Pulling Apart:

Wisconsin's Strong 1990s Growth Masked Growing Inequality

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Wisconsin could lose its standing as one of the most economically equal states in the nation. Despite our strong economic growth and tight labor markets in the late 1990s, income disparity is greater than it was two decades ago. Recent analysis by the Economic Policy Institute and the Center on Budget and Policy Priorities, shows that from the late 1970s (1978-1980) to the late 1990s (1998-2000), the average real income of the lowest-income families in the state grew by just three percent, while the average real income of the highest-income families in the state grew by 38 percent.

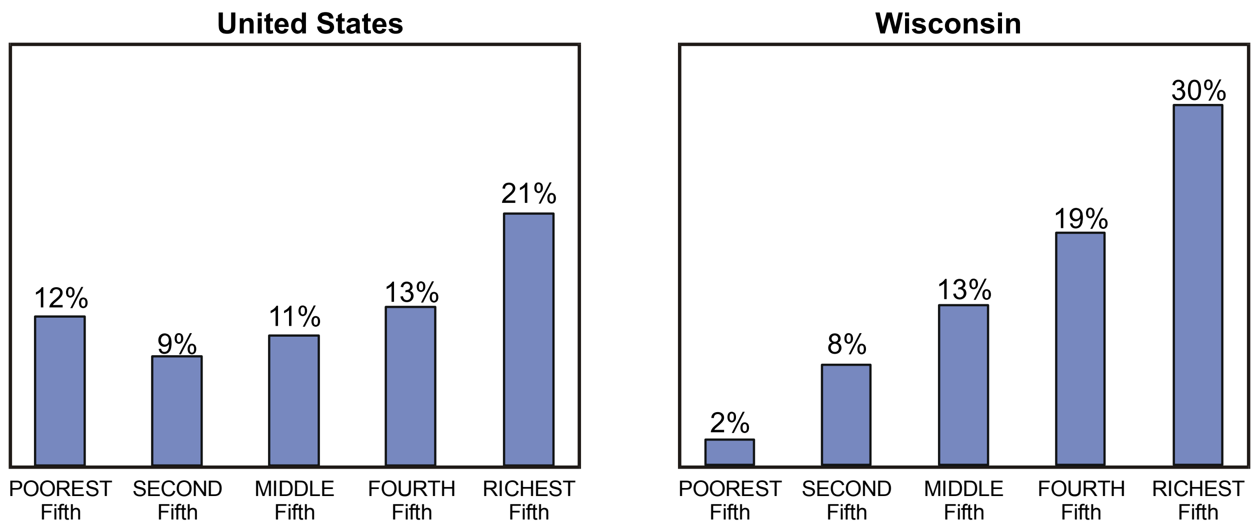
While the data available still leave out the current recession, it is very unlikely that the downturn will turn around the trend towards increasing inequality. In fact, it appears that most lay-offs have occurred at the bottom of the labor market not the top; if so, income inequality will only grow further during the recession.

Wisconsin's *recent* surge in inequality is particularly noteworthy. In the state, income inequality grew slowly in the 1980s; it is the 1990s when inequality surged. The income of our poorest families grew just two percent while the income of the richest families grew 30 percent. As Figure 1 makes clear, Wisconsin's recent growth in inequality far outstrips the national trend.

Wisconsin has traditionally prided itself on its relatively high level of equality, and it still can. Even with this growth in inequality, only nine states have a more equal distribution of income. However, our position relative to other states will continue to decline as long as inequality in the state grows so rapidly.

Figure 1

Booming Economy, Rising Inequality
Income Change Late 1980s to Late 1990s, by Income Quintile



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2002.

Pulling Apart: A State by State Analysis of Income Trends, issued April 23, 2002, by the Economic Policy Institute and the Center on Budget and Policy Priorities analyzes trends in income and inequality within each state over the last two decades.[1] Using Current Population Survey data from U.S. Census Bureau, they track earnings changes for households (two or more related people living together) in each income "quintile" (20 percent) of the state's population. Here we focus on their results for Wisconsin: What's going on? What does it mean? And, what, as a state, can we do about it?

