wage inequality began to rise in the early

1980s, just a few years after the invention of microcomputers". Moreover, thanks to adoption of new technology in production, "skill-biased techniques are more profitable, firms will have greater incentives to develop and adopt such techniques" (Acemoglu, 2002, p.12). Labor-intensive tasks have been replaced by personal computers, robots and computer-assisted production. In order to assess the level impact of technology on unequal income distribution, Acemoglu (2002), based on data of CPS, calculated the onward trend of income disparity on the basis of workers' skills along with technological changes and came to conclusion that earning inequality has increased sharply. In 1971, a person at the top 10 percentile earned 266 percent more than a person at the bottom 10 percent. By 1995, this number had risen to 366 percent (Acemoglu, 2002, p.1). In the light of this finding, Acemoglu (2002, p.8) has asserted that the increase in income gap over the past decades is the direct consequence of technological change. According to Jaumotte et.al (2008), technological progress has increased the demand for higher skills, thereby "exacerbating inequality in income" (p.15). Trend in applying high-tech facilities in manufacturing, even fully automating production line, has been prevailing in the last few decades. Due to invasion of technology, especially computers, and its bigger gains in productivity, the trend in using computers in job has suggested that "computer technology is complementary with human capital" (Card and Dinardo, 2002, p.740). In addition, workers are more expensive and less productive in comparison with technology. What is more, producers have to cover larger costs of labor-related issues compared to spending money in installing, repairing and maintaining machines. Supplementary benefits for labor force, namely labor insurance and financial support, health care and labor safety, also costly. According to Labor Department (2014), equipment and software prices have dropped 2.4 % after the recovery began. On the other hand, labor costs have climbed 6.7 % and compensation costs have accelerated by health care benefits. In an interview with the New York Times, Misek (2011) said that "I want to have as few people touching our products as possible. Everything should be as automated as it can be. We just can't afford to compete with countries like China on labor costs, especially when workers are getting more expensive".

Labor costs and production effectiveness are reasons for automating production line in factories. Krugman (2013) said that technology is partly blamed for growing income inequality because it has changed in a way that really favors capital over labor. That makes it possible to replace people with machine.

As technological change has displaced manual tasks, the middle class is most hard hit. According to Associated Press report (2013), millions of jobs for the middle class in the developed countries like the U.S. have been lost to technology because companies have been hiring fewer workers in favor of more machines. Meanwhile, low wage jobs, such as protective services, food preparation, have been rising.

In reality, with human's capacity, investment and attempt, technologies have continuously been improved to meet the demand of the market day to day. As a result, the more improvements have been made in technology, the higher the demand for skills to control and take full advantage of applications of technology innovation on production. For that reason, it leads to higher requirements for education background. In the last decades, the U.S. has witnessed increase in the number of people taking further education. The point is that people at the bottom end of income ladder cannot afford to pay for the expense for education. Gallagher (2013) has shown the result of Pew Research Center that three-quarters of respondents said that "college was too expensive to most Americans" (p.49). As a vicious cycle, they have continued their jobs requiring less skill and receiving the lower income. Those with high income can afford to take further education, so that they can improve their income. For that reason, income gap between those who have higher skills and those who lack skills is increasingly going up.

As analyzed, technological changes have influenced income of many employers because technology has increasingly replaced workers in performing routine tasks. As a consequence, a number of employees become redundant, especially unskilled workers because of effectiveness of advanced technology. More importantly, technology has promoted productivity and reduced production cost, so that the owners can be offered more capital gains and profits. From what have been taken into account, technological advancement is the root of growing unequal income distribution in the U.S.

3.2. Globalization

Globalization has opened the door for all the countries to integrate with one another. The rich nations like the U.S. are encouraged to boost investment in the poorer countries while labors in underdeveloped or developing areas stand more opportunities to immigrate to the U.S. to find jobs and better their life. In this situation, the U.S. investors are benefited most because they can widen the market share while domestic workers are suffered most for losing jobs to immigrants.

