

INCOME INEQUALITY AND ECONOMIC GROWTH

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ACKNOWLEDGEMENTS

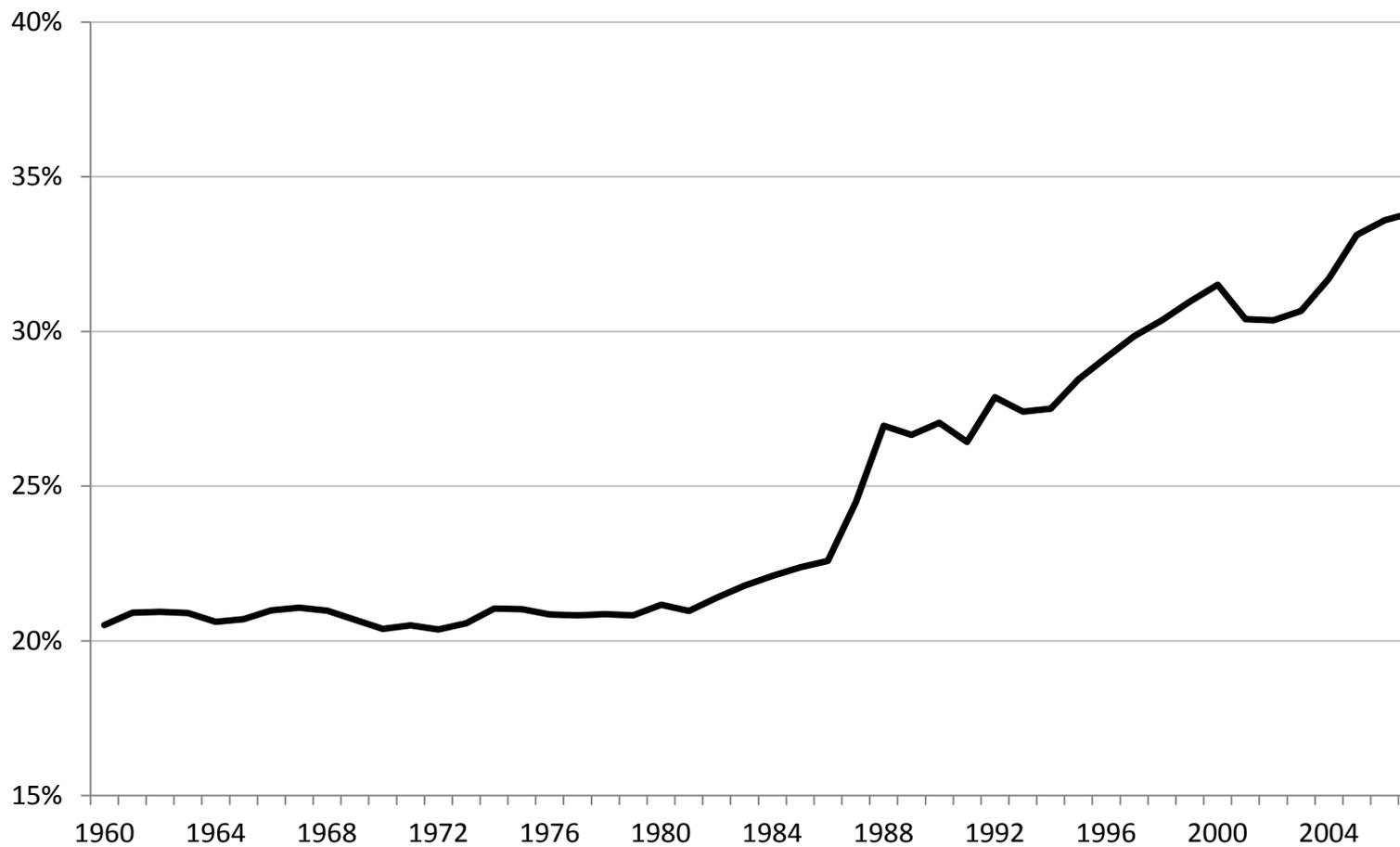
- Joint work with Steve Fazzari
- Generous support from INET
- Opinions are mine and not those of the Fed

BACKGROUND

- Income Shares
 - Share of top 5% stable from 1960 – 1980
 - Increases steadily between 1980 and 2007
- Consumption
 - Consumption share of GDP stable from 1960 - 1980
 - Increases steadily between 1980 and 2007
- Debt
 - Debt to income ratio stable from 1960 – 1980
 - Doubles between 1980 and 2007
- Great Moderation
 - Decline of GDP volatility starting in mid 1980s