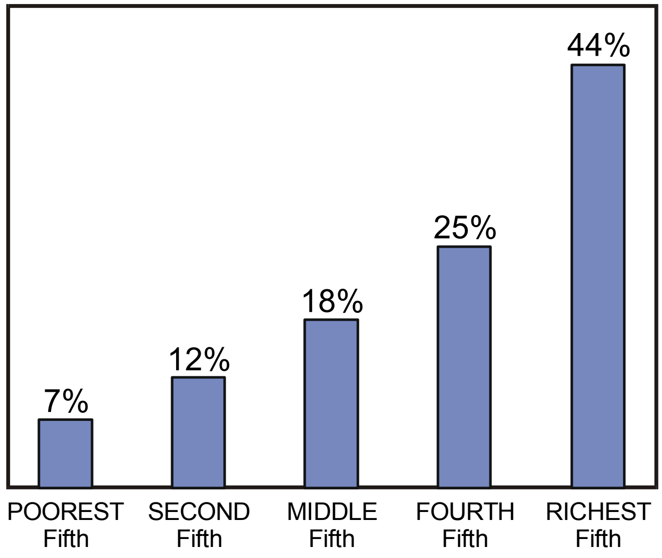
Increasing Inequality from the Late 1970s

Trends in average real (inflation adjusted) income for each fifth of the income distribution provide a good yardstick for measuring inequality. The national story of increasing inequality is well documented and is illustrated in Figure 2: from the late 1970s to the late 1990s, the average real income of the poorest fifth of families grew by $970, or seven percent.[2] (Throughout the report, all income values are inflation adjusted and expressed in 1999 dollars.) Over that same period, the richest fifth of families experienced a 44 percent income increase ($44,630 annually). At the very top of the income distribution, the story is even more extreme; income rose by 58 percent ($87,779) for the richest five percent of families.

Wisconsin mirrors these national trends (Figure 3 and Table 1). From the late 1970s to the late 1990s, the average real income of Wisconsin families in the bottom fifth of earnings grew only 3.3 percent (or $551) to $17,388. At the same time, families in the top income quintile saw their average income rise almost 38 percent ($38,919), to $141,858.

Figure 2

Income Change for U.S. Families
Late 1970s to Late 1990s, by Income Quintile
(Percent Change)

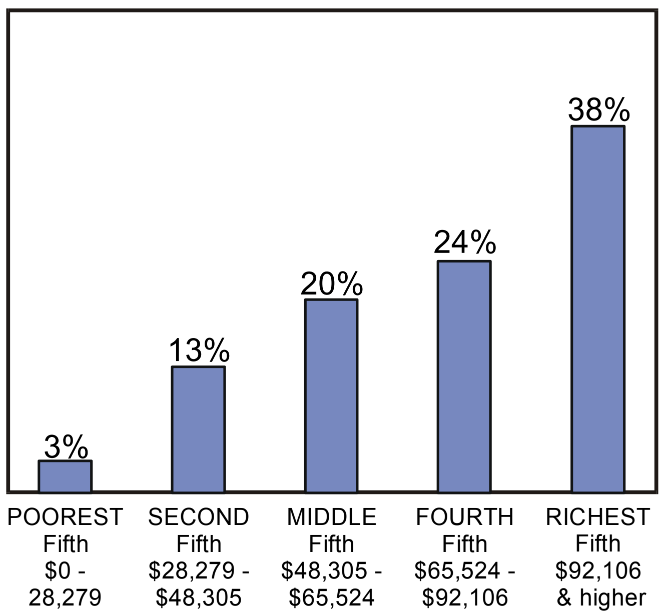


Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2002.

At the middle of the income distribution, the median family fared better than the bottom, but not as well as the top. For the middle fifth of families, real income grew almost 20 percent (up $9,405) to $56,553. So, while middle income families moved slowly upward, with an annual income increase of $470, the state's richest families sprinted forward, with average increases of more than $1,900 each year during that span. Figure 3 also shows the income range for each quintile in the late 1990s.

Figure 3

Income Change for Wisconsin Families
Late 1970s to Late 1990s, by Income Quintile
(Percent Change)



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2002.

