



Prosperity 2050

Is Equity the Superior Growth Model?

Sarah Treuhaft and David Madland April 2011

Introduction

As our country inches its way out of the Great Recession and looks toward the future, the need for a new policy framework to guide our economic growth is clear. The economic model of the past several decades is failing nearly everyone, save those at the very top. With the exception of the later years of the Clinton administration, economic growth has been slower and less broadly shared over the past several decades, leaving more and more families, even entire communities, to fall further behind and with diminishing prospects for catching up.

This is true not only for the poorest of the poor but also for lower- and middle-income families, who have seen their incomes stagnate and their quality of life decline. And it is especially true for people of color, who are rapidly becoming the majority population of the United States and will certainly be so by 2050.

Our country faces a mounting economic opportunity deficit and it is the exact opposite of the American promise that if you work hard, you can achieve the good life, exemplified by a secure paycheck that grows year after year, a nice home in a safe neighborhood with decent schools, retirement savings, health care, some leisure time to spend with friends and family, and the ability to send your kids to college and pass along to them a bigger share of the American Dream.

The long-term economic trends of greater inequality and stunted upward mobility clearly undermine American ideals of fairness and equity, and the notion that prosperity should be broadly shared. But could the eclipse of the American promise also be undermining our economic competitiveness? Is it possible that the traditional assumption that there is a tradeoff between growth and equity is wrong, and that broadly shared growth is ultimately better for the economy? Could a focus on equity—the economic and social inclusion of those left behind—be much more than a humanitarian or moral act but actually a superior economic growth model? And if so, what does an inclusive and sustainable growth trajectory look like?

Now is a critical moment to begin a national dialogue about the growing opportunity deficit and what it means for our economic future. Today, PolicyLink and the Center for American Progress host a convening to discuss the proposition that a focus on equity and economic inclusion is necessary to grow the U.S. economy. At this meeting, leading economists and policy experts will explore the connections between inequality, social inclusion, and economic growth; identify areas for further research; and discuss policies that can support stronger and more equitable economic growth.

This framing paper is intended as a starting point for that discussion. It highlights key economic and demographic trends, summarizes the literature on equity and growth, and suggests some next steps for building an inclusive growth agenda.

Critical trends: Increasing inequity, growing diversity

Economic disparities on the rise

Over the past several decades, longstanding inequities in income, wealth, and opportunity have steadily worsened—and are now reaching unprecedented levels. While there is no single causal explanation, broad economic and political transformations, including the decline in union membership and the shift from an economy based on manufacturing to one based on services and retail, have certainly played a role.

Entire neighborhoods, cities, and even regions—particularly older industrial areas in the Northeast and Midwest—have been devastated by deindustrialization. And in all places, continued residential segregation by race and income, along with the concentration of opportunity structures (such as high-quality schools, good jobs, and services) in higher-wealth communities, has physically separated people from the resources, markets, and institutions they need to get ahead. Key trends include:

- Increasing income inequality
- Rising productivity but stagnant wages
- A growing wealth gap
- Stunted economic mobility
- More and deeper poverty
- Persistent racial disparities

Let's examine each of these trends briefly in turn.

Increasing income inequality

The gap between rich and poor has widened since 1980 and the United States now has the third-worst income inequality among advanced industrial nations.¹ Economic gains are not being widely shared and instead are concentrating at the top. Between 1947 and 1976 the top 10 percent of earners took home a third of the nation's pre-tax income; by 2008 their share had increased to 48 percent. In the same time period, the share going to the top 1 percent grew from 8 percent to 18 percent.² Income growth is distributed even more unevenly: The bottom 90 percent of households only captured 16 percent of income growth between 1989 and 2007 while the top 1 percent received 56 percent.³

Rising productivity, stagnant wages

American workers produce more output per hour than ever before but their productivity gains are not translating into higher wages. In 2010 average annual productivity rose by 3.9 percent yet labor costs (workers' compensation) fell by 1.5 percent.⁴ During the last business cycle (2001 to 2007) before the Great Recession, worker productivity increased nearly 19 percent but the real income of the median working-age household decreased by about 2 percent while the costs of health care, housing, and college have increased.⁵

