

Globalization and Inequality: Explaining American Exceptionalism

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Globalization creates pressure for greater inequality throughout the world, but these pressures are expressed more fully in the United States than in other developed nations. Although the distribution of US income before taxes is no more unequal than other nations, after taxes it is considerably less egalitarian. This occurs because of specific institutional arrangements that fail to redistribute income effectively and allow the pressures of globalization to be fully realized. These arrangements represent a shift from the past and were deliberately enacted over the past two decades with divergent consequences for those at the top and bottom of the socioeconomic hierarchy. The realignment of the US political economy can ultimately be traced to America's legacy of racism. Once leaders in the Democratic party sought to include African Americans in the benefits of Roosevelt's New Deal, support for economic populism evaporated in the middle and working classes. The advantage of the wealthy is further enhanced by a political system in which those with money are better able to have their interests served legislatively than the poor or working classes.

So far, the world has witnessed two great eras of globalization. The first began around 1800 when the international circulation of goods, capital, people, and resources began to grow steadily as industrialization spread across the face of Europe and hopped across to current and former colonies around the world. This first wave of globalization culminated in the first decade of the 20th century. Economic interconnections grew faster than political integration between nations, however, and the rudimentary multilateral institutions of 1914 were unable to manage the shifting balances of power, leading to a catastrophic world war. From 1914 to 1918 the world's industrial powers engaged in a wanton destruction of land, labour, and capital that left most bankrupt. World War I opened a Pandora's box of contradictory forces: the intensification of the struggle between labour and capital, the polarization of political ideology between communism

and fascism, and a retreat from liberal democracy throughout the world.

The 1920s were characterized by the rise of autarkic economic nationalism. Chauvinistic restrictions were placed on trade, investment, and immigration to curtail international movements of goods, capital, and labour. Although the global economy hobbled along for a while on the strength of wealth accumulated in the New World, it came crashing down in 1929. Following a decade of economic depression, the ideological contradictions unleashed in 1914 were partially resolved on the battlefield between 1939 and 1945, as a coalition of communist and liberal democratic states came together to defeat fascism in the Second World War.

The ending of that war did not bring about an immediate resumption of globalization, however, because of the armed standoff between liberal capitalist

democracies and communist dictatorships, with two new superpowers at the core of each block: the Soviet Union and the United States. In the west, the US took the lead in laying the foundations for a new global market economy, joining with Western Europe and Japan to charter a new and more effective set of international institutions that could guarantee international security, liquidity, convertibility, investment, and trade. Institutions such as the United Nations, the World Bank, the International Monetary Fund, the General Agreement on Tariffs and Trade, and the World Trade Organization led to a revival of international trade, first among industrialized nations and then more generally throughout the world.

Until 1990, however, globalization could not reach its full potential because of the Cold War, which cut-off roughly one-third of all humanity from the global marketplace (the combined populations of China, The Soviet Union, and their various satellites) and mired much of the rest of the world in proxy confrontations (in the countries of Asia, Latin America, and Africa). The end of the Cold War finally allowed the global economy to return to the stage of development it had reached on the eve of First World War. Since then we have witnessed an evolution toward liberal democracy among trading nations, the emergence stable international institutions, an acceleration of free trade, and a new global security regime guaranteed by the hegemonic power of the United States.

Since the 1980s, markets for land, commodities, financial capital, human capital, goods, raw materials, labour, and information have globalized as never before, and once again the resulting international flows are accompanied by rising inequality within nations. In a global economy, the demand for financial capital, human capital, land, and energy is immense while supplies are limited, driving up returns for those who possess these resources. In contrast, the demand for labour remains limited even in a global economy but the supply is immense, putting downward pressure on the returns physical labour.

As markets have globalized over the past two decades, therefore, the general trend has been toward rising levels of within-country inequality. According to Goesling (2001), the average degree of inequality within nations grew by almost 40 per cent between 1980 and 1995. Despite the universality of the trend toward greater income stratification, however, inequality has surged more in the United States than elsewhere. When Smeeding (2005) computed the ratio of the 90th to the 10th percentile of the income distribution for selected nations, he found that the US ratio of 5.45 was well above the average level of 4.0

for all nations in the Organization for Economic Cooperation and Development. The United States thus stands out among developed nations for the severity of its inequality.

Rising inequality over the past 30 years has been attributed to a variety of factors, including, in addition to globalization itself, technological change and market segmentation (Massey, 1996; Levy, 1998; Danziger and Gottschalk, 1995). Nonetheless, all countries compete in the same global economy and face the same technological and market conditions, yet the United States is unique among advanced nations in the degree to which it allows these large, macro-level forces to generate inequality. When Smeeding (2005) computed Gini indices of income inequality before and after taxes, he found that the redistribution of income was much lower in the United States than anywhere else. America's pre-tax Gini coefficient of 0.45 was only slightly above that of Sweden (0.44), Germany (0.43), and The Netherlands (0.42) and well below the values of 0.50 and 0.49 in Belgium and France. In contrast, the after-tax Gini coefficient was 0.30 or below these countries whereas in the United States it stood at 0.37.

This hyper-inequality emerged not through globalization, technological change, or market segmentation, but because of institutional arrangements specific to the United States that fail to redistribute income to the same extent as other industrial nations. Over the past several decades, the US political economy has been systematically restructured to give producers, owners, and managers the upper hand over consumers, workers, and employees. In this article, I describe the new political economy of the United States and how American markets have been transformed to produce divergent outcomes at the top and bottom of the income distribution.

The New Political Economy of Poverty

During the 1930s, Franklin Roosevelt's New Deal created a political economy that worked to the benefit of the middle and lower classes at the expense of the wealthy. Markets were regulated in the public interest to moderate their excesses and failures. A system of social insurance was created to protect ordinary citizens from periodic downturns in the economic cycle, the misfortunes of life, and dependency in old age. To fund these state responsibilities, a progressive tax system was erected to redistribute income and wealth away from the rich toward the middle and lower classes. Lyndon Johnson's Great Society took the

New Deal a step further by seeking to eliminate racism from the welfare state that Roosevelt created.

The wealthy had long opposed these redistributive policies, but until the 1960s they gained little traction politically. As long as southern states remained solidly democratic, populist, and allied with northern workers, north-eastern liberals, and western progressives, conservatives could do little more than chip away at the edges of the New Deal. More than any other factor, it was the decision to enfranchise African Americans and include them under the protections of the welfare state that broke apart the New Deal coalition and led to a political realignment that restructured the American political economy in favour of the rich and powerful (Edsall and Edsall, 1991; Lemann, 1991; Quadagno, 1994; Massey, 2005).

