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The Economics and Politics of the Fall and Rise of Income Inequality in the United States in **The Political Economy of Inequality: U.S. and Global Dimensions**

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The Political Economy of Inequality

U.S. and Global Dimensions

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The Economics and Politics of the Fall and Rise of Income Inequality in the United States

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Income inequality in the United States has increased dramatically since the 1970s. However, the U.S. economy also experienced an equally dramatic *equalization* in the 1930s and 1940s. Consequently, if we are to develop a complete understanding of the evolution of the U.S. income distribution, we must analyze the earlier "Great Compression" or "Great Convergence," as well as the more recent "Great Divergence."

I begin with a review of the facts of the changes in income inequality over the past century in the United States. I will then discuss and evaluate the economic explanations for those trends. However, the *economic* trends cannot be understood fully without reference to *political* factors. I argue that both the Great Compression and the Great Divergence are primarily the result of deliberate political choices. Furthermore, I argue that race is the most important of the many factors leading to the political shifts that have, in turn, contributed to the Great Divergence of the past 40 years: Many whites, especially in the South, reacted to the Civil Rights movement by switching their allegiance to the Republican Party, and this has contributed substantially to the adoption of more antiegalitarian economic policies.

TRENDS IN INCOME INEQUALITY IN THE UNITED STATES

The best starting point for a discussion of long-term trends in U.S. income inequality is the paper by Piketty and Saez (2003). Their original paper contains data through 1998, but they have updated the data annually, so that we now have a complete series covering a full century, from 1913 to 2017.[1] Piketty and Saez use tax-return data, which allow them to produce extremely detailed estimates for the income shares of the very top income strata.

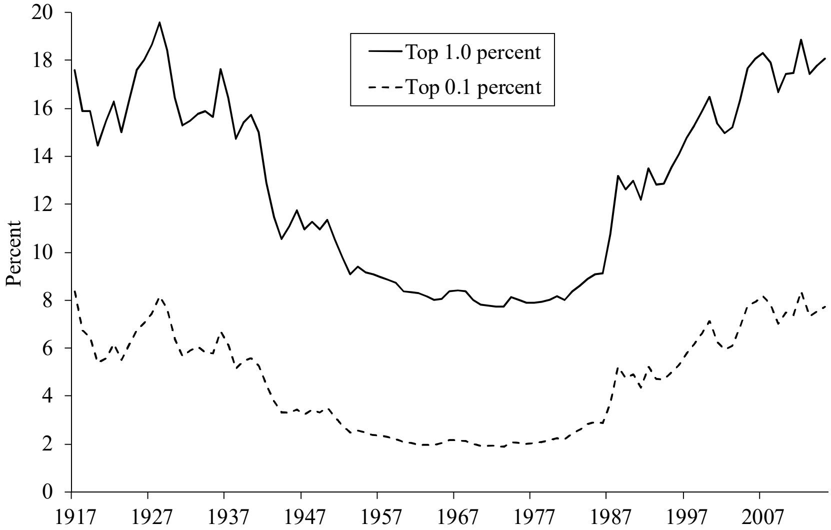
Some of the trends in income shares derived by Piketty and Saez are shown in Figure 3.1.

The data depicted in Figure 3.1 reveal that the shares of the top groups fell from the late 1920s to the early 1970s, and especially sharply in the early 1940s. The share of the top 1 percent plummeted from 15.7 percent of total income in 1940 to 10.5 percent in 1944. Top income shares surged upward in the 1980s, almost as dramatically as they had fallen in the early 1940s. In the most recent 10 years, the share of the top 1 percent has been around 18 percent of total income, which is higher than the average in the first 15 years, as shown in Figure 3.1. Thus, by some measures, the income distribution in the United States today is more unequal than it was a century ago.

The disequalization since the 1970s has been extremely top-heavy. A majority of the gains in share for the top 5 percent went to the top 1 percent, a majority of the gains in share for the top 1 percent accrued to the top one-tenth of 1 percent, and about half of the gains in share for the top one-tenth of 1 percent accrued to the top one-hundredth of 1 percent.

