Department: Economics

Semester: Fall, 2015

Economics 175: Wage and Income Inequality: Determinants and Policy Remedies

Instructor:

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 Office Hours: Tuesday, 10AM-11AM, Thursday, 11AM-12PM (4115D Tydings)

Teaching Assistants:

Ryan Malitz malitz@econ.umd.edu

 Section 0101 – LEF 1221 9AM - 9:50AM

 Section 0102 – ARC 1101 10AM - 10:50AM

 Section 0103 – ASY 3203 11AM – 11:50AM

 Office Hours: M 11:45AM-1:45PM (4101D Tydings Hall)

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 Section 0104 – TYD 2108 12PM – 12:50PM

 Section 0105 – PLS 1107 1PM – 1:50PM

 Section 0106 – TYD 0101 2PM – 2:50PM

 Office Hours: Tu, Th 3:30-4:30PM (4101D Tydings Hall)

Description:

Through most of the 20th century, the large gaps in income between rich and poor declined. However, since 1970, the United States has experienced one of the largest and most rapid increases in income inequality that the world has ever seen. In 1916, the top one percent of

income earners took home 18.5% of national income. By 1973, the share of national income earned by the top one percent had fallen to 7.7%. However, since then income inequality has risen dramatically to the point where, just before the crisis, in 2007, the share of national income earned by the top one percent had risen to 18.3%. The large increase in inequality has been at the heart of bitter public policy debates between Democrats and Republicans as well as the impetus between major social movements on the right (the tea party) as well as on the left (the occupy wall street movement).

In this course, we will investigate why people make different amounts of money, why income inequality has risen so dramatically in recent years, what public policy tools exist to counter inequality increases, and what different institutional arrangements different countries use to lower inequality. This course will introduce students to theoretical tools used by economists to understand the sources of inequality and will also show empirical evidence to better understand the changes in the wage distribution and, more generally, in the income distribution.

Students will read journal articles, magazine articles and excerpts from books. They will also engage in structured group debates during section.

Course Requirements: The final grade in the course will be based upon a final exam worth 35% of the grade, two opinion papers on topics of relevance to the course worth a total of 30% of the grade, a sequence of group debates and reading reports held in section worth 25% of the grade, an empirical exercise worth 5% of the grade and two short critiques of current newspaper articles on topics related to the course worth 2.5% of the grade each.

Final Exam: The final exam will consist of a combination of short answers and essays. Students will also be responsible for graphs illustrating major points in the course.

Debates: Students will be assigned teams and positions and will have a number of debates in section throughout the semester. Team members will rotate randomly from one debate to the next. Debate groups should meet outside of class to prepare. Debates will start with opening statements of five minute length from each team.

Opinion Paper: Two short opinion papers, one on a topic chosen by the student with TA approval due on October 31st and the second on whether the United States should adopt a welfare state and why is due at the end of the semester (December 12).

Empirical Assignment: Students will be given data from the top incomes database. They will be required to compute aggregate statistics summarizing the inequality of income for a number of countries over time. This assignment is due on Saturday, September 20 on Elms.

Newspaper Article Critiques: Students will be required to pick two articles in a major US newspaper on a subject matter related to the course and discuss problems with the statistical or theoretical reasoning in the article. They should begin by summarizing the article, then critique

the article, and finish by making suggestions to improve the article. The first is due on October 3rd in section. The second is due on November 7th in section.

Summary of the Components of the Final Grade: 35% Final, 30% Opinion Papers, 25% Debates, 5% Empirical Assignment, 5% Newspaper Article Critiques

Section 1: What is Inequality? Measurement of Inequality in Theory and Practice.

(1.) 8/31 (M): What is inequality? An overview of income inequality, wealth inequality, consumption inequality and inequality in power.

(2.) 9/2 (W): What is income? We will discuss the functional distribution of income: capital income and labor income. We will start with the historical insights of Smith and Marx that owners of capital were compensated purely for ownership rather than work. We will also discuss whether the capital share of income is stable (Kaldor) over time and how capital shares vary across countries. We will discuss in detail the sources of information on income: tax data and consumer surveys.

Readings: Thomas Piketty: **Capital in the 21st Century**, Chapter 2, pp. 31-71.

(3.) 9/9 (W): Measuring inequality: We will discuss different theoretical measures of inequality including the Gini coefficient, variance and the 90/10 ratio.

Empirical Assignment: Use data set given to class (Saez data set on top income shares) and compute various statistical summary measures of inequality for a few different countries over time. Due Friday, September 18 in section.

Section 2: Theories of Justice – Should we care about inequality? If so, why? If not, why not? Examination of philosophical argument for and against public action trying to limit inequality.

(4.) 9/14 (M): Values and inequality: Mills, Marx. We will discuss opposing normative philosophical theories of evaluating societies – Utilitarianism and Marxism.

