THE BROOKINGS INSTITUTION

40 YEARS LATER: THE RELEVANCE OF OKUN'S *EQUALITY AND EFFICIENCY: THE BIG TRADEOFF*

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Welcome:

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Keynote:

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Panelists:

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P R O C E E D I N G S

MR. PERRY: The mike is working. Well welcome all this is –- we're here of course to launch the new edition of Art Okun's book but also to celebrate Art himself and I'm especially pleased that there are so many people here from out of town, members of Art's family and people that have known him a very, very long time. I know some of you. Not sure where you're hiding on me but I do know Lois and Matt and Steve and Anita Summers is here with us and I think she's probably known Art longer than anybody else. Because I remember Art talking about when he and Bob started out as assistant professors you were good friends and I remember the first time I met Larry Summers was when we had him writing a paper for newspapers. And I said, "You see that guy over there it makes me feel old. I remember bouncing him on my knee." And that was from those days. So Anita it's great to have you here.

Let's see Janet Yellen is here and I want to welcome her especially. She and Art share a relationship to Yale. But they also connect loosely in many other ways. Janet and I were just talking before this that Art and I tried to hire Janet to come and help us with the Brookings papers, but she had a position at Harvard and wouldn't –- couldn't be pried loose. So that never quite happened, however Art had a great way with dealing with the press and a great way with words and communicating, so there was a time when I guess Arthur Burns' term as chairman was just ending and Jimmy Carter had become president that would date this I think.

And the Washington Post there were rumors running around that Art Brooke and Mike might replace Arthur Burns at the Fed and I have to read this just because it reflects how well Art communicated through the press.

"Just because my first name is Arthur I smoke a pipe, graduated from Columbia and from New Jersey and I'm Jewish some members of the Press are convinced I would be the next Chairman of the Federal Reserve Board."

Now that never happened. On the other hand Janet is not called Arthur, Janet graduated from Yale, not Columbia, Janet to my knowledge never smoked a pipe, but Janet did become Chairman of the Federal Reserve and the reason I bring all this up is because if Art was with us he would have been so enthusiastic about that and not the least bit surprised. Thank you for being here.

Now I'm also told that Charlie Schultz is here, Charlie? It's great to have you here. I know you are hiding somewhere, but it's wonderful that you came because there is a very strong connection here. When Nixon won the '68 election Kermit Gordon was the President of Brookings and he had the great wisdom to bring two young guys who had been at the top of presidential economic advising during the '60's. During the Kennedy and Johnson years. And those two guys were Art Okun and Charlie Schultz and bringing them to Brookings formed a very strong economics department. Those were the two pillars around which the department was built and prospered all of this time.

So, that's the connection between Art and Charlie which I've always thought of in my mind. So Charlie great to have you here. Kermit, let's see. I've become a very slow reader but I'm going to get there. Well my own friendship with Art, I mentioned that Kermit Gordon brought Art to Brookings. My own connection went back a lot longer than that, but I'll just mention it in passing because it's important to me.

When I first got out of graduate school Art had come into the Kennedy Council of Economic Advisors and was in charge of the macro-forecasting and all of that stuff which at that time was the center of things and I'd just graduated –- got out of graduate school and came to CEA as whatever –- the lowest rung on the ladder could possibly be, but I did get to be friends with Art and he became a mentor to me. And then we became great friends.

And I learned a lot from him and when Kermit brought Art to Brookings in '69 they ganged up on me and convinced me to take leave from the University of Minnesota which I did for two years.

And then at the start of my time here Art and I organized the Brookings panel and once we got into that wonderful activity I resigned from –- I never went back to Minnesota and I've been at Brookings ever since. And Art was always a big part of that.

Now I should say that not only was Art a great economist which he was, very creative economist, but also a wonderful human being and I think there are many of us who are still here who were here with Art during the '70's and who therefore still know him. His presence was -– he was not only the smartest guy in the room, but the nicest guy in the room too which is a wonderful combination.

I was reminded –- I recently had dinner with Bob Solo and he was reminiscing and I told him that I was going to be doing this and introducing Art's work to this audience, and I remembered because I've seen Bob that when he spoke at Paul Samuelson's memorial service several years ago he wrapped up his remarks by saying, "I don't believe in an afterlife, but if I did nothing would be fun than having lunch with Paul every day."

I can understand that perfectly because that's the way many of us felt about Art at Brookings. That having lunch with Art everyday was a great thing and – okay enough of my mushy reminiscences. And again I'm a little slow, but I will get to these things. I just don't want to miss anything really important. Yes, Art was always an advocate of activist fiscal policy. And in the '60's going back to that time when he was at the top of things, I remember there was a time early when they were trying to get fiscal stimulus because the recovery was lagging and the news came over that the government was thinking of starting up nuclear testing again. And Art said I hope they don't do that, but if they do I hope it's very expensive. But he could swing both ways, that's when he needed stimulus, but at the end of the 60's the Vietnam War had changed things drastically, the economy was overheating and they were trying to get a tax increase through.

And here comes the last quote and I offer this one mainly because Steve Okun is with us today, okay. Now this is the Washington Post quoting Art Okun complaining about why they can't get the tax increase they want to try to cool down an overheating economy:

"I must say that some recent public utterances against the tax increase remind me strongly of my seven year old son's argument against taking medicine. All in one breath."

And I can just see Steve --

"All in one breath he can reel off a multitude of objections, he's perfectly well, he's so sick that nothing can possibly help him. It might indeed cure his sore throat, but it will surely give him an even more painful stomach ache. He will take it later in the day if his throat doesn't get better. He would have taken the medicine without a fuss if his mother had given it to him the day before. And it isn't fair unless his brother's take it too."

So that's the Art that communicated so wonderfully. The press loved him. And I think it helped him.

Now when Art published *Equality and Inefficiency* which is the reason that we're really here, I admit it was a surprise to me, not the book but when I first read the Godkin lectures on which the book was based. Because it was a side of Art that well I would have predicted that those were concerns of his, I never imagined that he had such deep and thoughtful and intelligent treatment of that important subject to make.

So Art was always an egalitarian at heart and the things he did I think that they were always informed by this. Now at this point I was going to introduce Larry Summers, by saying that I thought many of those same things could be said of Larry and Larry is not here he had to attend a funeral in California. Ted is going to pinch hit for him. Ted Gayer. (Applause)

MR. GAYER: Good morning, everybody. In case there was any confusion I am most definitely not Larry Summers and as George said Larry had to go to a funeral of a friend so he has sent in his prepared remarks.

I want to say people talk about bucket lists. Impersonating Larry Summers with his mother in the crowd and I should say welcome to Dr. Summers, that was not on my bucket list. I don't think I have the imagination or certainly the chutzpah to put that on my bucket list. But I'll do my best. So with apologies to Larry and I know he regrets he can't be here. And that giggle from the crowd reminds me I should say hello and welcome to the Okun family. It's a real pleasure to have all of you here today. Okay: I am told that I first met Art Okun days after my birth though I confess to not remembering. I do remember calling him Uncle Art and playing baseball with his sons, my brothers and my father at the playground near the house where I grew up.

And I remember as a 14 year old hearing his FELS lectures on stabilization policy at Penn and finding the idea that scientific analysis could lead to better policies which would prevent people from being unemployed to be incredibly exciting. Not long after I started pressuring my parents to teach me economics and was lucky to have parents that could do a splendid job of it. I'll talk in just a moment about the great book that we are here to discuss but first I want to say something about Art. It was part of the highlight and one of the lowest lights of the early part of my career.

The first significant paper I wrote was my paper with Kim Clark on labor market dynamics published in the Brookings papers in 1979. We were graduate students and Art was the leader of the profession, but he and George Perry put tons of hours into getting our paper right, relevant and clear. Never before or since have I received a critique of my work that was as penetrating or as constructive. It was an immense gift and one that established standards I have tried to live up to ever since.

That was the highlight. The lowlight came a year or two later when not too long after Art died I propounded a somewhat half-baked argument at the MIT economics department lunch table. Skepticism was expressed, I persisted. Finally Paul

Sanderson ended the conversation by remarking in words I've never forgotten:

"Larry I recently wrote a eulogy for Art Okun. In it I observed that I had never heard him say a stupid thing.

Well Larry it looks like I will not be able to say that about you."