Piketty and Saez (2003) focus exclusively on the top 10 percent, but there have also been changes in the income distribution below the top 10 percent. Census data from Semega, Fontenot, and Kollar (2017) show that, since the 1970s, the income of the typical household at the 90th percentile rose by substantially more than the income of the household at the 80th percentile, which rose faster than the income of the household at the 60th percentile, which rose faster than the income of the median household. However, the incomes of the households at the 40th and 20th percentiles grew only slightly more slowly than the income of the median household. Thus, during the Great Divergence, those at the very, very top of the income distribution pulled away from those merely at the very top, those at the very top pulled away from those at the top, and those at the top pulled away from those in the middle. On the other hand, those in the middle of the income distribution have gained only slightly when compared with those at the bottom.

Figure 3.1 Percentage of Income in the United States Received by the Highest-Income Households, 1917–2015



SOURCE: Piketty and Saez (2003), with data updated to 2017 from http://eml.berkeley.edu/~saez/.

ECONOMIC EXPLANATIONS FOR THE GREAT CONVERGENCE OF THE EARLY AND MIDDLE TWENTIETH CENTURY

Each explanation described here is a phenomenon that could *potentially* push the overall degree of income inequality in a particular direction, but each could possibly be offset by any of several other factors. The story told here is definitely *not* one of historical determinism or inevitability.

Increased educational attainment. An increase in education will increase the supply of more highly skilled workers. All else being equal, this will tend to reduce wage differentials.

Educational attainment in the United States increased with stunning speed for the first three-quarters of the twentieth century, and the evidence suggests that this contributed substantially to the Great Compression. The high school graduation rate increased from about 9 percent in 1910 to about 70 percent in 1960. The rapid rise in attainment of a high school diploma was the result of a nationwide movement at the grassroots level. Compulsory attendance laws helped, but Goldin (1999) argues that an even more important source of change was the adoption of "free tuition laws," under which school districts were compelled to provide funds for secondary schools. As a result, by the 1930s and 1940s, the number of Americans who had acquired enough skills to compete for jobs above the rank of laborer had skyrocketed. The GI Bill of 1944 then provided the impetus for a surge in the college-educated population.

Wage-setting institutions. The National Labor Relations Act of 1935 made it much easier for labor unions to organize successfully. In 1935, about 13 percent of U.S. workers were members of a labor union. By 1945, the rate of union membership had risen to about 35 percent. The rapid rise in union membership contributed to the Great Compression, as labor unions helped boost the incomes of Americans in the lower and middle strata of the income distribution. The Fair Labor Standards Act of 1938 established, among other things, a federal minimum wage of 25 cents per hour. The minimum wage also contributed somewhat to the Great Compression.

Goldin and Margo (1992) document the crucial role played by the National War Labor Board during the Second World War. As part of the effort to control the inflationary pressures stemming from the war, the Board was given the power to approve or deny requests for wage increases. The Board was much more likely to approve wage increases for low-wage workers, and this contributed substantially to the Great Compression.

Social norms. Even after the wartime wage controls were dismantled, the income distribution remained much more equal than it had been a decade before. This was partly due to the continuing trends of rising educational attainment, stronger unions, and substantial increases in the minimum wage, as well as to other factors that we will discuss below. But it was probably also due, at least in part, to a change in social norms. It appears that the reduced wage differentials came to be widely accepted as fair, and that they remained widely accepted for a generation.

Regulation of financial services. The first century and a half of U.S. history is littered with financial crises. The largest financial crisis of all contributed to the Great Depression in the 1930s, and this led the 73rd Congress to establish a strong regulatory regime for the financial services sector. These regulations led to the only time in history that the United States went for a half-century without a financial crisis, and the regulations also reduced the incomes of financiers. Since those who work at Wall Street firms and big banks are very prominent in the extreme top of the income distribution, the reduction in their incomes was an important force for equalization.