Table 1

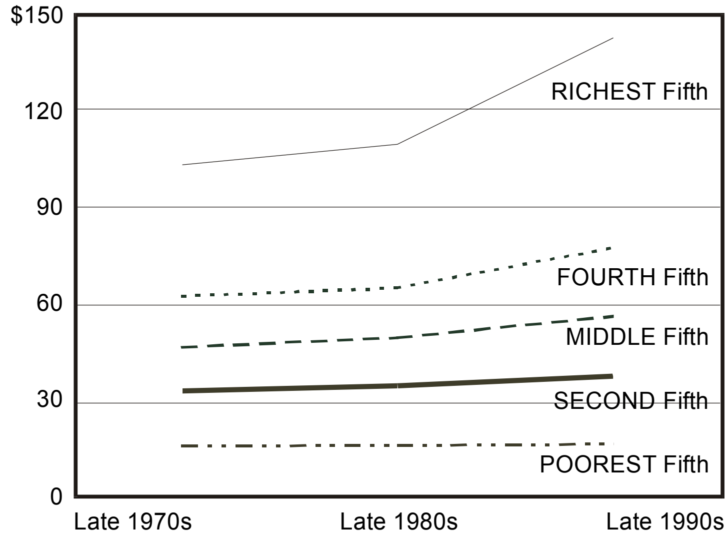
Wisconsin Family Income Trends
Average Family Income Late 1970s to Late 1990s

	Late 1970s	Late 1980s	Late 1990s	Percent Change, 1970s-90s	Percent Change, 1980s-90s
Richest Fifth	102,939	109,274	141,858	38%	30%
Middle Fifth	47,148	49,965	56,553	20	13
Poorest Fifth	16,837	17,037	17,388	3	2

Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2002.

Figure 4

Average Wisconsin Family Income Late 1970s to Late 1990s, by Income Quintile
(Dollars in Thousands)



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2002.

While the Wisconsin picture mirrors the national trend, there is an important difference in timing. Over the last two decades, the dramatic increases in inequality nationally were concentrated during the 1980s. In Wisconsin, however, income inequality grew slowly in the 1980s; it is the 1990s when inequality surged. This is especially evident in the trends in income for the top fifth of the income distribution (Figure 4). From the late 1970s to the late 1980s, income for this group increased moderately, up $6,335 (6.2 percent). Over the 1990s, however, the average income of the richest fifth of Wisconsin families grew by $32,584 (30 percent). That surge in income was unmatched in the rest of the economy, and median families and the poorest families have been left behind.

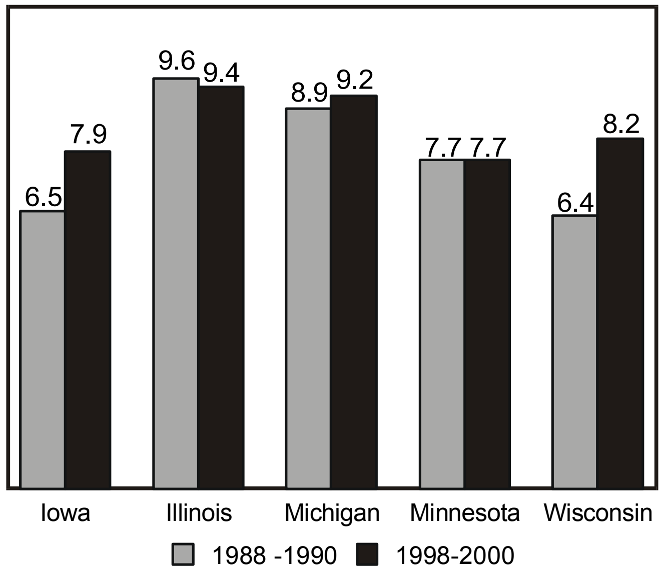
Stagnation of income for the poorest families and moderate increases for middle-income families stand in marked contrast to the dramatic gains that high income families in the state have secured over the last decade. In the past, rising tides have lifted all boats, but it is clear that the economy has changed; Wisconsin's growth has left behind a tremendous number of families at the lower end of the income distribution.

