Inequality and the Economics Profession
Politics, Economics, and Academic Agendas in the Reagan Era

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For my professors, friends, and parents,

who believed in me even during the bleakest hours
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Introduction

While there have been many attempts among scholars to separately analyze the Reagan era and American conservatism, the dynamic history of the economics field and profession, and the changing landscape of economic inequality in the United States over the last half-century, very few attempts have been made to connect the three themes together. Historians and academics in other fields have correctly marked the 1970s as a watershed decade that summoned broad changes in the three larger areas outlined above. “The conservative movement that brought Reagan to power in 1980” was in many ways completed and accomplished in the 1970s through changes in political and economic thought.1 “An eightfold increase in the price of oil stemming from Middle Eastern turmoil exacerbated inflation...which combined with a slowing economy to create the new dilemma of ‘stagflation,’” precipitating economic crises that facilitated the retreat of Keynesianism and called into question decades of consensus in the economics profession.2 Additional results of the economic crises and stagflation were the growth of economic inequality and difficult times for working class people. Rapid deindustrialization and labor laws seen as unbeneﬁcial to workers prompted United Auto Workers’ President Doug Fraser to declare in 1978 that a “one-sided class war” was being waged on American workers.3 These separate developments have been well-documented individually, but work combining them in an explicit fashion has not been produced.

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Specifically, analyses of how the members of the economics profession discussed and wrote about inequality during the years of and around the Reagan presidency have not been performed. Such analyses would yield information about how economists have written about inequality throughout the history of the profession, and how economists wrote about inequality during the 1970s and the Reagan presidency. The results produced by this study would help elucidate the ways in which the study of inequality fits into the economics profession, while expanding the knowledge of how the profession behaved and evolved during the 1970s and 1980s, reacting to the political, social, and cultural ethos in the Reagan era and the years leading up to it. Additionally, this analysis may illuminate the ways in which the study of a specific topic in a discipline, such as the study of economic inequality by economists, is shaped and affected by larger developments in politics and the academic field itself.

My honors thesis attempts to produce this type of analysis and fill an important gap in the historical literature. By looking at primary source documents including the work of the most famous historical economists, scholarly articles from the top economics journals, and conference proceedings from the most important annual economic gatherings, I will attempt to show the ways in which economic inequality was discussed by economists and show how this discussion may or may not have been shaped by larger cultural and political shifts, the state of the economy, and the changing face of the economics profession itself. Using a broad analysis of the Reagan era to include the years during which Reagan first became a prominent national political figure, the significant decade of the 1970s, and the Reagan presidency-dominated 1980s, I will attempt to augment these primary source reflections of the economics profession’s interest in inequality with historical analyses of major developments during this Reagan era.
Through secondary source analyses of the changing economics profession, the political
details and developments of the Reagan era, and the political economy of poverty, I will try to
explain my finding that economists’ discussion of inequality did not seem to comport with the
trend of inequality during the Reagan era. As inequality began to rise during the 1970s and then
accelerate during the Reagan presidency, the number of articles and conference proceedings
relating to the distribution of income and other means of discussing inequality did not rise in
frequency or intensity. Economists did not seem to respond to the real economic conditions on
the ground, perhaps justifying traditional fears of the isolation of academia’s “ivory tower.” My
thesis will investigate possible explanations for this phenomenon, including external forces such
as economic conditions and political movements, internal shifts that sought to remold the
economics profession from within, and the isolation of the economics profession from the real
world.

The rest of this thesis will go into more detail about specific developments during the
Reagan era which likely shaped the ways in which economists studied inequality.

Chapter one will look at the ways in which economic crises of the 1970s facilitated
seismic shifts in the study of the macroeconomy, including the retreat of Keynesianism and the
rise of alternate theories such as Monetarism and supply-side economics. Also discussed in this
chapter is the rise of microeconomics as the foundation for the study of rational choice theory,
law and economics, and game theory. These developments, combined with the possibility of
economics’ isolation from the real world, may help explain why inequality was an important
issue to economists’ during some periods and failed to arouse the focus of economists during
other periods.
Chapter two focuses of broader shifts in American politics during the late 1960s and 1970s that facilitated the rise of Reagan as a messianic hero on the right and an enemy of working class people on the left. The rebirth of a strong element of conservatism went hand in hand with the rebirth of the market as an idolized popular symbol of economic success and individual liberty. These larger political developments were indicative of the times and were largely occurring concurrently with the changes in the economics profession itself. However, specific political developments during the Reagan presidency may shed light on economists’ discussion of inequality that solely internal shifts in the field cannot adequately explain.

Finally, chapter three focuses on poverty and notions of an “underclass” in American society. Economists’ discussions of racial and gender inequality combine with “Ronald Reagan’s war on welfare in the 1980s” to highlight further ways in which economists’ discussed inequality and may have been affected by shifts in the political economy and public consciousness. The lack of discussion among economists in the 1980s about the state of inequality and poverty, just as Ronald Reagan was implementing policies injurious to the poor, is an important case study worth investigating.

The three chapters each tell a story of an important development that shaped the Reagan era and shaped the ways in which economists chose to write about economic inequality and how often they did so. Rising inequality, high incidence of poverty, a changing political climate, and a reformulation of the driving concerns and methods of the economics profession all characterized the Reagan era. While these have individually been acknowledge by historians and other scholars, a synthesis of these major characteristics in an attempt to explain the

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inequality agenda of economists has not been attempted. The following chapters and conclusion of this thesis attempt to explain this specific agenda in the context of American political economy and perhaps provide an understanding of academic agendas more generally.
Chapter 1: Inequality and the Changing Economics Profession

The historical literature indicates that the 1970s and 1980s were years of turmoil, unrest, and seismic change in the United States, as many of the traditional mid-century ideas about economics, gender and race, community obligation, and other long-standing ideas began to “fracture,” in the words of historian Daniel T. Rodgers.5 These fractures had very real implications for national politics and contributed to shifts in the economics profession that may help explain the absence of much discussion of inequality at the highest levels of the economics profession. Economic turmoil of the 1970s helped eradicate the Keynesian consensus, opening doors to greater popular support for supply-side economic ideas of Arthur Laffer and Monetarist philosophies articulated by publically visible economists such as Milton Friedman. These changes in macroeconomics were accompanied by the rise of microeconomics as the foundation for new fields in the economic profession, such as law and economics, rational choice theory, and game theory.

Despite social and political divisions in the late 1960s, “there [was] broad agreement on economic policy: a combination of active management of the economy to achieve high employment, and a welfare state based on progressive taxation.”6 Indeed, this consensus led President Richard Nixon to declare that “we are all Keynesians now.”7 The Keynesian consensus would soon give way to larger debates over the macroeconomy, however, as economists such as Milton Friedman at the University of Chicago and Martin Feldstein at Harvard University began to promulgate economic theories that questioned the role of the government in

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economic affairs. “Their skepticism was given weight by the emergence of stagflation in the 1970s.” Poor economic conditions in the 70s led to the questioning of Keynesianism’s assumption that active government involvement in the macroeconomy could produce positive outcomes in employment and price stability.

It is in this broader context of the state of the economy and the changing assumptions of the economics profession that my thesis enters. With the leveling off of real median wages in 1973 and the rapidly increasing income inequality of the 1980s, two developments that will be discussed in more detail later, one may expect to find a growing number of articles appearing in leading economics journals as the Reagan presidency progressed. However, a quantitative analysis of five of the field’s leading journals seems to indicate that that trend did not manifest itself. Through consultation with current professors of economics, I have selected five of the most respected journals in the field of economics and have looked through the articles in these journals for writings about inequality. The quantitative and qualitative analysis of these journal articles forms a large portion of the primary sources that I use for the rest of this paper. In analyzing these articles, I hoped to gain some insight into the ways in which economists studied inequality and the way these studies may have changed through the years.

Figure 1 shows the number of articles recovered for the period 1970-1989 for the five journals – American Economic Review, Journal of Political Economy, Quarterly Journal of Economics, Review of Economic Studies, and Review of Economics and Statistics. This analysis encompasses articles addressing inequality, a term which I have chosen to define very loosely.

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8 Krugman, Peddling Prosperity, 15.
Topics include income transfer and optimal redistribution schemes,9 racial discrimination and black-white pay differentials,10 the role of schooling and equal opportunity on wage differentials,11 gender pay inequities,12 inequality in faculty salaries,13 and the distribution of wealth and income, which dominates the bulk of this study and is reflected in many of the specific articles about which I have chosen to write. The outlier in Figure 1, the American Economic Review, contains many articles about wage differentials, human capital, and discrimination. These articles seek to explain how human capital, race, gender, and other factors determine the differences in observed wage rates and explain occurrences of discrimination in the labor market. Their abundance in the AER helps explain the larger number of articles in this journal that were categorized as having to do with economic inequality.

