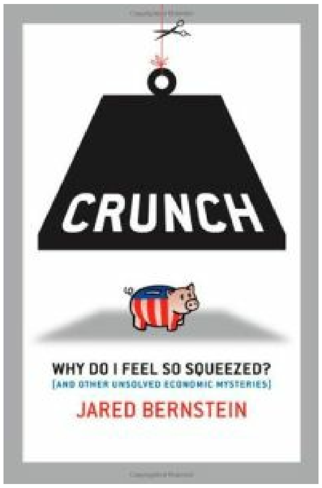

Book Crunch

Why Do I Feel So Squeezed? (And Other Unsolved Economic Mysteries)

Jared Bernstein
Berrett-Koehler, 2008
Listen now

- play
- pause

00:00
00:00

Recommendation

At last someone has written a lucid explanation of the American middle class's financial stagnation. Economist Jared Bernstein – chief economic adviser to Vice President Joseph Biden – provides a tremendous service to millions of Americans who wonder why so many two-income households remain financially insecure. Bernstein understands that most economics writing is impenetrable. He explains in lively prose why financial inequality is alive and well in 21st-century America. It's an issue the mainstream media rarely covers. The book is structured around the gimmick of answering American's most common questions about economics, and some of the miniessays don't connect, but *BooksInShort* recommends it to working people who want to know why they are entrenched in the proverbial rat race despite political promises that they are on the verge of financial security – a state, Bernstein emphasizes, that will remain elusive for most Americans.

Take-Aways

- The greatest challenge the U.S. faces today is finding a way to organize the economy so that it provides the goods and services that people want and need.
- Rising costs mean that even two-income households are struggling to save money.
- The real wages of U.S. college graduates rose less than 2% from 2000 to 2006.
- In 2005, the top 1% of U.S. households received 22% of the nation's total income.
- In the U.S., productivity gains translate into consumption increases, while in Europe, such gains lead to vacation-time increases and consumption decreases.
- The Federal Reserve has a bias toward restraining inflation, which reduces wages and holds back increases in living standards.
- Congress can spend $11 billion per month on wars only because elected officials are ignoring the will of the majority.
- The power to control the national economy lies in the hands of a few select people.
- Globalization has cost the average U.S. household $2,000 in lower wages.
- • When government invests in research, education and public projects, a budget deficit is not such a bad thing.

Summary

The Income Gap Widens

The greatest challenge the U.S. faces today is finding a way to organize the economy so that it provides the goods and services that people both want and need. That noble goal is also political, since governments determine the distribution of wealth, power, opportunity, social mobility and health care coverage, as well as rectifying environmental problems. Analysts use three principles to understand how governments allocate power and resources:

1. While market forces generally determine resource allocations based on merit, people with political power can shape these allocations.
2. Economic relationships often take unexpected turns and may not be logical.
3. Economics often requires trade-offs among scarce resources. Policy makers all have their own interests, and their decisions are rarely unbiased.

> "Something's wrong, something fundamental. Not Third World-poverty fundamental, not blood in the streets, massive homelessness or Great Depression fundamental. If the problem were that obvious...it would be less of a head scratcher."

Even when households include two wage-earners, many cannot save enough money for their health care premiums or their children's college tuitions. One reason is that inflation-adjusted incomes have declined in recent years. Financial pundits who talk about gains in the overall economy often ignore this fact as well as other events that affect average citizens.

> "The name of the problem is economic inequality, and it's been on the rise for decades."

While inflation has been "moderate" since 2000, the costs of health care, housing, child care and college tuition have all increased faster than the growth in the collective average of all prices combined. Even people who cannot articulate these changes know a problem exists. An ABC-*Washington Post* poll conducted weekly shows that, since the summer of 2001, more than 50% of people in the U.S. have had a negative impression of the economy. They felt financially stressed even as the productivity and gross domestic product numbers were rising.

> "How we organize our economy determines how we structure our response to the challenges from environmental deregulation, globalization, the lack of health coverage and staggering wealth inequalities."

Politicians avoid these unsettling issues and often use the same old arguments to rationalize their actions. For example, they claim that more education will alleviate social inequality. However, this solution is flawed because educated workers have a high chance of losing their jobs due to globalization. In addition, their incomes have stagnated. The real wages of U.S. college graduates increased less than 2% between 2000 and 2006. Meanwhile, in 2005, 1% of U.S. households received 22% of the nation's total income, the highest inequality since 1929.