Progressive taxation. Until the twentieth century, the revenue system of the United States relied primarily on customs duties and excise taxes, which tend to be regressive. However, during the Progressive Era, concern about the unequal distribution of income and wealth led to political pressure for enactment of more progressive revenue sources. In 1913, with the Sixteenth Amendment to the Constitution, the United States established a progressive income tax. The marginal tax rate faced by the highest-income Americans was increased dramatically during the Democratic administration of Franklin Roosevelt, reaching 94 percent in 1944, and it stayed at 91 percent throughout the Republican administration of Dwight Eisenhower.

Corporate-source income is disproportionately received by those with high incomes. Thus, the corporation income tax, established in 1909, also increased the progressivity of the tax system. During the Second World War, the top marginal rate in the corporation tax reached 53 percent, and the top rate stayed above 50 percent for two decades after the war. The third key element of the trend toward more progressive taxation was the estate tax—levied, as the name implies, on the estates of wealthy decedents, and established in 1916. The top marginal rate in the estate tax reached 77 percent in 1941, and it stayed there until 1976.

Restricted immigration. From 1890 to 1910, the rates of immigration into the United States reached all-time highs. The flood of immigrants in the early twentieth century put downward pressure on the wages of low-skilled native-born workers in the United States. In reaction against this, Congress passed laws in the 1920s that severely restricted immigration.

The reduced supply of immigrants led to an increase in wage rates for low-skilled workers through the ordinary interaction of supply and demand. Equally important, many of the immigrants who arrived in the late nineteenth and early twentieth centuries eventually became citizens and were able to vote. This, combined with the decrease in the number of new arrivals, greatly reduced the size of the low-wage population that had no political voice.

ECONOMIC EXPLANATIONS OF THE GREAT DIVERGENCE

I will consider the various explanations for the Great Divergence in what I consider to be their order of importance. However, I readily acknowledge that any judgment about the relative importance of these factors must necessarily be somewhat subjective.

Changes in technology. If technological changes increase the demand for highly skilled workers and decrease the demand for less-skilled workers, the technological changes will tend to increase wage differentials.

In the final third of the twentieth century, the growth rate of highly skilled labor slowed as the high school graduation rate leveled off and the rate of increase of college completion slowed. At the same time, it appears that the demand for highly skilled workers rose rapidly. Many jobs that involved simple, repetitive tasks were replaced by automated processes.

Predictably, this led to a widening earnings gap between college graduates and those with only a high school diploma. Not only that, but, as documented by Lemieux (2006), the earnings gap between those with education beyond a bachelor's degree and those with only a bachelor's degree has also widened.

Unions lose strength. As mentioned earlier, union membership soared in the decade following enactment of the National Labor Relations Act in 1935. Figure 3.2 shows that increase, as well as the subsequent erosion of the relative strength of unions, which has now continued fairly steadily for 60 years. As unions weakened, they lost some of their ability to secure more favorable wages and benefits. Blackburn, Bloom, and Freeman (1990) estimate that deunionization can explain 20 percent of the increase in wage inequality for U.S. men. Also, unions have long been a bastion of support for the Democratic Party, which has been more egalitarian (or at least less antiegalitarian) than the Republican Party during the period studied here.

Deregulation of financial services. We have seen that regulation of the financial-services sector was greatly strengthened in the 1930s. Not surprisingly, however, Wall Street fought back. Beginning in the 1970s, the financial regulations were slowly but steadily stripped away. As a

Figure 3.2 Union Members as Percentage of U.S. Workers, 1930–2018

SOURCE: For years 1930–1978: BLS (1980). For years 1979–2018: Unionstats.com, a union membership and coverage database from the Current Population Survey, constructed by Barry Hirsch and David Macpherson.

result, the incomes of financiers skyrocketed, and in the late 2000s, the financial system experienced its worst crisis since 1933.

Philippon and Reshef (2012) show that the increased regulation of the 1930s led to a society in which the earnings of financial workers were only slightly higher than the earnings of comparably skilled workers in other sectors. When the regulations were removed, it once again became possible for financial-service workers to earn a very substantial premium over comparable workers in the rest of the economy. Philippon and Reshef estimate that finance accounts for 15–25 percent of the overall increase in income inequality since 1980.

