Pulling Apart:

The Strong Wisconsin Economy Masks Growing Inequality

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Center on Wisconsin Strategy
University of Wisconsin-Madison
1180 Observatory Drive
Madison, WI 53706-1393

TEL 608-263-3889
FAX 608-262-9046
http://www.cows.org/

Wisconsin Budget Project
Wisconsin Council on Children & Families
16 N. Carroll Street, Ste. 600
Madison, WI 53703

TEL 608-284-0580
FAX 608-284-0583
http://www.wccf.org/

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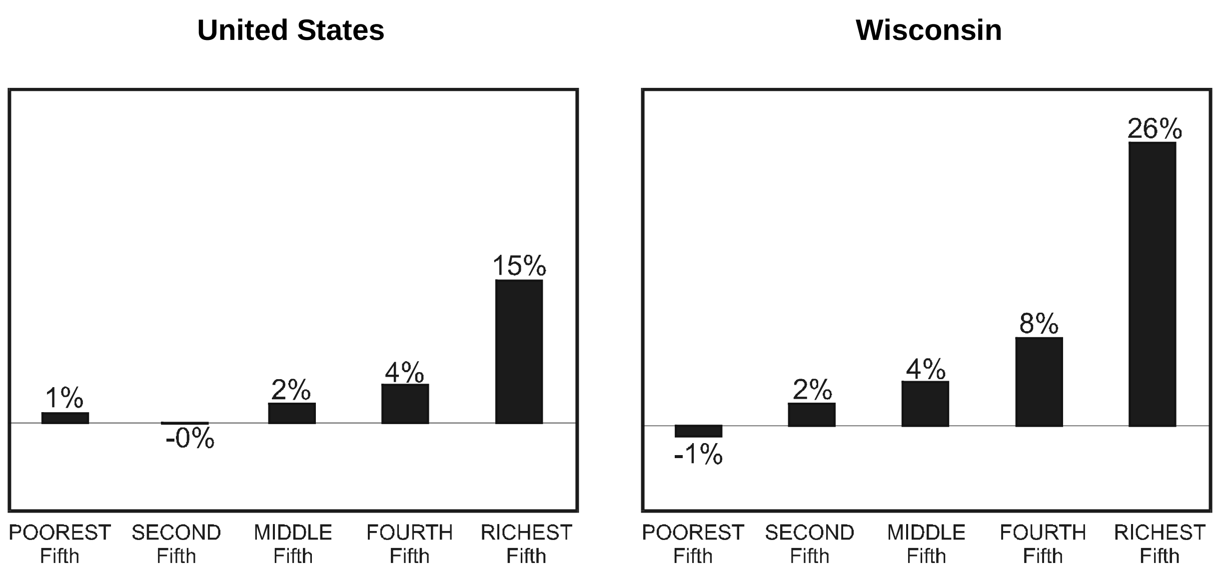
Despite Wisconsin's strong economic growth and tight labor markets, income disparity is substantially greater today than it was two decades ago. According to a recent analysis by the Economic Policy Institute and the Center on Budget and Policy Priorities, from the late 1970s to the late 1990s, the average real income of the lowest-income families in the state *fell* by 3 percent while the average real income of the highest-income families in the state grew by 30 percent.

Wisconsin's recent surge in inequality is particularly noteworthy. From the late 1980s to the late 1990s, inequality grew rapidly in the state, in spite of Wisconsin's strong economic performance. The income of Wisconsin's poorest families fell slightly while the income of the state's highest income families grew 26 percent (Figure 1). Nationally, over the same period, income at the bottom of the income distribution rose slightly while the richest fifth of families gained 15 percent. As Figure 1 makes clear, Wisconsin's recent growth in inequality far outstrips the national trend.

Wisconsin has traditionally prided itself on its relatively high level of equality, and it still can. Even with this growth in inequality, only seven states have a more equal distribution of income. However, our position relative to other states will continue to decline as long as inequality in the state continues to grow more rapidly than in the rest of the nation.