Brilliant. (Laughter) I learned something from Paul's put down and even more from Art's example. The stakes in economic policy are enormous. Economics is not physics. Economic theories do not just describe the world. They can change it. Rigorous modeling, effective polemic and elegant mathematics can be very dangerous when they are not informed by wisdom and good sense and a willingness to learn from experience.

Art's capacity for well-rounded wisdom regarding the most important issues of the day was nowhere better illustrated than in *Equality and Efficiency – The Big Tradeoff.* The book whose fortieth anniversary we celebrate today. I still remember the excitement with which I read it as a first year graduate student. It was the antithesis of the first year economic theory sequence in which I was mired. A thoughtful engaging rigorously logical analysis of real issues that were crucial to the well-being of the American people. Rereading the book in preparation for writing a new forward for it I was struck at one level by how well it reads today.

If a very bright student or policy maker or expert in another field were seeking an understanding of how economists think about the role of markets and issues of fairness I would even today recommend Okun's book. While recognizing the many virtues of markets he anticipates the arguments of subsequent critics like my Harvard colleague Michael Sandal when he discusses why it would be wrong to allow citizens to buy their way out of jury duty or sell themselves into bondage.

Okun is acute on the philosophical questions. I suspect he would have rejected the terms of the debate slated to follow these remarks. We'll see.

He would have said of course there are opportunities starting from where America is today to take measures like increasing access to higher education which would promote both efficiency and equity. And he would have had many more examples that likely would have included closing tax shelters, attacking monopolies and fostering economic cooperation.

At the same time he would have recognized that there were likely limits on the amount of inequality reduction that can be achieved with policies that also accelerated growth. And so he would have recognized that as usual in economics there are tradeoffs. The more of one objective you achieve the less you are likely to achieve some other objective. Substantial increases in redistribution are likely to come at some debatable cost in terms of economic efficiency. So his balanced advice would have been to first implement policies that increase growth while increasing equality. And then consider those measures that involve trading off efficiency and equality. At another level rereading Okun's book reminds one of how much the economy has changed since the 1970's or even since the 1990's and as a consequence how much a sensible policy agenda today is different than the one that was appropriate in the 1970's or '90's. In my forward to reprinting of *Equality and Efficiency* I describe the major changes in the economy and speculate about what Art would be recommending if he were with us today.

Rather than reprising that discussion here let me conclude by noting how in area's relating to equity and efficiency my thinking has changed in response to a changing economy over the last 40 years. This is not I believe because my value have changed, but is rather because of changes in the economy and our understanding of it. When Okun wrote and for some years afterwards economists believed that the distribution of income as reflected either in the profit-share or the share of income going to different quintiles of the population was relatively constant.

It followed that the dominant determinant of the growth rate of middle income families was the overall economic growth rate or essentially equivalently that average wages would attract productivity work. This led to great emphasis on measures that can be expected to raise productivity or productivity growth.

For many years now it has been the case that the income distribution has been growing much more unequal. In particular the share of income going to the top 1 percent has risen rapidly from about 8 percent of income in the late 1970's to above 20 percent today. And the share of capital income and total income continues to rise updating the calculation performed a few years ago by Jason Fuhrman and me I recently calculated that if the income distribution were the same as it was in 1979 about one trillion dollars more would be going to the bottom 80 percent of the population increasing their income by almost 25 percent and that about one trillion less would be going to the top one percent reducing their incomes about in half.

In this context unlike the one in which Okun wrote it is clear that influencing the distribution of income and its trend has the potential to have a major impact on the wellbeing of the middle class. How? With inequality higher and progressivity lower the case for progressive reform is strong.

Certainly because of what has happened in the economy I wouldn't be thinking about tax policy but much more emphasis on distributional issues relative to efficiency issues than I would have during much of my career. Similarly, I believe that concern with issues relating to the cost of capital and the adverse effect of taxes and increasing it has been very legitimate at points in the past.

At present when zero interest rates make capital costs as low as they have ever been but corporate profits are at record levels there needs to be much less concern with capital costs and more concern with the distributional aspects of capital taxation. The same basic idea that rising inequality tips the balance in fairness and efficiency applies in other areas of policy as well. So also does the emergency of deflation and low inflation as a threat to the American economy. Okun recognizes that minimum wage can be dangerously high and excessively strong unions can do damage if jobs are taken away and inflation is promoted. These risks are remote today.

Indeed more income for workers would likely contribute to more spending which would in turn increase employment. When the minimum wage is actually lower in real terms than it was when Okun wrote and when only six percent of private sector workers are covered by unions I would judge that the benefit cost ratio seems tilted towards minimum wage increases and towards relaxation of the rules regarding the rights of private sector workers to bargain with management. In other areas where conditions have changed over the years is with respect to policy directed at the financial sector and corporate governance.

The financial sector has shown itself to be less a source of diversification and stability and more of a source of instability -- the most judged a generation ago. At the same time, compensation levels in the sector and in firms engaged with the sector has gone up rapidly.

The simultaneous emergence of high profits and low interest rates raise the question of whether monopoly power is on the increase, so the question of regulatory actions looms much larger than it has for many years.

I could go on and talk about the equity benefits of a high pressure economy, mandated paid leave for those with family responsibilities, and a range of issues.

I will have made my point if I have wetted your curiosity with respect to Art Okun's most influential book and made the case that an economic policy with regard to issues of equity -- Abraham Lincoln had it right when he said "As our case is new, so we must think anew and act anew."

Thank you. (Applause)

MR. WESSEL: Good morning. I'm David Wessel. I'm Director of The Hutchins Center on Fiscal and Monetary Policy here at Brookings. It's a pleasure to sort of pick up where Art Okun left off this morning.

The striking thing to me as I reread this book, the new issue of it -- there are two striking things. One is it is incredibly lucid. That doesn't seem to be the standard in academic economics these days, and there is not one Greek letter in it, which I take as a huge plus.

The other thing, and Greg Mankiw and I were talking about this earlier, that it is striking that a book that was written 40 years ago -- if you adjust for the numbers are all off because of inflation -- can be so relevant today.

Let me just read you part of the opening passage which will then lead to our panel discussion. Okun writes "Contrast among American families in living standards and in material wealth reflect a system of rewards and penalties that is intended to encourage effort and channel it into socially productive activity.

To the extent the system succeeds, it generates an efficient economy, but that pursuit of efficiency necessarily creates inequalities, and hence, society faces a tradeoff between equality and efficiency."

"Tradeoffs," he writes, "are the central study of the economist. You can't have your cake and eat it, too, is a good candidate for the fundamental theorem of economic analysis. We can't have our cake of market efficiency and share it equally."

Joining me up here to talk about this today are Heather Boushey, who is executive director and chief economist at the Washington Center for Equitable Growth, and a senior fellow at the Center for American Progress.

Melissa Kearney, director of The Hamilton Project, senior fellow here at Brookings, a professor of economics at the University of Maryland. Melissa informs me they both had media training which went to the color of dress you are supposed to wear. (Laughter) They had the same training.

Greg Mankiw is the Robert M. Beren professor of economics at Harvard, a former chair of the Council of Economic Advisors, and co-chairman of The Hutchins Center Advisory Council.

Justin Wolfers, who is on leave from the University of Michigan, is a Non-Resident Senior Fellow here and a Resident Senior Fellow across the street at the Peterson Institute for International Economics.

I thought I might start with that opening quote from Art Okun's book. It seems to me there are three possibilities. One is there is the tradeoffs that Art Okun described, and the debate is how much we should favor equality and how much we should favor inefficiency.

The second possibility, there is a tradeoff, but our current policies are so inefficient that we can have both more inequality and more efficiency, and the third is that Art Okun is basically wrong, that there isn't as much of a tradeoff as he suggested.

Indeed, Paul Krugman recently wrote citing some new research at the IMF that "Taking action to reduce the extreme inequality of 21st Century America would probably increase not reduce the rate of economic growth."

Greg, can I ask you to start? To what extent is there still a tradeoff or where is it, or how do you think about this?

MR. MANKIW: The way I think about it is there's a tradeoff and some policies move us along the tradeoff, but other policies shift the tradeoff, sort of like inflation/unemployment tradeoff. Sometimes you move along and sometimes you shift it.

I'm just going to give you an example of each. I think when Art Okun was thinking about a tradeoff, he was basically thinking about tax and transfer policy. Tax the rich, give money to the poor.