Wisconsin's Income Inequality Catching Up to Neighboring States

Wisconsin has traditionally had among the lowest levels of income inequality in the nation. Even after posting such increases in inequality in the 1990s, only nine states have more equal income distribution. That is good news. Low inequality is highly correlated with low levels of poverty and high levels of all resources available to meet basic family needs, according to an October 1999 Urban Institute study (*"Sources of Support and Income Inequality among America's Children,"* by Gregory Acs and Megan Gallagher,

Figure 5

Inequality in the Midwest
Ratio of Richest to Poorest Income Quintiles,
Late 1980s and Late 1990s



Source: *Pulling Apart*, Economic Policy Institute and Center on Budget and Policy Priorities, 2002.

report No 99-15). Wisconsin's widening income gap does not bode well, especially for communities with high concentrations of low-income families, such as Milwaukee County, where more than one-fourth of children were living in poverty in the late 1990s.

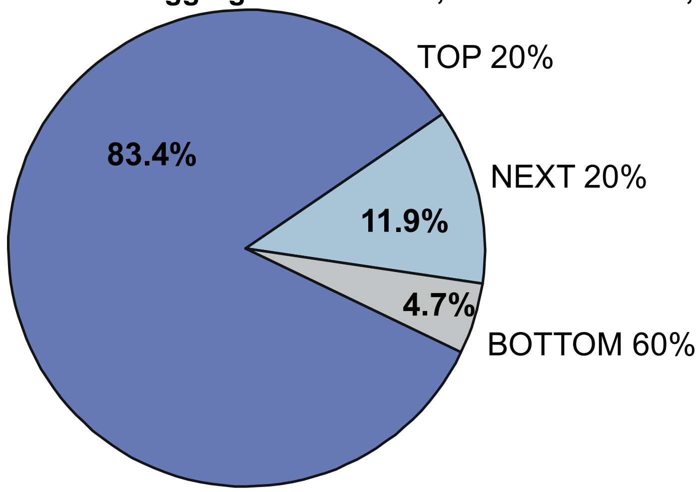
While Wisconsin has historically been a national leader in terms of income equality, the recent trends have narrowed the difference between Wisconsin and neighboring states. Figure 5 shows the ratio of the income of the richest fifth of families to the poorest fifth of families. In the late 1970s, Wisconsin and Iowa posted the most equal income distribution, with the income of the richest fifth of families at just over six times as much as the income of the poorest fifth of families. At that time, Illinois posted the most unequal income distribution; their richest families brought in more than nine times the income of the poorest families in the state. Over the last decade, however, the growth in Wisconsin's ratio outpaced every state in the region. Inequality decreased in Illinois, and it remained unchanged in Minnesota, which now is more equal than Wisconsin.

Inequality of Wealth is Even More Extreme

To focus on income disparity alone, however, provides only part of the picture. Differences in *wealth*, that is, disparities in ownership of stocks and bonds, real estate and other assets, between the upper and lower echelons of American society are even more pronounced and growing more rapidly than the disparities in income discussed above. Available data do not allow for the investigation of disparity of wealth at the state level, but the state trends can reasonably be expected to echo the national picture, which we outline below.

Figure 6

Distribution of Aggregate Net Worth, U.S. Households, 1998



Source: "Recent Trends in Wealth Ownership," Edward N. Wolff, Jerome Levy Economics Institute Working Paper #300, Bard College.

Researchers have long known that a small percentage of Americans own the bulk of assets. As Figure 6 shows, in 1998 the top 20 percent of households had 83.4 percent of the aggregate net worth of all households (the top one percent alone had 38.1 percent). By contrast, the bottom 60 percent of households had only 4.7 percent — and the very bottom 40 percent had only 0.2 percent!

The disparity in financial wealth (stocks, bonds, cash, etc.) is even starker. In 1998, the top one percent of households had 47.3 percent of financial wealth. While the top 20 percent had 90.9 percent, the bottom 40 percent had a negative financial wealth of 1.1 percent – that is, they owed more than they had in liquid assets (see *"Recent Trends in Wealth Ownership, 1983-98,"* by Edward N. Wolff, Working Paper No. 300, Jerome Levy Economics Institute, Bard College).

