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Trickle-down's middle-class massacre: Failure of conservative economics should discredit these bankrupt ideas forever

Supply-side economics hollowed out the middle class. It's time to stop listening to the architects of inequality

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Ayn Rand, Paul Ryan, Ronald Reagan (Credit: AP/Mary Altaffer/Photo montage by Salon)

Excerpted from "Hollowed Out: Why the Economy Doesn't Work Without a Strong Middle Class"

On April 30, 2012, Edward Conard, a former partner for the financial management company Bain Capital and a multimillionaire who retired at age 51, sat across from Jon Stewart, host of "The Daily Show," to promote his new book. Conard smiled and stared intently through his black-rimmed glasses as Jon Stewart, the liberal host of the comedy show, held up his book and described its contents. Conard's book argued that America's economy would be stronger if people like Conard were even richer and the country had even higher levels of economic inequality.

Stewart was puzzled by Conard's argument and joked that it didn't seem right because inequality in the United States was approaching the level in countries with "kidnapping-based economies," generating laughter in the audience. Then Stewart shifted to an opening that would give Conard a chance to explain himself. "My question to you about the premise of the book," Stewart stated, pausing for effect before setting up his punch line, "is huh?"

Conard laughed along with the audience, and then launched into his argument that great rewards for the "most talented" people were the secret to America's success. Making the rich richer is good for everyone, he claimed, because high levels of inequality provide strong incentives for risk taking and innovation that are essential for economic growth.

Though Conard's comments were provocative—indeed his book tour generated significant press, including a multipage feature in the New York Times Magazine—he was merely stating the barely hidden premise underlying supply-side economics. Supply-side economics, the misguided theory that has controlled economic policymaking for the past three decades, is built on the idea that inequality is good. Tax cuts for the rich and less regulation of business supposedly provide incentives for the wealthy to invest and work more. Enabling "job creators" to get richer helps us all, the theory goes.

Conard's former boss at Bain, Mitt Romney, the 2012 Republican Party nominee for president, ran on a platform of supply-side policies, as have virtually all Republicans since Ronald Reagan was elected president. Even a number of prominent Democrats support supply-side policies and logic. Not only do these wrongheaded ideas about inequality have great political influence, but—until quite recently—they were largely shared by academic economists. For the past several decades, the idea that high levels of inequality were good for the economy dominated economic thought.

Fortunately, these flawed ideas are beginning to be challenged. Academics have begun to rethink their views about the decline of the middle class and progressive politicians are finally starting to openly contest the logic underlying supply side after years of failing to do so. It is about time because our economy is suffering deeply from a financial crash caused in large part by high levels of inequality. And though we may not have a kidnapping-based economy, as Stewart joked, the American middle class is so weakened that we are experiencing the kinds of problems that plague less-developed countries, including high levels of societal distrust that make it hard to do business, governmental favors for privileged elites that distort the economy, and fewer opportunities for children of the middle class and the poor to get ahead, wasting vast quantities of human potential.

The American economy has been thrown off balance because the middle class is so weakened and inequality so high. An economy that works only for the rich simply doesn't work. To have strong and sustainable growth, the economy needs to work for everyone.

A strong middle class is not merely the result of a strong economy—as was previously thought—but rather a source of America's economic growth. Rebuilding the middle class would provide the stable base of consumer demand necessary to increase business investment and job creation. It would also enable the country to fully develop the human capital of its people, increase the social trust that makes transactions possible, and balance political power to produce a government that works for the whole country, not just those at the top.

Elements of this line of thinking date back to some of history's most prominent economists—from John Stuart Mill to John Maynard Keynes—but until the Great Recession of 2007–2009 snapped the field back to attention, most economists ignored the importance of the middle class.

Now, as they revise their models and assumptions that failed to predict the financial crisis, economists are rediscovering classic scholars, opening their eyes to the work of researchers in other fields such as history, political science, and sociology, and developing promising new lines of inquiry to try to understand the role of the middle class.

The weakening middle class

The United States was founded as a middle-class country. On the eve of the American Revolution, America's carpenters, shopkeepers, and farmers enjoyed a higher standard of living than workers in other parts of the world. Further, economic inequality was lower in the United States than any place else. In an era of kings and peasants, America's middle class stood apart.

America had its share of rich people, and of course it had slavery. But even so, the rich were not that much richer than the middle class. As Peter Lindert, an economic historian at UC Davis, explains: "Compared to any other country from which we have data, America in that era was more equal." Those who lived during America's founding sensed that the country's economic equality was special. Thomas Jefferson noted in a letter that "we have no paupers. . . . The great mass of our population … possess property [and] cultivate their own lands…. The wealthy, on the other hand, and those at their ease, know nothing of what the Europeans call luxury."

The strength of America's middle class ebbed and flowed over time, especially as industrialization took hold. But after World War II, America returned to its roots and built a mass middle class that was the envy of the world, with rapidly rising incomes and decreasing inequality. The mid-1940s to the mid-1970s was a period "without extremes of wealth or poverty," as Nobel Prize-winning economist Paul Krugman explains. To be clear, America in this era had rich people and poor people, but the bulk of society formed a prosperous middle class that was in relatively close proximity to both the top and the bottom.

Yet, over the past three to four decades, middle-class America has come undone. The American middle class was already hurting when the Great Recession struck and is now in deep trouble. While there's no official definition of the middle class, it's not hard to see that it is in decline. By most every measure, most Americans are struggling.

First, there is the basic level of income earned by the typical American. Median household income—meaning half make more and half make less—was lower in 2013 than it was in 1989. This means that middle-class households now earn less than they did two decades ago. Similarly, incomes for poor and even upper-middle-class households have also stagnated. It is true that over an even longer time period, the middle class have seen some income gains. But these gains have been quite small: over the past four decades, median compensation, including both wages and benefits, has grown at a snail's pace of just 0.27 percent per year—far slower than the overall economy or output per worker. The miniscule gains that households have made have largely come because women have increasingly entered the workforce—meaning families are working longer hours, as they run faster and faster to stay in place. Indeed, the hourly wage earned by a typical man is less than it was in 1973.

Even these gloomy figures may be too rosy because they show what is happening to the typical household—but the typical worker is getting older, and older workers generally make more than younger workers. Income trends are even worse when workers are compared to those of a similar age from a few decades ago. Median incomes for male workers now in their thirties are about 12 percent lower than the income was for their fathers' generation at the same age.