I think there, there really isn't a tradeoff because when you do that, you are raising marginal tax rates on both the rich and the poor, the rich, because they are paying the taxes, and the poor, because they are probably paying effective tax rates because the benefit they are getting is going to phase out as their income goes up.

I think that is sort of the classic case, and when he was talking about a leaky bucket, which I see now is on the cover of this new book, I think that is what he meant. He's thinking of a tax and transfer policy, and the question is how leaky is the bucket.

MR. WESSEL: Define for people who don't know what the "leaky bucket" is.

MR. MANKIW: Sure. "Leaky bucket" was a metaphor saying that when you take money from the rich and give it to the poor, it's like you're taking water from one part of a desert island to another part, but as you move water around, you only have a leaky bucket.

When you move this money from the rich to the poor, some money will leak out because you are reducing incentives, reduce efficiency costs, and he is saying how much of a leak are you willing to put up with. He sort of says 10 or 20 percent I'm willing to put up with, but not 90 percent. He contrasted himself to Rawls, who would be willing to put up with any amount to increase the people at the bottom.

I think that's an example of the tradeoff. I do think there are policies, and I think Okun believed, too, there are policies that shift the whole tradeoff out. Okun mentions schooling, increase schooling for under privileged people. For sure, that is going to mean more efficiency and more equality.

I think there are other policies that would do that, too. Let me give you a couple of examples. I think if we let more skilled immigrants into this country, it is going to change the mix of skilled and unskilled workers. That is going to tend to increase both efficiency and equality.

Let me give you one that I think is more controversial and not everybody will agree with me. There is a big debate about minimum wage. Some economists like the minimum wage, some economists don't like minimum wage.

I think most economists think the EITC is better than the minimum wage. Let me suggest we abolish the minimum wage, expand the EITC, and I think that is a policy that would increase equality and efficiency. I'm guessing not everybody is going to agree.

I think there are things we can do in terms of helping people at the bottom that aren't necessarily involving the tradeoff.

MR. WESSEL: Heather?

MS. BOUSHEY: I don't agree with the last point. (Laughter) First, we have sort of set this up as a debate, which I will sort of admit at least for me is a little bit tough when I know there are family members in the audience, so I want to start off by saying the book was really fantastic. (Laughter)

MR. WESSELL: But I don't agree with it.

MS. BOUSHEY: I'm sure he was a lovely person, and it was very lucid and well written. It really was a delight to read. I think the point about the minimum wage and EITC notwithstanding, for me, rereading this over the past couple of weeks really kind of hammered home that I think this is really more of a historical document than something we should be looking to as a guide for policy making today.

I think a lot of the comments that Larry Summers made were made -- when you tear away the first part and look at the actual recommendations he made in the second half of his remarks -- are consistent with this.

I think both our empirical starting point in terms of the economics today but also in terms of the political situation. The political economy is so different from the moment in which Okun was writing about in 1975, that I found as I was rereading it there were just these shocking, very jarring phrases that were hard to reconcile with our own political reality.

For example, at some point in the book he said something -- I don't have the exact quote in front of me -- of course, everyone agrees those people who aren't healthy should have access to health insurance, you know, if folks need it.

Of course, this is the same data I was reading in Politico that you know, many

Republicans are promoting work requirements for Medicaid, so this is certainly not an agreed upon starting place here in today's America, which I think is important as a starting place because so many of his analyses and his conclusions all stem from this shared vision of what is going on in the economy and the political economy, which I just don't think is relevant. We have to start from that.

Second, where he ends, both in the book and the afterward that is in this lovely publication, this republication that Brookings is doing, he has this plea where he steers social science researchers toward a research agenda that is focused on measuring the effects of the tradeoff.

As an economist and social scientist, I don't think that is the right research agenda, and I have also found that research agenda has been very frustrating over the past few decades, because I think it steered us away from some of the really big questions.

Contrast that phrasing with reading the introduction to Thomas Piketty's book, where he expresses this real frustration with the economics profession for focusing on narrow questions and not looking at the whole political economy.

I think understanding the pros and cons in a tradeoff is very important, but that is not the primary role, I think, of those of us who are advising policy makers. We need to think bigger. I think it is that kind of thinking dare I say that has allowed us to miss the real importance of this rising inequality that we have seen in recent decades, which is having such a pernicious effect on our economy.

My third point is there is this whole new body of research that is showing that rising inequality is bad for economic growth, and certainly there are nuances to it, and there is a lot more research to be done, but I think we can't ignore this framing of the tradeoff and especially as the shorthand for how we should be thinking about policy just isn't consistent with this new macroeconomic evidence.

I will stop there, I am sure we will get back to those.

MR. WESSEL: Melissa?

MS. KEARNEY: This is going to be fun. I disagree entirely. (Laughter) Let me start by saying, I went back and read the original because I just am in love with this book. I remember where I was sitting as a junior in college when I read this book in Firestone Library. I had been taking sociology and poverty classes, and a lot of contemporary American history classes.

I was always very interested in poverty. When I read this book, it was like, you know, light bulbs went off, and I thought this was tremendously clear and honest about the tradeoffs and how we can address poverty in this country, and yet still foster economic growth and productivity.

I have always been very influenced by this book. It sort of was the book that I think convinced me that I wanted to be an economist addressing these problems, and I have actually approached my own research about tax and transfer policies in the U.S. in exactly this framework, thinking this is exactly the framework, instead of tradeoffs, we should be using when we evaluate policies in both the big picture and the small picture -- I have been pushing this book on my students for over a decade and trained them this way.

I think this tradeoff is perhaps even more important today than ever, and as I reread the book this week, I was struck by just how relevant and how forward looking it was.

The quote you pulled out, David, it struck me 20 years ago, it struck me again this weekend, I think it really crystallizes the tradeoff in the aggregate, and I think Okun does a great job saying we need to value efficiency, we need to value equity, and we need to think about where our society should be in the balance.

Now, I agree with Heather, I think, in saying we are off kilter today. That doesn't make this a useful framework. It makes it a great framework and it says have we gone too far in allowing too much inequity such that now we are actually costing ourselves in our nation's productivity.

I think the answer to that is yes. The reason why I think the answer is yes is really because of what's going on at the bottom, so I am less concerned about the well concentration at the top say than maybe some others because I'm not sure what the cost is, but I am sure that the pervasiveness and persistence and the consequences of poverty and the lack of opportunity and upper mobility and the lack of jobs and well paying jobs for too many folks in our economy is a problem and it violates most of our notions of equity, and it also has tremendous costs to our society.

I think if we agree on that, we should do more. Then we have to take very seriously Okun's point about when we design policies and tax and transfer programs, there is a tradeoff implicit in the structure of those programs, and we can't get around this.

It's too flip to say we need to give more to the poor. Okay, but how? There are ways we can do it with more or less efficiency costs. I think exactly public finance economists and those of us who would advise policy makers need to take that into account when evaluating all programs, large and small, so the minimum wage and EITC are perfect examples.

I'll even make the point about the EITC. Everyone loves the EITC because we think this is the program that addresses Okun's point, we subsidize work. We give people incentives to work. That's true, unless you're a married couple, and you have two minimum wage workers. All the incentives for the EITC are for that second worker not to go to work. Why?

Because when we transfer money to low income households, we have to tax it away. When you tax it away, there are people who face a really high margin on tax rates.

Even in the program that we hold up at like this is our best answer to the equity/efficiency tradeoff, smart design of that program has to acknowledge tradeoff implicit in the design.

I think both in thinking about the aggregate challenges and where we are in the continuum of equity versus efficiency, and thinking about it at the micro level how we design our programs, using the framework that Okun set out for us, is a really productive and important way to go.

MR. WESSEL: Justin? You can't agree with everybody.

MR. WOLFERS: I'll be perfectly Brookings and split the middle in a wishy-washy way. (Laughter)

MR. WESSEL: This will limit your air time. (Laughter)

MR. WOLFERS: I'm willing to stipulate there's an efficiency/equity tradeoff. I think Okun's focus on it is the result of the great confidence of economists of the day 50 years ago that we lived in an economy where we were somewhat close to that frontier.

I think if you thought about today's politics, you would be less confident. If you looked at the policy development subsequently, you would be less confident. I also think the scope of economics has changed now from a discipline that's far more infused in both sociology and political science, and I think that pushes you to look beyond tax and transfer policy.

Tax and transfer policy is the obvious case where there is a sharp tradeoff. When you look beyond it, I think far less so.