The passage of the Civil Rights Act of 1964 began the process of realignment. In one stroke it ended the south's traditional support for populist economic policies and transformed the former confederacy from a Democratic to a Republican bastion. Blue collar voters in the north likewise began to abandon the Democratic coalition in 1968, when passage of the Fair Housing Act threatened to integrate schools and neighbourhoods (Massey and Denton, 1993), and when affirmative action began to force blacks into white unions (Skrentny, 1996). As northern blue collar workers and southern Democrats increasingly sided with economic conservatives (Phillips, 1969) and as the Republican Party turned rightward after being taken over by southerners (Lind, 2002), the wealthy finally began to make serious headway in reversing the New Deal.

Deunionization

Despite the rise of unions under the New Deal, the labour movement never achieved the same level of prominence as in other industrial democracies (Western, 1997). Owing to the decentralized political economy of the United States, collective bargaining took place on a firm-by-firm basis rather than across industries; unemployment programmes were run by 50 states rather than the unions themselves; and labour was never able to establish its own political party. These peculiarities of the American system limited the size and influence of unions in the United States compared with other industrialized nations. Whereas levels of unionization in 1985 were above 80 per cent in Belgium, Finland, and Sweden, in the United States the level stood at just 18 per cent (Western, 1997).

The decentralized nature of the American political economy, and the barriers to union organization that

follow from it, are in no small way attributable to the unique role of race in shaping the politics and policies of the United States. The US Constitution's granting to states of all powers not specifically allocated to the federal government stemmed from the need, unique among nations that would become industrial powers, to bind slave holders and freeholders in a common political union. In writing the US constitution, southerners were determined to create a weak national government that would not be able to end slavery and impose a system of free labour on the states. The resulting fragmentation of power between states and the federal government limited the legal tools available to promote unionization compared with other industrial nations.

Even at the height of the New Deal, when southern Democrats supported progressive, pro-union policies, they did so only as long as the policies did not threaten the racial status quo, which meant that sectors of the labour market with significant black employment had to be excluded from coverage in major pieces of labour legislation (Katznelson, 2005). Because of these wholesale exclusions, levels of unionization reached their natural limit much earlier than in Europe, weakening the power of workers in collective bargaining.

The heyday of union power and influence was the period 1935–1946. After the Second World War, however, northern-based unions began to achieve unexpected success in organizing black textile and service workers in the south, and southern congressional representatives came to fear that unionization would fuel demands for civil rights (Katznelson, 2005). In response, for the first time since Roosevelt's election, populist southern Democrats deserted labour interests and joined with pro-business Republicans in the north to roll back the National Labor Relations Act and attenuate enforcement of the Fair Labor Standards Act. Although President Harry Truman denounced the legislation a 'slave labor bill', with southern support it passed over his veto (Katznelson, 2005: 67–68).

The 1947 Taft-Hartley Act represents the first breach in the walls of the New Deal and was a harbinger of things to come. It prohibited requiring union membership and dues paying as a condition of employment and outlawed secondary labour actions—banning boycotts, strikes, and picketing against firms that were not engaged in a labour dispute, but did business with one that was. It also gave federal authorities new power to issue injunctions *against* collective labour actions and *to impose* an 80-day 'cooling off period' whenever a strike was deemed to 'imperil national health or safety'. The legislation also curtailed federal authority to investigate and prosecute unfair labour

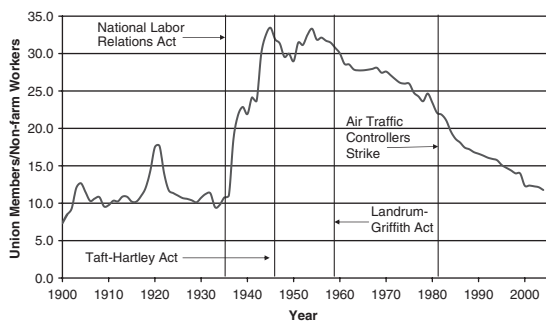


Figure 1 Level of unionization in the United States 1900–2004. *Source:* Historical Statistics of the United States Millennial Edition

practices and authorized employers to file suit against unions for monetary damages incurred during stoppages that were later determined to be unlawful under the act (Katznelson, 2005: 53–64).

In 1959 the Landrum-Griffin Act further tightened prohibitions on secondary labour actions and gave employers another tool in the fight against unionization by permitting non-union members to vote in certification and decertification elections. Employers could hire scab workers to replace those on strike and then have the scabs vote as employees to decertify the union that originally called the strike (Azari-Rad *et al.*, 2005). Together, the Taft-Hartley and Landrum-Griffin Acts took an increasing toll on the labour movement beginning in the 1960s, especially as manufacturing began to decline.

Figure 1 shows the rate of union membership in the United States expressed as a percentage of all non-agricultural workers between 1900 and 2004. Aside from a brief surge at the end of the progressive era in 1920–1921, unions achieved little success in penetrating the US workforce until passage of the National Labor Relations Act in 1935, whereupon union membership surged, more than tripling from around 10 per cent of workers in 1935 to a third of all workers just 10 years later.

With the passage of the Taft-Hartley Act in 1949, however, union membership ceased growing and then began to decline after 1959 when Landrum-Griffin strengthened the hand of employers. From a peak rate of 33 per cent in 1954, unionization fell to 23 per cent by 1980, at which time Ronald Reagan was elected to the presidency. His first year in office was pivotal, for in 1981 the union representing air traffic controllers went on strike for better working conditions and improved safety. Invoking Taft-Hartley,

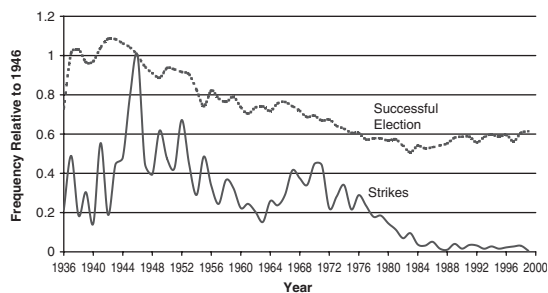


Figure 2 Relative frequency of strikes and successful union elections 1936–2000 with 1946=1.0. *Source:* Historical Statistics of the United States Millennial Edition

President Reagan declared the strike illegal and promised to fire all those who did not return to work within 2 days (Pels, 1995). He brought in replacement air traffic controllers from the military, and although flights were disrupted and air traffic reduced, the union was broken and 85 per cent of its members lost their jobs. This action sent an important message: Republicans were prepared to use all the tools available from Taft-Hartley and Landrum-Griffin to prevent public sector unionization, the only real pathway left for union expansion in the United States. After 1980, the pace of deunionization accelerated and by 2004 only 11.8 per cent of all American workers were union members, the lowest level since 1933.