RICH GOT RICHER

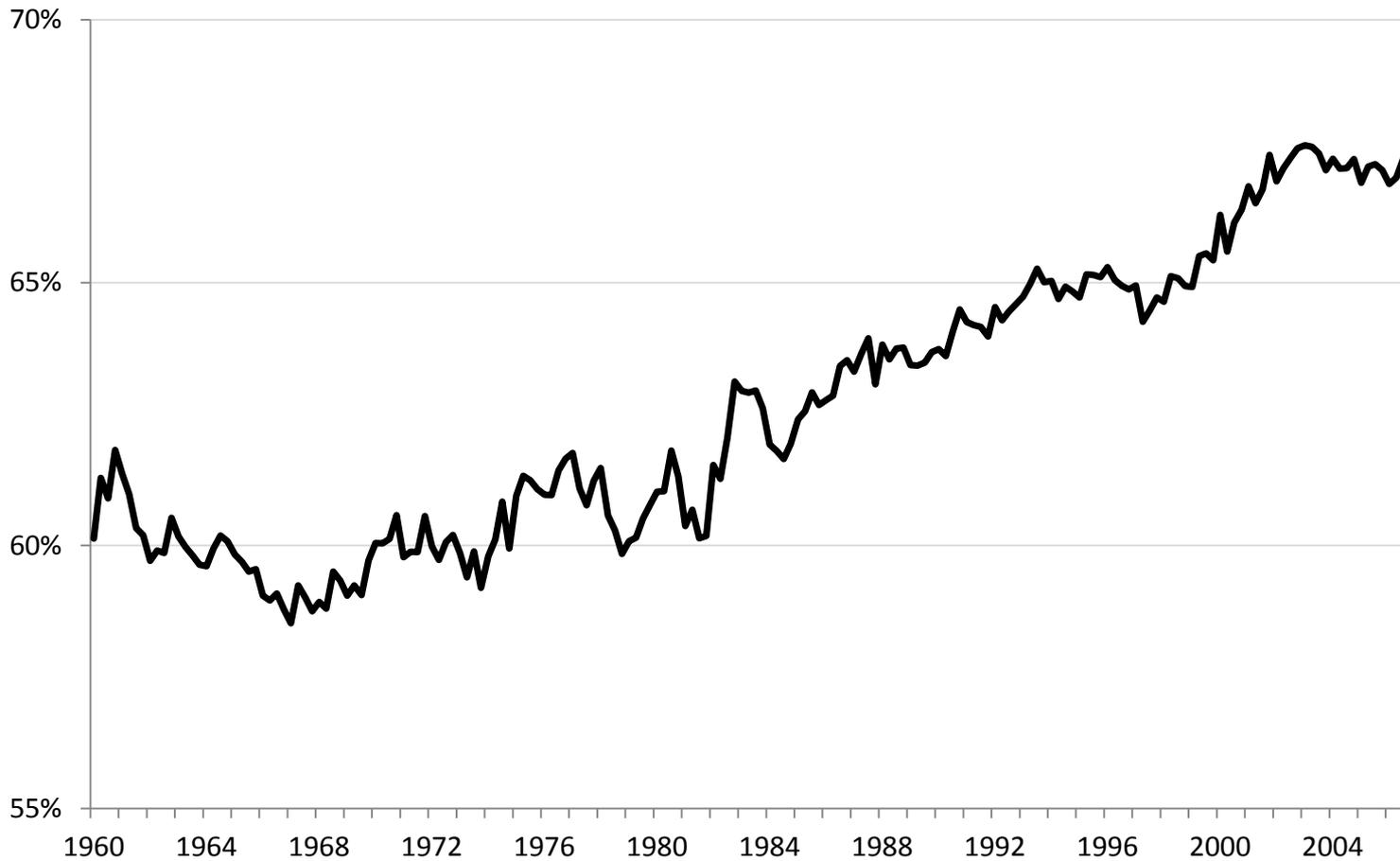
Income share of the top 5% of US households