I think there is a horse race here between the incentive problems and what we know to be the real consequences of inequality, health problems, mental illness, trust, social mobility, very different politics that arise when we have greater inequality.

So, if you turn the question around and said is the implication of Okun that the pie needs to be smaller in order for each of us to have more equal slices, I think the answer is certainly not. There is a huge list of policies, I think, that help us on both inequality and end growth.

The most important of which, I think, is discrimination. The effect of emancipation of women over the past 50 years has been one of the most important engines of economic growth, and of course, reducing inequality within households and within families.

We have seen in some industries a rise in monopoly power, monopoly power, it is just rents, it is not allocated, it doesn't necessarily help us get more of any stuff over the past 30 years.

Much of the American growth miracle was the result of people going to school. Thirty years ago, American men decided to stop going to school, so we haven't had increases in educational attainment in several decades. American women, I think, have been somewhat more sensible.

There are huge gains in human capital, which could improve both growth and inequality. Once you start thinking about those sorts of investments, you can't help but think about neighborhoods. When you look at pictures of Baltimore and you look at pictures of Ferguson, you see neighborhoods where investments could surely help both growth and inequality.

The problem with mass incarceration was not on the agenda in Okun's day, but surely is a huge issue in terms of both inequality and growth.

We have seen the decline of the American Union movement. Unions certainly helped hold inequality down, the more functional among them could also help raise productivity. The less functional, absolutely, I would agree, maybe not.

As an economist today, I'm far less confident we are anywhere near this frontier where we have to start worrying about tradeoffs. There is a bunch of stuff we can do, which I think will have enormous effects on reducing inequality and could have big effects on growth, too.

MR. WESSEL: Greg, do you agree with the point that we are far from the frontier, that we could reduce inequality substantially and not hurt efficiency, productivity, and growth?

MR. MANKIW: There were several examples in which I thought we couldn't increase both. I think those are politically difficult. I think there is also disagreement among economists -- my eliminate minimum wage and expand EITC is an example where we would not have agreement on this panel.

I think we have to acknowledge there is a tradeoff when you are talking about tax and transfer systems. I think that is mainly what Okun was focused on.

MR. WESSEL: It seems to me it is striking when you read Okun's book and he describes -- Larry talked about this a little bit -- the degree of inequality 40 years ago compared to today.

Just one example, Okun writes that the richest one percent of American families have about a third of all the wealth, and the bottom half hold about five percent of all the wealth. If you update that using similar datasets, the richest one percent have over 40 percent of the wealth, and the bottom half have only one percent.

Doesn't that suggest there is a chance we are farther from the frontier? No?

MR. MANKIW: The question is why is that? Why have we experienced increasing inequality? To mirror something that Justin said, which I think a lot has to do with education. I think one of the best books about this is not the Piketty book but actually a book by two of my Harvard colleagues, Claudia Golden and Larry Katz, and the title of the book is "The Race between Education and Technology."

Their basic story is technology tends to be a force driving towards increased inequality, because skilled workers use new technologies and unskilled workers are replaced by them, and education is a force in the other direction that turns unskilled workers into skilled workers.

I agree with Justin, we haven't done as good a job on the education front as we had in previous generations.

MS. KEARNEY: There are two things I want to pick up on. Often these facts about the top one percent are cited to say we have gone too far, but I want to challenge us to say if we want to keep saying that, why is that a problem. I just have not seen convincing research to tell me that one percent doesn't reflect increased productivity.

This is a minority view, but we focus so much as if just the fact that the rich have all this money is bad, and I really want to challenge those among us who are saying that to explain exactly why that is bad.

Again, I know why it is bad that we have mass incarceration. Why? Educational attainment has stalled. I know why those things are bad. For us to figure out what we need to do about the top one percent, I think we have to figure out what is driving that, how much of that increases economic productivity, the returns to a global market, how much of it increases rent. I don't think we know that.

The second point is -- the point about the mass incarceration, I think Okun mentions this. I was struck this time rereading it. He talks about why we don't allow people to buy votes, and he talks about the criminal justice system, and there are things we need to take out of the marketplace.

While he doesn't talk about mass incarceration in those words, he raises this issue very clearly, which is if people think that the system, the institutions, aren't fair, that leads to a lot of frustration, and he says, you know, those inequalities can produce compound inefficiencies, and I think that is what we are seeing.

MR. WOLFERS: An amazing euphemism, very good one. So but Melissa, here's the thing. You sort of shift the presumption here. You're like, you know, you have to prove to me beyond a reasonable doubt that all this money going to the one percent is a problem. That's a strange presumption but let me give you a different frame for it. We should be worried about incentives; we're economists, that's what we're paid to do. So let's think about whose incentives are we worried about? Which groups of people do we think are currently not working as hard as they could or using their talents as much as they should because the tax system, do we think it's the top one percent? Or do we think it's sort of you know, middle and working class families and secondary earners. If we think it’s the latter and I think the evidence is reasonably strong on that, then what we need to do is re-jigger our incentives to move the work incentives to where the workers are, rather than at the moment to where the money is.

MS. KEARNER: Or where the workers are not. We want more of those folks working.

MR. WOLFERS: Right, where the workers should be. Absolutely.

MS. KEARNEY: I mean I think that's right and I think -- I mean, why I worry about inequality is because I think the gap between those at the bottom and at the middle -- it's become so wide that there's too many folks at the bottom who don't see a way up, who are shut out of those networks and those institutions and we see that they're dropping out of school; they're becoming teen moms. They're not doing the things we think they should be doing to invest in themselves. I'm not sure it's irrational. I think they are responding to the environment around them, and that's why we do, I agree on the point that we need to do more to foster inclusion in our economy and our society for folks who are feeling marginalized.

MS. BOUSHEY: So if I could just jump in on just a couple of things. One, so the idea that what's happening at the top is not of concern when we're thinking about what's happening at the bottom and the middle, I don't think that -- I think that the evidence actually goes in the other direction. I would point first to a recent paper by Branko Milonovic and Roy van der Wiede, where they looked at the effective inequality on growth across states and have found that -- and they've disaggregated so they're basically able to show that rising inequality actually reduces incomes for the bottom and boosts them at the top. And so I think -- and so that in and of itself, one study doesn't, isn't enough for us to go on, but I think it brings up a whole series of questions about what that money at the top is being used for, what kinds of incentives its creating in our economy at large. But also the extent to which those gains at the top have been really at the expense of those at the bottom. When you look at the long term trends, one of the striking things about 1975 when Okun first wrote this book, is how that really is -- it's sometime in there, that magic moment where the world shifted from a world of equality where everyone was growing together, to a world where that was no longer the case. So, and many of those as we've seen from 1975 through today, (inaudible) sizes data show that 110 percent, or 109 percent of the gains have gone to the top relative to the bottom 90 percent.

So I think that that question I think -- it'd be good to spend a little bit more time discussing, but then second, I think we also need to understand how those gains at the top affect the opportunities not just for the bottom, but the way folks at the top are -- to use a term that I first learned from Richard Reeves here at Brookings, opportunity hoarding. And what that's doing to communities around the country, how it's bidding up prices for homes and neighborhoods with good schools, like what advantages are being sort of kept at the top and people are not being allowed to move up. Not just from the bottom to the middle, but importantly and I want to bring this into the conversation, the middle. I think that this trade off, part of my frustration with it is I don't think it’s just about the top and the bottom. That's not what's happened to America. What we've seen is this lack of growth in the broad middle, which is where we need to be focused A, if we care about democracy but also if we want people at the bottom to actually be able to attain and achieve a safe and decent middle class lifestyle, you have to care about what's going on in that place. So if you're seeing this opportunity hoarding at the top, that's effecting what's happening in the middle. But finally and my last point and then I'll let someone else talk, is I do think thinking about the effect on our political process, folks at the top just could not be -- I don't think it could be understated, earlier this last week we did a conference at Yale with a bunch of political scientists, where we spent a whole day and a half discussing the effects of economic inequality on political outcomes. And there appears to be a lot of evidence that today's high inequality and especially this pulling away at the very very top is having effects on our political debate, our political process, and that all has an effect on the lives and living standards of everyday people. So I think that we -- I mean all three points are really just sort of hammered home that I think that this tradeoff and Okun many times in the book, is like we don't need to be focusing at the top. Don't worry about that. We're regulating them; they can't affect the political process. We need to be focusing on the bottom. I think that's the wrong question. And we need to be thinking about the top a lot more.