What's more, the trend began even earlier. From 1979 to 2005 the incomes of the middle 60 percent increased by 18 percent (\$9,000) and the incomes of the bottom 20 percent increased by only 1 percent (\$200). Meanwhile, the incomes of the top fifth increased 75 percent (\$99,200). This is a stark departure from the 1947-to-1973 period when the incomes of the poorest fifth of families increased at about the same rate as the incomes of the wealthiest fifth.⁶

Growing wealth gap

The wealth divide in our nation has grown even more dramatically than the income and wage divide. The collapse of the housing bubble, followed by the foreclosure crisis, the decline in home prices, and the glut of "upside-down" mortgages, stripped many lower-income families of their most significant—and often, only—asset. Wealth was destroyed across the board but lower- and middle-income households were disproportionately affected.

From 2007 to 2009 the bottom 80 percent of Americans lost 25 percent of their wealth, on average, and the top 20 percent lost 16 percent. The share of total wealth held by the bottom 80 percent of the population dropped from 15 percent to 13 percent in the same time period while the share going to the top 20 percent increased from 85 percent to 87 percent.⁷

Stunted economic mobility

Americans tend to be tolerant of economic inequality as long as opportunities exist to move up the economic ladder. But the actual chances that a child born to a poor family will improve his or her lot are much lower in the United States compared to other

developed countries, and lower than the public perceives them to be. Moreover, those opportunities seem to be declining.

Consider these facts. Only 6 percent of children born to poor parents (those in the bottom fifth of income earners) grow up to become rich (entering the top fifth of income earners) while nearly half of them (46 percent) remain just as poor. Beyond the challenge of getting ahead, downward mobility is a serious risk, particularly for African Americans: 45 percent of middle-class black children end up poor, compared to 16 percent of middle-class white children.⁸

More and deeper poverty

Poverty has been on the rise since 2001 after significant declines in the mid-1990s. More than 43 million Americans now live in poverty—the largest number since the U.S. Census Bureau began tracking poverty in 1959—and the poverty rate, at 14.3 percent, is at its highest since 1994. Poverty is much worse for communities of color: One in four African Americans, Latinos, and noncitizens are currently living in poverty, compared to 12 percent of whites.⁹

Poverty is also deeper than ever. Nineteen million people are living in extreme poverty, which means their incomes are less than half of the poverty threshold (which many experts already consider to be too low to live on). At 44 percent of the poverty population, this is the highest extreme poverty share ever recorded in this country.¹⁰

Persistent racial disparities

People of color in America have long faced recessionary conditions and barriers to economic opportunity, and were hit first and worst by the Great Recession. Unemployment remains much higher for African Americans (15.5 percent, up from 8.6 percent at the beginning of the recession) and Latinos (11.9 percent, up from 6.3 percent) compared to whites (8.3 percent, up from 4.3 percent) and Asians (7.1 percent, up from 3.7 percent).¹¹ Persistent disparities exist across other economic indicators, such as underemployment and discouraged workers, as well.

Changing American demographics

These disparities do not bode well for the future economic growth of our nation. The reason: People of color in the United States will become the majority of Americans by 2050 (see chart on next page).