Changes in family structure. Increases in the prevalence of single-parent families are likely to exacerbate inequality. In 1950, 7.4 percent of families with children were headed by a single parent. By 2016, that fraction had grown to 31.6 percent. Haskins and Sawhill (2016) estimate that these changes in family structure are responsible for at least 15 percent of the increase in inequality, and possibly much more.

A substantial part of the change in family structure is probably due to changing attitudes toward marriage and divorce. However, mass incarceration has undoubtedly had an effect on family structure as well. The rate of incarceration in state and federal prisons was more than *five times* as high in the mid-2000s as it had been in 1972. Mass incarceration surely contributed to the breakdown of families, which, as we have seen, was a major force contributing to the Great Divergence. In addition to this indirect effect, mass incarceration has probably also played a direct role in the Great Divergence, since convicts often suffer permanent damage to their earnings prospects, even after they are released from prison. Finally, mass incarceration disenfranchises a part of the population that is disproportionately poor.

At the same time that the breakdown of the family was increasing income inequality by increasing the number of single-parent families, another change in family structure was increasing income inequality by increasing the incomes of many relatively more affluent families. Assortative mating is the practice whereby men and women with similar levels of education are more likely to form families than are men and women with different levels of education. The evidence suggests that assortative mating has increased in the past few decades. When we combine increased assortative mating with increased female labor-force participation, we have yet another factor that contributes to the Great Divergence. Greenwood et al. (2014) find that assortative mating made essentially no difference in 1960, but that it contributed very substantially to inequality in 2005.

Less progressive taxation. We have seen that U.S. tax rates on those with high incomes and large amounts of wealth were quite high in the middle of the twentieth century. However, the top marginal tax rate in the federal individual income tax was reduced to 70 percent in 1964 and to 50 percent in 1981. In 2017, President Donald Trump signed a reduction in the top rate to 37 percent, once again providing large benefits to the most affluent households.

The time pattern of top marginal tax rates in the federal individual income tax, shown in Figure 3.3, is roughly inverse-U-shaped. The pattern of top marginal tax rates is somewhat similar to the pattern of unionization, shown in Figure 3.2. The pattern for each of these is roughly the reverse of the U-shaped pattern for top income shares, shown in Figure

Figure 3.3 Highest Marginal Tax Rate in the U.S. Federal Individual Income Tax, 1913–2019

SOURCE: Tax Policy Center.

3.1. These data suggest that a wide variety of political and economic phenomena went in one direction in the early and middle decades of the twentieth century and then reversed course in the 1970s and 1980s.

The corporate tax rate stayed at 52 percent from 1952 to 1963. In 2017, it was reduced to 21 percent for domestic-source corporate income, and to zero for foreign-source corporate income. In 1945, the corporate tax raised 35 percent of the total revenues of the federal government. This proportion shrank to 22 percent in 1965 and to 10.6 percent in 2015.

The estate tax is a relatively small part of the revenue system, but it is strongly progressive, since it applies only to *very* wealthy decedents. The top rate in the federal estate tax was decreased to 70 percent in 1977 and to 50 percent in 1982. The top rate in the estate tax is now 40 percent, and the fraction of estates that is subject to tax has been reduced dramatically.

Finally, in addition to cutting the top marginal tax rate generally, the tax cuts signed into law by George W. Bush in 2001 and 2003 reduced the tax rates on dividends and capital gains. Each of these types of income is disproportionately received by high-income households.

International trade. Until the 1970s, international trade played a fairly small role in the U.S. economy. Thus, it does not appear that international trade had any substantial role in the Great Compression. However, the catastrophic effects of the Great Depression and the Second World War led the United States to take the lead in building a more integrated global economy in the postwar period. The relative importance of international trade increased significantly in the 1970s, and it has continued to increase since then.