Figure 1

Booming Economy, Rising Inequality
Income Change by Fifth of the Income Distribution, Late 1980s to Late 1990s



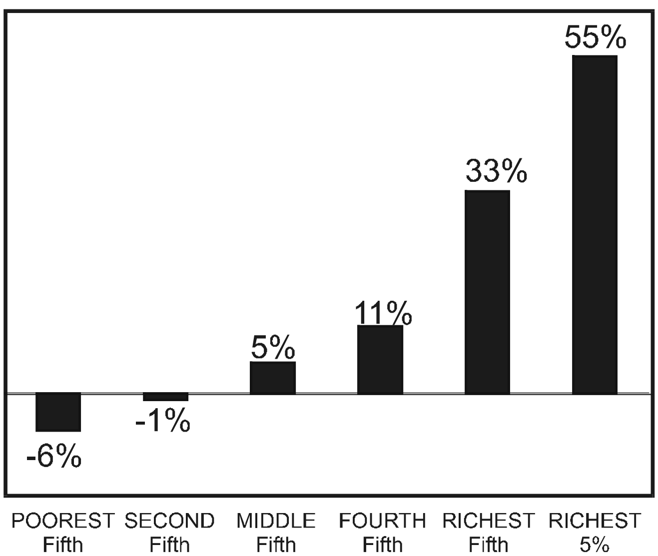
Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2000.

Pulling Apart: A State by State Analysis of Income Trends, issued January 18, 2000, by the Economic Policy Institute and the Center on Budget and Policy Priorities analyzes trends in income and inequality within each state over the last two decades.[1] Using Current Population Survey data from U.S. Census Bureau, they track earnings changes for households in each income "quintile" (20 percent) of the state's population. Here we focus on their results for Wisconsin: What's going on? What does it mean? And, what, as a state, can we do about it?

Increasing Inequality from the Late 1970s

Trends in average real (inflation adjusted) income for each fifth of the income distribution provide a good yardstick for measuring inequality. The national story of increasing inequality is well documented: from the late 1970s to the late 1990s, the average real income of the poorest fifth of families fell $900, or 6 percent.[2] (Throughout the report, all income values are inflation adjusted and expressed in 1997 dollars.) Over that same period, the richest fifth of families experienced a 33 percent income increase ($34,370 annually). Closer to the top of the income distribution, the story is even more extreme; income rose by 55 percent for the richest five percent of families (Figure 2).

Figure 2
Income Change for U.S. Families
Late 1970s to Late 1990s, by Fifth of Families
(Percent Change)



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2000.

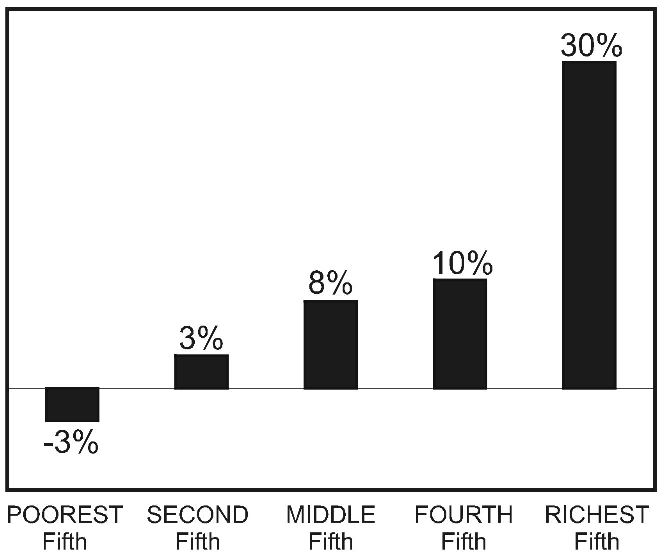
[1] Copies of the EPI/CBPP report may be obtained from COWS or the Wisconsin Budget Project, or from EPI Communication Director, Nan Gibson at 202-331-5546.

[2] All figures in the report are before-tax income for families from the Census Bureau's March Current Population Survey. Data are "pooled" across three most recent years available (1996, 1997, 1998, called "late 1990s" in the report) to allow for sufficient sample size. To compare to the past, three years of data from the late 1970s (1978, 1979, and 1980) and the late 1980s (1988, 1989, 1990) were pooled. The late 1970s, 1980s, and 1990s all represent peaks in the economic cycle and so provide for good comparison.