3.2.1. International trade openness

There is a theory that international trade, especially with labor – abundant countries like China or India, is a root cause of the onward trend in income inequality in the U.S. Accordingly, global integration leads to expanding market share and falling trade costs which enriches the high income group but harms the lower class.

The U.S. is a superpower which mainly is endowed with skilled workers and capital; meanwhile, the developing countries are the markets with abundant cheap labor force. Due to globalization, openness of international trade and finance has been larger among the countries. Underdeveloped countries tend to encourage foreign investment to promote economic development and enhance living standard of the people. These are factors leading to investment of advanced nations like the U.S. in the other poorer countries. The top 1 percent with a majority of CEOs and entrepreneurs is most benefited from globalization. They open foreign markets and invest their capital in developing countries where the cost for production, premises and labor is much cheaper than running business in the U.S. This trend increases income of the U.S. businessman because of their growing capital gains and profits. In contrast, unskilled domestic labors of the 99 percent class are hit hard when job opportunities decline. CEO-to-worker pay ratio shows the huge gap in income gap between the upper end and the bottom end in the U.S.

Mean	Exporters	Non-Exporters	Overall
CEO Compensation, Estimated	4487.7	3254.3	4197.1
CEO Compensation, Realized	4662.4	3340.4	4350.8
CEO-to-worker Pay Ratio, Estimated	91.9	80.8	89.3
CEO-to-worker Pay Ratio, Realized	91.8	79.6	88.9
Average-Top-5 Compensation, Estimated	2337.9	1656.6	2180.4
Average-Top-5 Compensation, Realized	2422.8	1707.7	2257.5
Average-Top-5-to-worker Pay Ratio, Estimated	48.7	55.5	50.3
Average-Top-5-to-worker Pay Ratio, Realized	48.4	57.8	50.6
N. Observations, CEO	13169	4054	17223
N. Observations, Top-5	12508	3760	16268

Table C.1.2: Summary Statistics, Public Firm Sample

Figure 1: CEO-to-worker pay ratio (Ma, 2013, p. 50)

The figure represents the massive income disparity between CEOs and workers ratio in the same firms. Although CEO-to-worker pay ratio differs in exporting and non-exporting firms, the rate is still high. It can be seen from the figure that the ratio was around 90 in general. Income of average top 5 percent was nearly 50 times than that of workers.

Furthermore, global trade openness leads to falling trade cost among the countries which partly cause income inequality in the U.S. because all the nations tend to loosen procedures, cut tariff and so on. As a result, in the win-win competition, all the nations can benefit from declining trade cost as a whole. However, labors in developed nations like U.S. are impacted negatively. Bivens (2007) has fully explained impact of trade cost on income gap in the labor force in his report. Due to market integration and falling trade cost, commodities from less developed countries are imported into the U.S. with the lower price because production cost in these countries are lower. As a result, price of domestically produced commodities fall as well to compete with imported products. The lower price leads to produce domestic goods less and employ fewer workers. In contrast, in industries requiring skills, the expansion of market creates jobs opportunities to those who have higher education attainment and high skills such as managers.

In short, international trade openness offers opportunities for the rich group to gain more because they can reduce production costs. In contrast, global trade resulted in falling trade cost among the countries does harm income of the lower class.

3.2.1. Immigration

In addition to international trade, immigration – product of globalization is one the “important drivers of the recent trends in income inequality” (Regev and Wilson, 2007). The U.S. is considered the market with abundant job opportunities and equalities; therefore, the U.S. receives flows of both legal and illegal immigrants. Martin (2013) has illustrated that the flow of legal and illegal immigrants is a contributing factor to increasing income disparity in the U.S.