Burtless (1995) suggests that import competition contributed to rising income inequality, and he was writing at a time when imports from China were relatively small. After China joined the World Trade Organization in 2001, the pressure on American manufacturing from Chinese imports intensified. Acemoglu et al. (2016) calculate that the increase in imports from China may have been responsible for the direct loss of more than 800,000 American manufacturing jobs between 1991 and 2011.

If we desire to slow down or reverse the increase of income inequality, many policies are available. For example, since the slowdown in educational attainment has contributed to the Great Divergence, the obvious policy prescription is to increase investments in education. Since deregulation of the financial-services sector has contributed to the Great Divergence, the obvious policy prescription is to strengthen the regulation of financial firms. And since the decrease in the progressivity of the tax system has also contributed to the Great Divergence, the obvious policy prescription would be to reverse the trend by making the tax system more progressive. Based on my values, which include a desire for a less unequal distribution of income, all three of the prescriptions described in this paragraph would be sound policies. However, when we consider the fact that import competition has contributed to the Great Divergence, the obvious policy prescriptions of tariffs and import quotas are associated with great risks. A cycle of retaliatory tariffs (such as that which followed the imposition of the Smoot-Hawley tariffs in 1930) could do profound damage to the export sector. Also, although tariffs can help domestic *producers*, they are unquestionably harmful for domestic *consumers*, since they bring fewer choices and higher prices. Although some may contend that tariffs and quotas are a "cure" for the "disease" of import competition, I believe that the cure could be much worse than the disease.

Immigration. After immigration restrictions were relaxed in 1965, the rate of immigration rose substantially. It appears that this increase in immigration has contributed to the Great Divergence, just as the earlier decrease in immigration contributed to the Great Compression. As before, the immigration increases of recent years have had both political and economic effects.

The size of the economic effect is a subject of controversy. Blau and Mackie (2017) have performed an extraordinarily comprehensive review of the literature. They find that "when measured over a period of 10 years or more, the impact of immigration on the wages of natives overall is very small. However, estimates for subgroups span a comparatively wider range" (p. 204). McCarty, Poole, and Rosenthal (2016) emphasize the political effect: there has been a large increase in the number of low-income Americans who are not eligible to vote.

The political economy of immigration stands in contrast to the political economy of the other issues discussed here. The antiegalitarian policy reversals in the 1970s and 1980s were pushed by conservative, antiegalitarian forces. However, the relaxation of immigration laws in 1965 was supported by those who were otherwise egalitarian. Ironically, a clampdown on immigration could have mild *equalizing* effects, despite the fact that today's most ardent advocates of reduced immigration are those who advocate *antiegalitarian* policies in other policy areas.

The minimum wage. The inflation-adjusted federal minimum wage rose substantially in the 1950s and 1960s and reached its peak in 1968. Since then, however, the minimum wage has failed to keep up with inflation. Autor, Manning, and Smith (2016) find that the reduction in the real value of the minimum wage increased inequality in the 1980s, especially for women. I conclude that minimum wage laws contributed somewhat to the equalization of the 1940s, 1950s, and 1960s, and that the falling real value of the minimum wage also contributed somewhat to the widening income gap of the 1980s.

Executive compensation. Davis and Mishel (2014) calculate the average ratio of compensation of chief executive officers (CEOs) to the compensation of the average worker in their firms, for a sample of 350 large U.S. companies. In the 1960s and early 1970s, this ratio was in the low 20s. The ratio then began to rise rapidly, reaching 383 in 2000, before falling back to "only" 296 in 2013. Bebchuk and Fried (2004) discuss the explosion of executive compensation in detail. It is possible that some of the rise in CEO compensation may be a response to improved productivity on the part of executives. However, it is difficult to escape the conclusion that the phenomenal increases in executive compensation are largely due to a change in social norms. Skyrocketing CEO compensation since the 1970s is consistent with a change in social norms, under which executives and their boards of directors lost the "outrage constraint" that might previously have prevented them from pushing CEO compensation to stratospheric heights.