In addition, it is often the case that wealthy people benefit from capital gains (frequently from selling stock). Nearly three-quarters of all capital gains are realized by taxpayers with income exceeding $100,000. One-quarter of all capital gains income is realized by taxpayers with incomes exceeding $1 million (*"Information and Misinformation about Federal Tax Burdens,"* by Iris J. Lav, published by the Center on Budget and Policy Priorities, January 21, 1999).

Finally, wealth disparity by race is especially pronounced. In 1998, the median net worth in black households was only 12 percent of that of (non-Hispanic) white households ($10,000 compared to $82,000), while the median net worth of Hispanics ($3,000) was four percent of that of white households. Additionally, 27.4 percent of black families and 36.2 percent of Hispanics had zero or negative net wealth, while only 14.8 percent of white families did (Wolff, op. cit.).

Causes of the Growing Income Inequality

Nationally, the single most important cause of increasing income inequality is the growth in wage inequality. Wage disparity between races and people of different educational levels is growing. Wages in Wisconsin are also becoming more unequal, both within and between groups. *The State of Working Wisconsin, 2000* (Center on Wisconsin Strategy), shows that in 1999 the median wages of college graduates were much higher than those of high school graduates. This gap has markedly increased since 1979. For men, the wage differential was 69 percent in 1999, up from only 16 percent in 1979. For women, this differential was 72 percent in 1999, compared to 40 percent in 1979. As in the United States in general, male wage inequality by race in Wisconsin is considerable. In 1999, white men's median wages were 23 percent higher than black men's. For women, the comparable gap was three percent — smaller than the U.S. figure.

The increase in wage inequality within and between groups has been substantial, and a multiplicity of causes is to blame. As the EPI/CBPP report points out:

> A variety of factors explain the growth of wage inequality including globalization, the shrinkage of manufacturing jobs and expansion of low wage service jobs, immigration, and the weakening of labor market institutions — including the lower real value of the minimum wage and fewer and weaker unions.

These trends have been as clearly documented for Wisconsin as they have for the nation (see *The State of Working Wisconsin, 2000*). While immigration has had less influence in the state, the expansion of low wage service jobs and the decline in union density — Wisconsin union membership fell from 33 percent of the labor force in the early 1970s to just 16 percent in 2001 — have certainly contributed to the increase in wage inequality.

Income disparity also results from the growing importance of income derived from capital, such as rental income, interest, dividends and capital gains. From the late 1970s to the late 1990s, the share of total income nationally that is derived from capital grew from 16 percent to 20 percent of total personal income. Total labor income fell from 74 percent to 71 percent during that same period. As indicated above, a small — and well-off — portion of the population holds assets; increasing returns to those assets pushes income inequality up.

The rising number of single parent families also contributes to the surge in income inequality in the nation and the state. In the U.S, from 1970 to 2000, single-mother families went up from 12 percent to 26 percent of all families, while the number of single-father families rose from one to five percent (*America's Families and Living Arrangements, 2000*, U.S. Census Bureau). An October 1999 study published by the Urban Institute found that the median income in Wisconsin for one-parent families with children was just $21,300 in 1997, compared to $51,982 for two-parent families with children. Obviously, as the share of families with single-earners increases, income inequality increases as well.

Wisconsin Can Choose a Different Course

Wisconsin's economy has consistently been one of the most equal in the nation, and this has been an appropriate source of pride for state residents. The fact that income inequality is increasing more rapidly here than in much of the nation should be a cause of concern. To be sure, Wisconsin remains among the most equal states in the nation, but it is unlikely to retain that status in the face of the trends of the last decade.

There is no "magic bullet" to rectify the situation, any more than there was a single cause. But some of the state policy options are clear enough.

Raise and Index the Minimum Wage

Increasing the earnings for workers at the bottom of the labor market is one way to increase equality of income. Adjusting for inflation, the current federal minimum wage, $5.15 per hour, remains below its value any year between 1961 and 1988 and about 20 percent below its value anytime during the 1970s. It leaves a family of three below the poverty line if that family has one full-time, minimum wage worker. In response to lack of federal increase in the minimum wage, 10 states have set state minimum wages that exceed the national minimum.