Figure 2 uses statistics from the same analysis to show the number of articles by year, across all five journals. The chart does not support the hypothesis that the number of articles

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addressing issues of economic inequality increased with inequality data through the given period. Indeed, a trend line of best fit that could be applied to the chart across the period would show an inverse relationship between the amount of economic inequality and the number of articles from major journals addressing the issue. The aggregate number of articles across the five journals in the 1970s is eighty-seven, while the aggregate number of articles in the 1980s is sixty-eight.
Figure 1: Number of “Inequality” Articles in 5 Leading Economics Journals, 1970-1989

Figure 2: Number of “Inequality” Articles in 5 Leading Economics Journals, By Year, 1970-1989
Despite the lack of an identifiable change in the frequency with which economists addressed inequality during the Reagan era, individual economists published articles in leading journals on a wide array on economic inequality issues. While inequality concerns during the Reagan era never trumped those of larger contemporary issues such as inflation, some economists published articles on the many different types of inequality highlighted above, including those on income inequality and the wealth distribution, the topic of primary interest in this thesis.

Throughout the 1970-1989 years, individual economists in the five major journals which I have analyzed looked at macro scale economic inequality\(^\text{14}\) in three major ways – the distribution of income, the proper ways to measure inequality, and the details of historical economic inequality. In addressing the first of these three main areas of writing about economic inequality, University of Indiana and Cornell University economists, respectively, George M. von Furstenberg and Dennis C. Mueller wrote an article in the September 1971 volume of the *American Economic Review* on the Pareto optimal approach to income redistribution.\(^\text{15}\) Citing contemporary “attempts...to reintroduce the income distribution question into mainstream economic literature,”\(^\text{16}\) they declare, “If a significant amount of redistribution can be provided without anyone losing welfare, social conflict and the need for

\(^{14}\) I use the phrase “macro scale economic inequality” here to refer to economic inequality viewed over the entire spectrum of the economy. Specific examples of this include the broad distribution of income and how this is measured. I consider articles addressing issues such as wage disparities between men and women or between blacks and whites to be micro in scale, as they affect individuals or groups of individuals specifically.

\(^{15}\) Von Furstenberg and Mueller, “The Pareto Optimal Approach to Income Redistribution.”

coercion can be minimized."\textsuperscript{17} While they ultimately conclude that a redistributive tax program may only effectively reallocate income without social welfare loss in an environment where those transferring the income are supportive of the measure – a highly dubious proposition – the fact that they and others are writing such articles suggests the widespread acceptance of Keynesianism in the economics profession at this time.

Keynes’ economic contributions in the wake of the Great Depression formed the foundation of much of modern macroeconomics and portrayed a world in which the government could play a legitimate and effective role in mitigating the harsh swings of boom and bust cycles through policies that shifted aggregate demand. In his classic work outlining these ideas, \textit{The General Theory of Employment, Interest, and Money}, originally published in 1936, Keynes briefly discussed economic inequality in Chapter 24:

For my own part, I believe that there is social and psychological justification for significant inequalities of incomes and wealth, but not for such large disparities as exist today. There are valuable human activities which require the motive of money-making and the environment of private wealth-ownership for their full fruition...But it is not necessary for the stimulation of these activities and the satisfaction of these proclivities that the game should be played for such high stakes as at present. Much lower stakes will serve the purpose equally well, as soon as the players are accustomed to them. The task of transmuting human nature must not be confused with the task of managing it. Though in the ideal commonwealth men may have been taught or inspired or bred to take no interest in the stakes, it may still be wise and prudent statesmanship to allow the game to be played, subject to rules and limitations, so long as the average man, or even a significant section of the community, is in fact strongly addicted to the money-making passion.\textsuperscript{18}

Keynes’ passage reflects the concern with the “animal spirits” of human nature that cause the desire to accumulate large amounts of wealth. His argument seems to suggest that government

\textsuperscript{17} Von Furstenberg and Mueller, “The Pareto Optimal Approach to Income Redistribution,” 628.

intervention to “lower the stakes” of the game of economics would serve to limit the extent of inequality and provide greater stability to the macroeconomy. The prevalence of his economic philosophies through the early 1970s may help explain the climate under which economists like von Furstenberg and Mueller wrote their analyses of the distribution of income.

It is important to note that a clear trend can be identified in the papers and proceedings of the American Economic Association meetings, as current political and economic conditions have a clear effect on the content of many of the panels at the most important annual gathering of economists. The 1972 meeting featured work on the Chinese economy, perhaps influenced by President Nixon’s groundbreaking visit to China during that year. The 1973 meetings featured panels on the International Energy Supply and Major Economic Problems of the 1970’s, reflecting not only the polarizing importance of the year’s oil shock, but also a more general concern with the need for focus on contemporary economic issues. This attention to contemporary details reasonably should extend to analyses of economic inequality, reflected in increases in the amount of articles written as the extent of inequality grew. As we will see later, however, this did not manifest itself, and the opposite hypothesis appears to be the reality.

An important development seen in the American Economic Association annual meeting papers around this time is the slow erosion of the Keynesianism consensus as the dominant economic philosophy. The 1971 panel discussing Keynesianism and its Pioneers soon was countered by a panel in 1974 taking A Critical Look at the Keynesian Model: Theory and Application. In between these panels was the year 1973, which has been recognized as an important year in the history of economics for a number of reasons. As Godfrey Hodgson has argued, “The biggest single cause of the economic transformation that ended the years of
almost continuous economic growth, and the corresponding optimism of the years of the liberal consensus, was the doubling of crude oil prices as a result of the Arab boycott in 1973.\textsuperscript{19} These economic conditions contributed to the fall of the “liberal” Keynesian consensus and created a vacuum for the rise of other economic philosophies.

Further erosion of Keynesianism can be witnessed in a 1976 panel on The Invisible Hand and Other Matters. Finally, in 1979 the Appraisals of Post-Keynesian Economics panel suggested a near-complete withdrawal of the dominance of traditional Keynesianism. The papers on this panel included “Post-Keynesian Economics: A Promise that Bounced?”,\textsuperscript{20} “On Keynesian Economics and the Economics of Post-Keynesians”,\textsuperscript{21} and “Post-Keynesian Economic Theory: An Overview and Evaluation.”\textsuperscript{22} The first of these papers criticized modern “Keynesian” economics as inadequate in reflecting the original work of Keynes and suggested a return to these founding principles. This decline of Keynesian economic philosophy was mirrored by a rise in supply-side and monetarist theories. The 1983 AEA conference in San Francisco featured panels directly related to these theories, including Tax Policy: A Further Look at Supply-Side Effects, and Monetarism: Lessons from the Post-1979 Experiment. The latter contained a paper delivered by Milton Friedman.\textsuperscript{23}

\begin{footnotesize}
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\item \textsuperscript{20} L. Tarshis, “Post-Keynesian Economics: A Promise That Bounced?” \textit{American Economic Review} 70, no. 2 (May 1980).
\item \textsuperscript{22} James R. Crotty, “Post-Keynesian Economic Theory: An Overview and Evaluation,” \textit{American Economic Review} 70, no. 2 (May 1980).
\item \textsuperscript{23} Milton Friedman, “Lessons from the 1979-82 Monetary Policy Experiment,” \textit{American Economic Review} 74, no. 2 (May 1984).
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One of the favorite tools of economists during the post-World War II period of Keynesian consensus was the Philips curve. Developed in 1958 from an analysis of British price-wage data and soon introduced in the 1961 edition of Paul Samuelson’s famous economics textbook, the Philips curve suggested an easily identified and interpreted tradeoff between inflation and unemployment. In short, macroeconomic policymakers could theoretically trade off inflation and unemployment, with higher levels of inflation resulting in lower levels of unemployment, and vice versa. The economic crises of the 1970s, however, produced conditions where policymakers could only tackle inflation or unemployment, but not both. “The Phillips data danced wildly across the economists’ graphs. The expected patterns of the business cycle seemed to disintegrate, its phases colliding into one another in the phenomenon Americans called “stagflation,” and the British, caught up in an even sharper version of the same troubles, called “slumpflation.””