POLITICAL EXPLANATIONS

How could the Great Divergence take place in a country like the United States, in which many important policy decisions are made by elected leaders? The policies of the last 40 years have been extraordinarily beneficial for a relatively small number of affluent Americans, but these beneficiaries are greatly outnumbered by those whose economic interests have been harmed by the changes. Thus, the question is why so many congressional and presidential elections have been won by those who espouse and carry out antiegalitarian economic policies.

Social issues. Very often, candidates for public office who espouse conservative, antiegalitarian views on economic issues also have conservative views on social issues, such as abortion and gay rights. Thus, when a voter casts her vote primarily on the basis of opposition to abortion or gay rights, she will usually be voting for a candidate who also has antiegalitarian views on economic issues. Unless this voter is fairly affluent, she will thereby be voting against her economic interests.

Frank (2004) argues that conservatives have skillfully used social issues to drive a wedge between many voters and their economic interests. My view is that, although social issues are only a part of the picture, they cannot be dismissed. Elections are often won by small margins. If even a relatively small number of voters are persuaded to vote against their economic interests by social and cultural appeals, the effects on policy can be large.

Political organization and voter turnout. Edsall (1984) describes a business community that developed a sense of class consciousness and class solidarity. Along with increasingly energetic conservative ideologues, the business community provided increasingly unified support, and plenty of money, to conservative, antiegalitarian candidates for public office.

Edsall also identifies a series of changes that unmoored the Democratic Party from its long tradition of strong connections with working-class voters. In the 1960s and 1970s, antiwar activists, environmentalists, and women's-rights advocates joined the Democratic Party in increasing numbers. These groups were not necessarily hostile to organized labor and working-class Democrats, but workers' issues and income inequality were not at the top of their agendas. Thus, the Democratic Party has been less effective than it might otherwise have been at resisting the antiegalitarian trend. The Reagan tax cuts of 1981 were passed by a Congress with a Democratic majority in the House of Representatives. Also, much of the deregulation of the financial services sector took place during the Democratic administration of Bill Clinton.

Edsall also emphasizes that lower-income voters tend to have lower rates of turnout than those with higher incomes. If turnout in American elections were anywhere near 100 percent, the Great Divergence might have been much smaller than it has been.

Electoral institutions. Proportional voting schemes are used in parliamentary elections in many European countries. These electoral systems stand in contrast to the “first-past-the-post” system used in elections for the U.S. Congress. Alesina and Glaeser (2004) argue that proportional voting schemes contribute to the adoption of egalitarian policies. The first-past-the-post system rewards political parties whose supporters are not geographically concentrated, such as the Republican Party in the United States today.

The first-past-the-post system is also subject to gerrymandering. Although gerrymandering has benefited Democratic candidates on some occasions in the past, it tends to benefit Republican candidates today, since so many state legislatures are controlled by Republicans. To the extent that the first-past-the-post system has come to favor Republicans, it has contributed to the Great Divergence. I believe that this is a relatively important effect.

In the United States, presidents are chosen according to the Electoral College, an eighteenth-century institution that was deliberately designed to reduce the influence of the broad public. In 2000, the Republican George W. Bush was elected, despite losing the popular vote to the Democrat Al Gore by more than 500,000 votes. The Republican Donald Trump was elected in 2016, despite losing the popular vote to the Democrat Hillary Clinton by more than 2.8 million votes. Of course, there is no guarantee that the Electoral College will only go against the popular vote in a way that favors the antiegalitarian candidate. Nevertheless, in 2000 and 2016, what actually happened was that antiegalitarian Republicans won the Electoral College while losing the popular vote.

Small effects can accumulate and reinforce themselves over time. An important example of this is that Supreme Court justices in the United States are nominated by presidents who win the Electoral College, regardless of whether those presidents won the popular vote.

Thus, the second-place vote getter in the 2000 presidential election, George W. Bush, was able to nominate two conservative justices (John Roberts and Samuel Alito) to the Supreme Court. It is quite likely that Gore nominees would have voted differently from Roberts and Alito in two very important cases. The first of these is the 2010 decision in *Citizens United v. Federal Election Commission*, in which the conservative majority voted to reduce substantially the restrictions on political expenditures. The second is the 2013 decision in *Shelby County v. Holder*, in which the conservative majority voted to eviscerate key provisions of the Voting Rights Act of 1965. If presidential elections were always won by the top vote getter, it is likely that the decisions in *Citizens United* and *Shelby County* would have gone the other way.