Wisconsin mirrors these national trends (Figure 3 and Table 1). In Wisconsin, from the late 1970s to the late 1990s, average real income of Wisconsin families in the bottom fifth of earnings fell 2.6 percent (or $439) to $16,690. At the same time, families in the top income quintile saw their average income rise over 30 percent ($31,678), to $136,404. At the middle of the income distribution, the median family fared better than the bottom, but not as well as the top. For the middle fifth of families, real income grew 7.7 percent (up $3,681) to $51,647. So, while middle income families moved slowly uphill, with an annual increase of income of just $200, the state's richest families sprinted forward, each year pulling in nearly $1,500 more than the year before.

Figure 3

Income Change for Wisconsin Families
Late 1970s to Late 1990s, by Fifth of Families
(Percent Change)



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2000.

Table 1

Wisconsin Family Income Trends
Average Family Income of the Richest, Middle and Poorest Fifths of the Income Distribution, late 1970s to late 1990s

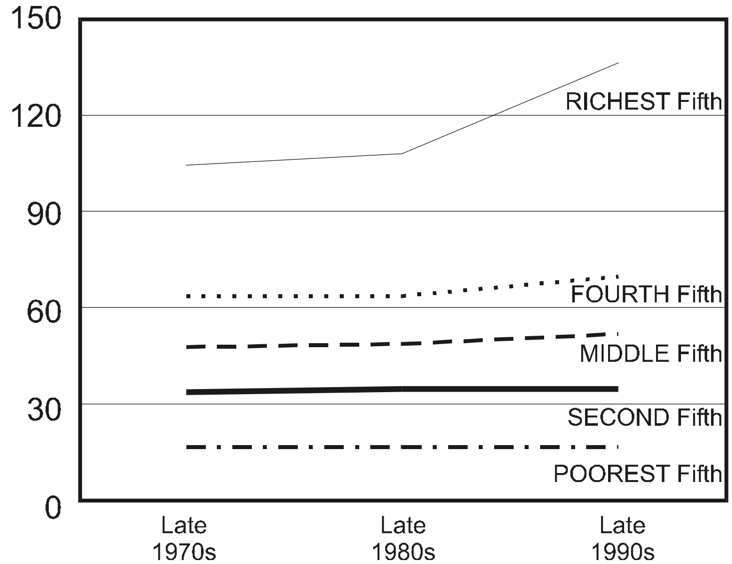
	Late 1970s	Late 1980s	Late 1990s	Percent Change, 1970s-90s	Percent Change, 1980s-90s
Richest Fifth	104,726	108,143	136,404	30	26
Middle Fifth	47,966	49,448	51,647	8	4
Poorest Fifth	17,129	16,861	16,690	-3	-1

Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2000.

Figure 4

Average Wisconsin Family Income by Income Quintile, Late 1970s to Late 1990s

(Dollars in Thousands)



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2000.

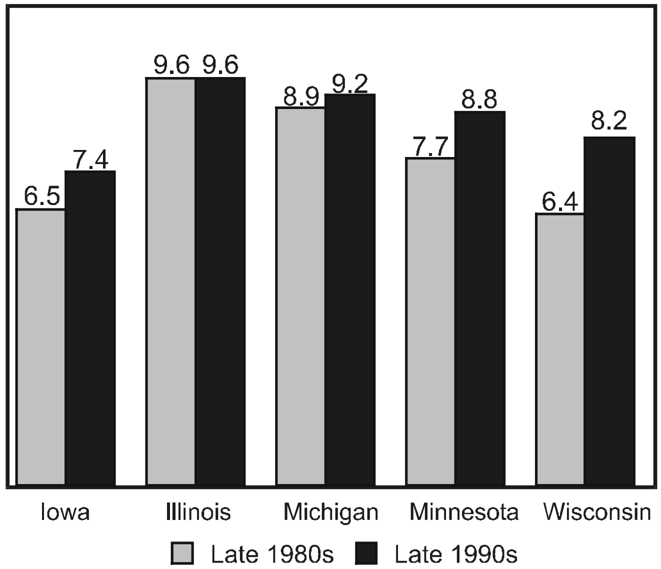
While the Wisconsin trend mirrors the national trend, there is an important difference in timing. Over the last two decades, dramatic increases in inequality were concentrated in the 1980s. In Wisconsin, however, income inequality grew slowly in the 1980s; it is the 1990s when inequality surged. This is especially evident in the trends in income for the top fifth of the income distribution (Figure 4). From the late 1970s to the late 1980s, income for this group increased moderately, up $3417. Over the 1990s, however, the average income of the richest fifth of Wisconsin families grew by $28,261. That surge in income was unmatched in the rest of the economy, and median families and the poorest families have been left behind.