Readings: Will Kymlicka, **Contemporary Political Philosophy: An Introduction,** pp. 10-48 (2nd edition), and John Roemer, **Free to Lose,** pp. 14-27.

(5.) 9/16 (W): Values and inequality: Rawls, Nozick.

Readings: Excerpts from John Rawls, **A Theory of Justice,** pp.3-46 and Robert Nozick, **Anarchy, State and Utopia,** pp. 149-182

(6.) 9/21 (M): Values and Inequality: Sen. Sen posits that both Nozick and Rawls want equality but of different things. Sen then discusses what should be equalized in society. Second half: wealth. What is wealth? We will discuss what wealth is and how we measure it. This will include a discussion both of Tangible wealth (equipment and structures) and intangible wealth (patents, knowledge, human capital).

Readings: Values and Inequality: Amartya Sen, "Inequality of What?" in The Tanner Lectures in Human Values, pp. 197-220

Debate #1: In section 9/25 (F): Utilitarianism, Marxism, Libertarianism, Rawls (four groups in section).

Section 3: History of Inequality

(7.) 9/23 (W): Establish facts about income inequality in the 20th century. We will discuss the great compression and the dramatic increase in inequality since 1970s. Data problems. How far back in time can we go? What data sources do we have going back in time? (Establishing Facts)

Reading: Thomas Piketty, **Capital in the 21st Century,** Chapters 7-8, pp. 237-271

(optional) Thomas Piketty and Emmanuel Saez (2005), "Income Inequality in the United States, 1913 – 1998", *Quarterly Journal of Economics* 118(1), pp.1 – 39.

(8.) 9/28 (M): Wage inequality in the 20th century: A more detailed look at wage inequality using the book by Goldin and Katz, we will establish facts about the evolution of wage inequality in the US. Discuss differences in using household survey data and IRS data.

Reading: Claudia Goldin and Lawrence Katz, **The Race Between Education and Technology,** Chapter 2.

Section 4: Theories of Inequality

(9.) 9/30 (W): Theories of Education and wage inequality: We will introduce labor supply and labor demand and how they jointly determine wages. We will use graphs. We will discuss impacts of increased labor supply and increased labor demand. What happens if more people get education (increase in labor supply for educated, reduction in labor supply for less educated)?

(10.) 10/5 (M): Theories of education and wage inequality: We discuss alternative theories of wage determination to the neoclassical supply and demand theories: signaling theories, bargaining theories, and economic sociology theories.

(11.) 10/7 (W): Theories of education and wage inequality: We discuss theories of change in wage structure; in particular, we discuss skill-biased technical change and capital biased technical change.

Section 5: Capital vs. Labor

(12.) 10/12 (M): What does capital do: returns to deferred consumption, returns to risk, returns to innovation, rent expropriation.

Reading: N. Gregory Mankiw, "Defending the One Percent", *Journal of Economic Perspectives* Volume 27(3): pp. 21-34.

(optional): Stephen Marglin (1974), "What Do Bosses Do: The Origins and Functions of Hierarchy in Capitalist Production", *Review of Radical Political Economy* Volume 6(2), pp. 60-112, Facundo Alvaredo, Anthony Atkinson, Thomas Pikkety, and Emmanuel Saez, "The Top 1 Percent in Historical Perspective", *Journal of Economic Perspectives* Volume 27(3): pp. 3-20.

(13.) 10/14 (W): The Dynamics of Capital Income Inequality

Reading: Thomas Piketty, **Capital in the 21st Century,** Chapter 5, pp. 164-198.

(14.) 10/19 (M) Management versus capital in historical perspective - the changing internal dynamics of the firm; chandler? Carola Frydman on inequality in pay and ceos, rents vs. efficient compensation in CEO pay.

Readings: Carola Frydman and Dirk Jenter, "*CEO Compensation"*, *Annual Review of Financial Economics* 2(1): 75-102 and Lucien Bebchuck and Jesse Fried, "Executive Compensation as an Agency Problem", *Journal of Economic Perspectives* 17(3): pp. 71-92.

(Optional): Greenwood, Robin, and David Scharfstein (2013), "The Growth of Finance", *Journal of Economic Perspectives*, Volume 27(2): 3-28 and John Cochrane (2013), "Finance: Function Matters Not Size", *Journal of Economic Perspectives,* Volume 27(2): pp. 29-50(22).

Debate #2: In section 10/23 (F): Group A: Does capital deserve the returns it gets? Group B: Do corporate executives deserve the returns they get? (Group B should look at the optional readings by Greenwood and Scharfstein and by Cochrane).

Section 6: Wage Inequality in the 20th Century: Assessing Theories

(15.) 10/21 (W): Skill-biased technical change and labor supply

Reading: Lawrence Katz and Claudia Goldin, **The Race Between Education and Technology,** Chapter 3.