MR. BOUSHEY: Let me pick up, I'm always reluctant to raise politics with four economists who will then tell me they're not experts. But both Justin and Heather have opened the door, so I feel -- so I think you've misstated Okun, and I think if you read Okun, he was worried about how money influenced politics, and if you were worried about that forty years ago, you can only worry about it more now. At one point he says how does capitalism survive in a democracy? What makes the not so affluent majority so charitable towards the rich minority? The tolerance of the masses for economic inequality is puzzling -- at least it is to me. He says radicals on the left say money buys votes, democracy is a sham. And I think a caricature says free market fundamentalists say capitalism provides higher standards of living for most families, the not so affluent recognize that, and therefore they tolerate it. But I do think that -- and this is a point that Joe Stiglitz has made, that he wrote that inequality isn't so much a matter of capitalism in the twentieth century as is of democracy in the twentieth century. So to what extent do we worry that the degree of inequality influences the political process so we can't pursue those policies that might, like Greg suggests both increase efficiency and equity?

MR. WESSEL: I'm more skeptical about the role of money in politics. I point out we probably have the most liberal president in half a century --

MR. WOLFERS: Probably in six or seven years.

MR. WESSEL: In whereas we now have high levels of inequality, so I'm skeptical that there's this direct link from money to politics and to the extent there is we should think about the political system. I think most things rich people spend on are not politics. Secondly, I should note that when we want to be so concerned with inequality right now, the period of time actually with the biggest increases in inequality is between the period of 1980 and 2000. It's been high, but more stable since then. But we're worried about inequality now. Why is that? Well I think it's because the economy has generally been pretty crappy, for the past few years. So I think we worry more about inequality when things are bad than when things are going well. And I think Okun is right. When things are going well for the typical person, we don't really worry about the fact that Mark Zuckerberg is doing reasonably well.

MR. WESSEL: So is there a relationship between stagnant middle wages and the amount of inequality we've had?

MS. KEARNEY: So I think this -- the question about or Okun pointing out he's puzzled by why Americans put up with this. I have to think that the reason is because Americans have believed for many generations; if they work hard they will get ahead. And so we have this winner takes all society, but we have this view that that opportunity to get ahead was open to most people. I feel like the political tides are shifting in part because the economic reality is shifting. Where that winner takes all -- not everyone has the same opportunity, or even close to the same opportunity to get ahead. We see in the past 30 years the divergence of childhood circumstances for kids born to college educated parents versus low educated parents. Those kids start out with so much disadvantage relative to their higher educated, higher income peers in such families, that that dream that everyone can get ahead, that aspiration that came from this winner take all economy that we were willing to put up with -- I think the appetite and allowance for that is waning.

MR. WESSEL: I think it's a really good point, and there's one place, I'll get to you in a minute Justin, where what Okun said struck me as jarring with the lens of forty years. He says, obviously, no one knows how much improving equality of opportunity, he refers to discrimination and income based loans for college, would enhance either equality of income or efficiency of the economy. But then he says, the right is convinced that opportunities are basically equal and no heroic efforts at reform are needed. The left argues, no amount of equalization of education or hiring practices will dent the amount of inequality, all I would claim, Okun writes, is that such efforts deserve a real try.

It seems to me that one of the most striking changes in the political debate over the last few years is that the Republicans, and some people on the right have stopped arguing that there's not a problem and that one of the few things that Republicans and Democrats agree on now is that we're a bit distressed that there's not more mobility. We know that there's probably no less mobility in a statistical sense than there was, but the inequality has risen. So you can see conversations, Hillary Clinton, Marco Rubio, Jeb Bush, Paul Ryan, all struggling to figure out some recipe for improving social mobility. So that's an argument that has changed and I think in Okun's day, and Justin you wrote today about Roz Cheti's latest work on this.

You can respond to either what I said or what Melissa said.

MR. WOLFERS: I like your quoting Republicans and their concern about a mobility agenda at the same time that they want to completely get rid of the estate tax for families above ten million dollars. It strikes me that you're taking speech a little bit too literally there. And if we talk bills that were been proposed instead I'm not sure we'd see such a bipartisan commitment to the mobility agenda.

So the comment, I want to come back to the earlier quote from, which I thought was beautiful, and in retrospect maybe looks stunningly naïve. You said, how is it capitalism can survive democracy? Why aren't the workers revolting and just pounding the rich into the ground, and fifty years later that doesn't seem to be the important question.

MR. WESSEL: Right.

MR. WOLFERS: Instead it seems the more important question is how is it democracy survives capitalism, and as we're on the cusp of the beginning of the Republican nomination and the Adelson primary soon to be followed by the Koch primary, it seems that this is like a much more important question today than it has been in the past.

MS. BOUCHEY: Okun even says people don't mind inequality and income distribution when it's associated with effort. And I think the concern among a broad swath of the population and folks on the right and the left is that increasingly people exerting a lot of effort are still not making a living wage. And that's where I expect the political appetite for a more -- a stronger safety net will take hold when it's like look at these individuals and these families, they're working hard, they're getting some college and they still can't afford the rising costs of housing and healthcare and education. So that's about the frontier again.

MR. BOUSHEY: So let me just respond this comment about the Republicans and the state tax. I can't let it go. (laughter) When the Republicans talk about mobility, they talk about trying to help people at the bottom go up. They don't view that as synonymous with how to getting people from the top to come down. And the estate tax issue I think, is really focused on the people at the very top, and you if prohibited the states over 10 million dollars, who paid 100 percent of the tax. The person at the bottom seriously living in inner city Baltimore isn't all of a sudden going to have a better life because Mark Zuckerberg can't leave his money to his kids.

MR. WOLFERS: You make sure those at the top can't fall. I can't see how you can create any mobility.

MS. KEARNEY: There is no mobility.

SPEAKER: The question, when the people at the bottom -- in terms of mobility, you want people to do well. We want people at the bottom to do better. We could have mobility pushing everybody going down. That's mobility. Everybody is just going down. That's not the same thing as actually getting people up.

MR. WOLFERS: I thought that after the first nine and a half million, my kids are already doing well. (laughter) Above that seems a little excessive.

SPEAKER: That's your judgment call, but that's not helping the person in inner city Baltimore. That is not -- saying Mark Zuckerberg, you have to spend the money during your lifetime, don't leave it to your kids, is not going to help anybody.

MR. WESSEL: Heather wants to defend the state tax here.

MS. BOUCHEY: A. It's not don't leave any to your kids, but it's putting a limit on what is taxed or not taxed, now let's be very clear, it's not don't leave anything, it's not zero --

MR. KEARNEY: Fine, you're putting a limit on it, that's fine.

MS. BOUCHER: But those dollars could be put to very good use, helping those kids in Baltimore.

MR. KEARNEY: What estate tax says, is spend money in your lifetime. Buy that big yacht, buy that big mansion, and buy the Ferrari. Because when you spend it while you're alive it doesn't get taxed, it's only the stuff that you leave to your kids that gets taxed. And so that's the main thing the estate tax does, it changes the relative price of your consumption and your kids' consumption.

MS. BOUCHEY: But don't we want young entrepreneurs to all -- at any rate, we could keep debating this until the cows come home, but it seems like we want that flexibility at the top. And it also seems so un-American to me to have this group of people that we want to just stay up there.

MR. KEARNEY: But that's what his point is, you don't like that they're rich but that is actually hurting productivity.

MS. BOUCHEY: Well is it hurting productivity -- so that the idea, right -- so I will answer that but I wanted to make one earlier -- I'm going to go back and come back. One of the points that -- one of the quotes that I had sort of pulled out from what Okun had said about folks at the top and the rich, was quote, if the uses of fat checkbooks in the political process can be tightly regulated, the plutocracy will lose much of its political punch. Which he says fairly early on in the book, which I think is important, which gets back to a point I made in my opening remarks, which was that he was writing in 1975. In 1975, a quarter of people were in unions, that was actually a thing that you had to study and learn about. There was some power there. That was the moment when Ralph Nader turned forty in 1975. That was the height of him as a consumer advocate, out there creating, working to advocate for many of the consumer regulatory agencies that were pushing back. It was right after Watergate and this notion that they were going to regulate campaign finance in ways that they just -- I mean sort of looking up what that was. I was like, wow that's so outside of my understanding of the political process -- but he did say that you need to do something for folks at the top, but he was pinning his hopes, at least that was my reading of the book over the past few weeks, on a regulatory infrastructure that isn't in place anymore today and I think that gets it one of the very deep concerns that I have at the top is not whether or not -- the state tax, that's important, but it's how it's effecting the regulatory process or what political issues are actually put on the table or not that effect all these different ways that allow some people to keep their gains and some people not to get them. But also have this perversion on democracy. So I didn't mean to dismiss his point, but he's working this particular political context.