Source: The World Top Incomes Database

CONSUMPTION DROVE ECONOMIC GROWTH

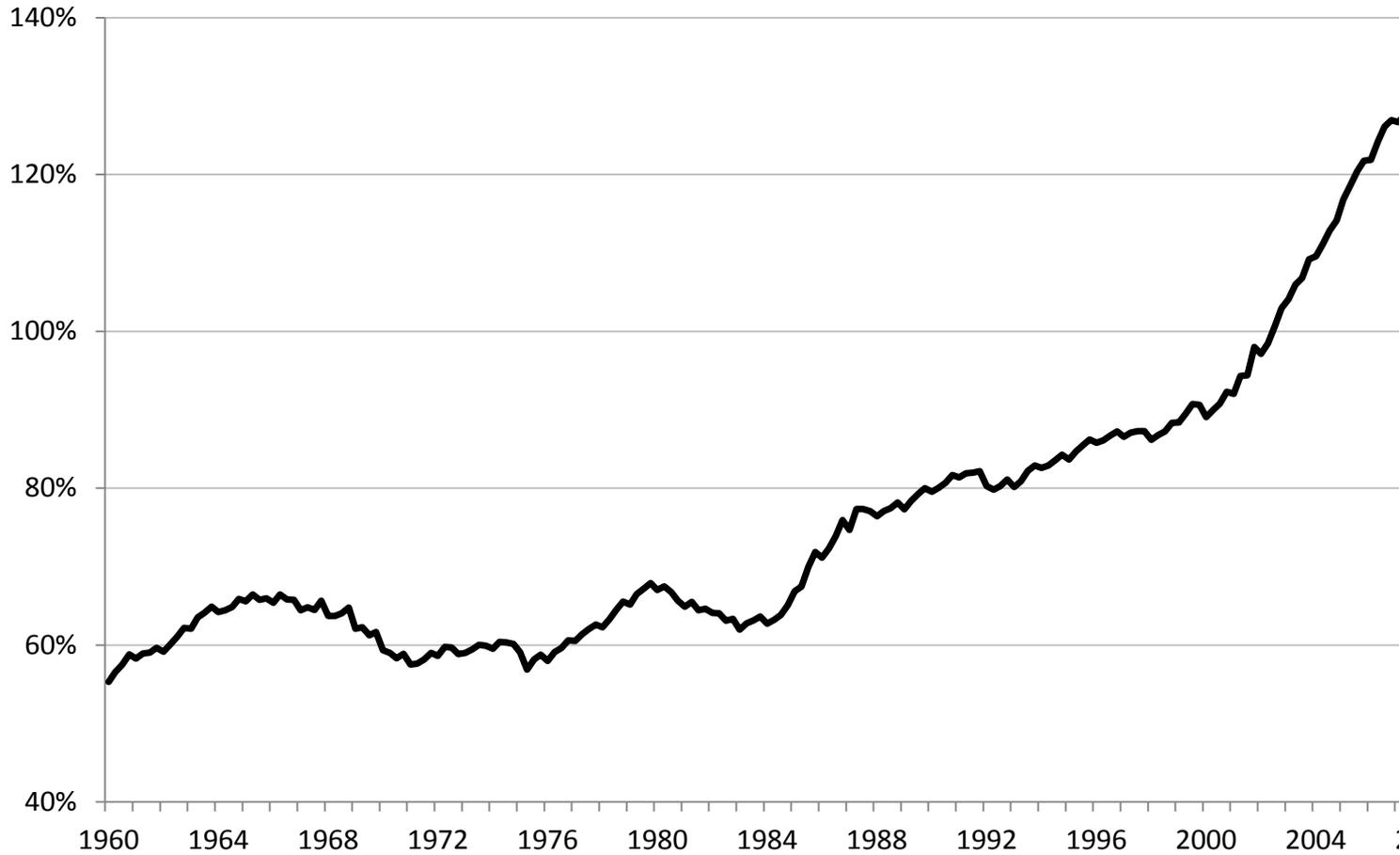
Consumption share of GDP



Source: BEA National Income and Product Accounts

HOUSEHOLDS DOUBLED THEIR LEVERAGE

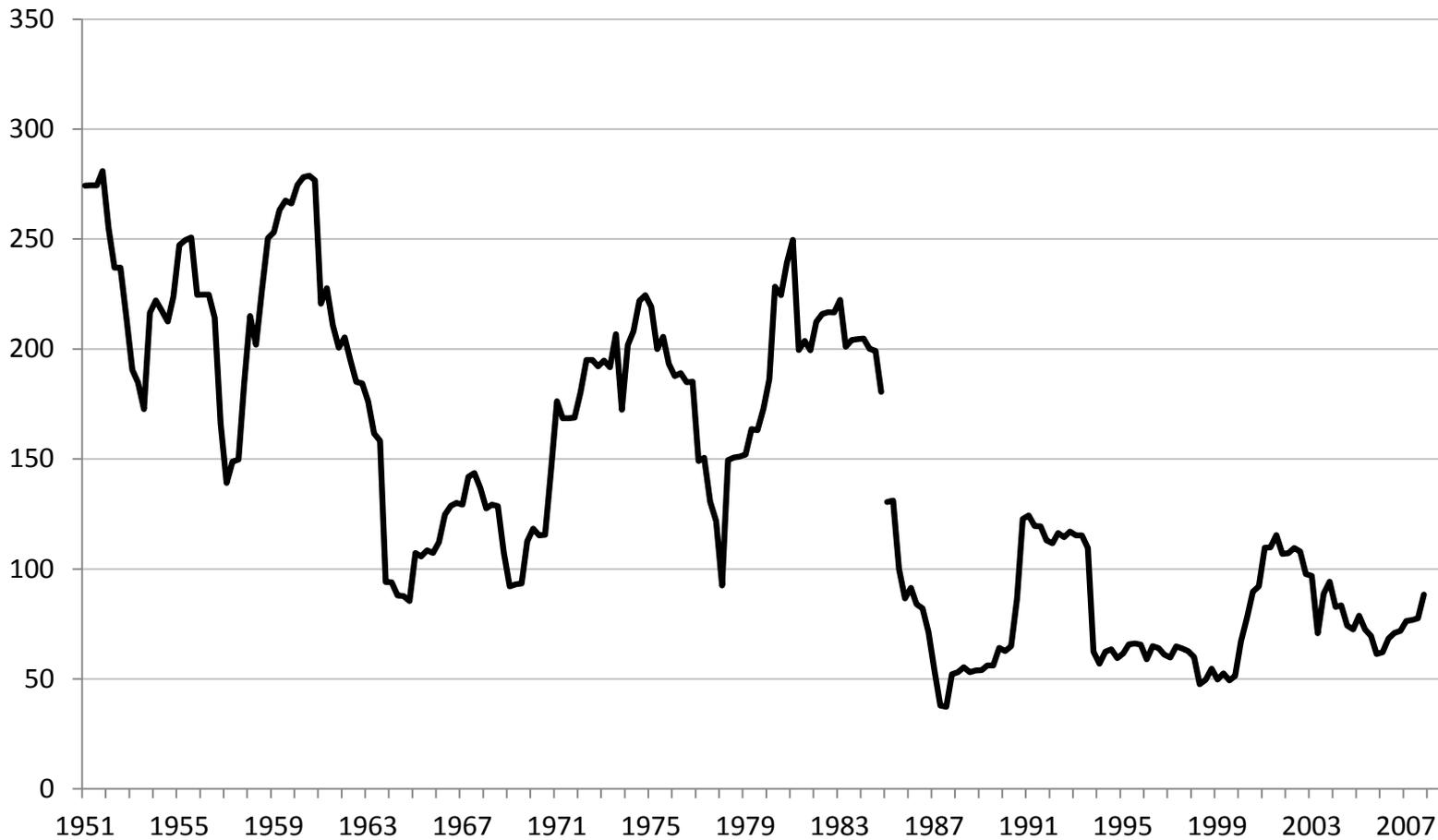
Debt to income ratio of US households



Source: FRB Flow of Funds

GREAT MODERATION OF MACRO VOLATILITY

Twelve quarter rolling S.D. of GDP growth (index = 100 in 1985)



Source: BEA National Income and Product Accounts

MOTIVATION

In 2007, should we bet on Lucas or Minsky?