Keynesianism suggested a predictable view of macroeconomics that was comforting and understandable. In conjunction with the central bank’s manipulation of monetary policy, the government could manage taxes and spending via fiscal policy to accelerate the economy in times of recession and put on the brakes in times of rapid economic expansion. As Rodgers indicates in a passage that deserves to be quoted at length, stagflation that formed the basis of economic malaise in the 1970s was harmful not only for its negative economic impacts but for the turmoil in which it thrust macroeconomic thought:

The economic crisis of the 1970s was, in short, not merely a crisis of management. It was also, at least as painfully, a crisis in ideas and intellectual authority. An extremely confident analytical system had failed to explain or make sense of the unexpected. In

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24 Rodgers, Age of Fracture, 48.
25 Rodgers, Age of Fracture, 48.
time, after the economy emerged from the recessionary wringer of 1980-1983, something like the Phillips curve would return. The Reagan tax cuts of the early 1980s, it would be said, ultimately functioned as Keynesian demand stimulus, just as the textbooks might have predicted. Conventional macroeconomics did not predict dramatically wrong. What was devastating to the reigning models was that none of their architects knew why they mispredicted.26

A decade of Phillips curve unrest helped facilitate the demise of Keynesianism as the dominant economic philosophy. Much like how the Great Depression shattered the popular economic ideas before the stock market crash and subsequent depression and produced the effective Keynesian consensus, the economic crises of the 1970s ushered in a new era of thinking about economics.27

The data highlight the inconsistencies in the Phillips curve. Historically, high unemployment would be seen in times of recession and would be accompanied by lower levels of inflation, an idea backed by the theoretical formulations of the Phillips curve. Figure 3 shows the Civilian Unemployment Rate, while figure 4 shows the Consumer Price Index measure of inflation for the period analyzed, 1965-1995. 1965-1970 backs the Phillips curve understanding of the macroeconomy, showing that as unemployment declined slightly during the period, inflation rose. This relationship would break down over the longer time frame, however, yielding stagflation. In 1980, for example, the unemployment rate hovered around 7% while inflation was averaging roughly 13% per annum. Both are rather high values that would normally not have been witnessed in concert. Policymakers could address one of these issues, but not both.

26 Rodgers, Age of Fracture, 49-50.
Figure 3

Civilian Unemployment Rate (UNRATENSA)

Figure 4

Consumer Price Index for All Urban Consumers: All Items (CPIAUCSL)
The fall of Keynesian attributable largely to the data’s refutation of the Phillips curve has been summarized very nicely by Hodgson:

At the heart of the prevailing Keynesian orthodoxy was the idea that there was a trade-off between inflation and unemployment. Let unemployment rise, the Keynesians assumed, and government had only stimulate aggregate demand, either by public investment or by cutting taxes, and all would be well. This orthodoxy was enshrined in the Phillips curve, a graph representing the relation between employment and inflation. Now, suddenly, instead of inflation rising as unemployment declined, and unemployment rising if inflation was forced down, both unemployment and inflation were running at historically high levels (emphasis in the original). For policymakers, the question was, as always, “What is to be done?” But for some economists, with varying degrees of excitement and even glee, it was, “Is the reign of Keynesian orthodoxy at long last coming to an end?”

The excitement of these economists more enamored of the Monetarist and supply-side philosophies was understandable, as the fall of Keynesian soon manifested itself in many ways, having residual impact on the study of inequality among those in the profession.

In addition to the fall of Keynesianism and the rising influence of monetarism, the economics discipline saw some other radical changes in the 1970s that persisted into the Reagan presidency. The first of these was the rise of law and economics, which fused the two previously largely unconnected disciplines. Largely based on Ronald Coase’s important 1960 article “The Problem of Social Cost” and its accompanying Coase theorem, law and economics sought to answer legal questions through the lens of economic market efficiency rather than purely through harm and restitution. According to Rodgers, the most influential piece of literature resulting from the work of Ronald Coase was Richard Posner’s Economic Analysis of

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30 Rodgers, Age of Fracture, 58.
Law (1973). Posner would go on to be one of the leaders in the law and economics field and would eventually deliver the Richard T. Ely lecture on the subject at the American Economic Association meeting in 1986. Now in its eighth edition, Posner’s book asks the rhetorical question, “Can the idea of ‘justice’...be deduced from the economist’s idea of efficiency?” This fundamental idea became the backbone of economic teaching that would gather support from conservative backers such as William E. Simon’s Olin Foundation and the Mont Pelerin Society, which offered “summer camps” in law and economics that provided graduates with copies of Milton Friedman’s *Capitalism and Freedom*. The connections between the law and economics movement and conservative politics become important when one considers how deeply the reliance on market-based, efficient solutions permeated legislative politics in the form of deregulation. The years between 1979 and 1982 featured substantial removal of regulation controls in the fields of trucking, long-distance bus transport, rail transport, telecommunications, oil, and savings and loan institutions.33

Mirroring the rise of law and economics, which focused largely on the ideas that utility and efficiency should be the basis of legal reasoning, academic economics began to incorporate connected ideas about microeconomic foundations for much economic study, game theory, and rational choice theory.34 The combination of these three ideas looked at individuals as rational actors who made decisions based on the maxim of utility-maximization. According to Rodgers, “The conceptual core of rational expectations was simple. Economic actors did not simply react to economic information; rather, [Robert] Lucas maintained, they learned to

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31 Rodgers, *Age of Fracture*, 58.
33 Rodgers, *Age of Fracture*, 62.
34 Rodgers, *Age of Fracture*, 63-68.
anticipate economic actions, decoding the rules of thumb of other economic actors and foreseeing their line of action."35 Robert Lucas’ work at Carnegie Mellon University and the University of Chicago in the early 1970s formed the basis for much of the work on rational expectations that would become the foundation for game theoretic models like the prisoner’s dilemma.36 The larger implications of the greater attention paid to these newly burgeoning fields in academic economics would help shift discussion away from economic inequality and the ways in which government could alleviate it. Backed by the fancy mathematics that has continually become one of the distinguishing marks of modern economics, “Lucas proposed that in monetary policy only truly unanticipated changes – decisions that successfully fooled and misled economic actors – actually made a difference in aggregate economic behavior.”37

Though Lucas did not have the public impact of a Milton Friedman and chose to write in highly mathematical, dense prose, he was one of the most, if not the most, influential economists of the 1970s.38 Much like the ways in which the downfall of Keynesianism and the rise of Monetarist influence eroded confidence in the government’s ability to manage the macroeconomy, the rise of game theoretic analyses backed by Lucas’ rational expectations models suggested a related impotence of fiscal and monetary policies to steer the macroeconomy in a world where individual economic actors had formulated their own expectations of how economic policymakers would behave and consequently already factored in these expectations to their decisions.

35 Rodgers, Age of Fracture, 64.
36 Rodgers, Age of Fracture, 64.
37 Rodgers, Age of Fracture, 65.
38 Krugman, Peddling Prosperity, 48.
The importance of the figures in law and economics and rational choice theory cannot be underestimated, as their contributions to economics went recognized at the highest levels of the field. Whereas Amartya Sen represents the only example of an economist working on welfare economics and inequality to win a Nobel Prize in Economics for his work, the niche fields of economics that expanded rapidly in the 1970s and influenced the economic and political ethos of the years during the Reagan presidency saw two of its leading figures win Nobel Prizes for their work in consecutive years. In 1991, Ronald H. Coase won the prize “for his discovery and clarification of the significance of transaction costs and property rights for the institutional structure and functioning of the economy.”

A year later, Gary S. Becker, a University of Chicago economist and frequent collaborator with Richard Posner, won “for having extended the domain of microeconomic analysis to a wide range of human behavior and interaction, including nonmarket behavior.” The influence of these figures and their strong belief in the efficient market helped further erode the confidence in government to effectively manage the economy, contributing to the shift away from discussion of economic inequality just as the issue should have reasonably become more important during the Reagan presidency.

The AEA conference proceedings also point toward the rise of law and economics as a major field of interest. A 1977 panel featured a discussion on Economics and Law, 1979’s featured Borderlines of Law and Economic Theory, and in 1980 the discussion was reflected in a panel entitled Law and Economics in an Environment with Imperfect Information. The influence

of law and economics on the AEA conferences culminated with Richard A. Posner, one of the pioneers and leading figures of the law and economics movement delivering the Richard T. Ely Lecture on the subject in New Orleans in 1986. The economists who pioneered the study of these newly burgeoning fields in the economics profession shared a level of influence and frequency of publication not matched by those working on inequality issues.

