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The Class War That Isn't

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Envy isn't what you might think. Tax cuts for the wealthiest prompt a trickle-down effect that burdens middle-income households.

By Robert H. Frank

"If class warfare is being waged in America, my class is clearly winning."

- Warren E. Buffett, annual letter to Berkshire Hathaway shareholders, March 2004

As they did in 2000 against Al Gore, Republicans are again deriding Democratic criticism of tax cuts for the wealthy as "class warfare." It's a deft linguistic ploy, for the term was originally used to portray the wealthy as elites who exploited workers unfairly. Many found this rhetoric compelling during the robber-baron era, more than a century ago, when employers hired armies of thugs to bust their labor unions.

Today, however, the rhetoric of exploitation falls largely on deaf ears. For despite the recent spate of examples of fortunes amassed by fraud, middle-class voters appear to accept that the current generation of wealthy Americans earned their money not through strong-arm tactics, but by offering services that others value highly.

The fact remains, however, that the behavior of the wealthy has been the root cause of a serious economic squeeze confronting the middle class, whose incomes have failed to keep pace with the prices of housing, tuition, health insurance, and a host of other basic services during recent decades. Through a chain of events, the increased spending of the top 1 percent, who earned three times as much in 2000 as in 1979, has placed many basic goals out of reach for the median family.

The links in this chain unfold roughly as follows. When the incomes of the wealthy rise, they eventually spend more on houses, cars, clothing and other goods, just as others do. Upon learning that someone at the top has built a 60,000-square-foot house or purchased a new Ferrari Scaglietti, most of us feel no inclination to alter our own spending.

But among those just below the top, such purchases have an impact. They subtly change the social frame of reference that defines what kinds of houses and cars seem necessary or appropriate. Additional spending by top earners thus leads others just below them to spend more. And when they do so, others just below them are affected in the same way, and so on, all the way down the income ladder.

In short, burgeoning incomes at the top have launched "expenditure cascades" that have ended up squeezing the middle class. An expenditure cascade in housing, for example, helps explain why the median size of a newly constructed house in the United States, which stood at less than 1,600 square feet in 1980, had grown to more than 2,100 square feet by 2001. During the same period, the median family's real income increased by less than 15 percent - not nearly enough to comfortably finance so much larger a house.

The steep rise in median house prices is one of the most important sources of the middle-class economic squeeze. It is an indirect consequence of the higher incomes and spending of top earners.

It might seem that a family could escape the squeeze by just buying a smaller house. But that option would entail a significant cost. The problem is that there is a strong link between the price of a house and the quality of the corresponding neighborhood school. Failure to buy a house near the median price for the area means having to send one's children to below-average schools, a cost that most parents seem unwilling to bear. The upshot is that despite a modest increase in their incomes, middle-class families must now work longer hours, borrow more, save less, and commute longer distances in order to continue sending their children to schools of just average quality.

Under the circumstances, it's no mystery that working- and middle-class voters are growing restive. What's surprising, however, is that they remain so free of resentment toward the rich. Indeed, almost two-thirds of low-income survey respondents favor repeal of the estate tax, a step that would benefit only the wealthiest 1 percent. And until recently, few political candidates dared even question the wisdom of large income-tax cuts for the wealthy, whose incomes have been growing at record rates.

One reason the middle class feels so little rancor toward the wealthy is that the two groups just don't compete directly with each other. As Bertrand Russell once observed, beggars don't envy millionaires. They envy other beggars who are doing just a little better than they are. The fact that Bill Gates might earn an extra billion or build another wing onto his mansion not only doesn't seem to bother middle-class voters, many of them actually enjoy following media accounts of his lifestyle.

And why not? Biologists teach that life is best understood as a competitive struggle for the resources needed to raise families, and for middle-class voters, the rivals who matter are not people like Bill Gates. In the quest for a better job or a house in a better school district, it's the people most like ourselves who really count. From the perspective of a middle-class voter struggling to get ahead, fretting about the good fortune of the rich is a complete distraction.

Even so, the expenditure cascade launched by top earners has placed a real burden on middle- and low-income families. This is not to say that top earners have done anything wrong. Certainly it was not their intent to cause trouble for those below. Yet the runaway prosperity they've enjoyed in recent decades has imposed significant tangible costs on the middle class.

That the link between spending at the top and the middle-class squeeze is indirect may explain why there is so little resentment toward the rich, but that provides no reason to ignore this link when evaluating economic policies.

Recently enacted federal tax legislation will steer almost \$700 billion in tax reductions to the wealthiest 1 percent during the next decade. In response, these people will build still bigger mansions and buy still more expensive cars. And a new round of expenditure cascades will put additional financial pressure on the middle class.

To question the wisdom of tax cuts for the wealthy is not to issue a battle call for class warfare. Repealing those cuts would not only alleviate the economic squeeze on families in the middle, it also might even make life more enjoyable for the wealthy. After all, managing a 60,000-square-foot mansion is a major headache. If fewer people built houses that large, fewer would feel any desire to own one.

Robert H. Frank is author of [Luxury Fever](#) and coauthor of [The Winner-Take-All Society](#). He is the Henrietta Johnson Louis Professor of Management and a professor of economics at Cornell University's Johnson School of Management. Contact him at rhf3@cornell.edu.