“[The] central problem of depression-prevention [has] been solved, for all practical purposes.”

-Lucas, AEA Pres. Address (2003)

“A fundamental characteristic of our economy is that the financial system swings between robustness and fragility...”

-Minsky (1974)

MOTIVATION II

Team Lucas

GDP growth volatility down

Steady economic growth

Team Minsky

Rising household leverage

Rising income inequality??

Need to look at disaggregated data.

DISAGGREGATED VIEW: INCOME

- Source of rising inequality?

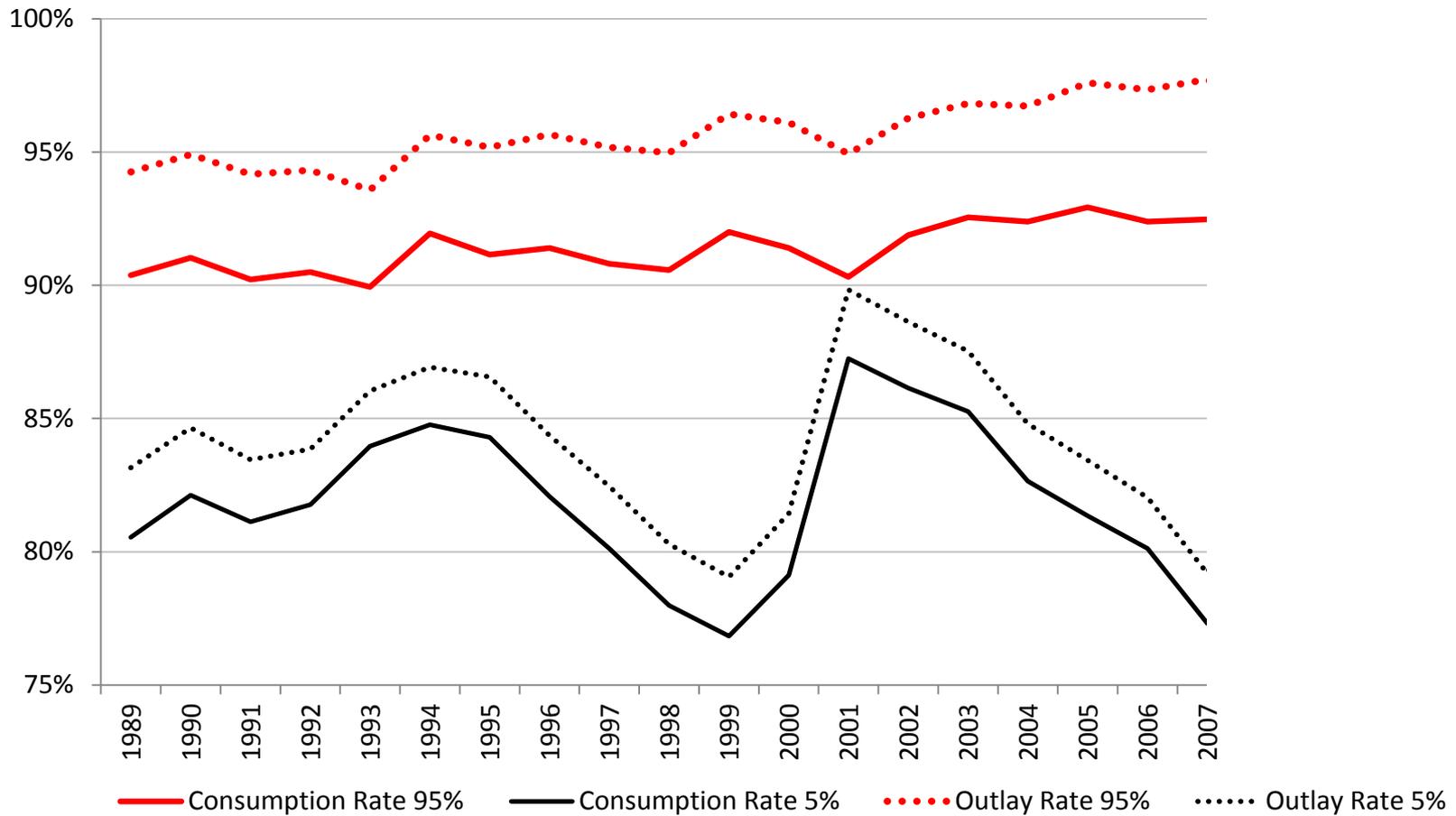
Acceleration at the top vs. stagnation at the bottom