As union power waned, so did the frequency and success of labour actions. Figure 2 shows frequencies of work stoppages and successful certification elections from 1936 to 2000. Each series is expressed as a fraction of its 1946 value to place trends on the same scale. In many ways, the year before passage of the Taft-Hartley Act can be considered the high point of the labour movement in the United States. Despite year-to-year volatility, the overall trend in labour actions has been steadily downward since then, with the exception of a brief period in the late 1960s and early 1970s during the Vietnam War. After Reagan's breaking of the air traffic controllers union, the frequency of strikes plummeted to near zero.

Over the same period, the frequency of successful certification elections steadily dropped. Whereas in the 4 years prior to the air traffic controllers strike of 1981, an average of 8,600 union certification elections were held each year, by the late 1990s the number had fallen to around 3,400; and as the number of union elections fell, so did the success rate. Until 1946, unions routinely won 86 per cent of their certification

elections. From peak success rates above 80 per cent in the 1940s, the rate fell to a nadir during the Reagan administration, when unions won just 40 per cent of certification votes.

Falling levels of unionization translate directly into lower wages. Holding constant a variety of job and worker characteristics, studies indicate that union jobs pay around 15 per cent more than non-union jobs (Freeman and Medoff, 1984; Robinson, 1989; Card, 1996) and as rates of unionization have declined, so has the share of workers enjoying this earnings premium, pulling down average wages. In addition, with unionization no longer viewed as a credible threat by employers, they had little incentive to pay workers higher wages as an inducement not to form a union. Studies reveal that in the past the threat of unionization boosted the wages of all workers, even those who were not union members (Freeman and Medoff, 1984; Leicht, 1989; Neumark and Wachter, 1995; Corneo and Lucifora, 1997; Rosenfeld, 2006b).

As a result, there is a strong positive relationship between the frequency of strikes and the wages earned by workers in the United States (Ashenfelter and Johnson, 1969; Ashenfelter *et al.*, 1972; Kalleberg *et al.*, 1984). The breaking of the air traffic controllers union in 1981 effectively ended the perception of unionization as a threat by employers and led to a ‘complete decoupling of the wage-strike relationship’ (Rosenfeld, 2006a). By the dawn of the new millennium, unions were no longer a significant institutional player in determining the wages and employment conditions for workers in the United States.

Minimizing the Minimum Wage

Specific policy decisions made by the US congress and the American president in 1947, 1959, and 1981 to weaken labour’s bargaining position had their desired effect. Without the collective power of unions behind them, workers moved out of the middle of the income distribution and downward toward its lower reaches. Benefits also disappeared as wages fell steadily toward the legal minimum, a benchmark that itself came under increasing attack from conservatives. As Figure 3 shows, through its actions and inactions congress progressively reduced the real value of the minimum wage to a level that is presently the lowest since the 1940s.

The golden age of the minimum wage was from 1948 to 1968, when in real terms it steadily rose from around \$3.50 an hour to peak at \$9.20 during the height of the President Lyndon Johnson’s Great Society. As inflation increased during the late 1960s

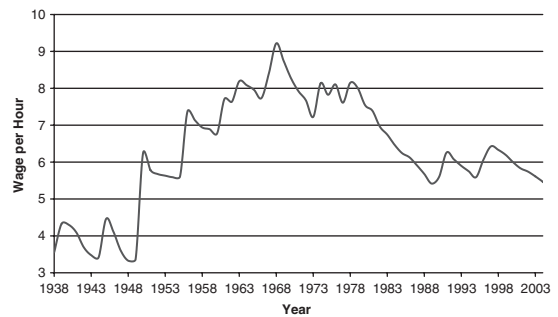


Figure 3 Real value of the US minimum wage (in 2002 dollars) 1938–2004. *Source:* U.S. Bureau of Labor Statistics

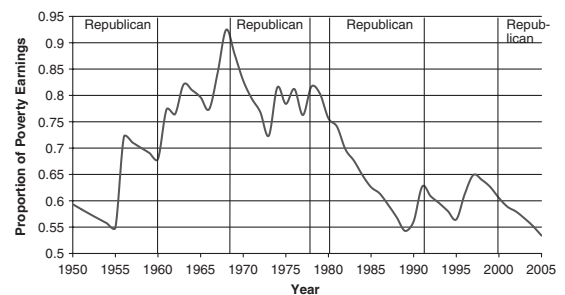


Figure 4 Earnings for a full-time minimum wage job as a share of poverty earnings for a family of four. *Sources:* U.S. Bureau of Labor Statistics and Statistical Abstract of the United States

and early 1970s, however, congress declined to adjust the minimum wage and in real terms its value fell sharply, reaching \$7.20 during the Nixon administration before stabilizing in the Ford and Carter years. With the accession of the Ronald Reagan to the presidency after 1980, the minimum wage resumed its race toward the bottom, reaching a value of just \$5.40 in 1989. After fluctuating around \$6.00 per hour during the Clinton years, the wage declined once again under President George W. Bush to end at \$5.30 in 2005, the lowest level since Taft-Hartley passed in 1949.

Figure 4 illustrates the effect of these wage reductions on the welfare of families supported by low wage workers using government data compiled by Smith (2006).¹ Specifically, it computes how much income is earned by working full time (38.5 h/week) for a full calendar year (52 weeks) and expressing the result as a share of the official poverty level for a family of four. As can be seen, never in the course of the past 50 years has the U.S. minimum wage been sufficient to lift a

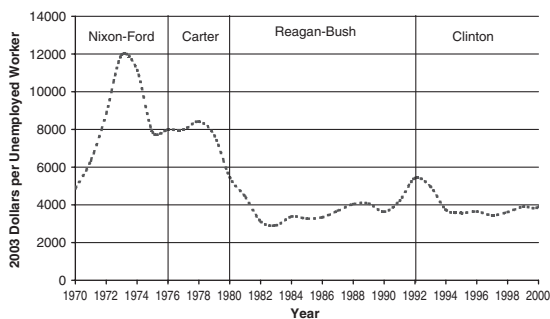


Figure 5 Spending on unemployment benefits per unemployed worker. *Source:* Statistical Abstract of the United States

family with one breadwinner out of poverty, although during Johnson's Great Society it came close. In 1968, a minimum wage worker employed full time would generate annual earnings equal to around 93 per cent of the federal poverty limit.

The figure has been labelled to show Republican versus Democratic administrations. After the 1960s, Republican administrations are very clearly associated with falling minimum wages whereas Democratic administrations are associated with steady, fluctuating, or rising minimum wages. A more comprehensive and well-controlled analysis by Bartels (2004) showed that Republican presidents indeed produce greater income growth for rich than poor families, and that rising inequality is reliably associated over time with Republican administrations.