MR. WESSEL: He said if you regulate money then you won't have power. It seems to me after reading the New York Times on the federal election commission that we haven't met the first condition. Let me switch before we go to the audience a little bit, on other policies. So Greg mentioned the EITC, but what other policies would you recommend that would help us achieve more equality with having a minimal or no impact on efficiency. So how would you change the tax code besides the EITC, what about the social security disability thing, how would you change the way we finance college education? Melissa do you want to start?

MS. KEARNEY: Sure I'll start with, one thing I've written about the tax code which I feel strongly about is this secondary earner penalty that is implicit because we pool income across, within a family, and we have a progressive --

MR. WESSEL: We could fix that. It's hard.

MS. KEARNEY: You could fix that. You can allow secondary earners, you can allow capitalist --

MR. WESSEL: That's the one percent to pay for it right?

MS. KEARNEY: Right now the tax codes explicitly favor married couples where a spouse stays at home.

MR. WESSEL: Okay, so give us another example.

MS. KEARNEY: Another one, I think DI is a great example, disability insurance. And I'll add SSI, which is the supplemental security program.

MR. WESSEL: Explain.

MS. KEARNEY: Okay. So DI is -- we award people, essentially if they qualify with medical conditions, verifying that they are unable to work, they're guaranteed an income stream. Now the problem is if they get better and start to work, they have now signaled the government that they are able to work and so they lose their check. And so this is a program that incentivizes people not to recover. Good academic research has shown for many it becomes -- for low wage folks in tough labor markets it becomes an early retirement program. There are ways that we could maintain our commitment to support those who are unable to work, and yet still improve equity and efficiency. One particular way is, the DI checks, the medical criteria, there's no variation. So if you are severely disabled or you have as your limiting condition back pain, which I don't mean to minimize but that's different than severely disabled, your check is the same. So we could have a partial payment system which allows some people to let's say, do part time work, work for a few hours and still collect some from the system. Other countries do this and we do not.

For the child SSI program, this is a program where families who are below a certain income level, and their child meets a certain medical criteria, they get like 570 dollars a month from the federal government. In previous work I actually empirically tried to estimate the leaky bucket of this program and I said look actually, for a dollar we transfer to a family, their income goes up by 72 cents. So a 28 cents efficiency lost by the family limiting their own earnings. And I thought this was a pretty -- that's a leak I'm willing to take and that's not that bad. But I have evolved in my thinking on that, the program really if you think about it in the long term; it gives the parents incentives not to get their kids the help they need, because if their kid's condition improves, they lose 570 dollars a month. That's exactly what we don't want to incentivize parents to do. Right, so we could change the nature of the program to again give more money to families with severely disabled children, and also to put in bonuses if there is occupational therapy going on or things to improve the condition. So that's another -- I have a long list. I think there are a lot of programs, because we're starting with a complex messy system much of which has been designed to satisfy political goals, I think there are a lot of programs -- the DI and the SSI are at the top of my list.

MR. WESSEL: Greg.

MR. MANKIW: I'm tempted to cede my time to Melissa. I agree with so many of the things she said. Can I say something broader about the book? I'm going to take exception to one word in the title and that's the word The. Equality efficiency -- the big trade off. I think it's a big tradeoff, and I think it's only one of the tradeoffs we face today in public policy. And indeed I think in the book, he's a little unfair to Milton Friedman. Because he wants this to be and if this is the big tradeoff then where does Friedman, he's like I only care about efficiency.

Let me suggest another big tradeoff, and that's liberty versus community. I think Okun basically assumes communitarian values. If this bucket weren't leaky, if it were a perfect bucket, he would move to perfect equality. And I think Friedman would have said, no no, if people work hard and they produce a great product and people want to spend lots of money on it, then they should keep their monies, they earned it. And that's a very explicit, if you read Robert Nosic, adequately stating utopia which of course Okun didn't have the opportunity to read because it came a few years later. He's very explicit that it's not the government's job to fix the slicing of the economic pie, if people earn something fair and square, it's theirs, and it's not the government's job to redistribute. Certainly, if I took my students, my A students, you've gotten a lot of A's already, I should give some of your points to the students who have already gotten so many C's on this transcript. People will say no no, I earned that A, and I think what Nosic is saying, well if Zuckerberg creates a product that everybody really wants, then he should keep his billions.

MR. WESSEL: So the book concludes an essay that Okun wrote a couple years later, and it does mention Nosic.

MR. MANKIW: Oh he does, I have not read that, I haven't seen the new version.

MR. WESSEL: Justin, pick a policy. Not the estate tax. We've already done that one.

MR. WOLFERS: So I worry that when we do these things we emphasize how much we disagree, more than how much we agree. And I think despite the fact that to be an appropriate carnival show, we have to, should both wear red dresses and disagree.

MR. WESSEL: Well you failed on one count. (laughter)

MR. WOLFERS: There's enormous agreement amongst economists. I think we all would agree there's real costs of inequality, and I think in terms of trying to think about -- I think we also all agree that there's a bunch of policies which do push the frontier out. And most of those I think actually come from taking a long term view. It's the short term-ism that I think leads us astray. So if you look at things like Roz Cheti's early work on teachers, teach equality. There's just unbelievably large long term effects. If you look at this stuff that came out this morning about neighborhoods, investments in neighborhoods are moving people to good neighborhoods, has humungous payoffs. I think another one of the important things that has come up, we had the behavioral economics revolution which gives us incredibly cheap interventions. So there's this body of work now showing that the barriers that prevent a lot of working-class kids from going into higher education is just about information. No one ever bothered to tell them that they could go to Harvard, or in fact that going to Harvard is cheaper than going to the nearest community college.

And then, you know, the flip side is we can also all agree, there's a bunch of stuff where you do see these tradeoffs, and a lot of it has got to do with dumb politics, and there's a lot of dumb politics with a lot of giveaways to bad guys, or they are completely unnecessary and, we, economists could and usually do stand up against them.

MR. WESSEL: Heather, pick a policy.

MS. BOUSHEY: So I want to pick -- Can I pick two? Well, let me just start with one.

MR. WESSEL: Surely. Melissa set the precedence.

MS. BOUSHEY: Yeah. And that’s why I (inaudible) --

MR. WESSEL: And if I would have let her she would have done 15.

MS. KEARNEY: I would have not done more than two, yeah.

MS. BOUSHEY: Well I want to pick up --

MR. WESSEL: We'll go to the seminar later.

MS. BOUSHEY: I want to pick up on something that was in Larry Summers remarks that actually touches on something that you've mentioned which is, he actually the words paid leave, which I thought was very interesting, because I've not been following his writings that closely to know whether or not he's been talking about that before, but I was pretty excited to hear that.

MR. WESSEL: He seems to be inching a little to the left.

MS. BOUSHEY: Yeah -- No -- Yeah, that's great. But I mean, I think that that actually pivots quite nicely off of the interventions around disability insurance. I mean, right now we are one of the only countries in the world that doesn't have a paid parental leave program, we also don't have a paid leave program for people who need to care for aging family members, or when someone is seriously ill.

We have an unpaid program that only covers about 60 percent of the workforce. And so one thing that we could do that would both increase labor supply, but would also probably affect some of the policies that you were just talking about was to -- would be to make them medical leave paid, and make it available to everyone.

So it wasn't just that 60 percent of people who were currently eligible for the Family Medical Leave Act, and that would be 12 weeks of paid leave. I think that would be really great, and I would love to work with Larry Summers if he wants to work on that with me, that would be great. The second --

MR. WESSEL: Send him an email.

MS. BOUSHEY: Yeah, okay. The second at the other end, I mean, I think, you know, one of the things that I would wonder, actually, Greg, what you would say, or Melissa, is, you know, what about something like equalizing the tax rate on carried interest, that the earnings that hedge fund managers make. You know, that seems to me something that would be -- you know, it seems eminently logical, and maybe that's something that we could all, up here, at least agree it's something we talk about.