Stagnation of income for the poorest families and only moderate increases for median families stand in marked contrast to the dramatic gains that high income families in the state have secured over the last decade. In the past, rising tides have lifted all boats, but it is clear that the economy has changed; Wisconsin's growth has really paid off only for the top 20 percent of the income distribution.

Wisconsin's Income Inequality Catching Up to Neighboring States

Wisconsin has traditionally had among the lowest levels of income inequality of all the states. Even after posting such increases in the 1990s, only seven states have more equal income distribution. That is good news. Low inequality is highly correlated with low levels of poverty and high levels of all resources available to meet basic family needs, according to an October 1999 Urban Institute study ("Sources of Support and Income Inequality among America's Children," by Gregory Acs and Megan Gallagher,

Figure 5
Ratio of Incomes of Richest to Poorest Income Fifths, Late 1980s and Late 1990s Midwestern States



report No 99-15). Wisconsin's widening income gap does not bode well, especially for communities with high concentrations of low-income families, such as Milwaukee County, where the number of children living in poverty has approached one third of all children during the 1990s.

While Wisconsin has been a national leader in terms of income equality, the recent trends have narrowed the difference between Wisconsin and its neighboring states. Figure 5 shows the ratio of the income of the richest fifth of families to the poorest fifth of families. In the late 1970s, Wisconsin and Iowa posted the most equal income distribution, with the income of the richest fifth of families at just over six times as much as the income of the poorest fifth of families. At that time, Illinois posted the most unequal income distribution; their richest families brought in more than 9 times the income of the poorest families in the state. Over the last decade, however, the growth in Wisconsin's ratio outpaced every state in the region. Inequality in Wisconsin grew twice as fast as it did in Minnesota, the neighboring state posting the second fastest growth in inequality.

Inequality of Wealth is Even More Extreme

To focus on income disparity alone, however, provides only part of the picture. Differences in *wealth*, that is, disparities in ownership of stocks and bonds, real estate and other assets, between the upper and lower echelons of American society are even more pronounced and growing more rapidly than the disparities in income discussed above.

Researchers have long known that a small percentage of Americans own the bulk of assets. In 1995, for example, one percent of households owned 39 percent of the nation's wealth (and had 13 percent of the nation's after-tax income). Eighty-four percent of all wealth is owned by the 20 percent of wealthiest households. By contrast, the remaining 80 percent of households hold only 16 percent of all assets. This disparity in wealth is the greatest at any time since the Great Depression, and the booming stock market has likely increased it. (See "The Widening Income Gap," by Isaac Shapiro and Robert Greenstein, published by the Center on Budget and Policy Priorities, September 4, 1999, p. 10.)

In addition, capital gains income and other income received by high-income taxpayers, have had extraordinary increases over the past few years as the stock market has soared. Most capital gains income is realized by high-income taxpayers; nearly three-quarters of all capital gains are realized by taxpayers with income exceeding $100,000. One-quarter of all capital gains income is realized by taxpayers with incomes exceeding $1 million. ("Information and Misinformation about Federal Tax Burdens," by Iris J. Lav, published by the Center on Budget and Policy Priorities, January 21, 1999.)

