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> Americans who want to know whether living standards have improved or stagnated during the past twenty years are faced with a puzzle.... [Real] personal consumption expenditures per person... climbed 37.3 percent between 1973 and 1993... however [other data suggest] that real median family income was essentially the same in both 1973 and 1993. [273]

This article offers a solution to the puzzle, reconciling the two sets of data (see Table 1) and revealing that growing income inequality is one among several factors causing the divergence between per capita consumption and median family income. It then examines some of the changing patterns of income distribution that have led to rising inequality.

Table 1: Alternative Measures of Change in U.S. Living Standards 1973-1993

Measure	% change, 1973-93	Explanation for difference from preceding line
Per capita consumption	37.3	
Per capita disposable income	30.2	Decline in personal savings
Per capita income net of employer and government health purchases	22.4	Increased employer and government-sponsored health spending
Average money income, all persons	22.9	(Different data source from above)
Average money income, persons in families	21.6	Growth in the number of unrelated individuals
Income per person in median-income family	7.4	Growth in inequality, median grows slower than average
Median family income	0.0	Decline in average family size

(Source: adapted from article, p.272; all figures in real terms. The first three lines are based on national income and product account statistics, while the last four are based on the Census Bureau's current population surveys.)

Understanding the Trend in Living Standards

There are five parts to the reconciliation of growing per capita consumption with stagnant median family income. First, consumption grew faster than income, because the savings rate declined. Personal savings fell from 9.0 percent of disposable (after-tax) income in 1973 to 4.1 percent in 1993. Thus, as seen in the top two rows of Table 1, real per capita consumption climbed by 37.3 percent, while per capita income rose just 30.2 percent.

A second important difference is that some consumption is not financed out of family income. A large portion of health care expenditure is financed by employers or government agencies. Employer and government reimbursements for medical services climbed from 6.2 percent of personal income in 1973 to 11.8 percent in 1993. The national income and product accounts, the data source for the first three lines of the table, includes such expenditures in personal income. If health care reimbursements are excluded, then net personal income grew by 22.4 percent (third row of table) – which is quite similar to the 22.9 percent real increase in per capita money income that households reported to Census interviewers (fourth row of table).

Third, the percentage of the population living outside of families has increased, from 8.8 percent in 1973 to 14.7 percent in 1993. Because there are so many unrelated individuals, it is possible for average income growth to be different for all individuals vs. those who live in families. However, this is a small effect in practice, as seen by comparing the fourth and fifth rows of the table.

Fourth, and much more important, is the increase in income inequality. Virtually all of the income gains between 1973 and 1993 went to the top 40 percent of the population, with an overwhelming share going to the top 20 percent. As a result, the average income of family members rose by 21.6 percent (fifth row of table), while the median income rose only 7.4 percent (sixth row).

Finally, the average size of families decreased from 3.44 persons in 1973 to 3.20 in 1993. Coincidentally, this was exactly enough to offset the growth in the median family's per capita income. As a result, median family income showed no change in real terms (last row of table).

Which of these numbers describes the experience of the typical family? The median family saw its real income per family member rise just 7.4 percent over 20 years. It is possible that something should be added for employer- and government-financed health benefits, though it is unclear if most people experienced an improvement in the quantity or quality of health care. Even with an allowance for health benefits, "it is unlikely that the median family enjoyed income or consumption gains exceeding 0.7 percent a year after 1973. This rate of improvement is roughly one-quarter the pace of median income growth from 1947 through 1973." [276]

Trends in Income by Source

As the intricacies of the data in Table 1 suggest, there is a need for careful adjustment for family size and other factors in analysis of income distribution. Using a common system of adjustment for family size, the Gini ratio for adjusted personal income rose from 0.358 in 1973 to 0.419 in 1993, a 17 percent increase. These data are based on public-use Census files, which lack accurate information on the top 3 percent of the population; thus the analysis presented here (and in other Census-based studies) refers only to people below the 97th percentile.

Examination of the sources of household income reveals growing inequality in all major areas. A household's income may include male head earnings, female head earnings (both parents are counted as heads in two-parent families), other family members' earnings (which are small and declining at all income levels), and nonlabor income of several types. From 1973 to 1993, the bottom income quintile saw a sharp decline in male head earnings (both due to the declining number of low-income households with male heads, and to declining earnings for low-income men), only a small increase in female head earnings, and a drop in nonlabor income due to the decline in per capita public retirement payments to this group. All other groups saw rapid increases in both female head earnings and nonlabor income. Male head earnings declined modestly in the middle three quintiles, and inched upward in the top quintile.

In other research the author has analyzed the effect of these and related factors on the Gini coefficient, finding four main factors that account for its 17 percent rise from 1973 to 1993: the sharp decline in the proportion of people who live in families with a male head; increased earnings inequality among men; the growing positive correlation of female earnings with male earnings; and the increase in unearned income, such as interest, dividends, and private retirement payments, that are correlated with other income sources. The first three are particularly important for working-age families, while the last is most important for those over 65.

The next section focuses on the third of these factors, the male-female income correlation.

Earnings Inequality

Inequality rose among women and among men between 1973 and 1993. On average, women fared better, experiencing rising median real wages while the male median declined. Common explanations for rising inequality of wages include the effects of technology and trade. However, the change in earnings disparities cannot by itself account for the jump in family income inequality since 1973. Equally important is the changing relationship between male and female earnings within the family.

If men are ranked by decile, their real earnings change from 1973 to 1993 rises monotonically, from a 40 percent drop in the bottom decile, to no change in the ninth decile and a small gain in the top group. The change in the average wife's real earnings can also be calculated for each male decile, counting zero wife's earnings both for unmarried men and for those with non-working wives. This figure rises smoothly from roughly zero in the second decile, to 157 percent in the top decile. As a result, male and female earnings changes reinforce each other, and family incomes grow faster in higher deciles. In the bottom six deciles, increases in women's earnings were too small to offset the decline in men's earnings, so family earnings fell.

Three factors determine the average wife's earnings: the percentage of men who are married; the percentage of married men who have working wives; and the average earnings of employed wives. Change in all three factors has tilted in the direction of greater inequality. The percentage of men who are married has declined at all income levels, but it has fallen much faster among lower-income men. The percentage of wives who work has increased at all levels, but it has increased fastest among wives of higher-income men. And the change in earnings among wives who work has likewise been positively correlated with their husband's earnings. Overall, in 1973 the correlation between male- and female-head earnings was negative; by 1993 it had become strongly positive.

In conclusion, there are several components to the rise of inequality after 1973. The much-discussed trend toward male earnings inequality and declining prospects for low-income male workers is only one part of the story. Changes in family composition have deprived an increasing proportion of families of the presence of a working male head. Less often noticed is the effect of rising employment and earnings among married women; this increase has been particularly concentrated among wives of high-wage husbands, further contributing to inequality. Trends in unearned income have also boosted inequality, with rising income from capital assets among upper-income groups. Meanwhile, government transfer payments had little effect in ameliorating the trend toward inequality. So long as the benefits of prosperity are so unevenly distributed, "a large minority – perhaps even a majority – of Americans will remain convinced that U.S. living standards are languishing." [289]