MR. MANKIW: I've actually written in favor of Carried Interest Reform. I think it's complicated from -- taxation in partnerships gets complicated, but I think the principle that they should be taxed, the sort of income because it is because it is basically compensation for labor, that I think is the right principle.

MR. WESSEL: Okay, so you really --

MS. KEARNEY: Can I? I'll be quick. One thing, because we've all focused on tax and transfer which is what Okun did. I think we will be wells served if our regulatory system paid more attention to this tradeoff. Right now we have a bunch of agencies imposing a lot of regulations on companies, and it doesn't seem to me that they do so with this equity efficiency tradeoff in mind.

So, I think thinking about occupational licensing which is something Hamilton Project has written about, or small business regulation, I think that could be a place where we could see benefits the most.

MR. WESSEL: Right. We have a lot of people here, if we can take some questions. There is a mic. Tell us who you are, and wait for the Mic. Doug Elmendorf, do you want to start?

MR. ELMENDORF: So, I'm Doug Elmendorf. I have a question about how the growing income inequality, since Okun wrote this book, should affect our view of the leaky bucket. So, Larry, in his remarks said that, well, inequality is a lot greater than it used to be, therefore, he concludes, we should be doing more redistribution, and I think the analogy here is one end of the island is getting pouring rain, and one end is a long drought, so it's more important to move water over.

That seems to me right, if the bucket is no more or less leaky than it was before. And I think whether this particular bucket of tax and transfer policy is more leaky than it was before, depends on why this income inequality has increased.

So if you raise taxes on higher-income people today, because they are yet higher income than they used to be to move the money over, you are potentially, I think, causing a greater loss of output if, I think, their higher wage -- higher earnings income comes because they have higher marginal product, a 1 percent reduction in the labor supply, or a 2 percent reduction in the labor supply, has a bigger economic cost if they really -- if their higher wages come because they are more productive.

So, is it clear that the rising income inequality even beside the political issues, is it clear that that makes the case for more distribution with the leaky bucket, or not?

MR. WOLFERS: Doug, I think you've got it half right. So what matters is whether the rise in income -- if we are going to start taking money from guys who are really, really, high marginal products then the bucket is even leakier, right. The other part of this though is, has all the rise in income gone to folks who are at the point where their sensitivity to incentives is higher, right?

And so, my guess, is a whole bunch of money now is with people who -- money is how you keep score, but the actually marginal utility of the money is not necessarily that high. Whereas, you know, in our (inaudible), or arguably more people in the people in the middle where you would expect labor supply incentives to matter more.

But I think, you know, it's a horse race between the two things that you suggested, and so, you know, the right -- part of the answer is so, if I look at a CEO today, I'm not that worried that if their tax rates rise by 10 percent that they'll stop working, but I should be extra worried if they are extra productive CEOs, and some of them are.

MR. WESSEL: Gentleman here, in the aisle.

SPEAKER: Good afternoon. A question directly -- Yes, pardon me.

The question is to Greg and to Justin, in that it's the role of monetary policy in financial markets in the exacerbation, unfortunately, of those inequality you've referred to. One of the -- and intended consequences of monetary policy, unfortunately, as we are learning, is the shift towards owners of assets.

So, I supposed the question is, how do you resolve that asymmetry which arises from the desire on the part of the monetary authorities to provide the amount of monetary policy, while at the same for exacerbation on the fiscal side?

MR. MANKIW: I'm sure that monetary policy by changing to alter price of various financial assets, has impacts on inequality of income and wealth. There is no doubt that's right. On the other hand, I'm pretty sure I don't think Janet should be spending her time worrying about that, she's got a lot of stuff on her plate to worry about, like inflation and unemployment.

And the main inequality picture, it's really long-run picture, it's a story that's basically been unfolding since the '70s to today, so it's a very long time, and I cannot think over that timeframe the monetary policy impacts are relatively small. And so the first of our impacts are really the technology and education. So that's the first sort of the story.

MR. WESSEL: And so, it is a claim one hears often, of Quantitative Easing, because it increased the price of assets, has raised the inequality. And it's a subject we are going to -- the Hutchins Center is going to take up in an event in June, but let me just make two responses.

First of all, it's a myth that somehow conventional monetary policy has no distribution effects. Obviously if you are a borrower or a creditor, it makes a big different what interest rates are. And secondly, it depends on what your counter-factual is, if you decided that the Fed didn't do QE, and we had 4 percentage points more unemployment, it's not clear to me that we would be better off. So I think picking your counter-factual is really important.

The gentleman there in the aisle, in the blue, and then one in the back.

SPEAKER: My name is Michael. I'm not an economist so maybe I'm a little simplistic, but it seems that the fact that the top 1 percent have gotten all this excess capital and money, you have to ask the question where does it come from, and it seems fundamentally, it comes from the fact that minimum wage is not going up, workers have lost their jobs, unions have been weakened considerably.

So, it's not like that money just came out of the sky, but it came out of not giving workers the gains they deserve for the increased productivity realized over the last 40 or so years. And it's actually, efforts that really drive down their real wages. So that's the reason why I'm concerned about the fact that the people at the top have so much, and the people at the bottom are falling behind.

MR. MANKIW: Right. I think it's a mistake to think of economic growth as zero sums, so the fact that Mark Zuckerberg has a lot of money, isn't the cause of people at the bottom not having money. Similarly, think of it internationally, so Sub-Saharan African is very poor, United States is very rich, do you think the fact that we are rich makes them poor?

I think a lot of people do -- make that argument, right? If Sub-Saharan Africa could do better, it doesn't mean we have to do worse. Okay. So, I think it probably a mistake to think of the economic pie as fixed in size.

MR. WOLFERS: I want to -- I think we are enormously more agnostic about that. Which is, supposed Mark Zuckerberg got richer, in an earlier era Mark Zuckerberg might have been negotiating with unions, which would have meant that Mark would have had to share more of it. So, I think there's strong argument in both directions, and we know very little a profession.

MS. KEARNEY: I think it's true that we know very little, but a generation earlier, he could not have created a platform that a billion people took up creating that value. I mean, we had a boxer this weekend who took home $100 million, which strikes me as ludicrous, but like there was a world of people watching it, who watch him.

I mean, where did that money come from? It's not clear that it was a $100 million that would have been split differently in an earlier generation, but you do make an important point, which is that the erosion of these institutions at the bottom had hurt folks at the bottom.

So, I don't -- you know, I don't want to just -- I don't want the top 1 percent to distract us from thinking about what's going on with the wages at the bottom, even if it's not that their wages are lower because the folks are the top are richer, their wages are lower.

Now, I think this gets back to an earlier point which Greg wrote about, of education. We know that the returns to higher education are as high as they've ever been. And so we can think about transferring resources not in the sense necessarily of wage supports or cash, but by putting a lot more money and energy into expanding access to education, to increasing the rate at which people get the right types of education, invest in training and those types of things.

MS. BOUSHEY: I think that that -- When you asked your question, Mike, I think the picture that came into my mind, is one that I feel like I've seen, if I've seen once I've seen a thousand times, which is when you look over the Post War period, you see that the trajectory of wages and productivity was in alignment from about the end of World War II until about the Okun wrote his book. I'm not blaming him, but then after that -- at any rate -- but at some point after that --

MR. WESSEL: Very generous of you.

MS. BOUSHEY: -- you start to see these two trends diverge in a really -- and it's remarkable because it's not -- it's not just one year, it's not the sort of one off, this is this long-term decades-long trend, and I think your question gets right at the heart of that, which is, like so America has been getting richer and richer, and richer. As a nation we continue to get wealthier, companies in America, the way that we measure productivity, they are getting richer.

But America's workers, on average, haven't. And so you are right, somebody is taking the money. Where is it going? That is the question that we should be asking. But I do think we need to deal with that fact that you have seen as divergence between wages and productivity. As economists, I think that's one of our most profoundly fundamental challenges.

MR. WESSEL: Right here, in the back. And then, Emily, there's one -- there's a gentleman right here, he's raising his hand, back, turn around.

SPEAKER: Just one comment on the sartorial aspects of media training, you might know that the men both chose to wear dark jackets.

MR. WOLFERS: It's a miracle I wore a jacket at all.