Voter ignorance. Bartels (2005, 2008) emphasizes voter misunderstanding of a variety of policies. For example, although surveys indicate that a majority of Americans favor a progressive tax structure, many do not seem to have comprehended the highly regressive nature of the 2001 tax cuts. However, there is no evidence that voter ignorance is a new phenomenon. It strains credulity to think that voters were well informed until the 1970s and then suddenly became ignorant 40 years ago.

An even more telling piece of evidence against placing too much weight on the ignorance hypothesis is that the shift toward voting against one's economic interests was confined almost exclusively to white voters. African American voters, who are disproportionately represented on the lower rungs of the income scale, tended to vote for candidates espousing relatively egalitarian policies in the early and middle part of the twentieth century (when they *were* allowed to vote). Black voters have continued to vote in overwhelming majorities for the Democratic Party, which is clearly the more egalitarian (or at least the less antiegalitarian) of the two major parties. Thus, in order to place a lot of weight on the ignorance hypothesis, it is necessary for us to believe that nearly all black voters avoided ignorance throughout the period studied here and thus retained their ability to vote in accordance with their economic interests, while substantial numbers of white voters suddenly became more ignorant and thus lost the ability to vote their economic interests. A related possibility is that large numbers of white voters were susceptible to being misled by disinformation coming from certain parts of the news media. This leads me to the conclusion that racial issues provide more fertile ground for understanding the Great Divergence.

Race. In my view, race explains more of the Great Divergence than any other single influence. This does *not* mean that I believe that the other explanations discussed above are invalid. In fact, I believe that all of them can explain some of what has happened. I cannot overemphasize the fact that many elections are won by margins of 52 percent to 48 percent, rather than, say, 93 percent to 7 percent. Thus, each of a number of factors can turn out to be critically important.

My emphasis on the importance of race also does *not* suggest that no real progress has been made on racial issues in the United States. African Americans have made very significant strides in education, earnings, and income. In addition, as a result of the dismantling of Jim Crow laws, most African Americans do not have to endure as many daily humiliations as they once were forced to endure. In 2008 and 2012, an African American, Barack Obama, won the presidential election (with victories both in the Electoral College and in the popular vote), which would have been unimaginable for almost all of American history.

My assertion about the importance of race also does *not* mean that the attitudes of a substantial portion of the white population have not changed for the better. Also, I am *not* saying that anyone whose policy preferences differ from mine is a racist. Nevertheless, I cannot avoid the conclusion that race has played a very important role in generating the Great Divergence, and that the role of race is more important than the roles of the other influences discussed above.

From 1900 to 1944, Democratic candidates for president averaged 68 percent of the popular vote in the 11 states of the former Confederacy. From 1948 to 2016, this average was 44 percent, a decrease of 24 percentage points.[2] Thus the South, and especially the Deep South, transformed in a generation from solidly supporting the relatively more egalitarian Democratic Party to instead supporting the relatively antiegalitarian Republican Party.

It is possible that the switch of political parties among white Southerners was due, at least in part, to something other than race. Perhaps white Southerners voted for Barry Goldwater in 1964 because of his lack of enthusiasm for Social Security, or his support for a strong military. However, the racial history of the South leads me to believe that race was the dominant factor.

The white backlash against the Civil Rights movement has been stronger in the South than elsewhere. But this does not mean that racial issues are unimportant in the rest of the country. Race is clearly very important in Michigan, a state whose largest metropolitan area, Detroit and its suburbs, is more heavily segregated by race than any other area in the country.