Finally, wealth disparity is especially pronounced by race. Available data do not allow for investigation of disparity of income or wealth by race for the state, but the state trends no doubt echo the national picture. In 1995, the average wealth in black households was only 17 percent of the average wealth of white households ($43,000 compared to $255,300). Additionally, fully 31 percent of black families have zero or negative net wealth while only 15 percent of white families do (*The State of Working America, 1998-99*, Mishel, Bernstein, and Schmidtt).

Causes of the Growing Income Inequality

Nationally, the single most important cause of increasing income inequality is the growth in wage inequality. Wage inequality between races and people of different educational levels is growing. Wages in Wisconsin are also becoming more unequal, both within and between groups. *The State of Working Wisconsin, 1998*, shows, for example, that wages of college graduates are 76 percent higher than those of high school graduates; in 1979, the wage advantage for college graduates was just 45 percent. Though data for income inequality by race are not available, we do know that wage inequality by race has surged in the state; black men's wages fell 33 percent over the last two decades and black women's wages fell 27 percent. These trends leave the state's black workers far behind their white counterparts.

Increasing wage inequality within and between groups has been substantial and there is no single source to credit for the change. But, as the EPI/CBPP report points out:

> A variety of factors explain the growth of wage inequality including globalization, the shrinkage of manufacturing jobs and expansion of low wage service jobs, immigration, and the weakening of labor market institutions — the lower real value of the minimum wage and fewer and weaker unions.

These trends have been as clearly documented for Wisconsin as they have for the nation (see *The State of Working Wisconsin, 1998*, Center on Wisconsin Strategy). While immigration has had less influence in the state, the expansion of low wage service jobs and the decline in union density in the state — Wisconsin union membership fell from 33 percent of the labor force in the early 1970s to just 19 percent today — have certainly contributed to increases in wage inequality.

Income disparity also results from the growing importance of income derived from capital, such as rental income, interest, dividends and capital gains. From the late 1970s to the late 1990s, the share of total income nationally that is derived from capital grew from 16 percent to 20 percent of total personal income. Total labor income fell from 74 percent to 71 percent during that same period. As indicated above, a small — and well-off — portion of the population holds assets; increasing returns to those assets pushes income inequality up.

The rising number of single parent families also contributes to increasing income inequality in the nation and the state. From 1979 to 1996 the portion of adults and children living in married-couple households fell from 74 percent to 65 percent of the US population. An October 1999 study published by the Urban Institute found that the median income in Wisconsin for one-parent families with children was just $21,300 in 1997, compared to $51,982 for two-parent families with children. Obviously, as the share of families with single-earners increases, income inequality increases as well.

Wisconsin Can Choose a Different Course

Wisconsin's economy has consistently been one of the most equal in the nation, and this has been an appropriate source of pride for state residents. The fact that income inequality is increasing more rapidly here than in much of the nation should be a cause of concern. To be sure, Wisconsin remains among the most equal states in the nation, but it is unlikely to retain that status in the face of the trends of the last decade.

There is no "magic bullet" to rectify the situation, any more than there was a single cause. But some of the state policy options are clear enough.

Raise and Index the Minimum Wage

Increasing the earnings for workers at the bottom of the labor market is one way to increase equality of income. Adjusting for inflation, the current federal minimum wage, $5.15 per hour, remains below its value any year between 1961 and 1984 and about 18 percent below its value anytime during the 1970s. In response to lack of federal increase in the minimum wage, 10 states have set state minimum wages that exceed the national minimum.

Such a policy could have a direct and positive effect on the earnings of many working adults in Wisconsin. Each 25 cent increase in the minimum wage boosts the income of a full time, year round worker by more than $500. And contrary to the popular image, most workers earning the minimum wage are making direct contributions to family income. More than 70 percent of minimum wage earners are adults (not teenagers). Nearly half (46 percent) of minimum wage earners work full time and another third work more than twenty hours a week.

More than 163,000 workers in Wisconsin benefited from the last federal increase in the minimum wage. A state increase in the minimum could help those workers who are struggling at the bottom of the labor market to move closer to self-sufficiency.