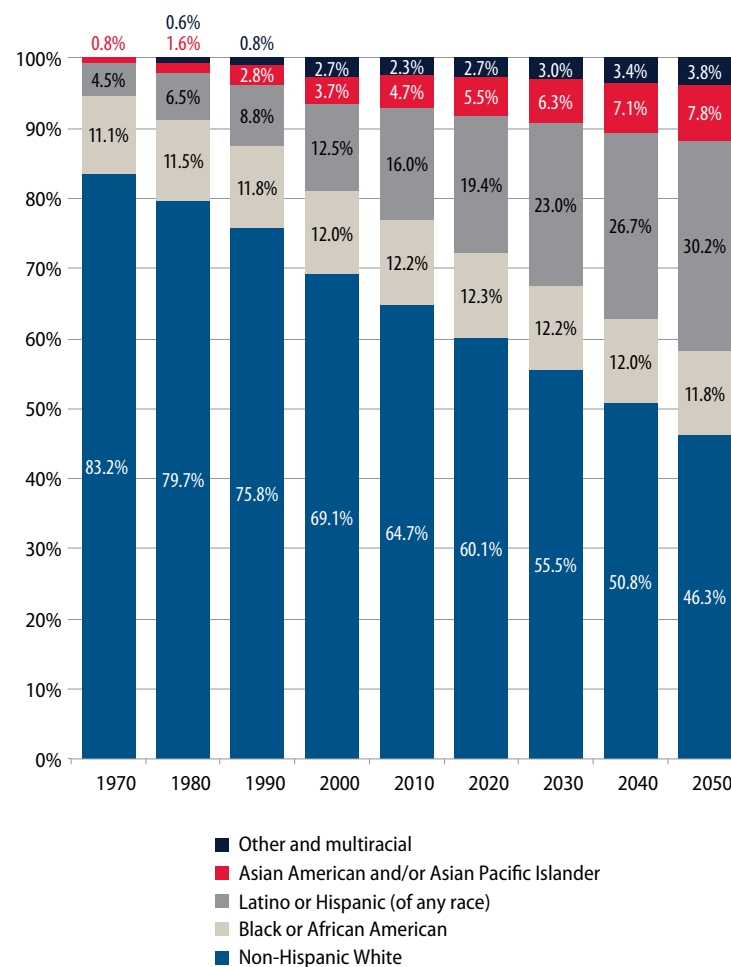
Indeed, a key takeaway from the Census 2010 data is that we are becoming a majority people of color nation at an even faster clip than demographers previously thought. People of color contributed 92 percent of our population growth in the past decade

and currently make up 36 percent of the U.S. population. Any day now the majority of babies born in this country will be nonwhite (the Census predicted this would be true for 2010 but the data by detailed age categories are not yet available). By around 2019 the majority of youth will be nonwhite. And the Census now predicts that by 2042 we will be a majority people-of-color nation.¹²

In many communities this shift has already taken place. Four states (California, Hawaii, New Mexico, Texas) and the District of Columbia are already majority people of color, along with 49 metropolitan regions. Another nine states and 40 regions are nearing a tipping point, with between 40 and 50 percent nonwhite residents.¹³

Another important trend is the growing generation gap between a mainly white senior population and an increasingly diverse youth population. The spread between the share of seniors that is nonwhite and the share of youth that is nonwhite is widening—just 20 percent of seniors are nonwhite compared to 46 percent of people under age 18. The senior population will continue to increase its share of total population over time (from one-eighth today to one-fifth by 2040) while the youth population is expected to remain stable at about a quarter of total population.¹⁴

The racial and ethnic composition of the United States, 1970–2050



Sources: Data for 1970 and 1980 from Statistical Abstract of the United States. Data for 1990, 2000, and 2010 from the U.S. Census Bureau. Data for 2020 through 2050 from the U.S. Census Bureau Population Projections by Race and Ethnicity (2008).

The economic consequences of demographic change

The rapid demographic transition underway will have many consequences for our economy, politics, and culture. The generation gap is likely to fuel political battles as the aging white population becomes increasingly averse to public spending and the diverse young population sees education, health, and other public investments as key to its economic success. But seniors also share a stake in the economic success of youth—the future earnings of those same youth are necessary to pay for their health care and Social Security benefits.

In relation to our economic future, the strength of the future workforce is a paramount concern. A key issue is the large and persistent educational achievement gap. By the fourth grade only 17 percent of poor children score at or above proficient levels in reading and only 22 percent are proficient or better in math.¹⁵ Just 6 in 10 black, Latino,

and Native-American students graduate from high school, compared to 8 in 10 white students and 9 in 10 Asian and Pacific Islander students.¹⁶ Children of color often attend the worst schools and lack the quality teachers, curricula, classrooms, and extracurricular supports that help middle-class children succeed.

