1 INTRODUCTION: THE CHALLENGE OF INEQUALITY

> *A bedrock American principle is the idea that all individuals should have the opportunity to succeed on the basis of their own effort, skill, and ingenuity.*
>
> —Federal Reserve Chairman Ben Bernanke

INCOME INEQUALITY HAS INCREASED dramatically in the United States since the late 1970s. The great economic and financial crisis that hit in 2008 and the persistent high unemployment that has come with it have drawn greater attention to the trend toward marked concentration of income at the top, little or no progress for the middle, and precariousness at the bottom of the income distribution. The problem is now squarely at the center of the political debate. Even among those who view inequality neutrally—or even positively—as the way in which markets reward performance, most agree that some of the features that accompany it, such as reduced opportunity and low social mobility, increased prevalence of poverty, and the stagnation of median household income, are undesirable. Those who traditionally are more concerned about high inequality worry that increased concentration of income is also leading to the concentration of political power, which impedes efforts to mitigate inequality and even may promote policies that exacerbate it. Meanwhile, a number of economists have argued recently that the extreme concentration of income at the top may undermine macroeconomic and financial stability by making it harder to sustainably maintain strong aggregate demand or by encouraging excessive borrowing.

Our objective in this review of the challenge of inequality is to assemble in one place a readable overview of the basic facts and the issues that is accessible to both policymakers and a wider public. Our focus is squarely on the United States, but we draw on international experience and comparisons to shed light on the trends and help sketch out some possible remedies. It is also clear to us that it is impossible to separate the purely economic or technological drivers of inequality from the political processes that shape the policies influencing the distribution of income. We hope to present a comprehensive picture, tying the various dimensions of the topic together but without going into technical detail. An informed discussion of policy needs an empirical summary of the facts and of the various available interpretations. That is what we aim to provide.

Whichever of many possible measures one looks at, inequality in the United States has increased very substantially. Certainly this increased inequality seems to be part of a global trend, yet among economically advanced countries the United States is an outlier. Although it is difficult to attribute the rise in inequality to any one specific cause, it is apparent that technological change, international trade, changes in labor-market participation, the increasing role of the financial sector in the economy, the increased size of markets, and a decrease in the degree of progressivity of taxes all play some role and that several of these factors have been especially pronounced in the United States. In addition, the political environment, the loss of power of organized labor, and apparent changes in social norms affecting compensation at the top also seem to contribute to increased inequality. Though detailed policy recommendations lie beyond the scope of this book, we suggest a number of general policy orientations that could help mitigate some of the more damaging consequences of high and rising inequality, approaches that are compatible with promoting an efficient and competitive economy.