However, some economists writing in the field’s most influential journals during 1970-89 decided to look at inequality. One thing with which they were very concerned was the correct methods for measuring economic inequality. In an influential article appearing in the September 1975 volume of the *American Economic Review*, Portland State University economist Morton Paglin offered a basic revision of traditional methods of measuring inequality.\(^{41}\) Paglin set forth technical criticisms of the foundations of the methods economists used to calculate the Lorenz curve and Gini coefficient. The Lorenz curve, developed in 1905 by Max O. Lorenz, is a graphical representation of the wealth distribution. The Gini coefficient is derived from the Lorenz curve and its accuracy is thus contingent upon the accuracy of the Lorenz curve. As Paglin acknowledged, the Lorenz curve had been the most popular tool for measuring economic inequality in the sixty years prior to the writing of his article. Ultimately, however, Paglin concluded, “An application of the new concepts to U.S. income and wealth data reveals that estimates of inequality have been overstated by 50 percent, and the trend of inequality from 1947 to 1972 has declined by 23 percent.”\(^{42}\) Though writing nearly a decade earlier, Paglin is clearly disagreeing with data that has formed the foundational underpinning of


\(^{42}\) Paglin, “The Measurement and Trend of Inequality,” 608.
the work of Dooley and Gottschalk, which will be discussed later. In retrospect, it is easy for present-day observers to note that inequality began to increase around 1973 and slowly accelerated after that, yielding analyses of inequality before this period to be less conclusive as they are dealing with smaller changes in the level of inequality. In effect, then, his writing reflects economists’ general concern with inequality throughout the profession’s history, in isolation from the actual events of economic importance. Despite there being a decrease in economic inequality in Paglin’s estimation of the data, economists such as Paglin still wrote about the issue sparingly in an effort to correctly identify the proper techniques for measuring inequality. This fact may point to economists’ agendas being set by historical concerns of the profession and debates among colleagues over new work in the field, rather than the economic conditions on the ground.

Indeed the Paglin article elicited a large number of responses from his colleagues around the country, not because of a crisis of extremely high levels of inequality, but because of the content of Paglin’s work and the opportunity for debate about an issue that had been of concern to economists since the advent of the Lorenz curve in 1905. Five economists wrote comments on Paglin’s article, and these were published alongside a reply from Paglin in the June 1977 volume of the American Economic Review. These comments generally deal with remedying flaws in Paglin’s methods and do not suggest writing about inequality in the context of contemporary macroeconomic conditions. As represented by these short, direct comments, economists continued to use Paglin’s work as the jumping off point for their discussions of economic inequality. For instance, John P. Formby and Terry G. Seaks, professors at the University of North Carolina – Greensboro, commented on Paglin’s work in a short 1980
comment, and with W. James Smith, a professor at the University of Colorado – Denver Center, published a slightly longer reconsideration of Paglin’s work in 1989. A footnote from the 1989 article indicates that the authors had compiled a list of over one hundred citations to Paglin’s article in the fourteen years since its initial publication. Not to be outdone, the three offer yet additional comments and modifications to Paglin’s work, adding to the never-ending stream of debate over the proper techniques for applying the Lorenz curve and Gini coefficient to measurements of inequality. In a telling example of how the debate among economists overshadowed the importance of external economic conditions on their work, Formby, Seaks, and Smith include a chart showing a specific aspect of the Gini coefficient to strengthen their discussion of inequality. The chart shows steep and persistent increases in inequality beginning in 1980, and while they acknowledge this aspect of the graph, they fail to address any larger concerns that may be connected with this development.

Articles written about macro scale economic inequality also took the form of historical inquiries into inequality during different periods. Jeffrey G. Williamson published an article in the November 1976 volume of the *Review of Economics and Statistics* in which he tried to determine the sources of American inequality in the years 1896-1948. He concedes that limitations on economists’ quantitative understanding of certain data prevent fully accurate understandings of the sources of inequality during the period he studies, but argues that inequality has something to do with the combination of factor demand and labor supply,

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especially of unskilled workers.\textsuperscript{47} Williamson importantly includes graphs highlighting the large amount of inequality before the stock market crash of 1929 that brought on the Great Depression. Looking even further back than Williamson, Ohio University economist Lee Soltow looked at wealth inequality in the United States in 1798 and 1860.\textsuperscript{48} Soltow presents his work with the idea that little is known about wealth inequality in the United States, as more attention has been given to the measurement of income inequality.\textsuperscript{49} Through his work he determines, “The conclusion I have reached is that there was extensive inequality in wealthholding in the United States in 1798, and that this condition continued at a level almost as high two generations later.”\textsuperscript{50} Despite their interest in looking at income and wealth inequality during different period of American history, Williamson and Soltow do not ground their interest in their topics in contemporary economic conditions and seem to rather be reflecting typical concerns of economists.

While it may appear that traditional concerns of economists prompted discussion of inequality, these articles were few in number. Rather, broad changes in the economics profession inhibited the number of articles about inequality. Economic crises produced a climate that existing Keynesian or neoclassical synthesis model foundations were not able to sufficiently answer.\textsuperscript{51} As the retreat of Keynesianism signaled a return to unfettered market ideology, the position of the government to effectively manage the macroeconomy – and, presumably, other matters such as inequality – became less certain and was called into

\begin{itemize}
  \item \textsuperscript{47} Williamson, “The Sources of American Inequality,” 397.
  \item \textsuperscript{49} Soltow, “Wealth Inequality in the United States,” 444.
  \item \textsuperscript{50} Soltow, “Wealth Inequality in the United States,” 451.
  \item \textsuperscript{51} Roger E. Backhouse and Philippe Fontaine, eds., \textit{The History of the Social Sciences since 1945} (New York: Cambridge University Press, 2010), 58-59.
\end{itemize}
question by those within the economics profession. Those internal thinkers who questioned the Keynesian consensus would become publicly influential figures and would play a very large role in the political movements that swept the 1970s and defined the Reagan era.
Chapter 2: Larger Political Developments in the Reagan Era

The rebirth of a strong conservative segment of the population coming out of seeds planted in the 1960s helped propel changes in economics as well as politics that culminated in the rise of Ronald Reagan, who became a semi-messianic figure to those on the right and an arch enemy of those on the left, a “villain of the piece.”\(^{52}\) His policies of deregulation, tax cut reform, and union busting reflected the ethos of a nation that became extremely dubious of the effectiveness of government intervention. The popularity of the hands-off, “trickle-down” approach to economics and government supported by Reagan and his supporters can be largely explained by the failure of the government to effectively address stagflation, and it therefore makes sense to begin the story of the Reagan era context with the story of the way the changes occurring inside the economics profession permeated the political sphere. First, however, some short background information on Ronald Reagan’s past and its placement in the broader scope of economic inequality is essential.

In 1962 Ronald Reagan switched his party affiliation and became a member of the Republican Party, citing the alienation he felt from his former Democratic party. He would later famously say in his campaign stump speeches, “I was a Democrat most of my adult life. I didn’t leave my party and we’re not suggesting you leave yours. I am telling you that what I felt was that the leadership of the Democratic Party had left me and millions of patriotic Democrats in this country who believed in freedom.”\(^{53}\) His famous televised “A Time for Choosing” speech in support of 1964 Republican presidential candidate Barry Goldwater raised $1 million for

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Goldwater and established Reagan as a national political force on the right.\textsuperscript{54} Reagan was overwhelmingly elected governor of California in 1966 and served in the state’s highest political office from 1967-1975.

It is during Ronald Reagan’s tenure as governor of California that national conditions began to shift and the trend of inequality began to change drastically. As writers in 1988 cogently perceived, a “great U-turn” was occurring and 1973 was a pivotal year:

After about 1973, the direction [of inequality] changed. Wages, adjusted for inflation, began a long downward trend. Median annual family income stopped growing, even though more family members were working than ever before...After 1980, at the other end of the extreme of the job distribution, the number of elite earning high wages rose as well, leaving a declining proportion of employees receiving middle-level incomes. Inequality was rising again, in the labor market and at the level of family income. The distribution of wealth – income from property, such as stocks, bonds, and real estate – was also becoming increasingly unequal. Worst of all, no longer could parents assume that their children would do better than they had at the same stage of their own careers.\textsuperscript{55}

This “U-turn” would, in retrospect, become one of the defining economic characteristics of the 1970-89 period and would imply radical shifts in inequality. Despite this fact, however, Reagan’s political rhetoric would include few references to the growing distribution of income, and the economics profession would not fill the gaps in the discussion. In fact, as we have seen and will see, economists’ discussion of inequality often entered on the early part of the U-turn curve and failed to expand in number as the gap between the rich and poor widened.

