

**PPA 730-10: Fundamentals of Policy Analysis**  
Efficiency and inequality SOLUTIONS

**Income inequality in the 1990s**

You have been asked a prominent member of Congress why information about economic inequality appears so subjective. Why is it that, when one political party tells a story about income becoming more unequal, the other party often uses the same data to tell a different story.

Demonstrate to her what's going on by writing a very brief memo that uses the Census historic data on income dispersion (<http://www.census.gov/hhes/income/histinc/ie1.html>) to tell three stories about income inequality in the 1990s.

- A story that makes it look like inequality is getting worse.
- A story that makes it look like inequality is getting better.
- A true story that uses the data appropriately and honestly.

Years	Percent change in real income, bottom quintile of earners	Percent change in real income, middle quintile of earners	Percent change in real income, top quintile of earners
1990-1994	-3%	-3%	9%
1994-2000	14%	14%	17%
1990-2000	11%	11%	28%

**Story 1. The 1990s were a sorry time for income inequality—the rich got richer, and over a large part of the decade, the poor got poorer. In fact, it took half the decade—the longest sustained period of economic growth in U.S. history—for the bottom 20 percent of earners, and even the middle class, to stop losing real income. As usual, the only earners to make out well over the early part of the decade were the richest fifth of the population. Over the entire decade, the rich had real income gains that were two and a half times greater than those in lower income groups, widening overall inequality considerably. The poor and middle class simply did not enjoy the full fruits of economic growth in the 1990s.**

**Story 2. After a devastating recession in the early 1990s, real income growth was in full force for all income groups by the early to mid-1990s. Indeed, by the time economic recovery had settled in by 1994, the poorest and richest fifths of the populations were experiencing virtually the same growth rates in their real incomes (14 percent versus 17 percent from 1994-2000). The bottom line is that the 1990s were a time a rising prosperity for all.**

**Story 3. The 1990s were mixed in terms of income growth and inequality. As is often the case, following the recession early in the decade, the upper income brackets were quickest to recover and see real income growth. People in derivative professions (e.g. service to the higher-income professions) saw their income growth start later (by about 1994). Over the latter half of the decade, all income brackets saw roughly comparable growth, and the decade ended on an up note for all groups. The net result was that inequality increased somewhat, as the upper income groups enjoyed more years of real growth than lower income groups.**

**Wage differentials in the U.S. and India**

Many experts in international relations see the next great bilateral alliance to be between the United States and India—the world's richest and largest democracies, respectively. This alliance will fuel product and labor market needs for both countries, it is believed, and also perhaps "contain" other countries (e.g. China, Pakistan) that the U.S. and India are worried about, militarily and economically. Social theorists worry about a free exchange of products and resources between the two countries, however. One of the things they frequently talk about is the possibility that greater openness will lead to higher levels of economic inequality in both countries.

You would like to help inform this debate. Consider each phenomenon below, and say how inequality would probably be affected in the U.S. and/or India—or whether you need more information to decide. Explain each of your answers in a sentence or two.

1. (1 point) Open borders lead to “Brain Drain”: Many highly-skilled Indian scientists move to the U.S.

**High-skill labor supply falls in India, driving both high wages and inequality up.  
High-skill labor supply rises in the U.S., driving both high wages and inequality down.**

2. Rising average household incomes in India lead to an expansion of high-tech services, so the number of high-skill jobs increases there.

**High-skill labor demand rises in India, driving both high wages and inequality up.**

3. In development, India becomes a more efficient producer of crops, feeding its people and exporting more agricultural products than at present to the rest of Asia.

**It is not clear what effect this would have on inequality—we need more information.**

4. Many of America’s low-skill industries also go to India, because of greater ease in bilateral commerce between the nations.

**Low-skill labor demand falls in the U.S., driving low wages down and inequality up.  
Low-skill labor demand rises in India, driving low wages up and inequality down.**

5. Jobless Indians (mostly with low skills) in search of jobs will find it easier to immigrate to the U.S.

**Low-skill labor supply rises in the U.S., driving low wages down and inequality up.  
No affect on India, because the workers were not in the labor market in the first place.**