(16.) 10/26 (M): Job Polarization: The updated version of the skill-biased technical change hypothesis - the job polarization hypothesis.

Readings: David Autor, "The Polarization of Job Opportunities in the U.S. Labor Market", *Hamilton Project Working Paper* and David Autor, Lawrence Katz and Melissa Kearney, "The Polarization of the U.S. Labor Market", *American Economic Review,* Vol. 96(2), pp. 189-194 and Lawrence Mishel, John Schmitt, and Heidi Hierholz (2013), "Assessing the Job Polarization Explanation of Growing Wage Inequality", *Economic Policy Institute* Working Paper.

(optional) John DiNardo and Jorn Steffen-Pischke (1997), "The Returns to Computer Use Revisited: Have Pencils Changed the Wage Structure Too?", *Quarterly Journal of Economics,* Vol. 112(1), pp. 291-303.

Opinion Paper #1: Due in section 10/30 (F).

(17.) 10/28 (W): Trade and wages: Krugman, Hanson

Readings: Jonathan Haskel, Robert Lawrence, Edward Leamer and Matthew Slaughter (2012), *Journal of Economic Perspectives,* Volume 26(2), pp. 119–140.

(18.) 11/2 (M): Top Wages: Superstar economics.

Readings: Alan Krueger, "Rock and Roll, Economics, and the Rebuilding of the American Middle Class", http://www.whitehouse.gov/blog/2013/06/12/rock-and-roll-economics-and-rebuilding-middle-class.

(19.) 11/4 (W): Institutions: norms, unions, internal labor markets - impact of unions; changes in social norms

Readings: (optional) Nicole Fortin and Thomas Lemieux (1997), "Institutional Changes and Rising Wage Inequality: Is There a Linkage?", *Journal of Economic Perspectives* Vol. 11(2), pp. 75-96.

(20.) 11/9 (M): Institutions: norms, unions, internal labor markets II

Readings: David Card and John DiNardo (2002), "Skill-Biased Technological Change and Rising Wage Inequality: Some Problems and Puzzles", *Journal of Labor Economics* Vol. 20(4), pp. 733-783.

Debate #3: In section: 11/13 (F): Which is responsible for the dramatic increase in inequality? (A.) De-unionization, (B.) Falling Minimum Wage, (C.) Skill-biased technical change, (D.) Slowdown in educational attainment.

Section 7: Inequality and Public Policy

(21.) 11/11 (W): Policy: We will discuss the minimum wage and the Earned Income Tax Credit (EITC) in terms of their impact on lowering poverty. We will also discuss policy complementarity between the minimum wage and the EITC.

Arindrajit Dube, *Senate HELP Committee Testimony*", pp. 1-21.

(22.) 11/16 (M): Labor Law: We will discuss the impact of labor unions and works councils on wage distributions.

Readings: Richard Freeman and James Medoff (1984), **What Do Unions Do?,** pp. 43-60 (Chapter 3), pp. 78-93 (Chapter 5) and pp. 150-161 (Chapter 10)**.**

(23.) 11/18 (W): Tax Policy: We will discuss the various different types of taxes in the United States – Federal, state and local income taxes, social security taxes, property taxes, the capital gains and dividends taxes, and sales taxes. We will give empirical evidence on how much each of the different sources of tax revenue contribute to total revenue collection by the government and how progressive the different types of taxation are.

Readings: Thomas Piketty, **Capital in the 21st Century**, Chapters 14 and 15, pp. 493-540

Oral Report: In groups, read and report on assigned chapters of **Works Councils: Consultation, Representation, and Cooperation in Industrial Relations,** edited by Joel Rogers and Wolfgang Streek and report in section: 11/20 (F).

(24.) 11/23 (M): Social Safety Net Policy: Here we will discuss social safety net policy for the elderly such as Medicare and Social Security and well as for the poor such as Medicaid and Housing Vouchers. We will discuss the progressivity of Social Security and Medicare. We will also discuss criticisms of these safety net programs.

Reading: Rebecca Blank and Maria Hanratty (1993), "Responding to Need: A Comparison of the Social Safety Net in Canada and the United States" in David Card and Richard Freeman editors, **Small Differences That Matter: Labor Markets and Income Maintainence in Canada and the United States.**

Debate #4: In Section: 12/4 (F): What policies should we adopt to reduce inequality in the United States? (Decided upon by the groups).

Section 8: Varieties of Capitalism

(25.) 11/25 (W): Cross-country comparisons: Sweden vs. Switzerland vs. US;

Readings: Richard Freeman, **Working Under Different Rules**, pp. 1-29.

(26.) 11/30 (M): Cross-country comparisons: Sweden vs. Switzerland vs. U.S.; universalist vs. particularist policies; varieties of capitalism

Readings: Alberto Alesina and Edward L. Glaeser, **Fighting Poverty in the US and Europe: A World of Difference,** pp. 15-54.