Real annualized growth rates

	1960 - 1980	1980 - 2007
Top 5%	4.0%	5.0%
Bottom 95%	3.9%	2.6%

DISAGGREGATED VIEW: CONSUMPTION

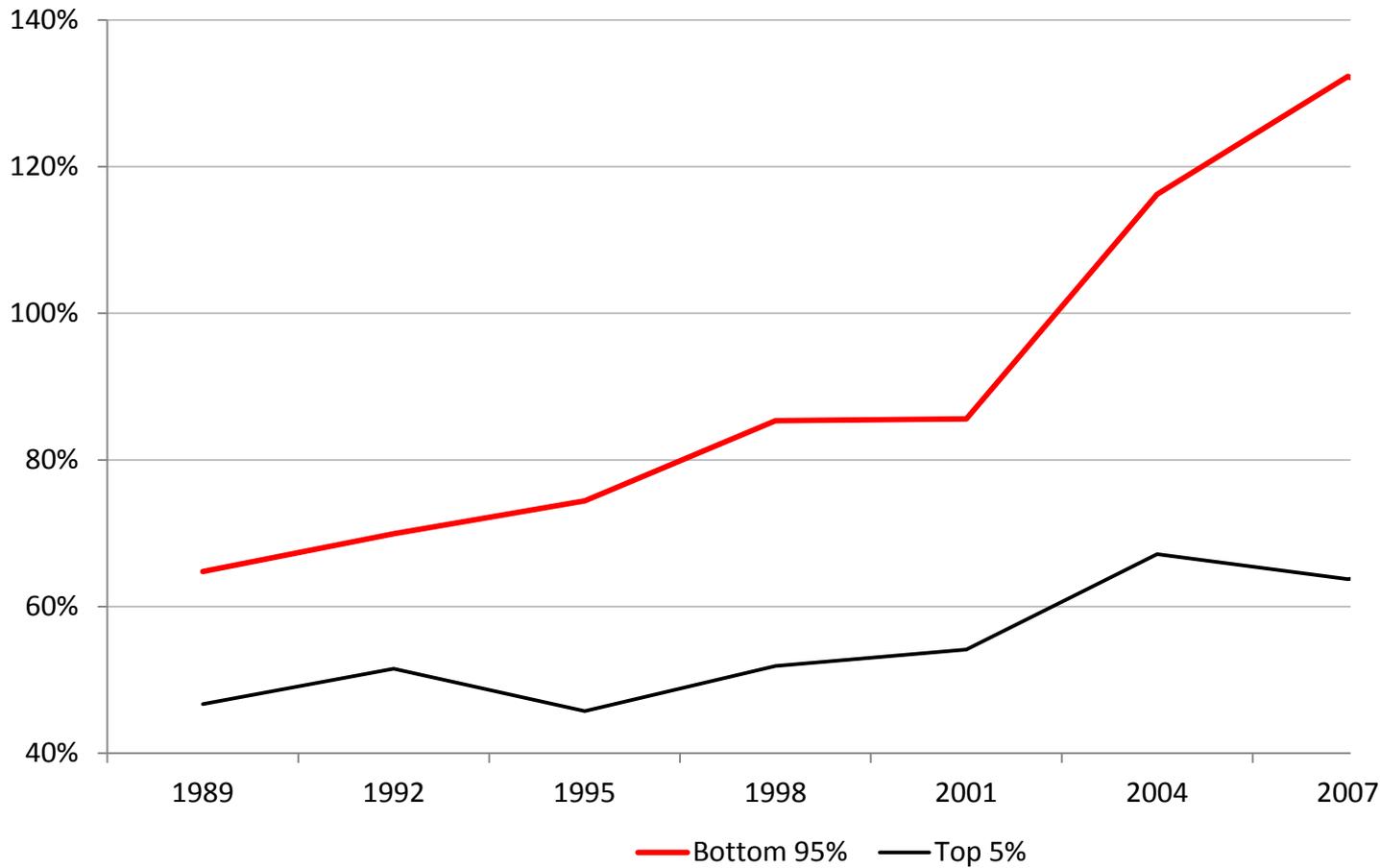
Consumption to income ratio of US households



