

DO SKILL SHORTAGES DRIVE WAGE INEQUALITY?

Lawrence Mishel and Jared Bernstein, Economic Policy Institute

The main source of rising income inequality among families is the increased disparity of wages, particularly hourly wages (rather than disparities in hours of work). But what drives wage inequality. The conventional wisdom suggests that groups whose wages have deteriorated increasingly do not have skills to be able to compete in an information age economy. Likewise, it is the skilled workers, usually identified as those having a college degree, that have done well because they have the necessary skills. In economics terms, the growth of wage inequality is said to be driven by “skill-biased technological change (SBTC)” such that low-skilled fare worse than mid-skilled workers who, in turn, fare worse than the most skilled workers. This is usually illustrated by the rise in the wage premium between those completing college and those with a terminal high school education, which has risen from a 40% advantage in 1979 to a 77% advantage in 2007.

In fact, skill shortages have not been the primary driver of wage inequality and may have played no role at all, especially in the manner associated with SBTC explanations. First, this explanation only fits the basic descriptive data trends for the 1980s and has no relationship to the trends of the 1990s and 2000s. This can be seen by the relatively flat trends in key education differentials while wage inequality rose continuously. Second, a deeper look shows that SBTC is even a poor explanation of the 1980s trends. Third, estimates of the demand for ‘skill’ or college graduates show a remarkable deceleration over recent decades, a finding which directly controverts a SBTC explanation. Fourth, a major component of rising wage inequality is the surging share of earnings attained by the top 1% of earners, a phenomenon that SBTC doesn’t explain. Fifth, the SBTC explanation most explicitly fails the recent period since 2000 or 2001 which has seen both college graduate and high school graduate wages (or compensation) stagnate while inequality soared and productivity grew at a rapid pace. Last, occupational projections and the looming factor of offshoring of white-collar work suggest that we will not face a shortage of college graduates in the future.