Research Department
Federal Reserve
Bank of
San Francisco

December 14, 1979

FRBSF Weekly Letter

More or Less Equal?

A mysterious trend in income distribution has emerged over the past decade. Certainly the economy has been growing, although somewhat erratically in the last few years, so that living standards on average have improved somewhat. But relative income matters too, particularly to those at the bottom, and recently they have been losing ground.

Most Americans would probably guess, if asked, that the distribution of income has been growing more equal. Up until about 1968, they would have been right. But this trend was abruptly reversed at the end of the last decade, and since then the pre-tax income distribution (inclusive of transfer payments) has become decidedly less equal. In focusing on pre-tax income, of course, we potentially exaggerate the increase in inequality. A progressive tax system can help to even out these disparities. Also, many low-income families receive subsidized services (health and housing services, for example) which are not counted in the transfer payments included here. Nevertheless, the initial distribution of rewards is still important, especially if tax revolts and limitations on government spending lead to reductions in redistributive effort.

Measuring the shift

Before trying to decide how this change came about, it would be worthwhile to define the problem—in other words, to decide what we mean by equality of income distribution, and how it can get better or worse. After all, we know the distribution of income in the United States is not exactly equal. Not all of us live like the Kennedys or the Rockefellers. On the other hand, the dire poverty that exists in many countries doesn't seem to be prevalent here. One popular measure of equality is the Gini coefficient of family-income concentration. This is a summary measure of the share of income each fraction of the population, by family unit, receives. The more equal the distribution, the lower the Gini coefficient. Another useful measure is the quintile distribution, which shows the percentage of total income accruing to each fifth of the population, from poorest to richest.

As it turns out, both measures tell a similar story. The Gini bounced around quite a bit, but moved generally down as distribution became more equal until 1968. Since then it has gone steadily up, wiping out about half the gain of the 1950-68 period. The quintile distribution, shown in the chart, indicates that the shifts have been widespread, with the poorest two-fifths losing out to the upper two-fifths since 1968, while the middle group has stayed about even. The biggest losers are in the second quintile, which had an even smaller share in 1977 than in 1950. The big winners over the past quarter-century were not the very richest, though. They were the relatively well-off people in the fourth quintile. But since 1968, the rich have gotten relatively richer too.

Worker's share

Have the capitalists, in true Marxist fashion, been enriching themselves at the expense of the workers? Because property income is highly concentrated among upper-income groups, any gain in the overall share of capital at the expense of labor would tend to increase the Gini coefficient. But far from this being the case, the trend has been in the *opposite* direction—the labor share of income has been steadily increasing. In 1950, workers received 66 percent of the total, but in 1968 they received 73 percent—and in 1977, 76 percent. This should have made the distribution more equal, not less.

If workers as a whole have been receiving more but poor people are getting less, perhaps better-paid workers are gaining at the expense of the lower-paid. Here the

Research Department
Federal Reserve
Bank of
San Francisco

evidence becomes rather murky. Incomes of managers and administrators increased faster than those in any other occupation between 1968 and 1977, putting them ahead of professional and technical workers as the most highly paid group. But at the same time, sales and clerical workers gained on professional and technical employees, who are higher on the white-collar ladder. Differentials also narrowed within the blue-collar group, as both operatives and laborers gained a little in relation to more-highly paid craftsmen.

In contrast, a tendency toward growing differentials was quite evident during the earlier (1950-68) period. Sales and clerical workers lost in relation to professional and technical people, operatives' and laborers' wages grew more slowly than those of craftsmen, and all categories of blue-collar workers received relatively less than their white-collar counterparts in 1968 than in 1950. Again, the big success story of the 1950-68 period was managers and administrators, as they almost eliminated the salary gap between themselves and top professionals.