Such a policy could have a direct and positive effect on the earnings of many working adults in Wisconsin. Each 25 cent increase in the minimum wage boosts the income of a full time, year round worker by more than $500. And contrary to the popular image, most workers earning the minimum wage are making direct contributions to family income. About 70 percent of minimum wage earners are adults, not teenagers. A study examining 1999 statistics found that among workers making less than $6.15 an hour, 37 percent were the head of a household or a spouse contributing to family income, and 33 percent were parents with children under 18. (*The Minimum Wage: Increasing the Reward for Work*, National Economic Council, March 2000)

More than 163,000 workers in Wisconsin benefited from the last federal increase in the minimum wage. A state increase in the minimum could help those workers who are struggling at the bottom of the labor market to move closer to self-sufficiency.

Build an Educated Workforce

Research has consistently shown that increased education and job training have a very positive effect on earnings. Studies have indicated that each year of postsecondary education increases earnings by six to12 percent ("*State Opportunities to Provide Postsecondary Education under TANF*" Greenberg, Strawn, and Plimpton, Center on Law and Social Policy, 1999). One study tracking 20 years of earnings found that women with associate degrees earned about 20 percent more than other women, even after controlling for differences in who enrolls in college. For a Bachelor's degree, the increase was about 30 percent ("*Labor Market Returns to Two- and Four-Year College*" Kane and Rouse, *American Economic Review*, 1995). One year of college cuts the poverty rate for African American women heads of households by more than half, from 51 percent to 21 percent, and for Latinas the rate drops from 41 percent to 18.5 percent ("*College Education Is a Route out of Poverty for Women on Welfare*" Wolfe and Gittell, Center for Women Policy Studies, 1995).

Wisconsin should assist lower income adults advance their educations and improve their chances of climbing the economic ladder by:

- putting a much greater emphasis on education in the W-2 program;
- increasing need-based financial aid for higher education by at least the rate of increase in tuition;
- maintaining a strong vocational education system; and
- ensuring that an appropriately large proportion of Workforce Investment Act resources go toward vocational training services (in the form of individual training accounts).

Make Work Pay and Support Working Families

State government can help lessen the burden of income inequality by carefully structuring benefits to lower-income families to ensure that work pays. Wisconsin has historically been relatively generous in the benefits that it provides and has been a leader in developing policies to make work pay. For example, Wisconsin was one of the first states to establish a refundable earned income tax credit for working parents. Yet the structure of taxes and benefits in Wisconsin makes it difficult for low-income families to work their way out of poverty.

A study by the Public Policy Forum (*Making Work Pay in Wisconsin: An Update*, August, 2000) examined the impact of state benefit and tax policies on low-income families in Wisconsin. The report concluded that as poor families with children earn more they experience a flat growth in disposable income which leaves them hovering near the poverty line even as gross income rises into the mid-$30,000 range. The combined effects of taxes, loss of benefits such as food stamps, and increased co-payments for child care make it very difficult for parents to climb the economic ladder out of poverty.

One way to make work pay is to increase and modify the earned income tax credit (EITC). The federal tax bill passed last year made a little progress in that direction by phasing out the credit more slowly for married couples. However, the credit should be changed further by:

- increasing the maximum federal EITC by $500 for working families with three or more children;
- easing the EITC marriage penalty for married, two-earner couples; and
- making the credit phase out more slowly (as income increases) for families with two or more children.

If these changes were made to the federal EITC, they would also indirectly boost Wisconsin's earned income credit (unless the legislature severs the link with the federal credits).

In conjunction with changes in the EITC, the state should examine the relationships between public assistance programs and strive to find ways to ensure that low-income parents get ahead as they earn increased wages or work longer hours.

Continue to Modernize the Unemployment Insurance System

Unemployment insurance is, or at least should be, a critical safety net for the vast majority of laid-off workers. Its importance has grown for low-wage workers in particular, now that the former welfare system has largely been dismantled. However, only about 53 percent of unemployed workers in Wisconsin receive any unemployment insurance (UI) benefits. Many low-income workers are ineligible because their jobs are more commonly intermittent, seasonal, and part-time, and are less likely to qualify for benefits.