Dismantling Safety Nets

Although declining rates of unionization and a falling minimum wage may have lowered the wages of workers after the 1960s, in a sense they were the lucky ones, for despite their reduced earning capacities at least they had jobs. After the 1970s, as the earnings of workers stagnated in response to legislated changes in the US political economy, the safety nets erected by the New Deal to catch those falling out of the labour market were cut back through reductions in funding and coverage. Figure 5 shows per capita spending on unemployment insurance from 1970 through 2000. During the early 1970s unemployment benefits steadily rose based on momentum carried over from the Great Society, going from \$4,900 per unemployed worker in 1970 to \$12,000 per unemployed worker in 1973. During Nixon's second term (completed by Gerald R. Ford) benefits were cut back before stabilizing at around \$8,000 per unemployed worker during the first

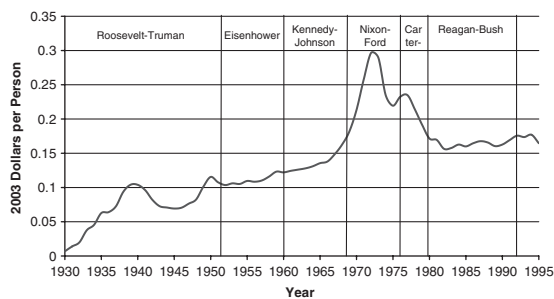


Figure 6 Per capita public spending on social services for the poor 1930–1995. *Source:* Historical Statistics of the United States Millennial Edition)

half of the Carter administration. As inflation eroded the value of unemployment benefits during the late 1970s and early 1980s, real spending on unemployment benefits plummeted. With the exception of a brief period during 1993–1994, spending on unemployment has remained below \$4,000 per unemployed worker since the early 1980s.

Unemployment insurance payments are time-limited, and once eligibility is used up families must fall back on other forms of relief. Figure 6 shows real per capita spending on social services on the poor from 1930 to 1995 in constant dollars.² From virtually nothing before 1932, the Roosevelt administration increased spending on the poor to around 10 cents per capita by 1940. Although expenditures on behalf of the poor fell during the Second World War they rebounded after 1945 and funding remained at around 10 cents per capita during Eisenhower administration.

During the Great Society spending on social services for the poor soared and the legislation enacted by President Johnson carried this acceleration well into the Nixon administration. From a per capita level of around 12 cents in 1960, spending on anti-poverty programmes more than tripled to peak at 30 cents in 1972 before falling precipitously during Nixon's second term. The free-fall in poverty-related social services was checked early in the Carter administration but then resumed during the inflation of the late 1970s as Congress failed to make adjustments to transfers to reflect the rising cost of living. Throughout the presidencies of Ronald Reagan and George H. W. Bush anti-poverty spending remained flat, only slightly above the level it had been on the eve of the Great Society, a level that persisted through the early years of the Clinton administration.

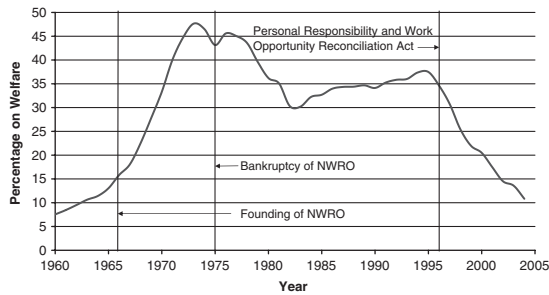


Figure 7 Percentage of poor families receiving AFDC or TANF. Sources: Historical Statistics of the United States Millennial Edition and U.S. Bureau of the Census

Thus, in terms of social spending on the poor, by the early 1990s it was as if Johnson's War on Poverty had never happened. Even this reduced level of spending on the poor was too much for conservatives in Congress, however, who in 1996 succeeded in passing the Personal Responsibility and Work Opportunity Reconciliation Act, essentially forcing mothers of dependent children off of welfare rolls and into the labour force by ending the entitlement to open-ended income transfers. Aid to Families with Dependent Children (AFDC) was replaced by a new programme called Temporary Assistance to Needy Families (TANF), which gave mothers only 2 years of assistance before requiring them to work. According to the terms of the legislation, 25 per cent of all families were supposed to leave the welfare rolls by 1997, with 50 per cent expected to be working by 2002.

As indicated by Figure 7, which depicts the percentage of poor families receiving AFDC or TANF benefits by year, the effect of the new law on welfare use was sudden and dramatic. Historically, the rate of welfare use in the United States had been low because congress wrote the Social Security Act to exclude black workers and delegate to states the right to determine eligibility. Given the over representation of African Americans among the poor and the disproportionate location of all poor families in southern states with stringent eligibility requirements and low payments, only a tiny fraction of the poor actually received welfare before the 1960s. Indeed, until 1965, the share of poor families receiving income transfers ranged only from 10 per cent to 15 per cent.

The passage of civil rights laws and other federal reforms during the Great Society made it more difficult for states to deny relief to poor families, and in 1966 the National Welfare Rights Organization was

formed to organize poor minority women, get them to apply for AFDC, and go to court if necessary to force reluctant state officials to honour entitlements (Katz, 1986). At its peak, the NWRO had around 30,000 members, mostly poor, black women with dependent children, and the organization's militant tactics indeed overcame the administrative deterrents to enrolment (Piven and Cloward, 1977).

As a result, the number of women on welfare increased dramatically after 1965. Figure 7 shows that the share of poor persons supported by AFDC jumped from around 15 per cent in 1966 to 48 per cent in 1973. As Richard Nixon scaled back the War on Poverty and reduced federal funding for anti-poverty organizations such as the NWRO, the movement experienced financial difficulties and in 1975 it was forced into bankruptcy (Abramovitz, 2000). In the wake of the NWRO's collapse, the share of poor women receiving AFDC fell to 30 per cent in 1982 before levelling off and slowly rising back up to 36 per cent in 1995.

Although the demise of the NWRO brought about a decline in the rate of welfare usage, the situation did not return to the status quo ante. The welfare rights movement had raised awareness of entitlements among poor women and welfare use remained at more than twice its pre-1965 level. Ironically, however, the very success of the NWRO laid the foundations for the ultimate demise of AFDC as a programme, for after 1965 welfare came to be irrevocably associated in the public mind with poor, African American women, who were portrayed in political rhetoric and the media as undeserving, irresponsible 'welfare queens' who bore children out of wedlock to increase the size of AFDC payments and prosper at the expense of overburdened taxpayers (Neubeck and Cazenave, 2001). Through such racialized portrayals, in their minds the public came to overestimate the cost of the welfare system and the representation of black women within it, causing AFDC and related entitlements to become increasingly unpopular with white voters (Gilens, 1999, 2003).