Changes in Society

Men in the U.S. earn less today than they did a decade ago, partly due to a decline in unionized factory jobs and an increase in service jobs. This problem is especially acute for men who aren't college graduates, because service-sector jobs pay significantly less than factory positions and lack fringe benefits. As union jobs evaporated and men's salaries declined, more women entered the workforce. During the 1960s, about 40% of American women worked. By 2006, the figure had risen to 60%.

> "Over the course of this highly touted economic expansion, poverty is up, working families' real incomes are down, and some key prices are growing a lot faster than the average."

Tuition, medical and housing costs have risen much faster than inflation, constraining the nonessential spending of the middle class. The consumer-price index, which measures overall prices, rose 30% from 1996 to 2006, but college tuitions increased 80% and the cost of child care rose 60%. Since 2000, medical insurance premiums have increased three times faster than inflation. Employers pay a large portion of health care costs, but when employers subsidize health care benefits, they are less likely to be able to offer wage increases. In effect, workers pay for health care in the form of lower wages. Washington policy makers could control these costs if they were willing to battle the "medical industrial complex." Other nations control their health care costs by removing medical insurers from the political process. Those nations' policy makers consider health care a right, which market forces should not be able to manipulate.

> "Those who hold a privileged position in the economic power hierarchy...the CEOs and the holders of large capital assets – are able to steer the bulk of growth their way."

Governments that remove insurance companies from health care pricing and delivery systems often create single-payer or regulated systems, which hold down costs by creating a large risk pool. The majority of the people in the pool – those who are healthy – subsidize the larger expenses of the minority of people, who are sick. These nonprofit systems have no large advertising budgets, and often include rationing and price controls. Critics in the U.S., who focus on the rationing in these kinds of systems, often neglect to note that the U.S. system also rations health care, by discriminatory pricing. And 47 million people in the U.S. lack any health care coverage at all.

Rethinking Some Economic Terms

Some longstanding economic vocabulary obscures more than it explains. For example:

- **"Gross Domestic Product" (GDP)** – This supposedly measures the dollar value of the economy, indicating its growth or decline. Yet, as a measurement, GDP has limitations: It ignores the environmental impact of expenditures and it includes the value of things that get destroyed. For instance, after Hurricane Katrina devastated New Orleans in 2005, the U.S. GDP increased, since it added in the high disaster-relief spending but did not subtract the cost of the city's destruction. Wars boost GDP, since government spending increases to replace used or destroyed equipment. Even though replacement costs cannot be considered productive spending, the GDP registers them as an increase.
- **"Unemployment"** – This figure indicates the number of individuals who are not only out of work but searching for new positions. It affects institutions such as the stock market and the Federal Reserve. Low unemployment often signals a future increase in wages and inflation, and a concomitant decrease in corporate profits. This prompts the Fed to raise interest rates to prevent recession, creating tension between Wall Street, which wants rising stock and bond markets, and Main Street, which wants low unemployment. Inflation harms the wealthy, but unemployment hurts lower-income, working families. Education and race go into determining unemployment. College grads have about one-third the unemployment rate of those with only a high school education, and blacks are generally twice as likely to be unemployed as whites.
- **"Underemployment"** – This happens when people hold jobs that don't use their skills, or can find only part-time work when they really want full-time employment, for example college graduates who wait tables until they find something else or blue-collar workers who lost their jobs as the U.S. manufacturing

sector shrank. In 2006, 8.2% of the U.S. population (5.5 million people) was underemployed in addition to the 4.6% that was officially unemployed. The U.S. Bureau of Labor Statistics does not consider part-time workers or people who have stopped looking for work to be unemployed, so it understates the actual rate of unemployment.
- "**Productivity" –** This measures total output per hour of work. It is a critical determinant of living standards. Technical improvements induce higher productivity, which lowers the costs of certain goods, such as computers, making them more affordable. While productivity in the U.S. translates into greater consumption of goods and services, other countries, such as France, prefer to cash in their productivity gains for increased vacation time rather than more consumption. Economists traditionally assumed that rising productivity meant rising incomes for everyone, but, since the 1970s, only high-income families have received the benefits of increased productivity.