More prosperous workers

Another possibility is that prosperous families have been sending more members into the work force than the poor, and thus increasing their share of total income. And yes, in fact, they have. Between 1968 and 1977 the average number of earners per family fell in the lowest two quintiles, while it rose among the upper three. The women's movement and a decade-long rise in unemployment rates may together account for this conflicting picture. Cyclical unemployment tends to raise income concentration because it affects lower-income groups more heavily than higher-income groups. Since 1977 was at a lower point in the cycle than 1968, this may have had some effect. And since husbands with relatively high salaries also tend to have well-paid wives, any increase in female participation in upper-income groups would have a magnified effect on family inequality. However, this trend does not explain the reversal since 1968, because the increase in the number of workers per family was even stronger in the period between 1950 and 1968. The increase in labor-force participation rates was quite pronounced in the earlier period in all but the lowest quintile.

Since changing incomes within occupations do not explain the growing disparity of income distribution, what about shifts in employment between occupations with different distributional patterns? Income from some types of work, notably farm and nonfarm self-employment, tends to be much more unequally distributed among its recipients than income from either blue-collar or white-collar jobs. And there are also substantial differences within these subgroups. Thus increased employment in some occupations with less equally distributed income would raise the Gini coefficient, while increased employment in the jobs where income is more evenly distributed would lower it toward a more balanced distribution.

Unfortunately for our thesis, there have been no major shifts recently in the occupational distribution of employment. There was some movement out of farming and out of self-paid managerial jobs—which should have increased income equality—but the movement was small. In contrast, there were sizable shifts between 1950 and 1968, which worked in the direction of greater equality. The big movements were out of self-paid farm and nonfarm jobs and into salaried professional, technical and managerial employment, all of which have relatively low indices of income concentration. Moreover, considering the fact that farm incomes are generally much lower than nonfarm incomes, the movement away from farming tended to increase the share of lower-income groups during that period.

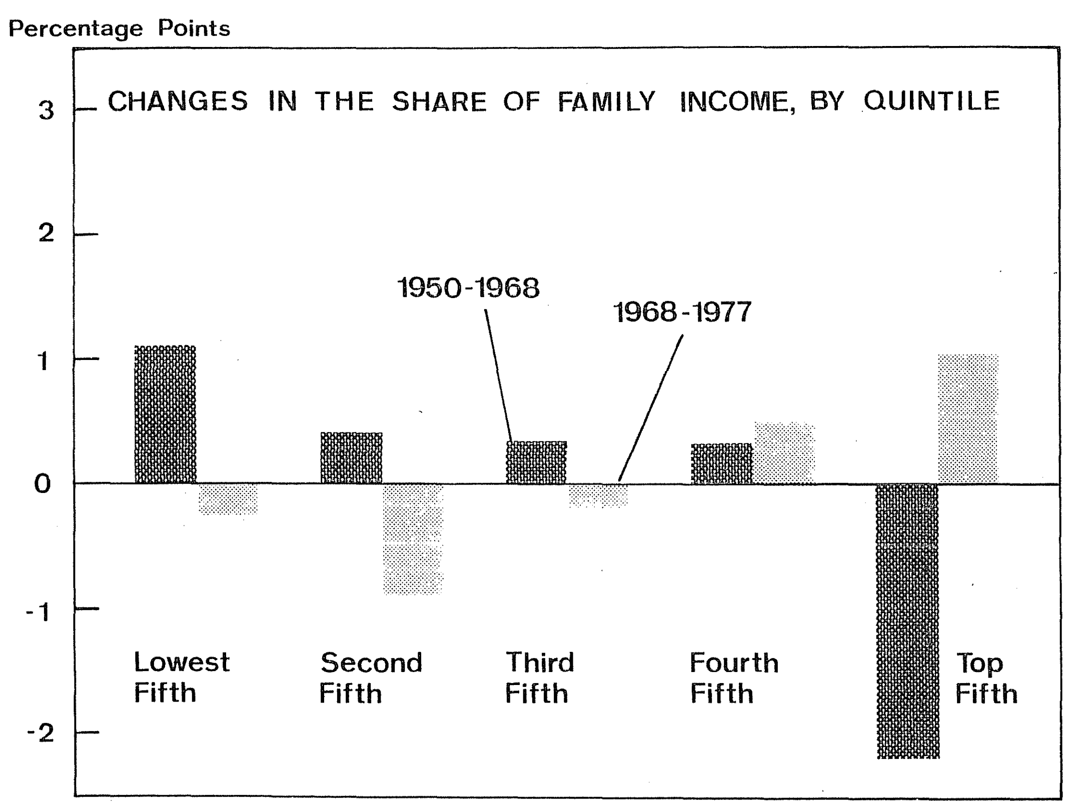
Causes summarized

Here, then, is at least part of the answer.