Make Work Pay and Support Working Families

State governments can help lessen the burden of income inequality by carefully structuring benefits to lower-income families to ensure that work pays. Wisconsin has historically been relatively generous in the benefits that it provides and has been a leader in developing policies to make work pay. For example, Wisconsin was one of the first states to establish a refundable earned income tax credit for working parents. Yet the structure of taxes and benefits in Wisconsin makes it difficult for low-income families to work their way out of poverty.

A study by the Public Policy Forum (*How Taxes and Benefits Discourage People from Working*, July 26, 1999) examined the impact of state benefit and tax policies on low-income families in Wisconsin and seven other states. The report concluded:

> As poor families (in Wisconsin) earn more, they experience a flat growth in disposable income which leaves them hovering near the poverty line even as gross income rises into the mid-$30,000 range.

One way to make work pay is to increase and modify the earned income tax credit (EITC). President Clinton's recent proposal would address the problem identified in the Public Policy Forum's report, by:

- increasing the maximum federal EITC by $500 for working families with three or more children;
- expanding the credit for married, two-earner couples; and
- making the credit phase out more slowly (as income increases) for families with two or more children.

If these changes were made to the federal EITC, they would also indirectly boost Wisconsin's earned income credit (unless the legislature severs the link between the state and federal credits).

In conjunction with changes in the EITC, the state should look closely at means of modifying eligibility levels and co-payments for child care and health care benefits. Although improvements were made in the last budget, additional changes are necessary so families do not face major barriers to working their way out of poverty.

Continue to Modernize the Unemployment Insurance System

Recently, Wisconsin's Unemployment Insurance Advisory Council recommended changes to accommodate Wisconsin's changing workforce, which were enacted as 1999 Wisconsin Act 15, and took effect on January 1, 2000. Unemployment insurance was designed to serve employees with long-term attachment to an employer. Low-wage workers, whose jobs are more commonly intermittent, seasonal, and part-time, are less likely to qualify for benefits. To make more of these workers eligible for benefits, the new law:

- institutes an "alternate base period" that makes it easier, especially for workers new to the labor force, to qualify for benefits;
- eases eligibility of workers who must quit jobs because they are transferred to a shift during which they can't find child care; and
- extends eligibility to domestic abuse victims who have good reason to fear that their abusers will violate restraining orders.

These measures are a good start to ensuring that the state's unemployment insurance system better covers low wage and women workers. Further improvements that should be considered include:

- expanding eligibility to individuals available for only part-time work or work on specific shifts;
- extending benefits during periods of high unemployment; and
- providing dependent allowances (as 12 states already do) that acknowledge the special needs of parents with children.

Reform Regressive Taxes

Perversely, state and local taxes in Wisconsin *increase* income inequality rather than reduce it. Analysis of the burden of the combined package of Wisconsin taxes — property, sales and excise, and income — shows Wisconsin's tax structure to be almost perfectly regressive *(Who Pays? A Distributional Analysis of the Tax Systems in All 50 States*. Institute on Taxation and Economic Policy, 1996). The higher your income, the lower the portion of income paid for taxes. The poorest fifth of the income distribution pays nearly 14 percent of their income in state and local taxes while the richest fifth pays between 10 and 7 percent of their income in state and local taxes. This takes the state's EITC into account. The problem is that, even though the state's income tax structure is progressive (with lower incomes paying a lower portion of their income in tax), the state's sales and property taxes are quite regressive.

Recent income tax changes in the biennial budget bill help improve the progressivity of that part of the state tax system. Expansion of the Homestead Tax Credit is also a very positive development. However, further tax reforms (such as indexing the Homestead Credit) should be considered to decrease burdens on the poorest of Wisconsin's families, and the entire package of taxes needs to be examined.

Conclusion

Wisconsin long avoided the levels and increases in inequality that the rest of the nation exhibited. The data in this report make it clear that the gap between the rich and the poor has grown more rapidly in Wisconsin than in the nation as a whole. Economic growth and prosperity are not being equally shared; in fact, rewards of prosperity in the

1990s are heavily concentrated on the richest 20 percent of families. As a state, this should be of substantial concern, not only because of the stagnation in incomes for the remaining eighty percent of families, but also because increasing disparity comes with substantial social costs.