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MEGAN McARDLE

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On Income and Consumption Inequality

16 Jul 2009 11:30 am

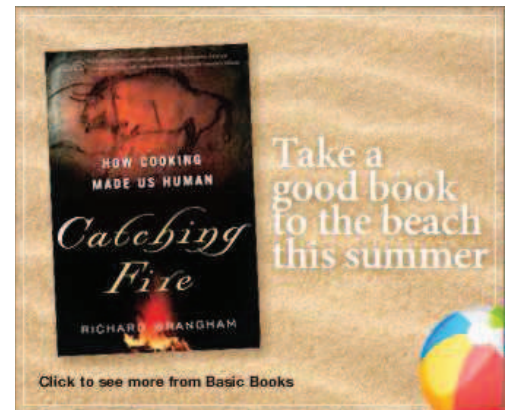
Will Wilkinson has a [new paper](#) out on inequality, which I will be blogging about later. But Ezra Klein has an interesting response, which focuses on the difference between income inequality and consumption inequality.

I broadly agree with Will that consumption inequality, not income inequality, is what matters. If the rich have access to broad classes of goods that the poor can't have, I find this worrying. On the other hand, if the problem is that Bill Gates has a really awesome 80 inch flat panel television, while the poor have to be content with a 32 inch CRT, well, I can't say my heartstrings are plucked very tight by this injustice. So it's important to know what the real differences are.

This theory was very popular with conservatives and libertarians over the last few years; I'm sure I referenced it myself. But of course, as Ezra [points out](#), some of that consumption inequality may well have been due to rising credit inequality: people borrowed money from their houses to buy consumption goods.

But I think it's easy to overstate the contribution of debt, for two reasons. First, many of the discussions on consumption equality focus on the poor, who were still relatively credit constrained even at the height of the bubble. And second, income inequality figures exclude both taxes and government benefits. Things like the EITC and Section 8 vouchers really have made a quite substantial improvement in the ability of the poor to consume.

So I don't think we actually know how much of a difference consumer credit made to equalizing consumption between rich and poor. I suspect that the continued mechanization of formerly labor-intensive tasks has made a greater difference, but then you'd expect me to say that. The data we want will not be available for several years, especially since period immediately following the financial crisis will be very atypical*, and therefore not useful in assessing the longer term trend.

**ABOUT MEGAN McARDLE****EMAIL MEGAN**

The world's tallest female econoblogger delivers her opinions on economics, business, and other moral hazards

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* Before you accuse me of cherry-picking, I expect that the data following the financial crisis will actually show income and consumption inequality falling, because financial crises tend to make bigger relative cuts in the income of the wealthy. That doesn't mean that they "suffer more" in any meaningful sense--losing 5% of a \$30,000 annual salary is almost certainly a greater hardship than losing 25% of \$300,000. But the numbers will still show shrinkage.

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Ken Magalnik July 16, 2009 12:45 PM

Megan:

Where do you draw the line of "broad classes of goods"? I assume you mean, if the poor could no afford televisions at all, while the rich could buy giant flat screens. But I don't see the line that isn't arbitrarily set. I could complain about the lack of affordability of just flat screen tv's or sport cars, or elective surgery, or whatever. The rich will always be able to afford more than the poor, that's sort of the point of being rich. What am I missing?

REPLY

Brandon Berg (Replying to: Ken Magalnik) July 16, 2009 1:18 PM

Furthermore, this inequality has social value. If being rich doesn't have any advantages, and being poor doesn't kind of suck, what's the point of working hard to be rich rather than poor?

Don't get me wrong. It's a fine thing that we live in a time and place prosperous enough that the poor don't have to live in absolute squalor. But the fact that being rich is much better than being poor has been one of the primary factors driving the progress it took to get us to the point where that's possible.

REPLY

Foobarista (Replying to: Ken Magalnik) July 16, 2009 1:27 PM

If you read Will's paper, he's talking about things like \$300 Haier fridges versus \$11,000 SubZero fridges, which aren't functionally much different, but that "the rich" buy, more for signaling reasons than anything related to utility. So, the poor can have access to life-improving "stuff" - it's just not as fancy as the stuff the rich buy. But most poor Americans do have access to kitchens that are basically functionally identical to those used by rich people.

One thing I should point out is how this is largely a US phenomenon, as far as I can tell. When I lived in China, it was clear that non-crappy stuff *is* more expensive there than it is in the US, and poor Chinese simply can't buy refrigerators. Poor Chinese (and I guess Africa is probably worse) often still use coal or even wood in kitchens, and don't have much in the way of useful electric appliances.

REPLY

Brandon Berg July 16, 2009 12:55 PM

Megan:

The income chart Ezra posted makes me curious about something: I've heard it suggested that the rise in income inequality was in part driven by a rise in income volatility. Hypothetically, if each year nine people make \$50,000 and one person makes \$500,000 (e.g., by selling a business or cashing in several years' worth of stock options), and the person making \$500,000 is a different person each year, income equality is high only on paper.

Are you aware of any statistics on trends in the inequality of multi-year income?

Also, I don't see that Ezra mentioned the poor anywhere in his piece, though he did mention the middle class. I suspect that Ezra Klein is more concerned about the inequality between the rich and Ezra Klein than between the rich and the poor.

REPLY

market karma (Replying to: Brandon Berg) July 16, 2009 2:23 PM

Brandon -- sorry to jump in--

there is at least one study on the top 400 returns ranked by AGI from 1992 to 2000 (

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