Unless we reverse current trends in educational outcomes, the American labor force will be less skilled as the global knowledge- and technology-based economy demands skilled workers. Half of all new jobs over the next 10 years will require postsecondary education, yet the share of adults with some advanced education is projected to decline in all but six states.¹⁷ Among 18-to-24-year-olds, only 44 percent of whites, 32 percent of African Americans, and 26 percent of Latinos are enrolled in college. The Educational Testing Service calls this a “perfect storm” of demographic, labor market, and educational trends that threatens the American dream.

Inequality is bad for sustained economic growth

Economists have long considered the relationship between equity and economic growth. Early economic thinking was heavily shaped by Simon Kuznets, a Nobel Prize-winning economist, who argued that economic inequality increases while a country is developing, and then after a certain average income is attained, inequality begins to decrease.¹⁸ His explanation for this pattern was that shifting from agriculture to industry caused inequality to rise but further growth led to increased economic opportunities as well as equalizing government policies.

This argument and its graphical representation—the inverted U-shaped Kuznets curve—suggested that inequity was good for economic growth, at least at the early stages of development. Alas, overwhelming evidence has accumulated that development does not quite work like Kuznets predicted.¹⁹

Many countries have not become first less and then more equal as they develop. Instead, there have been a wide variety of development patterns, with some countries growing relatively equally at all points in their development and others growing unequally at all points in their development, and still others vacillating between relatively equal and unequal. South Korea, for example, has seen relatively equitable economic growth throughout the past 60 years as it developed from a relatively poor country to a middle-upper-income country. Brazil, historically one of the most inequitable countries, has in very recent years begun to grow more equally. And in the United States, from the 1940s to the 1970s, economic growth went with increased equality, but since the 1970s, additional growth has reduced equity.

The real world has not conformed to the Kuznets curve. Still, the idea that there is a tradeoff between growth and equity did not just go away. Instead, it remained influential, even for advanced countries, though the hypothesis was largely untested. The hypoth-

esis that there was a tradeoff between equity and growth fit with economists' prevailing ideas about incentives—inequality was believed to provide incentives for people to work and invest and thus grow the economy—and also was advanced by prominent economists such as Arthur Okun, chairman of the Council of Economic Advisers between 1968 and 1969.²⁰ In more recent years researchers have begun to more closely and directly examine the relationship between equity and growth.

Though some empirical research suggests that inequality is good for growth, a large body of research has found the world to be much more complicated. One significant strand of research finds that there is no tradeoff between equity and growth. In their frequently cited historical analysis, Peter Lindert of the University of California, Davis, and Jeffrey Williamson of Harvard University examine the U.S. economy since colonial times and the British economy over a similarly long period and find no pattern between growth and equality.²¹ Instead, they argue that inequality is driven by the supply and demand of labor and capital.

Similarly, researchers such as Oxford University's Tony Atkinson, Princeton University's Jonas Pontusson, and Walter Korpi of the Swedish Social Institute have all separately examined whether welfare states designed to increase equality harm economic growth.²² They all have found strong evidence that it does not.

Perhaps most importantly, a growing body of research argues that inequality is actually harmful to economic growth. Harvard's Philippe Aghion finds that inequality is negatively related to growth and argues this is largely because of imperfect credit markets that prevent the nonwealthy from making significant economic contributions.²³ And New York University's William Easterly argues that societies that are not economically polarized have higher levels of growth because they have better institutions and higher levels of human capital accumulation.²⁴ Easterly analyzed data from 1960 to 1990 in more than 100 countries to conclude that "middle-class societies have more income and growth."

Then there is the work of Harvard economists Alberto Alesina and Dani Rodrik, who studied economic growth in the period between 1960 and 1985 in advanced and developing countries. They find that countries with high inequality have lower subsequent levels of growth and argue this is because the poor in unequal countries promote policies that stunt growth.²⁵ A host of other researchers have similar findings and arguments.