The economics profession’s inability to fill these gaps in the inequality discourse can be directly attributable to the changes in the field of economics discussed in chapter one and the political developments which were partially a consequence of those changes. These changes in


economics as a discipline produced some important figures that became publicly influential political leaders. As Rodgers indicates in his history of the economics profession, the vacuum left by Keynesianism attempted to be filled by monetarism, a philosophy based on the work of Milton Friedman’s retooling of the old quantity theory of money. Essentially, “Monetarism offered a strikingly simple rule for the hard times: let the money supply be prudently managed and markets would provide the rest.” In 1979, however, only a handful of economists agreed that the Federal Reserve Board, the United States’ central banking unit, should keep the money supply at a constant rate. Monetarism’s influence seems to have been short in length, but revolutionary in the ways in tried to fill the gap in macroeconomic theory left by the retreat of Keynesianism. “Monetarism, in short, turned out to be a bulldozer that could raze a building but could not erect one,” Rodgers argues. “A powerful collector of anti-Keynesian sentiments, monetarism did a great deal to delegitimize the conventional economic wisdom, to break down the case for macroeconomic fine-tuning, and ultimately to transfer business-cycle management from Congress and the Council of Economic Advisers to [Paul] Volcker’s heirs at the Federal Reserve.” Whereas Keynesianism argued for two-pronged government intervention in the economy through the legislature’s control of fiscal policy and the Federal Reserve’s control of monetary policy, Friedman’s vision of monetarism sought to restrict the power of the government in the economy by eliminating fiscal policy as a tool to manage the economy and by limiting the leeway with which the Federal Reserve could adjust the money supply to control interest rates and inflation. Friedman’s idea of a “natural rate” of unemployment endured,
resulting in a persistent belief in the limitations of effective macroeconomic management. These philosophies would imply less justification for large-scale governmental involvement in economic affairs, a tenet that became a cornerstone of the revitalized American conservative movement.

The rise of Friedman’s ideas and their influence on the economics profession also may help explain the waning interest in inequality witnessed in the late 1970s and 1980s at the highest levels of the economics field. In his classic 1962 work *Capitalism and Freedom*, Friedman addressed the distribution of income acknowledging, “A central element in the development in the collectivist sentiment in this century, at least in Western countries, has been a belief in equality of income as a social goal and a willingness to use the arm of the state to promote it.” Unlike Keynes and even Adam Smith, however, Friedman does not seem to acknowledge the innate negative human response to vast amounts of inequality. His analysis of distribution policy rests on his fundamental belief that governmental involvement to reallocate resources from well-off to less well-off members of society would prove injurious to economic and political freedom, and to the efficient functioning of the market. Friedman argues that a healthy market capitalist economy actually will have lower inequality than non-capitalist societies and will promote social mobility. In other sections of his book, Friedman even suggests benefits to economic inequality. In arguing that economic freedom is a requisite for political freedom, Friedman says that capitalism will provide a system where some individuals with large amounts of wealth will have the ability to purchase advertising and distribute

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59 Rodgers, *Age of Fracture*, 55.
61 Friedman, *Capitalism and Freedom*, 162-166.
pamphlets or other media advocating for political change, while those with the financial resources to do so in socialist countries would be mere puppets of the state. Friedman remarks, “This is a role of inequality of wealth in preserving political freedom that is seldom noted – the role of the patron.”⁶³ As Friedman’s economic ideas became more influential, the decline in discussions of inequality and the accompanying push for less government involvement in the economy are understandable as signs of the prevailing political economic ethos.

Friedman’s ideas were so prominent as to permeate the public consciousness in a way that the ideas of no other contemporary economist had been able to do. By the latter half of the 1970s, Friedman had become an incredibly visible and influential public figure as a Nobel Prize winner and columnist for Newsweek. He was brought in as a consultant to Chile after that country’s 1973 coup left the door open for economic experimentation in free market ideas. He worked on a miniseries, Free to Choose, with his wife that aired on PBS from 1977 to 1980. His influence was very public and related to the broader appeal of the market in the community eye.⁶⁴

The rise of the market through the economics of Friedman and others was mirrored in the rise of the market in the 1970s through the influence of pro-business intellectuals. Seen as a facilitator of democracy, individual liberty, and economic efficiency, the market became an idolized tool by members of the business elite. New conservative think tanks sprung up during the decade and older ones received new infusions of large sums of cash. The Heritage Foundation, the Cato Institute, the Manhattan Institute, and the American Enterprise Institute all argued fervently for the spread of market values as the appropriate medicine for sustained

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⁶³ Friedman, Capitalism and Freedom, 17.
economic and political health. Business leaders themselves advocated for market ideals and backed Ronald Reagan for the Republican presidential primary in 1980, helping to bring about the triumph of the market. These conservative think tanks and business leaders represented a conservative “Counter-Establishment” and reflected its “passage from isolation to influence” throughout the 1970s.

The political currents of the free market ideology were strong as well, as unfettered markets were thought to enhance individual liberty. Offshoots of the conservative movement, such as libertarianism and novelist/philosopher Ayn Rand’s Objectivism, lauded this aspect of free market ideology. Though they were distinct and often conflicting movements, libertarianism and Objectivism came into vogue during the 1970s. “Rand’s [Objectivist] moralism grounded and bounded libertarian freedoms by emphasizing rationality, self-interest, individual rights, and capitalism.” This philosophy was especially influential on economists such as Alan Greenspan, who would become Chairman of President Gerald Ford’s Council of Economic Advisers in 1974 and later Chairman of the Federal Reserve Board of Governors. Greenspan was influenced so heavily by Rand that he invited her to the White House for his swearing-in ceremony as Chair of the CEA. Rand’s influence extended beyond Greenspan, however, affecting other libertarian-leaning economists and libertarian-leaning members of the general public. Seventy percent of readers of Individual Liberty surveyed in 1977 said that Rand

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65 Borstelmann, The 1970s, 130.
66 Phillips-Fein, Invisible Hands, 236-262.
69 Burns, Goddess of the Market, 260.
70 Burns, Goddess of the Market, 269-270.
71 Burns, Goddess of the Market, 245.
was “most influential in initially causing our readers to adopt libertarianism,” and in 1987 *Liberty* magazine readers ranked Rand as more influential than Thomas Jefferson and economists such as Hayek and Friedman.72

Between the influence of Rand, Friedman, conservative think tanks, and business intellectuals, the market revolution was largely completed in the 1970s. Reagan won the presidency in 1980 and entered into a decade that had already incorporated many of the prevailing market ideas. The ideas of market dominance, the ineffectiveness of governmental policymakers to affect macroeconomic outcomes, and the goal of deregulation became cornerstones of Reagan’s policies as president. Reagan entered office during a recession, a time that he would call “the worst economic mess since the Great Depression” in an influential speech early on in his presidency on February 5, 1981.73 Reagan outlined many of his anti-tax, anti-regulation sentiments in this speech, criticizing the bloated size of the federal government. In an appeal to smaller government as a means to bring forth the ingenuity of the American people while solving crises in debt and inflation, he remarked:

> Since 1960 our government has spent $5.1 trillion. Our debt has grown by $648 billion. Prices have exploded by 178 percent. How much better off are we for all that? Well, we all know we’re very much worse off. When we measure how harshly these years of inflation, lower productivity, and uncontrolled government growth have affected our lives, we know we must act and act now. We must not be timid. We will restore the freedom of all men and women to excel and to create. We will unleash the energy and genius of the American people, traits which have never failed us.74

His speech used statistics to indicate precisely the horrors of the contemporary state of economic affairs while using Reagan charm to appeal to the hearts and minds of the American people.

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74 Ronald Reagan, “Address to the Nation on the Economy.”
citizens. He backed up his broad ideological preferences with specific policy proposals meant to solidify the ideas of smaller government, individual economic freedom, and supply-side policies to stimulate a sagging economy. In May 1981, the House of Representative passed a budget reflecting Reagan’s desire to deeply cut the size of the federal government. In August, Reagan fired over 11,000 striking air traffic controllers in a show of force limiting the influence of unions and symbolically restoring greater power over labor contracts to the hands of private employers. Reagan helped push through tax reforms in 1981 and 1986 that reflected his philosophies of lower tax rates, less governmental involvement in the lives or ordinary American citizens, and the purported benefits of supply-side economic policies.