Source: FRB Flow of Funds, Survey of Consumer Finances, Calculations by Mark Zandi and authors

DISAGGREGATED VIEW: DEBT

Debt to income ratio of US households



Source: FRB Flow of Funds, Survey of Consumer Finances, authors' calculations

DISAGGREGATED VIEW: ASSETS

Financial net worth to income ratio of US households



Source: FRB Flow of Funds, Survey of Consumer Finances, authors' calculations

SUMMARY OF EVIDENCE IN 2007

Top 5%

- Income share rising
- Evidence of consumption smoothing
- Rising leverage
- Rising financial net worth

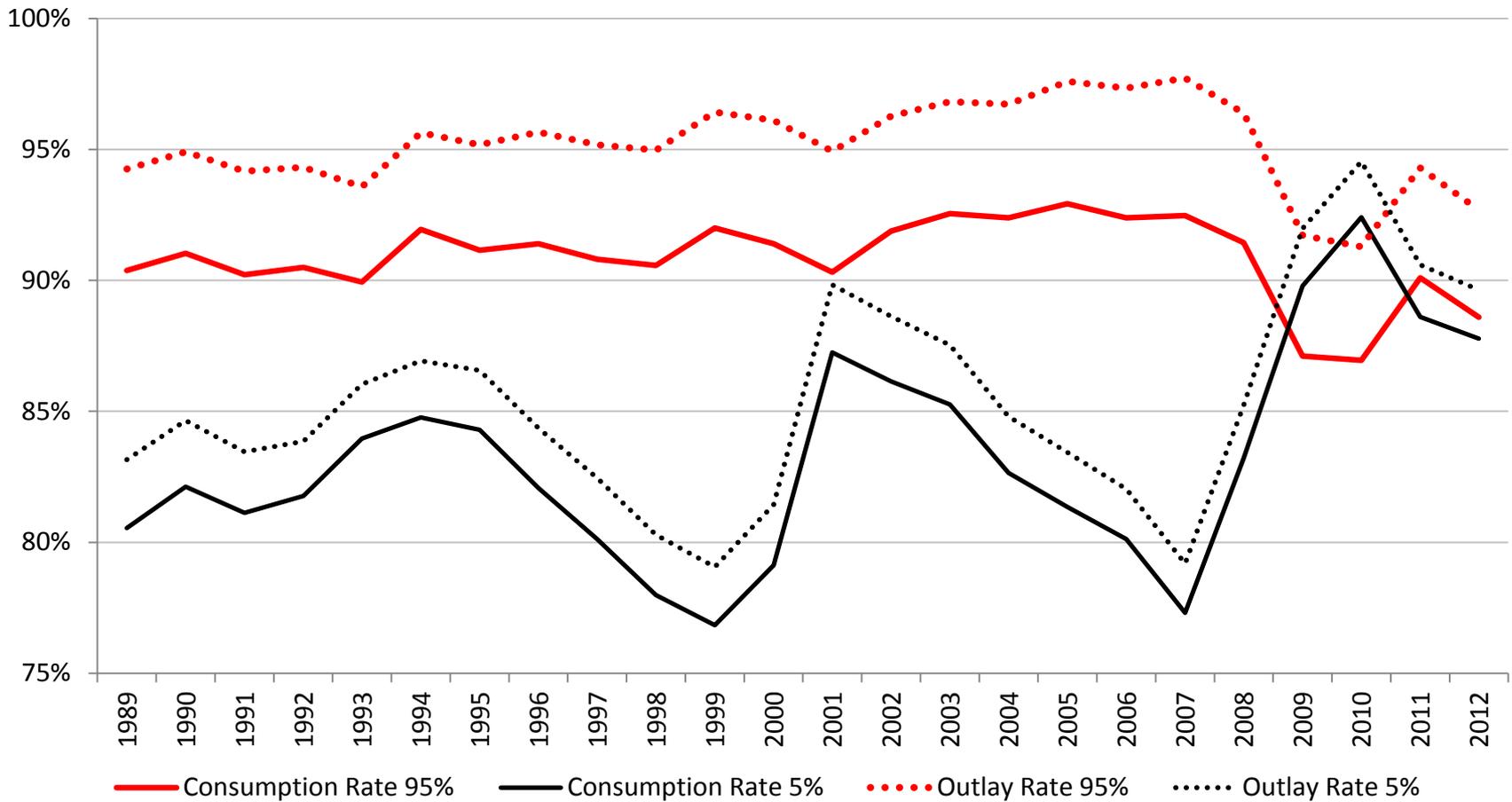
Bottom 95%

- Income growing slowly
- Rapidly rising leverage
- Shrinking financial net worth

What happens when the leverage ratio of the bottom 95% stops rising?

DISAGGREGATED VIEW: CONSUMPTION RATES

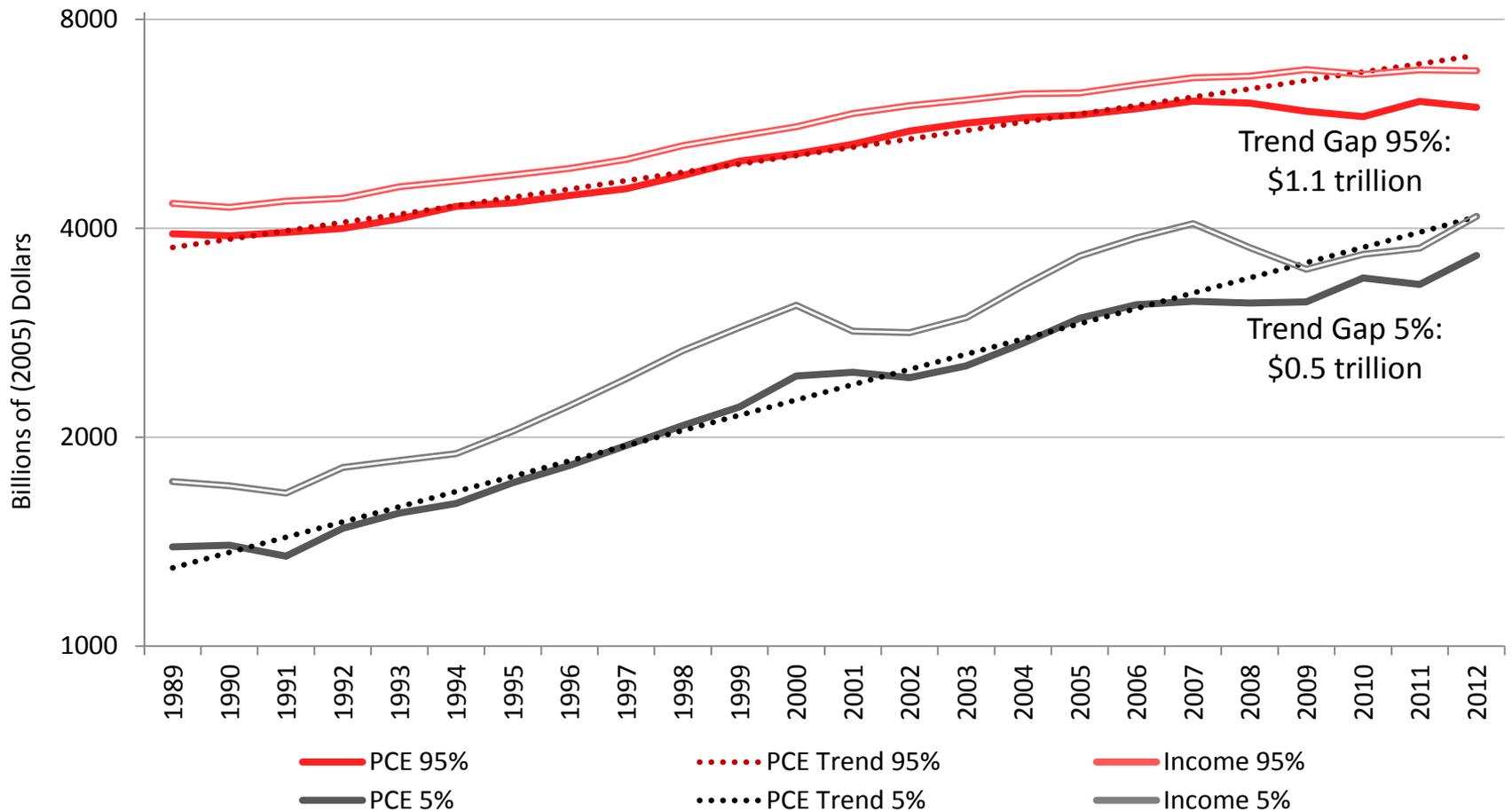
Consumption to income ratio of US households



