# Myths of the 1 Percent: What Puts People at the Top

nytimes.com/2017/11/17/upshot/income-inequality-united-states.html

By Jonathan Rothwell November 17, 2017

Income inequality inspires fierce debate around the world, and no shortage of proposed solutions. As global billionaires bid up the price of a da Vinci painting on Wednesday, to $450.3 million, Congress debated tax reforms that many analysts said would give the largest benefits to the richest 1 percent of taxpayers.

In the United States, the richest 1 percent have seen their share of national incomeroughly double since 1980, to 20 percent in 2014 from 11 percent. This trend, combined with slow productivity growth, has resulted in stagnant living standards for most Americans.

No other nation in the 35-member Organization for Economic Cooperation and Development is as unequal among those with comparable tax data,and none have experienced such a sharp rise in inequality.

In Denmark, the share of income going to the top 1 percent rose to 6 percent from just 5 percent. In the Netherlands, there was essentially no increase from 6 percent levels. Britain (6 percent to 14 percent) and Canada (9 percent to 14 percent) had notable increases in top-income earnings, but not as large as those in the United States.

Before looking into some of what's behind this, let's address common misconceptions.

## No, It's Not Trade

A rise in international trade — as a share of G.D.P., measured as either imports or exports using data from the Penn World Tables — is associated with equality, not inequality. The United States imports only a small fraction of the value of its total economy, whereas Denmark and the Netherlands are highly dependent on imports.

## Or the Rise of Information Technology

Countries with higher rates of invention — as measured by patent applications filed under the Patent Cooperation Treaty, an indicator of patent quality — exhibit lower inequality than those with less inventive activity.As it happens, tech industries in the United States have contributed just a tiny bit to the rise of the 1 percent, and the salaries of engineers and software developers rarely reach the 1 percent threshold of an annual income of $390,000.

## What About Unions?

Unions are thought to redistribute income from owners to workers, but there is no correlation across countries between the change in labor's share of G.D.P. since 1980 and an increase in the income share of the top 1 percent. Britain saw an increase in the labor share of G.D.P. but also one of the sharpest increases in inequality. The Netherlands saw a large fall in labor's share but no rise in inequality.

Image

A woman holds up a paddle with an image of Leonardo da Vinci's "Salvator Mundi" as she arrives at Christie's before bidding on the painting Wednesday night in New York. The work sold for a record $450.3 million.CreditTimothy A. Clary/Agence France-Presse — Getty Images

Scandinavian countries are heavily unionized and egalitarian, but Denmark experienced a large decrease in the share of workers represented by unions from 1980 to 2015, according to O.E.C.D. data, and very little change in inequality. Unionization rates dropped precipitously in the Netherlands and especially New Zealand over the period, but inequality rose as much if not more in Spain, where unionization rates rose.

## Not Immigration, Either

Nationalists attribute rising inequality to mass immigration and the supposedly low skills of immigrants.

There is no correlation between changing immigration shares since 1990 and rising top-income shares. In fact, the countries that have absorbed the most immigrants — on a per-capita basis — have seen overall income inequality (measured by the Gini coefficient) fall.

An assumption implicit in this argument is that immigrants drag down earnings at the bottom of the distribution, making inequality worse. If this were an important factor, rising inequality should coincide with large gaps in income between foreign-born and native-born adults. It doesn't.

My analysis of data from the Gallup World Poll from 2009 to 2016 shows that foreign-born adults earn 37 percent less than native-born adults in the Netherlands, after adjusting for age and gender. This is the largest gap among O.E.C.D. countries, and yet, the country saw no change in top-income inequality. Canada (minus 8 percent) and Britain (minus 7 percent) have small gaps but high and rising inequality.

## In the U.S., Managers Are a Minority of Top Earners

Most top earners in the United States are neither executives nor even managers. People in those occupations make up just over one-third of all top earners in the United States. This share has been falling — particularly for corporate executives — and is lower than in many other advanced countries.In Denmark, Canada and Finland, close to half of top earners are in managerial occupations, according to my analysis of data from the Luxembourg Income Study.

## So What's Going On?

Almost all of the growth in top American earners has come from just three economic sectors: professional services, finance and insurance, and health care, groups that tend to benefit from regulatory barriers that shelter them from competition.

The groups that have contributed the most people to the 1 percent since 1980 are: physicians; executives, managers, sales supervisors, and analysts working in the financial sectors; and professional and legal service industry executives, managers, lawyers, consultants and sales representatives.

Without changes in these largely domestic services industries — finance, health care, the law — the United States would look like Canada or Germany in terms of its top income shares.

The United States also stands out in terms of how much money its elite professionals earn relative to the median worker. Workers at the 90th percentile of the income distribution for professionals make 3.5 times the earnings of the typical (median) worker in all occupations in the United States. Only Mexico and Israel, which have very high inequality, compensate professionals so disproportionately. In Switzerland, the Netherlands, Finland and Denmark, the ratio is about 2 to 1.

This ratio, the elite professions premium, is very highly correlated with income inequality across countries.

Others are noticing these trends. A new book, "The Captured Economy" by Brink Lindsey and Steven Teles, argues that regressive regulations — laws that benefit the rich — are a primary cause of the extraordinary income gains among elite professionals and financial managers in the United States and of a reduction in growth.

This year, the Brookings Institution's Richard Reeves wrote a book about how people in the upper middle class have shaped both legal and cultural norms to their advantage. From different perspectives, Joseph Stiglitz, Robert Reich and Luigi Zingales have also written extensively about how the political power of elites has undermined markets.

Problems cited by these analysts include subsidies for the financial sector's risk-taking; overprotection of software and pharmaceutical patents; the escalation of land-use controls that drive up rents in desirable metropolitan areas; favoritism toward market incumbents via state occupational licensing regulations (for example, associations representing lawyers, doctors and dentists that block efforts allowing paraprofessionals to provide routine services at a lower price without their supervision).

These are just some of the causes contributing to the 1 percent's high and rising income share. Reforming relevant laws can make markets more efficient and egalitarian, and in contrast with trade, immigration and technology, the political causes of the 1 percent's rise are directly under the control of citizens.

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