(27.) 12/2 (W): American exceptionalism: slavery, majoritarianism (sassoon - one hundred years of socialism), cultural values and beliefs

Jonus Pontusson (2006), "The American Welfare State in Comparative Perspective: Reflections on Alberto Alesina and Edward L. Glaeser, **Fighting Poverty in the US and Europe,** *Perspectives on Politics* Vol. 4(2), pp. 315-326 and Donald Sassoon, **One Hundred Years of Socialism: The West European Left in the Twentieth Century,** pp. 137-166.

Section 9: Income Inequality and Politics

(28.) 12/7 (M): Income inequality and political inequality

Excerpts from Larry Bartels (2008), **Unequal Democracy: The Political Economy of the New Guilded Age**, pp. 252-282.

(29.) 12/9 (W): Inequality and social movements: the tea party, occupy, the communist party, organizing capital vs. organizing labor.

Ethan Kaplan and Arindrajit Dube (2012), "Occupy Wall Street and the Political Economy of Inequality", *Economist's Voice* 9(3), pp. 1-5 and Adam Bonica, Nolan McCarty, Keith Poole, and Howard Rosenthal (2013), "Why Hasn't Democracy Slowed Rising Inequality?", *Journal of Economic Perspectives*, Vol. 27(3), pp. 103-124.

Last two sections: presentation (5 minutes each) on literature review of topic related to income inequality (i.e. impact of NAFTA)

Opinion Paper: Due in section 12/11 (F).

Due Date Summary:

Empirical Assignment: Due via Elms on 9/18 (F). Use data set given to class (Saez data set on top income shares) and compute various statistical summary measures of inequality for a few different countries over time.

Debate #1: In section 9/25 (F): Utilitarianism, Marxism, Libertarianism, Rawls (four groups in section).

Newspaper Critique 1: In section 10/2 (F).

Debate #2: In section 10/23 (F): Do capital and executives deserve the returns they get?

Opinion Paper #1: In section 10/30 (F).

Newspaper Critique 2: In section 11/6 (F).

Debate #3: In section: 11/13 (F): Which is responsible for the dramatic increase in inequality? Skill-biased technical change, a slowdown in educational attainment or changes in institutions?

Oral Report: Read a chapter of **Works Councils: Consultation, Representation, and Cooperation in Industrial Relations,** edited by Joel Rogers and Wolfgang Streek and report in section: 11/20 (F).

Debate #4: In Section: 12/4 (F): What policies should we adopt to reduce inequality in the United States?

Opinion Paper 2: Due in section 12/11 (F).

Course Policies:

Please read through this section of the syllabus at the beginning of the semester and refer to it again throughout the semester, particularly in advance of exams and assignment due dates. Additional notes on assessments:

1. Department of Economics policy on grading requires instructors to use the grading system announced at the beginning of the semester in all cases and with no exceptions. There will be no opportunities for extra credit.

2. University policy regarding the circumstances in which professors are obliged to provide make-up examinations is available online at www.inform.umd.edu/ugradcat/

3. If you have questions or concerns about a grade awarded for any specific assignment, you must submit a written request for a grade review to your TA; send an email that describes your concerns in detail.

Disability Support Services: If a student has a documented disability and requires academic accommodations for test taking or other needs, please provide your TA with documentation from

Disability Support Services (301-314-7682). We are not able to accommodate students who are not registered with DSS or who do not provide the documentation at least one week in advance of exams and deadlines. Complete information about disability support services and accommodations are available online at www.counseling.umd.edu/DSS/receiving_serv.html.

Academic Integrity: The University's code of academic integrity is designed to ensure that the principle of academic honesty is upheld. Any of the following acts, when committed by a student, constitutes academic dishonesty:
• CHEATING: intentionally using or attempting to use unauthorized materials, information, electronic items, or study aids in an academic exercise.
• FABRICATION: intentional and unauthorized falsification or invention of any information or citation in an academic exercise.
• FACILITATING ACADEMIC DISHONESTY: intentionally or knowingly helping or attempting to help another to violate any provision of the University's code of academic integrity.
• PLAGIARISM: intentionally or knowingly representing the words or ideas of another as one's own in any academic exercise.

The Honor Pledge is a statement students are asked to sign on examinations, papers, or other academic assignments. The Pledge reads: I pledge on my honor that I have not given or received any unauthorized assistance on this assignment/examination.

The Code of Academic Integrity sets standards for academic integrity at Maryland for all undergraduate and graduate students. Students are responsible for upholding these standards for this course. It is very important for students to be aware of the consequences of cheating, fabrication, facilitation, and plagiarism. For more information on the Code of Academic Integrity or the Student Honor Council, please visit http://www.shc.umd.edu/SHC/Default.aspx