While most of this research is based largely on analyses of developing countries, a small but growing literature specifically focusing on the United States is finding that equality is good for growth. The University of Geneva's Ugo Panizza's econometric analysis of economic growth among U.S. states from 1940 to 1980 shows that equality leads to growth.²⁶ Similarly, in an econometric study of U.S. economic growth at the state level between 1960 to 2000, Ohio State University's Mark Partridge found that a greater share of income going to the middle-income quintiles within states leads to higher

levels of growth.²⁷ And after analyzing the growth of 74 U.S. metropolitan regions in the 1980s, Manuel Pastor at the University of Southern California found that greater equality within regions (measured by poverty reductions in central cities) corresponds with stronger regional economic growth (measured by growth in per capita income).²⁸

In a paper published by the Cleveland Federal Reserve Bank, Randall Eberts of the W.E. Upjohn Institute for Employment Research and colleagues analyzed growth in 118 regions in the 1994–2004 period and found that racial inclusion and income equality were positively correlated with economic growth measures including employment, output, productivity, and per capita income.²⁹ A later analysis by Pastor and Chris Benner at the University of California, Davis, found that concentrated poverty, income inequality, and racial segregation exerted a significantly stronger drag on growth in older industrial cities—the same places where growth is most needed—than on cities with stronger markets.³⁰

Although the new literature arguing that equality is good for economic growth is still in the early stages, it is clear that the old view of inequality being unambiguously good for economic growth is inaccurate. There is no need to choose between growth and equality. Further, it is possible that the old view was completely backward and inequality actually harms growth. More research is needed to understand how and why equity and growth are related.

Promoting growth *through* equity

The implications of this new economic thinking for policy and practice are enormous. When policymakers and private-sector leaders think about how to promote economic growth and development, equity tends to be a last consideration—something distant from immediate concerns about attracting, growing, and sustaining businesses. The assumption is that growth will trickle down to those at the bottom of the income distribution. But while a rising-tide economy does create more economic opportunities in an absolute sense, growth in and of itself does not automatically benefit the poor or reduce economic disparities. Even during our last period of economic growth, for example, the racial income gap grew rather than shrank.³¹ Growth might be a necessary *but insufficient* condition for increased equity.

In contrast, if equity is in fact good for economic growth, then the inclusion of those that have been left behind cannot be seen as an afterthought or a separate policy realm but rather as a goal to be pursued in tandem with economic growth strategies. Leaders seeking to foster economic growth and competitiveness will need to develop a new focus on equity, not to gain recognition for social responsibility or community-mindedness but to achieve their primary goals of growth and competitiveness in the long run.

To secure our economic future, we need to begin developing a robust economic growth and competitiveness agenda that incorporates equity and achieves equitable outcomes.

For the policy community, this means building political and public will, expanding our knowledge base, cultivating new leadership and institutional infrastructure, and articulating a set of public- and private-sector strategies to achieve equitable growth. Some key steps to building this agenda include:

- Reframing the national conversation about equity and economic prosperity
- Crafting a policy platform for equitable economic growth
- Disseminating local innovations that advance economic equity
- Cultivating equity leadership in the economy
- Prioritizing, measuring, and tracking equity goals

Let's look at each of these recommendations in turn.

Reframe the national conversation about equity and economic prosperity

As a first step, we need to change our collective understanding about what, why, and how economic and social inclusion matters. A new national narrative about inclusion is needed—one that positions equity as a pursuit that is essential to our economic prosperity and inseparable from our strength as a nation.

This should be a broad and open discussion that seeks to bridge divides of race, ethnicity, and age, and build a diverse, multigenerational coalition for change. The conversation must engage new voices—particularly from unexpected sources such as private-sector leaders and moderate and even conservative politicians—as well as from progressive thought leaders.

Craft a policy platform for equitable growth

The progressive advocacy community needs to define a set of priority policy strategies at the federal, state, and local levels that link disconnected people and places to the economy and rebuild the middle class. This policy platform should cover the realms of economic development, education, workforce development, infrastructure, and tax policy. Strategies should focus on two goals: increasing and improving employment opportunities and earnings for the unemployed, underemployed, and working poor; and ensuring economic growth is more broadly shared, with reduced income inequality and greater returns accruing to those at the bottom of the income spectrum.