Immigrants into the U.S. include both legal and illegal labors coming from undeveloped and developing countries with different education background. However, 76.6 % legal immigrants and almost illegal immigrants have low education attainment and lack of English (Martin, 2013, p.3). While immigrants with higher education attainment tend to get jobs of the middle-class in the U.S., the low-income class is suffered from immigrants with lower education background because most of them work for manual jobs which do not require high skills such as constructions, housework and so on. Salary for these immigrants is much lower in comparison with that for the domestic workers who have lower education attainment. For that reason,

income of domestic workers is under influence of immigration. Borjas (2013), as cited in Martin (2013, p.1), has asserted that

Some groups of workers face a great deal of competition from immigrants. These workers are primarily, but by no means exclusively, at the bottom end of the skill distribution, doing low-wage jobs that require modest levels of education. Such workers make up a significant share of the nation's working poor.

The influx of authorized and unauthorized immigrants of which unskilled employees take major share, has influenced earnings of lower income labor force in the U.S. The most affected population is the low wage local labor, which causes growing income gap in the U.S.

3.3. Government policies

Under tax cuts policies of Reagan and Bush, income inequality in the U.S. has been worsening because the two policies favor the rich, influence the middle class and impoverish the poor.

3.3.1. Tax cuts in Reaganomics

In 1981, Ronald Reagan became the 40th president of the United States and immediately implemented a new economic policy for the country called "Reaganomics" or it is known as tax cuts policy or "trickle – down" policy which is considered the contributing factor to income inequality. The late economic professor Viksnins in his paper "Reaganomics after Twenty Years" has overlooked content and results of the policy. Accordingly, the tax policy cut 10 percent in the mid-1981 and additional 10 percent reductions two years later. Reagan's tax cuts program was estimated about $750 billion which is the centre controversy (Viksnins, n.d).

The U.S. under Reagan presidency is considered "the decade of greed and welfare for the rich" (Viksnins, n.d) because tax cuts benefited the top income groups while it became "punitive even for middle-class families" (Viksnins, n.d). In the 1980s, the distribution of income worsened when the share of the bottom 20% fell, while the share of the top 1%, 5%, or 20% rose. There were obscene increases in corporate profits and personal incomes of the filthy rich (Viksins, n.d). According to Canterberry , as cited in Vilskins (n.d), "the dramatic dislocation of wealth to the top reflected the staggering trundling of financial wealth upward during the 1980's . 95 percent of American families have become not only relatively but absolutely worse off".

Reagan held the belief that if government economic policy gave focus on making the rich richer, the benefits would "trickle down" to everyone. This policy is regarded as the saying that "a rising lifts all boats". However, the effect of the policy contrasted to Reagan's expectation. In reality, "the rising economic tide has certainly lifted a lot of yachts, but at the same time it has left most of the row boats stuck in the mud" ("American Pie", 2013). According to Phillips (1991), during the 1980s "the bucket of liberty and economic freedom rose, while the bucket of income equality fell. Upper-tier Americans significantly expanded their share of national wealth, while low-income citizens lost ground. Reagan policies were critical to the shift" (p.52)

Niskanen and Moore (1996) evaluated the effects of Reaganomics on income gap among all the classes in the U.S. during Reagan years that the wealthiest group witnessed "the share of total income because they gained income at a faster pace than did he middle class and the poor" (p.19). Krugman (1990) stated that the 1980s was the first decade in which large numbers of American suffered a serious decline in the living standard since 1930s (p.22).

3.3.2. Bush tax cuts

Another policy has been criticized because it has worsened income disparity in the U.S. society is the tax cuts policy under Bush administration. According to Lewandoski (2008), in 2001, the tax cuts officially came into effect when President Bush released his tax relief agenda on February 2001 in which individual income tax was a major priority. The policy was implemented in the hope that lower – income tax payers would be benefited the greatest percentage tax reduction. The President projected a tax reduction of $1,600 to the average family (Lewandoski, 2008, p.5). However, tax cuts policy was opposed by a number of people. After the policy was enacted and undergone expansion in 2010 by Obama's administration, statistics have shown the policy's impacts contrasting to Bush's expectation.