To Wisconsin's credit, it has done a better job than many other states in extending benefits to low-wage workers. In a recently released report card on the UI systems in all 50 states, Wisconsin received a passing grade overall, but failed one of the five general categories the study examined. Specifically, our state received a failing grade with respect to eligibility standards because it does not extend benefits to people only available for part-time work, even though UI taxes are being applied to their salaries (*Failing the Unemployed: A State by State Examination of Unemployment Insurance Systems*, Emsellem, et. al., March 2002).

Improvements that should be considered by Wisconsin's Unemployment Insurance Advisory Council include:

- expanding eligibility to individuals available for only part-time work or work on specific shifts;
- correcting an inequity in the state law authorizing benefit extensions during periods of high unemployment, which excludes about half the potentially eligible workers; and
- providing dependent allowances (as 12 states already do) that acknowledge the special needs of parents with children.

Reform Regressive Taxes

Perversely, state and local taxes in Wisconsin *increase* income inequality rather than reduce it. Analysis of the burden of the combined package of Wisconsin taxes — property, sales and excise, and income — shows Wisconsin's tax structure to be almost perfectly regressive *(Who Pays? A Distributional Analysis of the Tax Systems in All 50 States*. Institute on Taxation and Economic Policy, 1996). The higher your income, the lower the portion of income paid for taxes. The poorest fifth of the income distribution pays nearly 14 percent of their income in state and local taxes while the richest fifth pays between 10 and 7 percent of their income in state and local taxes. This takes the state's EITC into account.

The problem is that, even though the state's income tax structure is progressive (with lower incomes paying a lower portion of their income in tax), the state's sales and property taxes are quite regressive. A recent study by the Center on Budget and Policy Priorities concluded that Wisconsin's taxes have become more regressive since the early 1990s because the tax cuts have been in the more progressive taxes and the tax increases have been in regressive taxes such as gas, cigarette and sales taxes (*The Rising Regressivity of State Taxes*, December 27, 2001).

One progressive element of the state tax system is the Homestead Tax Credit, which helps lessen the burden of property taxes for many low-income homeowners and renters. However, the maximum credit has not been increased since 1991 and the program has been substantially eroded by inflation. In addition, the state could do a better job of informing families with children that they are eligible for the credit. Wisconsin should index the credit for inflation and continue working to improve outreach.

Finally, there are other tax system characteristics that place an undue burden on the poor while offering benefits to the rich, including our treatment of capital gains and the exclusion of services from the sales tax. As such, the distribution of the entire package of taxes needs to be examined, as part of a comprehensive review of the adequacy and equity of state and local taxes.

Conclusion

Wisconsin long avoided the levels and increases in inequality that the rest of the nation exhibited. The data in this report make it clear that the gap between the rich and the poor has grown more rapidly in Wisconsin than in the nation as a whole. Economic growth and prosperity are not being equally shared; in fact, rewards of prosperity in the 1990s were heavily concentrated on the richest 20 percent of families. As a state, this should be of substantial concern, not only because of the stagnation in incomes for the remaining eighty percent of families, but also because increasing disparity comes with substantial social costs.

To prevent a deepening divide between the rich and poor in our state, Wisconsin should pursue a number of strategies:

- Raising and indexing the minimum wage.
- Improving access to educational opportunities and training for low-wage parents.
- Modernizing the unemployment insurance system.
- Reviewing the structure of benefits and taxes to reduce the current disincentives for certain parents to seek higher-paying jobs.
- Ensuring that our tax system does not require low-income families to pay a higher percentage of their income for taxes than other Wisconsin families.

Taking these steps would help keep Wisconsin growing, and ensure that all residents of the state would benefit from the growth.

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[1] Copies of the EPI/CBPP report may be obtained from COWS or WCCF, or from EPI Senior Media Coordinator Karen Conner at 202-775-8810.

[2] All figures in the report are before-tax income for families from the Census Bureau's March Current Population Survey. Data are "pooled" across three most recent years available (1998, 1999, 2000, called "late 1990s" in the report) to allow for sufficient sample size. To compare to the past, three years of data from the late 1970s (1978, 1979, and 1980) and the late 1980s (1988, 1989, 1990) were pooled. The late 1970s, 1980s, and 1990s all represent peaks in the economic cycle and so provide for good comparison.