Having gained control of both houses of Congress in 1994, Republicans translated this public animus against welfare into legislation. The 1996 Personal Responsibility and Work Opportunity Reconciliation Act was a self-proclaimed effort to 'end welfare as we know it' and as is obvious from Figure 7, the effect on usage rates was immediate and profound. From a figure of 36 per cent in 1996 the share of poor families receiving federal income transfers fell sharply to reach just 10 per cent in 2004, a level of welfare utilization last observed in 1963. Along with the decline in welfare

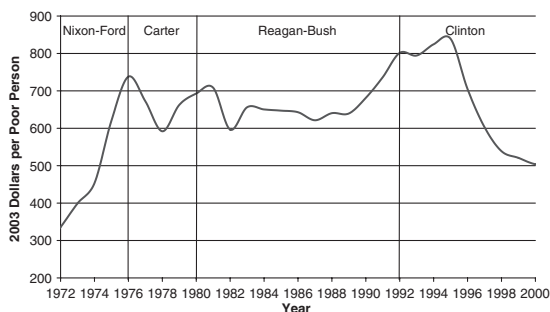


Figure 8 Real per capita spending on food stamps 1970–2002. *Source:* Statistical Abstract of the United States

receipt came a drop in spending for other entitlements that were tied to it, such as food stamps. As shown in Figure 8, real expenditures for food stamps fell dramatically as the new welfare policy pushed women off of welfare and into ineligibility for food assistance. Whereas federal spending on food stamps totalled \$840 per poor person on the eve of welfare reform by 2000 the figure had fallen to just \$500, about the same amount spent just after the programme’s founding in 1973. The decline in welfare receipt and income transfers did not stem from a drop in the rate of poverty, but from the systematic shifting of poor women away from public supports. In essence, poverty was privatized as poor mothers were forced into the labour force and made to bear the full cost of their meagre lives.

The foregoing trends are emblematic of broader shifts throughout the American political economy that have undercut income supports available to families at the lower end of the class hierarchy (Scholz and Levine, 2001). Since the 1970s the only forms of social spending that have reliably increased in real terms are those associated with the elderly. While spending on medicare and old age survivor’s insurance steadily increased, funding for supplemental security income, low income housing, early childhood education, food supplements for women and infants, and the school lunch programme remained flat (Scholz and Levine, 2001). The only anti-poverty funding that increased in real terms is that for Medicaid, the medical insurance programme for the poor, which does not stem from rising state generosity toward those with limited means but more from the mandatory provision of emergency and stopgap medical services to the rising number of Americans who lack private health insurance.

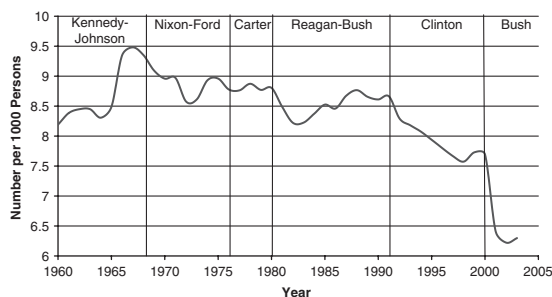


Figure 9 Non-defence government workers per 1000 population. *Source:* Historical Statistics of the United States Millennial Edition and Statistical Abstract of the United States

Downsizing Federal Employment

For many poor minorities, the public sector historically has served as an employer of last resort, and federal employment has been particularly important as an anchor for the black middle class (Landry, 1987). For this and other reasons a long-cherished dream of conservatives has been to shrink the size of the federal government to the point where, in the words of one Republican strategist, it could be ‘drowned in the bathtub’ (Massey, 2005). Figure 9 shows the number of non-defence federal employees per 1000 persons in the United States. In relative terms, the high water mark of federal employment came during Lyndon Johnson’s war on poverty, when the number of federal workers per 1000 rose from around 8.5 to 9.5. The number then declined during the Nixon and Ford administrations and stabilized at around 8.8 workers per 1000 under President Jimmy Carter.

The decline in federal employment resumed during the first Reagan administration, but then recovered somewhat before experiencing a sustained decline over the course of the two Clinton administrations. The election of George Bush in 2000, however, brought an unprecedented assault on federal employment and the number of federal workers per 1000 fell to a record low of 6.2 within 2 years of his assuming office, the fastest drop in federal employment in American history. In relative terms, the federal government is now smaller than at any point since 1940, reflecting its reduced capacity for managing and regulating the US political economy.

The New Debtors

Falling rates of unionization, a declining minimum wage, reduced welfare coverage, falling income

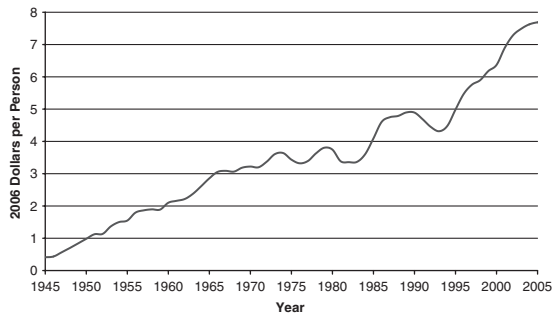


Figure 10 Per capita consumer debt 1945–2005. *Source:* U.S. Federal Reserve

transfers, and declining federal employment have placed families in the lower portion of the income distribution in very precarious circumstances. Living so close to the edge of financial solvency on a daily basis, Americans are increasingly vulnerable to negative income shocks caused by illness or injury, the loss of a job, a reduction in work hours, or some other family emergency. For the rising share of Americans who lack health insurance, in particular, a visit to a hospital can quickly overwhelm household finances to create an acute financial crisis.

When funds coming into a family budget cannot cover current spending, in the absence of government transfers the only way to make ends meet is through private borrowing, and in recent years Americans have accumulated unprecedented levels of debt, most commonly by running up balances on credit cards in a desperate effort to make it from 1 month to the next. Contrary to popular belief, most families become mired in consumer debt not because of frivolous shopping sprees, but in response economic shocks lying beyond their control—family emergencies that force them into a downward spiral of debt and borrowing (Manning, 2000; Sullivan *et al.*, 2000; Warren and Tyagi, 2003).

Figure 10 shows trends in per capita consumer debt from 1945 to 2005. Up through the mid-1970s, per capita consumer debt rose at a steady pace of around 10 cents per year in real terms, going from around \$0.40 in 1945 to \$3.40 in 1975. With high rates of inflation and interest in the late 1970s and early 1980s, however, consumer borrowing slowed, but then accelerated once again in the late 1980s. After a lull in the early 1990s, borrowing grew at an unprecedented and breakneck pace after 1993, increasing by around 25 cents per year through the year 2005, when per capita consumer debt approached a record level of \$8 per person, or \$2.3 billion in the aggregate.