Tax cuts enacted in 2001 was assessed that "remain expensive, ineffective and unfair" (Fieldhouse and Pollack, 2011, p.1). The tax cuts made "the tax code less progressive and delivered a large windfall to the highest income taxpayers" (Aron-Dine, 2008). According to Huang and Frentz (2012, p.1), Bush tax cuts made the highest –income tax payers receive the immense tax cuts. Fieldhouse and Pollack (2011) shared the similar perspective that this policy "conferred disproportionately benefits on those at the top of the earnings distribution, exacerbating a trend of widening income inequality" (p.1). Accordingly, in 2010, the top 1 percent income group received 38 % of the breaks in the 2001-2008 tax changes; 55% of the tax breaks went to the top 10% of earners. Meanwhile, the bottom 20 percent with 1 % share of the tax cuts and 75% of these low-income families saw no reduction. Fieldhouse and Pollack (2011) have generated data as follows.

The top 0.1% of earners received an average tax cut more than 450 times larger than the share received by an average middle-income family. A middle-income family received roughly one-eighth of the average tax cut received by a family in the top 20% of the income distribution; a family in the lowest 20% received less than one-hundredth of the average tax cut received by a family in the top fifth of the earnings distribution (p.1).

Goldfarb (2013) in the article "The Legacy of the Bush Tax Cuts" represented the similar finding on the effect of the 2001 Bush's tax cuts based on data Tax Policy Center.

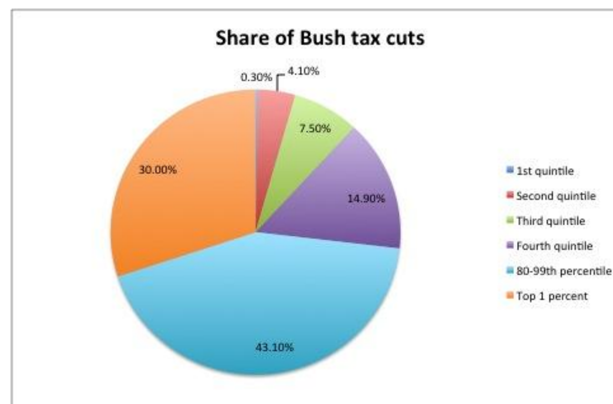

Figure 2: Share of Bush tax cuts (The Washington Post, 2013)

As can be seen from above figure, the top 10 percent after-tax income took about 43 % in total income. The massive gap between the top and bottom end of social ladder. While the top richest 1 percent accounted for nearly one-third in total income share, 30 %, the lowest income group made up one-hundredth of the top 1 percent's proportion.

It can be said that American has "the government of the 1 percent, by the 1 percent and for the 1 percent" (Stiglitz, 2012, p.95). Stiglitz (2012) reviewed on the tax cuts of both Reagan and Bush that the tax cuts made tax system less progressive by lowering taxes for the top income (p.105). In short, both policies in Reagan's and Bush's years have triggered growing income gap in the U.S.

IV. Conclusion

Based on above analyses, the research question has been answered to illustrate income problem does matter in the modern American society. The paper has concentrated on three central triggers: technological changes, globalization and tax cuts policies. In terms of causal relation between technology and income distribution, the paper has explained why technological achievements cause "skilled-biased" which prefer skilled workers over unskilled employees. More than that, thanks to benefits from technology, especially computer-based achievements, the owners improve capital gains, productivity and profits. In addition, international trade openness and immigration resulted from globalization provide benefits for the top income but restrict job opportunities and wage of the middle as well as the bottom income class. As a consequence, globalization triggers increasingly growing income gap among American classes. In the final analysis, effects of tax cuts under Reagan's and Bush's presidency have influences on favoring wealth of the richest group and declining that of the bottom end income group.

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