In conjunction with these policies and fueling them, the influence of Arthur Laffer, member of Reagan’s Economic Policy Advisory Board (1981-1989), grew and ushered in the ideas of supply-side economics. The associated Laffer curve, which legend has it was scribbled down by Laffer on the back of a napkin, showed an ideal tax rate between 0%-100%, implying that tax rates beyond certain levels would eventually reduce the amount of government revenues. The assumptions underlying Laffer’s philosophies and supply-side economics more generally rested on Say’s Law, a cornerstone of classical economic theory named for late-18th and early-19th century French businessman and economist Jean-Baptiste Say, which most neatly can be summarized as “supply creates its own demand.” This longstanding idea was questioned after the Great Depression by John Maynard Keynes, whose economic philosophies ultimately

rested on the speeding up and slowing down of aggregate demand. “Thus Say’s Law, that the aggregate demand price of output as a whole is equal to its aggregate supply price for all volumes of output, is equivalent to the proposition that there is no obstacle to full employment,” Keynes remarked in his General Theory. “If, however, this is not the true law relating the aggregate demand and supply functions, there is a vitally important chapter of economic theory which remains to be written and without which all discussions concerning the volume of aggregate employment are futile.”79 This “vitally important chapter” of economics had been developed in the post-Depression world as Keynesianism became the dominant macroeconomic philosophy and demand-side economic thought slowly discredited Say’s Law. With the economic crises of the 1970s and the concurrent retreat of Keynesian macroeconomics, however, Say’s Law was permitted to return as the foundational underpinning of supply-side economics.

In the late 1970s, political conservatism helped foster a return to supply side economic thought. As Princeton University economist professor and New York Times columnist Paul Krugman has argued:

A powerful conservative movement [had] arisen. The ideological core of this movement [was] a group of so-called supply-siders, who combine[d] a rejection of Keynesianism with a belief that sharp tax cuts will produce a tremendous surge in economic growth, so much so that one need not worry about offsetting these cuts by reducing expenditures. The supply-siders draw some legitimacy for their ideas from economists like Martin Feldstein; but the supply-siders themselves are primarily journalists and political staffers, with only a few renegade professors.80

Krugman highlights the lack of economic support for supply-side economics, but explains its sustained success by citing the inability of left-leaning economics to sell its product to the wider

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80 Krugman, Peddling Prosperity, 16.
public with a cute and succinct name like “supply-siders.” The prevalence of supply-side economics was of fundamental political importance in the Reagan era and helps explain some of the reasons why economists failed to adequately study inequality during the Reagan presidency.

It is against this political backdrop that few economists in the Reagan era attempted to write about inequality. Citing research that indicates steady increases in the Gini coefficient based on data from the Current Population Survey from the 1958-77 period, Martin D. Dooley of McMaster University and Peter Gottschalk of Bowdoin College and Institute for Research on Poverty published an article looking at the effects of labor force growth on earnings inequality among males. Their 1984 publication in the *Journal of Political Economy* provides a rather surprising and worrisome find. Looking at data from 1968-79, they observe that “evidence was provided of substantial increases in earnings inequality within labor force cohorts even after the levels of education, experience, and un-employment were controlled for.” Additionally they remark that “recent growth in the dispersion of earnings among all males cannot be explained solely on the basis of widening earnings differentials among age groups or on the basis of recent growth in the proportion of young (high-variance) workers.” Their findings proved troublesome because they implied that larger forces were at work in explaining income inequality. No longer, their analysis suggested, could wage differentials be explained away solely by gender or race discrimination, or by differences in the level of one’s education.

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84 Dooley and Gottschalk, “Earnings Inequality Among Males,” 86.
85 Dooley and Gottschalk, “Earnings Inequality Among Males,” 86.
attempting to provide an explanation, they argue that “recent increases in male earnings inequality may have been caused in part by the post-World War II baby boom and baby bust acting through the unprecedented large swings in labor force growth rates during the last half of the twentieth century.” However, their demographic explanation for the rise in earnings inequality seems inadequate when one considers how inequality has persisted and led to the “great divide” of the early twenty-first century. The concerns raised by Dooley and Gottschalk in one of the profession’s most influential journals may be expected to have led to an increase in discussion of earnings inequality among their colleagues, but widespread discussion of the topic at the highest levels of the profession seems to have retreated in the mid to late 1980s, and their analysis can be seen as an anomaly.

Of course, economists do not merely discuss their areas of scholarly interest through journals and book publications. Rather, they convene for conferences to share ideas and hear presentations from their colleagues on a wide range of subjects in economics. At the annual meeting of the American Economic Association, for instance, the world’s top economists will assemble to discuss various concerns in the discipline which are heard on different panels with presenters and discussants. Upon first glance, these panels seem to reflect signs of the economic times more closely than the journal articles discussed previously, as issues such as inflation, centrally planned economies, and the role of monetary policy appear where one would expect in relation to important historical events in economic history. Therefore, one may expect to find a higher number of panels occurring with greater annual frequency concerning economic inequality as inequality increases throughout the Reagan presidency. My thinking,

86 Dooley and Gottschalk, “Earnings Inequality Among Males,” 87.
therefore, was that the number of papers presented during panels about inequality would begin at low amounts during the early 1970s and would slowly increase as inequality increased throughout the Reagan era. Figure 5 shows data for the Gini Coefficient, reflecting increases in inequality during the Reagan presidency.

Figure 5

While the various ebbs and flows of the economics profession seem to have been adequately reflected in the conferences of the most influential professional economics association, the same cannot be said for economic inequality specifically. Despite having a large number of panels on the topic in the early 1970s and sustained annual appearance, the topic disappeared just as inequality started to accelerate during the Reagan presidency. In fact, discussions about inequality at the annual AEA conference vanished in 1981 and did not return for seven years after being present in some form for almost every year in the period analyzed.
In the interim period, economists focused on timely and important issues such as debt crises, stagflation, and deregulation, and one may surmise that these issues bumped inequality off the economists’ radar. However, less important issues still garnered their own panels. For instance, economists found it essential to devote an entire 1985 panel to The Political Economy of Outer Space. When inequality finally resurfaced in December 1988 at the Hundred and First Annual Meeting of the American Economic Association in New York City, a panel on American Income Inequality included papers entitled “How the Rich Have Fared, 1973-1987”;87 “Deficit Reduction and Income Redistribution”,88 and “Inequality Among Children and Elderly in Ten Modern Nations: The United States in an International Context.”89 As indicated by the first of these articles, 1973 becomes widely-identified in the late 1980s as a critical year in economic history. Inequality appears to finally have been an important issue facing economists due to its prevalence in everyday American life.

Most writings in the top journals seem to have been continuations of old debates among economists, debates that would often take place over many years, as witnessed in the continuing discussion of Morton Paglin’s slight change in the means of calculating the Gini coefficient. Additionally, articles in the top journals seem to have come from a small group of economists who were not affiliated with the top economics programs in the country. Some other notable works outside the top economics journals such as Joseph Stiglitz’s article “The Distribution of Income and Wealth among Individuals” from the July 1969 publication of

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Econometrica, Amartya Sen’s 1973 book On Economic Inequality, and British economist Anthony Atkinson’s 1975 book The Economics of Inequality were written during the period discussed, but few articles seemed to have galvanized top economists in top programs to address inequality in new ways or with greater frequency. These earlier works were products of their time and did not sustain through the highly unequal conditions of the Reagan presidency. Furthermore, the content of journal articles seems to have been impervious to the contemporary economic conditions and did not reflect concerns with growing inequality during the Reagan presidency. While very little change can be observed in my chart highlighting the number of articles relating to inequality in the top economics journals over time (Figure 2), the slight majority of journal articles written about the distribution of income, the measurement of inequality, and historical analyses of inequality appeared before inequality began to accelerate in the 1980s. These conditions may indicate that journal articles about inequality reflect long-term concerns of economists that are not directly related to economic conditions during the times in which economists are choosing what to write.

This possible insulation of the economics profession from the real world is tougher to measure than the impact of the political climate. Many scholars have noted the rise of Friedman as a political figure and the concurrent rise of the market values. These developments shaped the political climate of the 1970s and brought about the conservative counterrevolution that culminated with the election of Ronald Reagan in 1980. During the Reagan presidency, the power of the conservative movement based on individual liberty, the prominence of the market, and the inability of the government to effect positive change in the macroeconomy yielded a climate in which academic economics did not focus on inequality despite its continued
rise during the time period. The changing aspects of the economics profession helped yield political changes, and these two developments worked together to stifle the economics profession’s interest in writing about inequality and the distribution of income.
Chapter 3: Poverty, Inequality, and the “Underclass”

In addition to changes in the economics profession and the broader political developments that occurred during the Reagan era, conceptions of poverty and an “underclass” in American society help explain some of the ways in which inequality was discussed by economists. Economists have long been concerned about poverty, and these concerns manifested themselves as explicit writings about poverty and discrimination in the Reagan era. Curiously, however, policies implemented by Reagan that were seen as attacks on the welfare state in the 1980s did not necessarily produce increased interest in the subject among economists during that decade. Rather, the supposed testaments to the timeliness of economists – journal articles and conference proceedings – indicate the 1980s to be a barren time for serious discussion of inequality and poverty among economists. As scholars such as Michael Katz have argued, poverty is in many ways a “social product” and becomes “not the product of scarcity, but of political economy.”90 In a world where poverty was conceived of as a social product, one may expect to find economists – scholars from one of the fields most well-equipped to study poverty and inequality – discussing the subject vigorously. However, it appears that discussions of poverty seem to have gone the way of broader discussions of inequality – victims of broader macro shifts in the economics field and the political climate.