Disseminate local innovations that advance equity

Across our country, a cadre of practitioners and advocates working for economic justice and inclusion have developed methodologies to understand how policy choices affect poor communities and communities of color, and have advanced programs and

policies linking growth and investment with concrete benefits for the most vulnerable, providing the needed lifts and ladders for upward mobility.

Career pathways approaches that connect vulnerable people to jobs that pay good wages and provide opportunities for advancement, for example, can address the workforce needs of employers while reducing poverty and strengthening regional industry sectors. Case in point: After California's largest utility company, PG&E, recognized that a wave of Baby Boomer retirements was creating a shortage of new employees, it teamed up with local community colleges to pilot a training program that prepares young people for entry-level utility jobs. Launched in 2008, the PG&E PowerPathway program has graduated 200 students, more than half of whom have been women or people of color. A majority of these graduates have taken utilities jobs that pay between \$19 and \$29 per hour.³²

Other innovative equitable growth practices and policies that have taken root in local communities include local hiring, living wage policies, community workforce agreements, inclusionary zoning, local procurement, and minority contracting. These innovations should be shared more widely and lifted up to inform national policy. Several new federal initiatives, including the Promise Neighborhoods effort (based on the Harlem Children's Zone) and the Healthy Food Financing Initiative (based on the Pennsylvania Fresh Food Financing Initiative) exemplify how such "scaling up" can occur.

Cultivate equity leadership in the economic growth arena

To begin integrating equity concerns into strategies for growth and competitiveness—and producing more equitable growth—we will need to tap into the wisdom and experience of local equity leaders. These leaders should be recruited to sit on the policy bodies (such as commissions and task forces) that are deliberating about the economic future of our regions and nation and developing strategies to strengthen competitiveness.

This is already happening in many places. In Detroit, several of the 16 board members who will join foundation executives to guide the New Economy Initiative's \$100 million philanthropic investment in the region's economic revival are entrepreneurs of color who are long-time advocates on behalf of their communities. Community development and antipoverty leaders in the Twin Cities have recently been appointed to the governing boards of the region's agencies that are deciding how to invest in the region's transportation, housing, park, and water systems.

Equity advocates are also helping to govern the regional transportation agency in New Orleans and have restructured the agency's minority contracting and local hiring programs to increase economic inclusion. And in Los Angeles and the Bay Area, equity leaders are now on the board or staff of agencies and commissions in charge of redevelopment, ports, and public utilities.

As equity leaders, who are often people of color, join such policy bodies, they not only bring critical expertise to the table but also begin to bridge the racial gap between these institutions and the constituencies they represent.

Prioritize, measure, and track equity goals

If greater equity should be pursued within economic growth and competitiveness efforts, then equity goals need to have the same status as traditional economic development goals such as increased GDP. Some regional groups concerned with economic development have begun to do this. Boston's Metropolitan Area Planning Council, for example, launched an equity indicators project earlier this month. And Cleveland's Fund for Our Economic Future, a philanthropic collaborative focused on regional economic competitiveness, has been tracking equity indicators alongside business growth, talent development, and government efficiency and collaboration since 2006—after learning that racial inclusion and income equality were highly associated with regional economic growth (from the analysis of growth factors in 118 metros described above). The Fund is now allocating resources toward these inclusion goals as well, with some payoff. One program they developed, the Minority Business Accelerator 2.5+, has assisted 17 minority-owned businesses since 2008, creating 250 jobs and generating \$131.6 million in new revenue.

Conclusion

More than ever, our future depends on integrating everyone—but particularly those who are currently isolated—into the mainstream economy. We should do so not only because equal opportunity is a fundamental American value (though it is) or because excessive inequality could threaten civil society (though it might), but because our future prosperity as a nation will depend on the people and places that have been left behind. To truly do this we must begin to embed strategies that integrate the poor into the economy at every turn.

Doing so would have a ripple effect. Disparities in life outcomes such as health and well-being based on race/ethnicity, class, and neighborhood would begin to disappear. A child's zip code would no longer predict their health, success at school, or adult class standing. More people would participate in rebuilding the economy and more would prosper. And we would be much closer to attaining the ideal of American prosperity.

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