MR. WESSEL: Is that the (inaudible) comment of the day? (Laughter)

SPEAKER: I'd like to pick up on Heather's last remark; it's striking the publication date, which really did mark the end of an era of an increase in equality, along with a lot of economic growth in the United States. The first oil shock had just occurred when Art was writing his book, and it's sort of before and after the publication of this book, that the trends diverge greatly.

Picking up on Doug Elmendorf's question, one other thing has changed enormously since then, which may affect the degree to which the buckets leaks at least for the United States, and that is the very substantial increase in the openness of the U.S. economy, and in particular of capital movements around the world. This is the real question, I don't know the answer, but I'd be curious as to what the Panel thinks about the impact that has on our capacity to rein in inequality, particularly at the top, and particularly for capital income.

MR. WESSEL: Globalization, Greg, do you want to take that one?

MR. MANKIW: The two of them is globalization, one is just trade, in trading goods, which probably hasn't been a contributing factor to increased inequality, because we tend to import stuff produced with unskilled abroad, and export stuff produced by skilled labor, and that tends to increase the demand for skilled labor relative to unskilled labor.

Then there's the international flows of capital, which means things are more complicated, it's hard to want to get your mind around. I think what it has meant is that Wall Street is leveraging itself around the world, and there's a lot of big incomes on Wall Street, and I think it's superstar-like phenomenon, we've talked about, probably it doesn't apply to Wall Street, a few people on Wall Street really figure out how to leverage their skills, not just in their local bank, but really in a worldwide financial community.

And so if the Sherwin Rosen story about superstars probably has applied to a few people on Wall Street, then globalization probably has contributed to that.

MS. KEARNEY: There's also the issue of workers from around the world, and this is where I get worried, we can't just think that, gosh, let's raise the minimum wage, and let's get back to really high rates of unionization, and not think that employers in the U.S. will either, you know, move those jobs or import those goods from abroad, or shift to technology. So it's both the global labor market and the rapid pace of technological development, and I think makes it very challenging to figure out how to bolster wages in a way that doesn't have disincentives for employment in the U.S.

MR. MANKIW: Can I just add one, really the important fact we have not said yet, is while inequality has been going up in the United States inequality has been going down around the world. If you take your global citizen, whereas in the United States, but the world, we are much a more equal world than we were 30 years ago, and that's largely because of tremendously rapid growth in China and India, which has brought many, many people out of very, very deep poverty.

So if you want to take a global perspective, there's good news about inequality, and then, too, the typical American voter may not take much solace in that fact, that China and India is doing just fine, but if you have to think of somewhat a more global view it's not -- the picture is not nearly as dire as we are making it sound.

MS. BOUSHEY: But the benefits to trade here in the U.S. have not accrued to -- I mean, when you look at the effect on worker's wages, and you know, one of my -- one of the papers I think that's most interesting -- that's new in this area is of course, David Otter's work with Dawn, and a bunch of other authors, looking at the effect of the increase in Chinese imports after the opening up of trade with China in 2000, and what that did to communities around the country, and that it lowered wages for U.S. workers.

So I mean, thinking about trade issue and who is bearing the cost of this, is an important question for inequality. But I think it also comes back to this question about, you know, as we've seen the gains of productivity not going to U.S. workers, you know, where are they going? Are the -- I mean, maybe they are all going to higher-paid workers in China that U.S. firms are paying, and that's we've seen this gap in wages and productivity in the U.S.

My gut is that that's probably not true, I've not seen a paper to prove that, but I do think, you know, there do seem to be some serious consequences that we should be thinking about.

MR. WOLFERS: Heather, I think what you are missing here, is what we care about is real wages, real wages is how much stuff you can buy, so that's partly a wage, and it's partly the price of stuff. And it turns out trade drives down the price of stuff, and poor people buy stuff, rich people buy services which are not traded, and those prices aren't going down as much. China is one of the greatest gifts to the American working class we've had.

MR. WESSEL: Gentleman, there in the back?

MR DINGES: My name is Casey Dinges, an old family friend of the Okuns, but I've lived in town for 35 years. My question is fairly simple --

MR. WESSEL: That's all right. A longtime friend of the Okuns, but I've lived in town, is that so?

MR. DINGES: And I have, (inaudible) --

MR. WESSEL: I'm trying to defend Washington a little bit.

MR. DINGES: No, I've loved living here. The question is, as we watch Congress kind of dance with letting the Highway Trust Fund go bankrupt at the end of the month. Would not an infrastructure investment policy allow the nation to move forward on both issues?

MR. WESSEL: Well, on behalf of Larry Summers, yes. Anybody wants to disagree?

MS. BOUSHEY: If only we could get both sides to agree to it, yeah.

MS. KEARNEY: No, but I have to advertise now. Next Monday, join us here; the Hamilton Project will be sitting up here talking about investment in infrastructure and ways to move forward. I do think there's broad consensus on your point, how to do that in an efficient way, raises more challenges.

MR. WESSEL: Greg, do you want to stand so the mic can find you?

SPEAKER: My name Greg, I'm with the Wall Street Journal. We know in retrospect that when Okun was writing this is a period at which the economy had exceeded potential unemployment had fallen below its natural rate. We had a really serious inflation problem. It's been a long time since we've had that set of problems, and if you look at the last 30 years, the only time when we really made progress reversing inequality was during the late 1990s, which was a high-pressure economy with very low unemployment.

A long way of saying, if we can get that economy back with the sustained period of very low unemployment, perhaps below its natural rate, maybe all the institutional factors you’ve been discussing here will turn out to be very second or third order, in terms of turning this around. Perhaps, a long way of saying maybe it is all up to Janet Yellen.

MR. WESSEL: I'm sure she appreciates that, Greg. (Laughter) For those who don't know, the high-pressure economy concept, the notion that when the economy us running with very little unemployment, and workers have more -- when employers have less choice, was one that Okun wrote about, and he may even have coined the term, I don't know. So anybody, how much of this is cyclical? How much better off would be on the inequality front if we had (inaudible)?

MR. MANKIW: I don't know, the financial crisis was actually pretty good for inequality, because those people -- I know -- Alan Greenspan sort of made this point a long, long time ago, during the '70s, actually he was Chairman of the Council of Economic Advisors, and he was testifying in front of Congress, and some members said, in the -- this was during the '70s -- mid '70s recession, and so the Congressmen said, you know, Chairman Greenspan, isn't this recession particularly hard on the poor?

And Greenspan said, well, statistically speaking, Congressman, actually it's the stock brokers that are suffering the worst. And of course, that was a very political answer, but we saw the same thing in the recent financial crisis. You know, if are hedge fund manager and it said, prices are falling, it's very, very bad for your incomes, and so if you actually look at the inequality measure, it's more equal during the financial crisis. That's not a good, I'm not saying it's a good thing, but I'm not sure the cyclical --

MR. WESSEL: I was worried there for a while.

MR. MANKIW: No. No. No. No. I wasn't going that way. But I think the story with the -- what's going on in the business cycle and with inequality, I think is a little -- is a little bit more complicated.

MR. WESSEL: Isn't there possibility if we had closer to full employment we'd see more wage increased at the bottom 80 percent?

MR. WOLFERS: So, we've got good evidence on this. There was a Brookings Paper a couple of years ago by Annette Vissing-Jorgensen and Jonathan Parker, so a high-pressure economy tends to lift the bottom end of the distribution exactly the way we thought it would. Interestingly, the thing we hadn’t seen before, but Greg seen, is that it actually also listed very top -- the very top end of town. So Janet is in the process, of helping the work in the middle classes and the super-rich, if she --

MR. WESSEL: I want to close by reading something that just struck me, this the last paragraph of the essay that Okun wrote two years later, and you'll see why I read it. He says, "At the moment --" he's writing this 38 years ago, "At the moment we are experiencing a disturbing divisiveness. Recent efforts to curb the market's transgression on equal political rights have frightened those that hold the bulk of the wealth, and think that they therefore hold the bulk of the truth.

There is a more obvious growth of anti-capitalist sentiments by the non-affluent. Profits and rich are often dirty words in the halls of Congress. The rationing and allocative functions of the price system are blindly ignored by many of our legislators. Instead of blending the values of capitalism and democracy many are putting them against each other. Instead of compromising, we are polarizing. The nation sorely needs a serious dialogue and a major educational undertaking to develop the enlightened attitudes of compromise."

I can't think of a better way to end this than to read that old passage. And join me in thanking our Panelists for helping us develop the enlightened attitude to think on. (Applause)

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