Source: FRB Flow of Funds, Survey of Consumer Finances, Calculations by Mark Zandi and authors

DISAGGREGATED VIEW: CONSUMPTION LEVELS

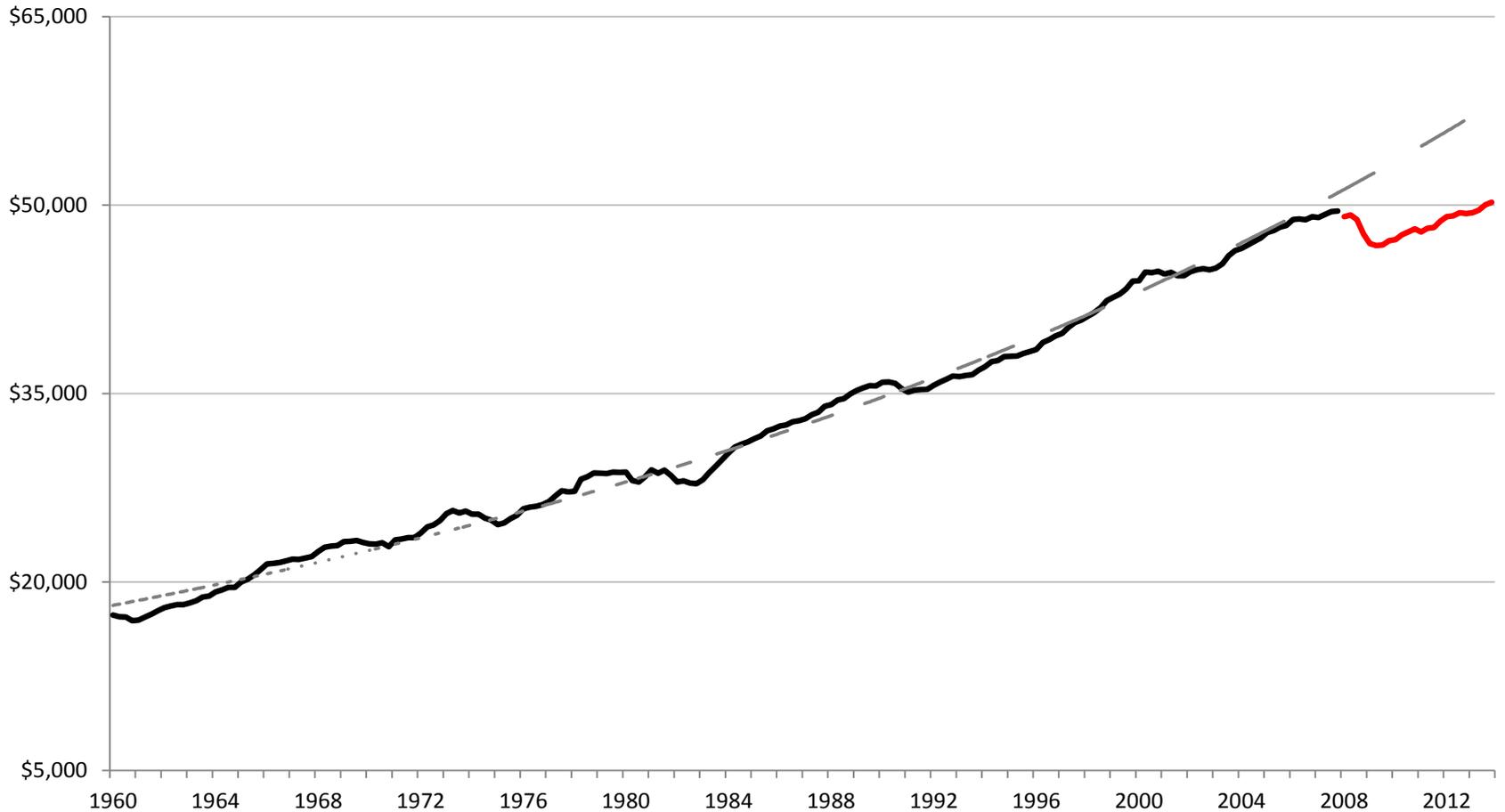
Real consumption of US households



Source: FRB Flow of Funds, Survey of Consumer Finances, Calculations by Mark Zandi and authors

GDP AFTER THE CONSUMER AGE

Real Gross Domestic Product, Chained Dollars (exponential trend)



Source: BEA National Product Accounts

CONCLUSION: A NEW ERA?

- Short history of U.S. demand generation
 - Postwar shared prosperity
 - Rising inequality and unsustainable Consumer Age
 - Recession and secular stagnation
- Link between income distribution dynamics and macro dynamics: not a coincidence