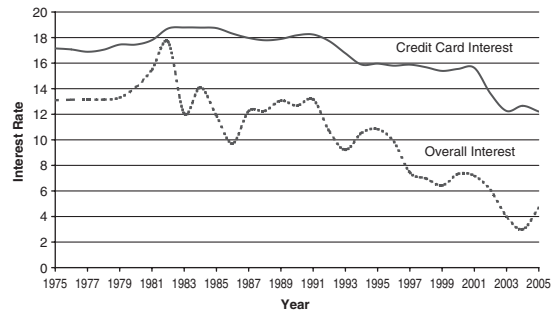


Figure 11 Interest on credit card debt versus overall interest rates 1975–2005. *Source:* U.S. Federal Reserve

Much of this debt is held in revolving credit card accounts whose interest rates have steadily risen in real terms as the total amount owed has increased, generating immense profits for banks. Figure 11 plots the average interest rate charged on credit cards compared with the interest rate prevailing in the rest of the economy. As can be seen, the gap between the two series was relatively narrow during the 1970s, averaging only 4.4 percentage points. Over the course of the 1980s and 1990s, however, the gap steadily widened, which means that in real terms credit card lenders were earning more money per dollar loaned. Thanks to the deregulation of banking, during the period 2000–2005 the average gap between the interest rate on credit cards and the prevailing rate averaged 8.2 percentage points.

The rising mountain of consumer debt is not without risks to banks, of course, for despite high interest rates and record profits if the debt becomes too burdensome to sustain, credit card holders might simply walk away from their obligations by declaring bankruptcy. Historically, bankruptcy laws in the United States were quite lenient, allowing consumers to go to court and wipe away most of their credit obligations and begin their financial lives afresh. For bankers left with the unredeemable loans, however, this act represented an ‘abuse’ of the bankruptcy system and at their behest Congress in 2005 passed the ‘Bankruptcy Abuse Prevention and Consumer Protection Act’.

The law placed new barriers on the road to bankruptcy and forced struggling consumers to pay down more of their accumulated debt. After 2005 debtors were obligated to undergo ‘credit counseling’ in a government-approved programme before being allowed even to file for bankruptcy and then once a filing had been made, to pay all back taxes before being allowed to proceed. The new law eliminated automatic

stays in eviction proceedings, license suspensions, divorce proceedings, and child support cases and for the first time it applied a means test to filers. After 2005, those debtors whose monthly income fell above the median in their state had to continue making payments to creditors based on a strict expenses-to-income formula (Henry, 2006). Henceforth families that got into financial trouble by accumulating large debts would have a much harder time starting over, no matter what the reason for their insolvency. The country may not yet have returned to debtors prisons, but the new law clearly moves it in the direction of indentured servitude.

The Political Economy of Affluence

As the political economy of poverty has become steadily more unforgiving over the past several decades, the political economy of affluence has moved in the opposite direction. As political leaders rewrote the rules of the American market to reduce the bargaining power of labour, lower the minimum wage, curtail social safety nets, limit transfer payments, constrict public employment, and make debt more expensive to acquire and difficult to escape, they also rewrote the rules of the economic game to make life easier for the affluent by reducing their financial obligations in support of the public good. This restructuring was achieved, first and foremost, by dismantling the system of progressive taxation that had been created during the New Deal and shifting the tax burden from rich to poor.

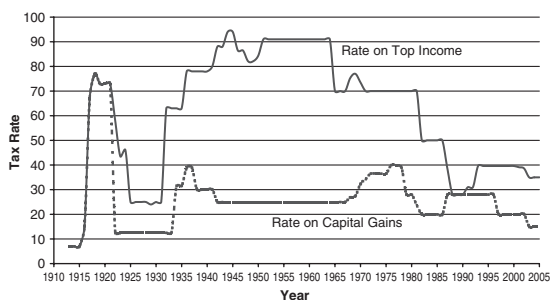


Figure 12 Top marginal tax rates and capital gains tax rates 1913–2005. Sources: Historical Statistics of the United States Millennial Edition and Statistical Abstract of the United States

Shifting the Tax Burden

The federal income tax was first authorized in 1913 by the 16th amendment to the US Constitution. Figure 12 summarizes the history of federal income taxation by showing the top rate on regular income and the overall rate on capital gains (profits realized from the sale of assets). Initially, the top tax rate was set at 7 per cent and there was no differentiation between earned income and capital gains. When the United States entered the First World War top tax rates climbed dramatically, going to 15 per cent in 1916, to 67 per cent in 1917, and reaching 77 per cent in 1918, again with no differentiation between capital gains and regular income. The end of the war brought a slight reduction in taxes, with the top rate falling to 73 per cent until 1922 when a Republican administration and congress lowered the top rate to 58 per cent before easing it steadily downward to 44 per cent in 1923 and 25 per cent in 1924, where it remained until the election of Franklin Roosevelt in 1932. At the same time, beginning in 1922 congress also differentiated capital gains from regular income, reducing the rate of tax on gains from the sale of assets such as stocks and bonds to just 12.5 per cent.

The advent of the New Deal revolutionized American tax policy by introducing a progressive system that taxed additional income at steadily higher rates as earnings rose. From 1932 through 1935, the wealthiest Americans paid 63 per cent on regular income over \$1 million and the tax on capital gains rose from 12.5 per cent to 31.5 per cent. During the remainder of the 1930s the top tax rate rose to 78 per cent and that on capital gains increased briefly to 39 per cent before falling back to 30 per cent in the last years of the decade. In the political economy of the New Deal, in other words, those with the most resources were expected to shoulder the lion's share of payments toward the collective good.

Although the capital gains tax fell to 25 per cent beginning in 1942, the top tax on income went to 94 per cent during 1944 and 1945 to finance the war effort. Beginning in 1951 and continuing through 1964 the top tax rate stabilized at 91 per cent and the rate on capital gains held steady at 25 per cent. A tax cut in 1965 reduced the top rate to 70 per cent, but President Johnson soon found he had to raise taxes upward to finance the Vietnam War. During 1968–1970 the top tax rate rose briefly to 77 per cent before falling back to 70 per cent again in 1971. In the end, the war was financed more by an increase in the capital gains tax, which rose steadily to peak at 40 per cent in the late 1970s before being scaled back to 20 per cent.

