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The Effects of Economic Growth on Income Inequality in the US

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Abstract:

The paper analyzes the relation between growth and income inequality in the US during the post-war years (1953–2008). We show that the income of the top income groups is more sensitive to growth, defined broadly as current growth and changes in expectations of future growth, compared to the income of the lower income groups. We provide evidence that this increased sensitivity arises for two reasons: (a) the top income groups receive a large portion of their income from wealth, which is more sensitive to growth than labor income, and (b) the top income groups receive a large portion of their labor income in the form of pay-for-performance (equity compensation), which is also sensitive to growth. Consequently, we conclude that growth and income inequality are positively associated.

Keywords: GDP, Growth, Income inequality, Compensation, Stock market return

JEL: D31, J33

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