As far back as Scottish philosopher Adam Smith, widely credited as the founder of modern capitalism, economists have expressed interest in the causes of inequality and what its scope means for the proper functioning of the economy. Dating back to Smith, as well, is the sentiment that a society with vast inequality and large numbers of poor members is not a

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90 Katz, The Undeserving Poor, 7.
successful society. In Book One, Chapter Eight of his classic work *The Wealth of Nations*, Smith wrote:

Is this improvement in the circumstances of the lower ranks of the people to be regarded as an advantage or as an inconveniency to the society? The answer seems at first sight abundantly plain. Servants, labourers and workmen of different kinds, make up the far greater part of every great political society. But what improves the circumstances of the greater part can never be regarded as an inconveniency to the whole. No society can surely be flourishing and happy, of which the far greater part of the members are poor and miserable. It is but equity, besides, that they who feed, clothe and lodge the whole body of the people, should have such a share of the produce of their own labour as to be themselves tolerably well fed, clothed and lodged.\(^9\)

Smith’s attention to inequality and the plight of the poor reflected his background as a philosopher and was overshadowed by his famous idea of the “invisible hand” that guides efficient capitalist market outcomes. But it also set a precedent for concerns about economic inequality for economists through the history of the profession. The first half of 20\(^{th}\) century ushered in better understanding of the ways to properly measure economic inequality as the Lorenz curve and Gini coefficient became respected tools heavily utilized by economists. Therefore, periods of high inequality may be thought to have been accompanied by greater study of the issue among economists.

Surprisingly, however, the opposite result appears to have been the case. The first conference at which I looked, the Eighty-Second Annual Meeting of the American Economic Association (AEA) held in New York City from December 28-30, 1969, featured a few panels that seemed to represent the broad look at inequality and discrimination issues that were featured in the leading economics journals. Panels related to these concerns during this AEA meeting of late 1969 included Increasing the Supply of Black Economists, Distribution Issues: Trends and

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Policies, and Dynamics of Income Distribution: Poverty and Progress. Similarly, next year’s meeting in Detroit featured panels on Current Status of Income Maintenance Experiments, Intra and Intergeneration Transfers, and Earnings Differentials. Through the types of panels observed in meetings during 1969 and 1970, one can see the traditional concerns of economists seen in journal articles of the time. Topics of interest include incorporating diversity into the economics profession, understanding the trends in income distribution, and analyzing earnings differentials that may result from gender or racial discrimination. Perhaps the prevalence of these articles reflects the relative strength of liberal politics in the 1960s that carried over into the early 1970s.

Indeed the Eighty-Fourth Annual Meeting in New Orleans in December 1971 featured a very large number of panels that may be seen as manifestations of leftist politics from the preceding period marked by the prevalence of Great Society programs. Panels of interest to the study of economic inequality included: On the Emerging Problems of Development Policy, The Economics of Full Racial Equality, Issues in Incomes Policy, Inequality: The Present Tendency and the Remedy, What Economic Inequality for Women Requires, Issues and Perspectives of Black Political Economy, and Taxation of the Poor and the Rich. Here economists’ discussions of inequality seemingly included a very large number of broad concerns including taxation, discrimination, and development economics, all related to ideas of poverty and discrimination, in one year’s meetings. The meetings’ details seem to have been influenced by the political and social climate in which its researchers were working, and concerns about inequality seem to focus on the issues of discrimination as opposed to the broad distribution of income.
Two years after the meeting in New Orleans, Edmund S. Phelps published an article in the *Quarterly Journal of Economics* entitled “Taxation of Wage Income for Economic Justice.”

Coming on the heels of the publication of Harvard philosopher John Rawls’ *A Theory of Justice*, the “purpose in [his] paper is to derive the implications of the Rawls criterion for the graduated taxation of wage incomes within the context of two simple models of households earning decisions.”

During this time, Rawls’ work became extremely influential and “cast its mark over social and political theory in a way that few books ever dominate a scholarly field. It generated hundreds of articles and thousands of citations.”

Phelps acknowledges the traditional approach in economics of looking at the economics of taxation through the lens of “Paretian efficiency,” but he chooses instead to use a Rawlsian approach to analyze the taxation of wages. His approach effectively alters the ways in which economists solely used mathematical tools in their analyses to a fusion of economics and philosophy. In fact, Phelps thanks “the two dozen mathematical economists and philosophers” who provided him assistance on the paper in a note at the beginning of his work. This fusion of mathematical economics and philosophy has a history in the roots of economics. Adam Smith, author of *The Wealth of Nations* (1776), also produced *The Theory of Moral Sentiments* (1759), a fusion of ethics, philosophy, psychology and other related disciplines. In the 1970s, however, this fusion seems to have been a distinct niche in economics and did not manifest itself in larger ways in discussions of poverty and inequality.

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94 Rodgers, *Age of Fracture*, 182.
In addition to some economists reflecting philosophical ideas of a base level of living standard for all Americans, encapsulated in the Rawlsian maximin principle, ideas about poverty were seen through the lens of racial and gender discrimination. The concentration of much of this work is in the 1970s and appears to draw upon the political ethos of the 1960s and liberal policies. As one article discussing black-white wage differentials began:

It is likely that at no time in recorded history has racial equality received as much attention as during the 1960's in the United States. It is also likely that economists will associate the last decade most closely with the beginning of a dramatic erosion in some of the more historically persistent wage differentials in the United States. This paper documents changes in black-white male earnings as these changes are revealed in two surveys, the 1 in 100 Public Use Samples of the Census of Population in 1960 and 1970. However one slices the data, the improvement in the relative income of black males during the 1960's is impressive. Equally eye-catching is the universal sharing of these gains across experience and schooling classes. But even though all black age and experience groups gained on average relative to whites, the gains were not equally distributed: those whose relative position improved most are more likely to be the most educated and the more recent entrants into the labor market.\footnote{Smith and Welch, “Black-White Male Wage Ratios,” 323.}

Here economists in 1977 are discussing a retreat of racial wage discrimination due to the liberal policies of the 1960s. While I had previously only considered that economists’ agendas in regards to inequality would be determined by vast amounts of inequality, I had failed to consider that vast improvements in the state of something like wage differentials between members of different classes may also give economists a reason to write articles about the specific subject. With that said, this article appears to be one of a few examples of this phenomenon and is not indicative of a larger trend. Perhaps, however, the perception that conditions were improving with regard to specific measures of inequality produced a sense of complacency among members of the field that did not encourage them to write about the subject at length.
The reduction in wage differentials in the 1960s would prove to be a small, transient victory in the fight against eliminating inequality and fighting poverty, however. As Ronald Reagan ascended to the presidency in 1981, presidential policies began to tilt toward restricting the impact of the welfare state. Constrained by the economic realities that caused President Carter to pursue similar policies on a smaller scale, yet energized by the revolution in political ideology, Reagan took strides to limit expenditures on food stamps, unemployment insurance, child nutrition, AFDC [Aid to Families with Dependent Children], and other programs.\textsuperscript{98} The Omnibus Budget Reconciliation Act (OBRA) of 1981 took aim at AFDC recipients and increased poverty by roughly 2\% in two years.\textsuperscript{99} Governmental decisions deeming certain people able to work eliminated disability benefits for 500,000 people by 1984.\textsuperscript{100} Racial strides toward wage equality seen during the 1960s were supplanted by dangerous statistics in 1984, when 47\% of all black children and 39\% of all Hispanic children were considered to be poor.\textsuperscript{101} Despite these disturbing statistics, however, very little attention was paid to these issues among those at the highest levels of the economics profession during the majority of the Reagan presidency.