Ronald Reagan was elected in 1980 on a campaign pledge of cutting taxes, which he proceeded to do with alacrity upon assuming office. Over the course of his presidency, the top tax rate was more than halved and by the time he left office the top rate for both income and capital gains both stood at just 28 per cent, the lowest point since Roosevelt was first elected. In 1991, however, his successor George H. W. Bush famously broke his pledge not to raise taxes and raised the top tax rate from 28 per cent to 31 per cent. Although modest in size, this increase was enough to cost him the election, though under his successor Bill Clinton things the wealthy fared even worse as Clinton raised to top rate to 39.6 per cent. Vowing not to repeat the mistake of his father, George W. Bush entered the White House with a firm commitment to cut taxes and the top rate was reduced to 35 per cent and the rate on capital gains to just 15 per cent, with more cuts proposed for the future.

Clearly, since 1980 taxes paid by the wealthiest Americans have been substantially reduced. The data in Figure 12 are incomplete, however, because they refer only to income taxes and exclude payroll taxes, which constitute a large share of the burden for most Americans. The two principal payroll taxes are social security (6.2 per cent of earned income) and medicare (1.45 per cent). Moreover, whereas the medicare tax applies to all earned income, the social security tax only applies up to an income ceiling that in 2005 stood at \$90,000. Earnings over this amount were not subject to the 6.2 per cent social security tax, which means that the burden of supporting social security falls disproportionately on poor and middle income families.

In terms of social security, the greater the income above \$90,000, the lower the average tax rate, which is the relative share of income that people contribute

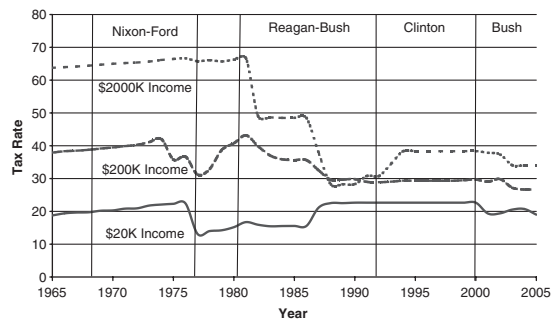


Figure 13 Effective tax rates for household earning \$20,000, \$200,000, and \$2,000,000 per year. *Source:* Author's calculations

given payroll taxes and whatever progressivity is built into income taxes. Figure 13 shows average tax rates estimated for households at three levels of income from 1965 to 2005 (expressed in constant 2005 dollars): \$20,000 (roughly the poverty level for a family of four), \$200,000 (an affluent household), and \$2 million (a wealthy household). Despite some fluctuations, the progressivity built into the tax system during the New Deal persisted through 1980 as wealthy taxpayers consistently paid around two-thirds of their income in taxes compared with 30–40 per cent among affluent families and 10–20 per cent of poor families. By design, those with the most income at their disposal contributed more to the common good than others.

This progressivity largely evaporated during the Reagan and Bush years, with the average tax rate for wealthy households going from around 67 per cent to 28 per cent in just 8 years. Given an income of \$2 million, this shift yielded tax savings of around \$780,000 *per year*. Although affluent households saw their average tax rate drop as well, the change was considerably more modest, going from around 41 per cent in 1980 to around 29 per cent in 1988. The poor, meanwhile, saw their tax burden *rise* under President Reagan, with the average rate after 1986 going from around 16 per cent to around 23 per cent.

With respect to net after tax income, therefore, the changes introduced under Reagan dramatically increased the take home pay of the wealthy, modestly increased that of the affluent, and actually lowered that of the poor. Despite the political price he paid in the 1992 election, moreover, George H. W. Bush's tax cut had little real effect on the average tax rate of the wealthy, raising only slightly. It was Bill Clinton who restored a modicum of progressivity to the system, raising the average tax rate to nearly 40 per cent for wealthy households while leaving the rates paid by affluent and poor household about the same.

Most recently George W. Bush's tax cuts reduced the average rate for all three classes, but progressivity was substantially reduced compared with the Clinton years and the burden of paying for government was shifted downward in the income distribution. As of 2005, poor households paid around 20 per cent of their income in taxes, affluent households paid 27 per cent, and wealthy households paid 34 per cent—not quite the bonanza for the rich achieved at the end of the second Reagan administration, but a far cry from the progressive taxation that prevailed from 1932 to 1980 under arrangements set by the New Deal.

Not only have taxes for the wealthy been dramatically reduced since 1980, but also federal enforcement

efforts have shifted away from their historical focus on the rich (who make most of the money, pay most of the taxes, and have the greatest incentive to cheat, therefore) as IRS auditing efforts have been redirected toward the poor. Whereas 11.4 per cent of taxpayers with incomes over \$100,000 were audited in 1988, only 1.2 per cent of such people were audited in 1999. In contrast, the percentage of audits done to taxpayers with incomes under \$25,000 *rose* slightly, going from 1.0 per cent to 1.4 per cent over the same period (Phillips, 2002: 327). At the end of the 20th century, in other words, a household with an income barely above the federal poverty level was more likely to be audited for tax compliance than an affluent household earning more than twice the median income.

Buying Political Influence

As the foregoing sections indicate, the political economy of the United States has been radically transformed to benefit the rich at the expense of the poor and middle classes. The egalitarian capitalism that prevailed from 1935 to 1975 has been replaced by a stratified political economy characterized by an unprogressive tax structure, regressive tax enforcement, and a shrunken state that is no longer capable of regulating the American political economy in the public interest. An obvious question is how policies that so obviously benefit the few have been implemented and ratified in an electoral system ostensibly controlled by the many.

The simple answer to this question is that money talks and politicians listen. In the contemporary political economy of the United States, wealthy donors provide politicians with the money they need to get elected. Around \$3 billion was spent on electoral campaigns during the year 2000 (Public Campaign, 2003). In the 2002 elections, less than one-tenth of 1 per cent of all Americans accounted for 83 per cent of all campaign funds expended (Ivins and Dubose, 2003). Among donors to congressional elections in 1996, one study found that 20 per cent had incomes of \$500,000 or more; 26 per cent had incomes of \$250,000–\$500,000; and 35 per cent had incomes of \$100,000 to \$250,000; but only 5 per cent had incomes under \$50,000 (Phillips, 2002).

Given these numbers, it is hardly surprising that policies enacted by politicians favour the class interests of those whose financial largesse is responsible for their continuation in public office. When Gilens (2005) used national surveys between administered between 1981 and 2002 to determine the policy preferences for poor, middle class, and affluent voters, he found that on

issues where preferences differed by class, legislative outcomes were strongly associated with the preferences of the affluent, had a weak relationship to those of the middle class, and bore no relationship at all to the opinions of the poor. Likewise, in his analysis of roll call votes in the U.S. Senate, Bartels (2005) found that senators were significantly more responsive to the views of affluent constituents than to those of the middle class and that the political views of the poor had no effect at all on voting patterns. He also found that Republican senators were more than twice as responsive as Democrats to the political views of affluent constituents. Rather than honouring than the ideal of ‘one person one vote’ the political system of the United States has increasingly shifted to a *de facto* policy of ‘one dollar one vote’.