The Power Imbalance

Traditionally trained economists do not consider the political implications of economic power, even though the political power structure shapes economic theory and policy. In fact, just a few powerful people shape the national economic agenda. Over the past few decades, they have called for deregulation and increased laissez-faire market forces to redistribute income – which end up enriching the already wealthy. These powerful political forces shape the national debate by eliminating collective political responsibility for the economically disenfranchised. The new political mantra calls for substituting individual responsibility for health care and other economic challenges, even as working people are losing their collective bargaining power.

> "We should thank the unions for trying to keep teachers' pay high enough to attract decent people to the job."

The idea that Social Security will not be able to provide benefits for years to come is simply a myth. In fact, the system will continue to function and to transfer wealth from one generation to the next. The population of children will decrease, and the U.S. will be able to redirect more resources toward older people. The proportion of people older than 65 will increase from 12% in 2000 to 20% in 2030. At the same time, productivity increases will produce more tax money for Social Security.

> "If people feel that the system is rigged against them, they're less invested in that system."

Many economists underestimate the U.S. president's power to influence the economy. Presidents control the country's investing priorities and decisions to redistribute or ration resources. The Federal Reserve also shapes the economy. Its main tool is raising or lowering the federal-funds rate (FFR) to control the cost of borrowing, to adjust the market when the economy is growing too quickly or slowly. However, the Fed has a bias toward restraining inflation. This leads to reduced wages, higher unemployment and stagnation in living standards.

> "Unemployment and inflation are, in no small part, class-based concerns."

While no one likes budget deficits, they can actually be good for the economy if the government uses the money productively for investment into research, education, public projects or services that the private sector does not provide. Deficits are a problem only when they get too big or when the expenditure does not benefit the public. Then, future generations are stuck with the debt. If government creates a deficit today, it should plan how to allocate or raise revenues that will offset it in the future.

> "We can no longer assume that workers will get their fair share of the growing pie, even if its growth reflects their contributions."

Economics is about trade-offs. The U.S. could spend more on human services if Congress reprioritized its policies and spent less on war, on which the U.S. currently spends $11 billion per month – contrary to the will of the majority of voters.

Rethinking Globalization

Free trade advocates don't acknowledge that globalization and unregulated trade have eliminated three million manufacturing jobs in the U.S. and contributed to a reduction in workers' wages. Economist Josh Bivens estimates that globalization cost the average household about $2,000 in lower wages since the 1970s. The problem affects not only blue-collar workers but also white-collar workers. Economists point out that expanded trade has decreased the price of imported goods, saving U.S. consumers between $4 billion and $20 billion annually – but it has also decreased workers' incomes.

> "The military-industrial complex, a concept introduced in the 1950s, is alive and well."

The flip side of globalization is immigration. During the current recession, some have claimed that immigrants are depriving less-skilled, native-born Americans of jobs. However, this debate is more often about racism and nativism than economics. The real problem is that immigrant workers now dominate entire sectors of formerly unionized, well-paying blue-collar jobs, such as meatpacking and construction. Thus, one study found that since the early 1990s, immigrant labor has reduced the wages of native-born citizens by between 5% and 10%. If immigrants felt more socially secure, they could demand better pay, and wages for everyone would rise.

> "Our biggest economic reform challenges...have been and will continue to be a struggle to wrest power from those with deeply vested interests in maintaining their privileged positions."

Other outstanding issues with thorny economic policy implications include:

- Restoring the bargaining power of American workers.
- Improving educational opportunities. Educational inequality hampers national progress. Students need public financial support.
- Fighting global warming.
- Cutting the rising U.S. poverty rate. The increase in poverty, especially among children, highlights the contradiction between overall growth and living standards.

> "Learn this well if you want to get what's going on in these seemingly arcane, but vitally important spending debates: Those that control the budget constraints control the debate."

In recent years, policy makers have misdirected their power to create class inequality rather than a society that is efficient and equitable.

About the Author

Jared Bernstein is senior economist and director of the Living Standards Program at the Economic Policy Institute in Washington, D.C. He wrote *All Together Now: Common Sense for a Fair Economy* and is the co-author of eight editions of *The State of Working America*.