The racial fears and hatreds of whites have also helped stimulate the antigovernment sentiments that have become widespread in recent decades. For most of American history, governments were openly and actively hostile to the interests of African Americans. Thus, the Civil Rights Act, and especially affirmative action programs, represented a dramatic reversal. This was enough to turn some whites against "government" generally. A watershed moment was the assertion in 1981 by Republican President Ronald Reagan, in his first inaugural address, that "government *is* the problem." Of course, Reagan was really referring only to *some* governmental actions. In the same speech, he called for a more active policy to confront the Soviet Union. This policy was to be carried out by a large increase in spending by the Department of Defense, which is indeed a part of the federal government. Thus, antigovernment rhetoric came to be used as code for opposition to some activities of government but not others. (Antigovernment rhetoric has been used most prominently by Republicans, but it has also been used by Democrats such as President Clinton, who famously said in 1996 that "the era of big government is over.")

Egalitarian government policies were essential to the Great Compression. In my view, although the antigovernment rhetoric of the past 40 years has sometimes had a libertarian element, its main effects have been to promote antiegalitarian policies, which have contributed to the Great Divergence.[3]

If the assertions that I have made here are correct, they represent a remarkable irony. White voters of modest economic circumstances supported the egalitarian policies that led to the Great Compression, and this advanced their economic interests. Economic inequality was reduced dramatically, and the standard of living of low- and middle-income whites skyrocketed. However, when the federal government moved to reduce *racial* inequality, the support for political candidates espousing egalitarian *economic* policies among low- and middle-income white voters fell dramatically. This reduction in support was enough to usher in the antiegalitarian tide of the past 40 years, to the detriment of many of those same white voters.

WHAT DOES THE FUTURE HOLD?

Acemoglu and Robinson (2012) describe "critical junctures"—moments in history that disturb the established system. They show that small differences in initial conditions can lead to large differences in the response to a critical juncture. Is the abrupt policy reversal of the 1970s and 1980s a critical juncture, and if so, where will it lead?

On the one hand, there is plenty of reason to believe that the Great Divergence will continue, and that income inequality in the United States will remain very high. Wall Street firms have fought strenuously to water down the implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The strength of labor unions continues to erode. In 2017, a Republican Congress and president passed a set of tax cuts that were very favorable to those with high incomes, especially those who owned large amounts of corporate stock. Wealthy antiegalitarians, such as Charles Koch and his brother, the late David Koch, continue to provide strong financial support for antiegalitarian causes and candidates. The flood of money into the political system was further encouraged by the Citizens United decision (*Citizens United v. Federal Election Commission*), and enforcement of the Voting Rights Act was weakened by the Shelby County decision (*Shelby County v. Holder*).

On the other hand, many of the egalitarian victories of American history are still intact. We still have universal elementary and secondary education. Despite huge reductions in public funding, we still have the strongest system of higher education in the world. No one is seriously suggesting that we should repeal the Thirteenth, Fifteenth, or Nineteenth Amendments to the U.S. Constitution. Despite the fact that it is not in long-run balance, the Social Security system continues to provide income support for tens of millions of elderly Americans. We still have an income tax. Moreover, income inequality is probably getting more attention than ever before, and some candidates for public office are campaigning on egalitarian platforms.

Thus, I believe it is impossible to know for certain the future direction of income inequality in the United States. There is a growing clamor in the press and among Democratic challengers on the campaign trail, who contend that the majority of Americans would prefer to see a substantial reduction in inequality, and I believe that American democracy is still sufficiently vital that it is possible this will occur.

Notes

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1. The updated series can be found at http://eml.berkeley.edu/~saez/. Because of data limitations, some of the authors' series begin in 1917.
2. Note that few blacks were able to vote in these Southern states in the first six decades of the twentieth century. Thus, the decrease in the overall fraction of the southern vote going to Democrats is an understatement of the extent to which white southerners switched parties.
3. The wave of antigovernment rhetoric has sometimes generated remarkable ironies and paradoxes, such as when a South Carolina woman in 2009 shouted to a member of Congress that he should "keep your government hands off my Medicare." Appelbaum and Gebeloff (2012) report on the tendency for conservative critics of the social safety net to rely on the social safety net, apparently without noticing the irony.

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