The economics profession’s study of inequality and poverty with regards to race were eventually renewed through the lens of “the underclass.” As Michael Katz has indicated in his study of the language of poverty, “By the mid-1980s, a new image dominated poverty discourse. Invoked unreflectively and automatically by commentators on poverty, the concept of the underclass captured the mixture of alarm and hostility that tinged the emotional response of more affluent Americans to the poverty of blacks increasingly clustered and

\textsuperscript{98} Patterson, America’s Struggle Against Poverty, 212.
\textsuperscript{99} Patterson, America’s Struggle Against Poverty, 212.
\textsuperscript{100} Patterson, America’s Struggle Against Poverty, 212.
\textsuperscript{101} Patterson, America’s Struggle Against Poverty, 212.
isolated in postindustrial cities.\footnote{Katz, The Undeserving Poor, 185.} The idea of an underclass elicited mixed responses of sympathy and fear among the affluent, and reflected general concerns about the homeless and those of minority races.\footnote{Patterson, America’s Struggle Against Poverty, 227-234.} Although the data reflect fundamental flaws and vary widely on the organization creating them, they show high levels of homelessness that increased throughout the 1980s and the Reagan presidency.\footnote{Katz, The Undeserving Poor, 185-6.} Adding to the plight of the homeless were cuts in federal and state programs assisting those with less economic status. For instance, “the median value of AFDC benefits declined about one-third in constant dollars” between 1970 and 1985.\footnote{Katz, The Undeserving Poor, 187.}

In addition to the large amount of homelessness that became synonymous with the underclass, the term also carried large racial connotations, as black teenage mothers and black jobless youths were the two largest categories in the underclass.\footnote{Katz, The Undeserving Poor, 189.} Therefore, discussions of the underclass can be thought of as the offspring of previous discussions about addressing poverty and inequality resulting from racial and gender discrimination, which were thought to contribute to inequality in wage differentials. Economists historically discussed these concerns as previously noted, and as the ideas of the underclass took hold in the public discourse, economists would begin to discuss the underclass as a new manifestation of poverty and inequality.

Indeed, the public became aware of research being done that popularized the terminology of the underclass. A 1987 New York Times article about the subject began:

\footnote{Katz, The Undeserving Poor, 195.}
While the number of Americans living below the poverty line has risen steadily in recent years, new research is finding a much faster rate of growth among the most severely disadvantaged.

Social scientists have focused new energies on an "underclass" of Americans who live in near total isolation from mainstream society, and scholars are trying to learn more about the deteriorating inner-city areas where not working is the norm, crime is a commonplace and welfare is a way of life.\(^{108}\)

Articles such as these in the country’s most influential newspapers, combined with the popular writings of William Julius Wilson, Douglas Glasgow, Nicholas Lemann, and others, helped to raise awareness of the plight of the underclass in the public consciousness.\(^{109}\) It is within the context of this raised public awareness of the issues surrounding the underclass that economists began to view inequality through that lens.

As a reflection of the times, the 1989 meeting of the American Economic Association included a panel entitled Poverty and the Underclass. The three papers on this panel included: “Effects of Family and Community Background on Economic Status,”\(^{110}\) “AFDC Participation Across Generations,”\(^{111}\) and “Welfare and Work in Chicago’s Inner City.”\(^{112}\) The author of last of these papers asserts, “What distinguishes the urban underclass from the poor in general is the persistence of these behaviors in the context of social isolation from mainstream institutions.”\(^{113}\) Recognition among both the economics profession and the general public of an underclass stuck in a persistent and largely immutable cycle of joblessness and poverty marks a

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serious transition away from a large portion of the 1980s where poverty and inequality did not manifest itself frequently in the economics literature.

While the name of the final paper of the three on the panel alludes to welfare and work, like much other work in the scholarly economic literature it fails to acknowledge “workfare,” the combination of welfare and work programs that marked some of the new ways in which policymakers attempted to combat poverty in 20th century America. These programs took many forms. Early ones, like the one in California during the governorship of Ronald Reagan, required participants to work even make-work jobs if they were to retain their benefits.114 Later programs were more likely to incorporate training services such as job search, job training, community work experience, and education programs.115 The former programs had extremely low participation rates, while the latter had effects that were ambiguous and less positive than many commentators believed.116 Although the record on workfare was mixed due to its different manifestations and specific details, by the end of the 1980s, workfare and concepts of the underclass became the two leading lenses through which those on both sides of the aisle viewed issues of inequality and poverty.117 While economists responded to these changing phenomena with greater incorporation of the notion of the underclass in their work, they failed to address notions of workfare programs as a means to reduce poverty, perhaps reflecting to a degree the insulation of the profession.

Despite some discussion of the underclass, racial and gender inequality, and Rawlsian notions of welfare maximization, economists’ study of poverty throughout the 1970s and 1980s...

114 Katz, The Undeserving Poor, 225.
115 Katz, The Undeserving Poor, 226.
did not reflect the necessity the conditions on the ground seem to have posed. Early considerations of gender and racial inequality connected to later ideas of an underclass based on race. Some incorporation of the rise of Rawlsian philosophy into economic discussion of inequality early on reflected a waning segment of the political and economic contemporary ethos. The largest and most surprising story of the economics profession’s relationship to poverty during this time, however, was its noticeable absence in the most important journal articles and conference proceedings at the most crucial point in the history of poverty in the Reagan era. As welfare programs fell to the Reagan ax and poverty and inequality grew, the economics profession was largely silent. As the end of the 1980s came and the public’s awareness of the dangers faced by the underclass grew, the economics profession began to respond with articles and paper presentations about the relevant issue. While this may indicate a lag in the time it takes economists to respond to a certain issue, this explanation does not suffice. Issues such as crises in the world energy market and inflation elicited quick responses from economists in their annual meetings. Therefore it appears that specific discussions of poverty among economists fell victim to the same broad internal economic and external political forces discussed in chapters one and two that reduced the number of articles and conference discussions related to inequality and poverty.
Conclusion

Throughout my thesis, I have attempted to show the ways in which economists wrote about economic inequality and how frequently they did so. Using primary sources in the form of top scholarly journals in the field and conference proceedings of the annual American Economic Association meetings, I have attempted to show how these discussions evolved and fit into the broader sweep of the Reagan era in the years 1970-1990. Combining historical context of changes in the economics profession, political developments including the resurgence of conservatism and the market, and state of poverty and conceptions of the underclass, I have created a historical synergy that begins to explain how and why economists wrote about inequality specifically, and how academic agendas are influenced more generally.

The trajectory of discussion of economic inequality in the annual meetings of the American Economic Association seems to follow a similar arc as the topic’s discussion in the profession’s leading journals. A broad look at inequality in both media shows discussion of topics including wage discrimination based on gender and race, the proper measurement of inequality through analyses of the Gini coefficient and Lorenz curve, and the macro-distribution of income, which has commanded a large fraction of this paper’s attention. The majority of investigation into inequality in both the journals and the conference panels came in the 1970s and tapered off in the 1980s during the Reagan presidency, despite inequality accelerating during this time. While economists appear to have adjusted their studies to reflect developments in the field, they do not seem to have been swayed by the changes in economic inequality data, at least until the very end of the 1980s. Work done in the economics field may lend some support to those who criticize academics for residing in the “ivory tower” and failing
to be cognizant of current events. These concerns were echoed in the economics field itself, as a Commission on Graduate Education in Economics (COGEE) was set up in 1988 to address the “view that economics as taught in graduate school had become too divorced from real world questions.”\textsuperscript{118}

However, heightened attention paid to issues such as inflation, deregulation, and energy policy show that economists did not fully live in an academic bubble. Why, then, did inequality seem to disappear from the radar of most economists, just when the data show it began to become an important material issue? Forces inside the economics profession and in the larger political climate seem to have exerted influence on economists’ focuses. In the ideological “war of ideas,”\textsuperscript{119} a conservative “counterintelligentsia”\textsuperscript{120} was working to propel seismic shifts in the economics world and facilitate the Republican’s party’s return to prominence, manifested in the polarizing and highly visible president that was Ronald Reagan.

The retreat of Keynesianism and growing influence of monetarism and supply-side economics occurred in a world in which the boundaries of microeconomic thought were stretched, law and economics became a powerful force outside of the University of Chicago, and game theoretic analyses with rational choice foundations became more widespread. These developments brought a forth a political climate where inequality was rarely discussed by the champions of new economic thinking. This progression may help explain some of the reasons why economists writing in the most important journals and attending the most important conferences did not discuss economic inequality much during the Reagan presidency.

\textsuperscript{119} Rodgers, \textit{Age of Fracture}, 1-3.
\textsuperscript{120} Rodgers, \textit{Age of Fracture}, 7.
My thesis has sought to explain the ways in which broader developments in political economy affect the ways in which a specific academic agenda is driven. While there appears to be some isolation from real economic conditions among economists writing about inequality, at least at the most influential levels of the field, they also appear to have been affected by the economics profession itself, external, yet connected, political developments, and public discussion of poverty. Further research would attempt to draw a causal arrow from these broader developments to the amount and types of articles about inequality or some other similar topic in academia. These causal arrows would help reveal what drives academic agendas and how insulated scholars truly are from the real world.
Works Cited

Books


**Articles**


**Web Sites**
