



Economics Group

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Income Growth: The Taxman Cometh

Roughly five years into the recovery, income growth has been notoriously slow to pick up. Between 2009 and 2013, before-tax income grew a mere 1.5 percent. After taxes, income shrank 7.2 percent.

Stuck in First Gear

The story of tepid income growth is by no means a new one. Our group has previously discussed the lack of income growth in this recovery as a sign of stagnation. As can be seen in the top chart, only the highest income quintiles have been able to generate any increases in before-tax income, while the lower quintiles have only seen decreases. Even for those high earners, growth has been meager when compared to the same four-year period following the previous recession. However, changes in tax policy in 2013, including the expiration of a 2 percentage point payroll tax holiday and tax increases for the highest income earners, have significantly affected the income picture in the United States.

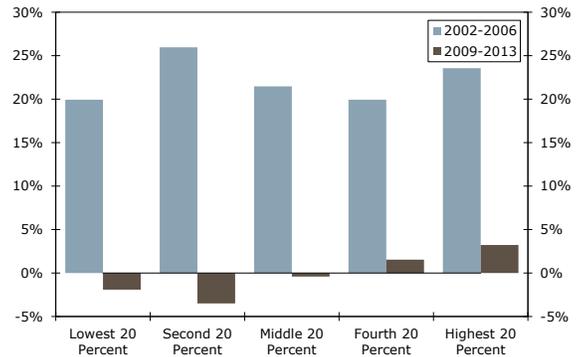
Read My Lips

After subtracting taxes and adding transfer payments, the income picture looks decidedly different than the before-tax figures (middle chart). Since 2009, the highest income households have suffered the most, seeing their after-tax incomes slip 10.6 percent. Over the same period, the lowest income households have actually seen an increase, albeit slight, in after-tax income, bolstered by transfer payments. Compare this to the four-year period from 2002-2006, when before-tax and after-tax income grew at almost identical rates for all income groups. Looking at the average of all consumer units, after-tax income has contracted 7.2 percent since 2009, compared to a 23.8 percent gain between 2002 and 2006. By comparison, before-tax income for all consumer units increased 1.5 percent over the same period. In fact, after-tax income for all consumer units has now retreated to levels not seen since 2005 (bottom chart).

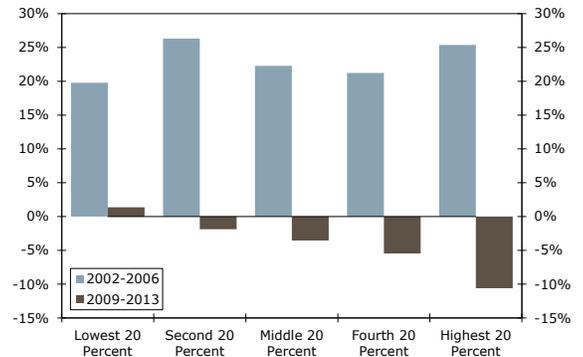
Arguably the most important result of this data can be seen by looking at the period from 2009-2013. The top chart shows that before-tax income has contracted for all but the highest earners since 2009. However, after-tax income has fallen for nearly every income group, excluding the lowest earners. In addition, after-tax income declines for the highest and second-highest 20 percent of earners have amounted to 10.6 percent and 5.5 percent, respectively, far more precipitous than any changes in before-tax income. Moreover, the lowest 20 percent of income earners have only seen their after-tax income increase 1.4 percent since 2009. Thus, it seems that although some of this income has been redistributed in the form of transfers to lower-income households, most of it has not made its way to the other end of the income spectrum.

The lack of before-tax income growth in the United States is undoubtedly a cause for concern. The Great Recession clearly had a significant negative impact on the health of all households and many consumers are still feeling the effects today. Nevertheless, the effects of tax policy will be important to watch in the coming years as the recovery continues.

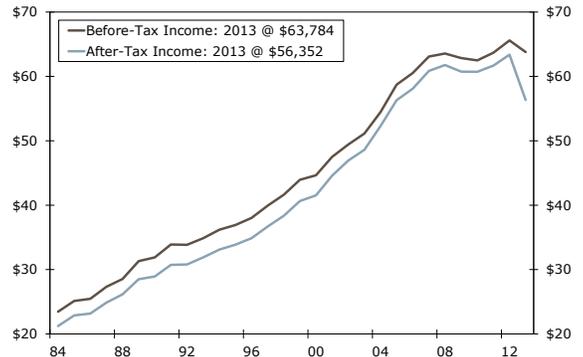
Income Growth During Economic Recoveries
 Percent Change Since Recession End, Before-Tax Income



Income Growth During Economic Recoveries
 Percent Change Since Recession End, After-Tax Income



Before and After-Tax Income
 All Consumer Units, Thousands of Dollars



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