Nation of Change

The Strange Case of American Inequality

By J. Bradford DeLong

Unless something goes unexpectedly wrong in 2014, the level of real *per capita* GDP in the United States will match and exceed its 2007 level. That is not good news.

To see why, consider that, during the two business cycles that preceded the 2007 downturn, the US economy's real *per capita* GDP grew at a 2% average annual pace; indeed, for a century or so, the US economy's real *per capita* GDP grew at that rate. So US output is now seven years – 14% – below the level that was reasonably expected back in 2007. And there is nothing on the horizon that would return the US economy to – or even near – its growth path before the 2008 financial crisis erupted. The only consolation – and it is a bleak consolation indeed – is that Europe and Japan are doing considerably worse relative to the 2007 benchmark.

The US economy's annual *per capita* underperformance in 2014 will thus amount to $9,000. That means $9,000 per person per year in consumer durables not purchased, vacations not taken, investments not made, and so forth. By the end of 2014, the cumulative *per capita* waste from the crisis and its aftermath will total roughly $60,000.

If we project that forward – with nothing visible to restore the US to its pre-2008 growth path – at the annual real discount rate of 6% that we apply to equity earnings, the future costs are $150,000 *per capita*. If we use the 1.6% annual real discount rate at which the US Treasury can borrow via 30-year inflation-protected Treasuries, the future *per capita* costs are $550,000. And if we combine the costs of idle workers and capital during the downturn and the harm done to the US economy's future growth path, the losses reach 3.5-10 years of total output.

That is a higher share of America's productive capabilities than the Great Depression subtracted – and the US economy is 16 times larger than it was in 1928 (5.5 times larger in *per capita* terms). So, unless something – and it will need to be something major – returns the US to its pre-2008 growth trajectory, future economic

historians will not regard the Great Depression as the worst business-cycle disaster of the industrial age. It is we who are living in their worst case.

One would think that such a macroeconomic disaster – one that robs the average American family of four of $36,000 per year in useful goods and services, and that threatens to keep Americans poorer than they might have been for decades, if not longer – would focus policymakers' minds. One would think that America's leaders would be clambering to formulate policies aimed at returning the economy to its pre-2008 growth path: putting people back to work, cleaning up underwater mortgages, restoring financial markets' risk-bearing capacity, and boosting investment.

But no. Part of the reason is that, at the top, there is no crisis. According to the best estimates, the income share of America's top 10% probably crossed 50% in 2012 for the first time ever, and the 22% income share that went to the top 1% was exceeded only in 2007, 2006, and 1928. The incomes of America's top 10% are two-thirds higher than those of their counterparts 20 years ago, while the incomes of the top 1% have more than doubled.

Those who fall into the top strata thus regard themselves as doing well in the current US economy. And indeed they are. Only those who spend more time talking to competent macroeconomists than is healthy know that they could be doing even better if the economy were rebalanced at full employment. So the absence of distress among America's top 10% and its top 1% – and hence political pressure for measures to return the economy to its pre-2008 growth path – is understandable.

But, for everyone else – roughly 90% of the US population – there has been no jump in income share relative to ten or 20 years ago to offset what now looks to be a permanent lost decade. On the contrary, the bottom 90% has continued to lose ground.

When income inequality began to rise in the 1980's and 1990's, those of us who cut our teeth on the long march of North Atlantic history expected to see a political reaction. Democratic politics, we thought, would check the rising power of a largely parasitic economic over-class, especially if its influence caused governments to fail to live up to their commitments to provide full employment with increasing – and increasingly shared – prosperity.

After all, in early-nineteenth-century Britain, growing inequality caused by the Industrial Revolution gave rise to movements for government regulation in the interests of the middle and working classes, and for a rebalancing of real incomes away from rich landlords. Similarly, the Great Depression produced enormous political pressure for reform and change (often for destructive and dangerous

change, to be sure, but pressure nonetheless).

Why can't America launch similar movements today? To the extent that this has become a valid question, most Americans should be as worried today about the quality of their democracy as they are about the inequality of their incomes.