

The influence of earnings on income distribution in the United States

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Received 30 September 2003; accepted 21 November 2005

Abstract

This article discusses whether the so called “skill-biased technological change” hypothesis is able to explain the individual earnings inequality in the U.S. during the period 1968–2000. Using the statistic information supplied by the *Census Bureau* and the *Bureau of Labor Statistics*, the article analyzes the earnings evolution, explaining the reasons why earnings inequality has increased, and the relation of this increase with the household income distribution. The main conclusions are the following: (a) changes on labor productivity are not the main cause of the increase in earnings’ inequality, and (b) this earnings’ inequality is not the only reason for the increase of the households’ income inequality.

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JEL classification: D31; D33; D39; E24

Keywords: Earnings; Household income; Income distribution; Income inequality; Wages

1. Approach and methodological clarifications

A significant part of the literature dealing with income distribution in the U.S. suggests that the growing disparity between earnings is a consequence of the dynamics of technological change and that this behaviour is the factor explaining the increasing inequality of income between households. This explanation of the “skill-biased technological change” argues that technological change has caused a critical change in the demand of labour, producing a strong growth of the best-paid and most skilled jobs (with a higher level of education and professional training), at the expense of

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the less skilled and low wage jobs. This change would be the main cause of the increasing wage inequality among the employees and, consequently, of the greater gap among the households' money income (Danzinger and Gottschalk, 1996). To the new technologies introduced in the 80s, that theory adds the complementary effect of some other factors, such as international trade, the increase of immigration and the delocalization of some production activities of U.S. firms. External trade promotes the internal specialisation in goods and services with a higher technological content and greater export orientation, which accentuates the demand of skilled labour, whereas both the growth of imports and the productive delocalization affect the low technology and low-skilled labour-intensive activities. The arrival of workers coming from other countries increases the low-skilled labour supply, widening the gap between demand and supply in that type of labour and, consequently, the gap in wages.

According to this explanation, based on the neo-classical theory, the differences in productivity explain the wages dispersion and the restructuring the labour market according to criteria of meritocracy, and therefore the technological change provides a “retributive prize” to the labour segments that contribute most to greater productive efficiency. This is the justification behind the liberalizing policies of the labour market that were carried out by the republican administrations from 1981 to 1992 and continued later on, with some nuances, by the Clinton administration. The argument of an existing trade-off between efficiency and equality, defended by Okun (1975) to support the redistribution measures adopted by the democrat governments in the 1960s—despite its impact on efficiency—is now inverted to justify the inequality in favour of greater efficiency (Feldstein, 1996; Autor et al., 1997; Lucas, 1990). In order to complete this theory, the authors offer an explanation of the existing differences in the labour markets of the U.S. and Europe, pointing out that the former seeks efficiency, with greater inequality and lower unemployment, whereas in the European countries, the aim of achieving greater equality reduces efficiency and maintains greater unemployment rates.¹

However, this work intends to show that, according to the data of the *Census Bureau* and the *Bureau of Labor Statistics*, there is not a direct relation between the evolution of productivity and the wage differences. This relation is more complex and other features of the economy also influence it. At the same time, this paper intends to show that the increase of inequality of the household's incomes is not solely due to the increase of earnings, but it is also important the evolution of other sources of the household's income (property income and public transfers). This article begins with an analysis of the quantitative scope achieved by the inequality of income distribution among the households in the interval 1968–2000. Herein after, it examines the evolution of the earnings and the factors that have influenced its behaviour, explaining the reasons behind the growth of inequality among employees and its relation with the distribution of the households' income. Finally, it comes to a conclusion that derives from the mentioned analysis, which rejects the hypothesis that the growing disparity in earnings is due to the variations of labour productivity and also that the inequality of earnings is the unidirectional factor influencing the growth of income inequality among households.

Before coming to the analysis, it is useful to introduce some methodological remarks about the statistical information provided by the U.S. Census Bureau (USCB). The first one regards the population unit that is used as a reference to study income distribution. The USCB considers that, due to the social changes that have happened, the reference unit is the household, not the family.

¹ This is arguable since European countries present a diversity of experiences regarding the characteristics of its labour markets and its effects on unemployment. See, for example, Atkinson (1999).

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