Although the concentration of wealth and income have clearly played an important role shifting the political economy rightward in recent years, the influence of money by itself does not account for all of the change, for as America has grown more unequal economically, it has also become more polarized politically. Over the past several decades, Democrats and Republicans have increasingly split along ideological lines in ways that have little to do with economic equity, differing fundamentally on issues such as sexuality, religion, feminism, patriotism, and, as always in the United States, race. It is the ability of these cultural concerns consistently to trump economic self-interest that has prompted liberals such as Thomas Frank (2004) to ask plaintively ‘What’s the Matter with Kansas?’ and Paul Krugman (2003) to lament the nation’s ‘the great unraveling’.

Over the course of the 20th century ideological polarization and income inequality have moved hand-in-glove. Both fell beginning in the 1930s, bottomed out in the 1960s, and rose again after the middle 1970s. McCarty *et al.* (2006) used detailed data on congressional voting behaviour to derive a quantitative measure of political polarization between the parties. On a year-to-year basis, from 1947 to 2003 they found a very strong temporal correlation of 0.94 between the Gini index for income inequality and the index of political polarization.

Over the longer term, from 1913 to 2000 the correlation between ideological polarization and the share of income earned by the top 1 per cent of the population was 0.78 (McCarty *et al.*, 2006). Figure 14 reproduces McCarty *et al.*’s graph to show the timing of trends in income inequality and ideological polarization over the 20th century. It is clear from the figure that from 1930 until around 1960 declines in ideological polarization *preceded* declines in

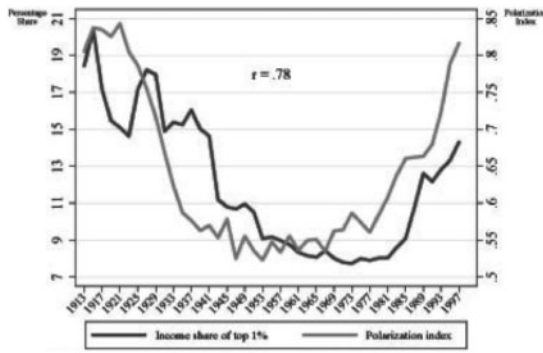


Figure 14 Top 1 percent income share and house polarization. *Source:* From pikotty and Swez (2001). Used by permission

economic inequality. Republicans grew more liberal and increasingly supported redistributive policies that reduced inequalities with respect to income while voting for programmes that mitigated the concentration of wealth.

During the 1960s, however, something happened to reverse this pattern. Income inequality and political polarization both reached low levels and somewhere in the middle of the decade there was a structural shift and the two trend lines crossed. Polarization turned upward decisively beginning in 1969, followed by income inequality around 1979. After 1969 increases in political polarization *preceded* increases in income inequality, turning the historical pattern on its head. The obvious explanation for the 'structural shift' of the 1960s is the definitive turn of the Democratic Party toward civil rights.

As soon as the Democratic Party committed itself to dismantling Jim Crow in the south, combating *de facto* segregation in the north, and deracializing New Deal programmes throughout the nation, southern and blue collar support for the New Deal's populist economic agenda evaporated. Southerners bolted the Democratic Party to push the Republican Party rightward and engaged in a systematic ideological campaign to reverse the progressive policies of the 1930s. According to McCarty *et al.* (2006), the relationship between income inequality and political polarization represents a complex choreography, a 'dance of ideology and unequal riches' in which polarization inhibits support for redistribution, which produces greater inequality, which feeds more polarization, which generates even more inequality.

They argue that power of this choreography has been exacerbated by an increase in the number of poor

people without political rights, who cannot vote, and thus cannot exert political pressure from the bottom in support of redistributive policies. They point to the post-1965 revival of immigration and note that the correlation between the percentage foreign born and political polarization is 0.92. The current potential for polarization and inequality is even greater than they suppose, however, for they do not take into account the huge increase in the share of immigrants who are not only foreign (and therefore cannot vote) but also undocumented (and therefore have no rights at all). Political polarization also follows directly from the mass incarceration of black men (Patillo *et al.*, 2004).

All but three US states practice some form of felon disenfranchisement with respect to voting. Aside from Maine, Utah, and Vermont, all states and the District of Columbia prohibit prisoners from voting during their incarceration. In addition, 29 states forbid convicts on probation from voting; 32 prohibit convicts on parole from voting; and 15 ban ex-felons from voting even after they have served their time (Sentencing Project, 2006). The rising share of ex-cons in the black population has thus significantly reduced the number of poor people eligible to vote (Uggen and Manza, 2004).

American Exceptionalism

As the foregoing analysis has shown, over the past 40 years class lines have substantially been redrawn in the United States. The Democratic Party's support for the civil rights movement and its attempt to deracialize the welfare state created an opening for conservatives to reverse ideological trends set in motion during the 1930s. The decision by the Democratic Party to embrace civil rights in the 1960s promoted a mass exodus of southerners from the party, estrangement from blue collar voters in the north, and the end of the New Deal coalition. On the heels of this realignment, the rules of the American political economy were rewritten to favour the rich at the expense of the middle and lower classes. Unions were weakened, entry level wages reduced, access to social protections curtailed, anti-poverty spending cut back, and taxes on lower income families were raised while those on upper income families were reduced, yielding a sharp reduction in the size of the welfare state and a significant decline in the social well-being of most Americans.

Although globalization may have produced rising pressures for inequality throughout the world, only in the United States have these pressures been allowed to

be expressed so fully and the resulting inequality allowed to persist without redress. The United States is exceptional among developed nations for the amount of inequality it tolerates. The conundrum is why policies that benefit, at most, 20 per cent of the population have been allowed to move forward in a democratic republic where the rest of the 80 per cent have a regular opportunity to vote for alternative policies more in line with their material interests. This article suggests two answers to that question. The first is the rising role of money in American politics and the shift from a system of 'one person, one vote' to a new politics of 'one dollar, one vote'. The second is the legacy of race, which continues to divide poor, working class, and middle class Americans from one another and deliver their political support to politicians who serve the powerful, wealthy, and affluent. As always, America's heritage of racism render it unique among developed nations and quite exceptional in how it has responded to the inequality-producing pressures that inevitably arise from globalization.

Notes

1. I thank Courtland Smith of the Department of Anthropology at Oregon State University for making available statistics he compiled for his Website on Poverty and Inequality.
2. The social services included in the tabulation include AFDC, General Assistance, WIC, WIP, and other services targeted to low income Americans.

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