Income equality increased in the earlier period because people in self-employed work where income is *more concentrated* moved into wage and salary jobs. But this trend had run its course by 1968. Then the other unequalizing forces took over, in the form of increasing wage differentials and relatively higher participation rates among upper-income families. Even the continued shift away from property and toward labor income has not been able to offset this trend.

What are the prospects for the future? Probably toward greater inequality, at least for a while. The shift toward labor income probably will be limited at some point, simply because labor's share is already three-fourths of the total. And as long as other recent trends continue—such as relatively large income gains by managers and administrators, and rising labor-force participation rates among upper-income families—pretax family income may continue to be distributed in an increasingly unequal fashion. To the extent that subsidized services to the poor are not eliminating the differentials, this poses challenges for progressive income-tax and transfer policy.

Jane Haltmaier



Research Department
Federal Reserve
Bank of
San Francisco

Alaska • Arizona • California • Hawaii
Idaho • Nevada • Oregon • Utah • Washington

FIRST CLASS MAIL
U.S. POSTAGE
PAID
PERMIT NO. 752
San Francisco, Calif.

FIRST CLASS

BANKING DATA—TWELFTH FEDERAL RESERVE DISTRICT

(Dollar amounts in millions)

Selected Assets and Liabilities Large Commercial Banks	Amount Outstanding 11/28/79	Change from 11/21/79	Change from year ago @ Dollar	Percent
Loans (gross, adjusted) and investments*	134,929	+ 48	+ 15,884	+ 13.34
Loans (gross, adjusted) — total#	111,911	− 71	+ 15,330	+ 15.87
Commercial and industrial	31,094	− 50	+ 2,630	+ 9.24
Real estate	42,578	+ 175	+ 8,709	+ 25.71
Loans to individuals	23,997	+ 49	NA	NA
Securities loans	1,409	− 149	NA	NA
U.S. Treasury securities*	7,384	+ 91	− 771	− 9.45
Other securities*	15,634	+ 28	+ 1,325	+ 9.26
Demand deposits — total#	43,388	−1,166	+ 2,477	+ 6.05
Demand deposits — adjusted	30,920	− 153	+ 630	+ 2.08
Savings deposits — total	28,592	− 244	− 1,847	− 6.07
Time deposits — total#	58,330	+ 147	+ 8,791	+ 17.75
Individuals, part. & corp.	49,784	+ 73	+ 9,432	+ 23.37
(Large negotiable CD's)	21,753	− 171	+ 2,315	+ 11.91

Weekly Averages of Daily Figures	Week ended 11/28/79	Week ended 11/21/79	Comparable year-ago period
Member Bank Reserve Position			
Excess Reserves (+)/Deficiency (−)	19	− 10	+ 31
Borrowings	107	+ 187	+ 36
Net free reserves (+)/Net borrowed(−)	− 88	− 197	− 4
Federal Funds — Seven Large Banks			
Net interbank transactions [Purchases (+)/Sales (−)]	+ 712	+ 269	+ 989
Net, U.S. Securities dealer transactions [Loans (+)/Borrowings (−)]	+ 81	− 6	+ 357

* Excludes trading account securities.
# Includes items not shown separately.
@ **Historical data are not strictly comparable due to changes in the reporting panel; however, adjustments have been applied to 1978 data to remove as much as possible the effects of the changes in coverage. In addition, for some items, historical data are not available due to definitional changes.**

Editorial comments may be addressed to the editor (William Burke) or to the author . . . . Free copies of this and other Federal Reserve publications can be obtained by calling or writing the Public Information Section, Federal Reserve Bank of San Francisco, P.O. Box 7702, San Francisco 94120. Phone (415) 544-2184.