Chapter II
Interpreting the Evidence: The Two Narratives

The parable of the self-made man

On September 11, 2017, CNBC news—arguably a center-left media outlet—ran the story "10 billionaires like Oprah Winfrey who grew up poor."[1] As I will discuss below, rags-to-riches stories like these are not only the stuff of 19th century optimists like Horatio Alger. They remain common in all forms of media—TV and cable news, films, theater—to this day.

This particular story, which briefly chronicles the financial transformations of Oprah Winfrey, Ralph Lauren, author J.K. Rowling, and the CEOs of Oracle, Starbucks, and Home Depot, among others, does more than report the facts of these truly remarkable transitions from poverty to billions. The story is peppered with aphorisms like these:

> "Whether you're in need of some inspiration to start your own business, or you want to learn how to become a billionaire, take a look at how these famous folks made it to the top."
> "Growing up poor didn't stop these CEOs, celebrities and business experts from reaching the pinnacle of success — and it shouldn't stop you, either."

And it includes testimonials from the well-heeled such as:

> "I worked like hell to become part of the one percent" (Kenneth Langone, co-creator of Home Depot, worth about $3 billion);
> "Everyone who works hard, and maybe a little cleverly, has the opportunity to make almost anything possible." (Larry Ellison, college dropout and CEO of Oracle, worth over $60 billion).

To their credit, many of these "self-made" billionaires now give a substantial portion of their riches to the less fortunate.

The inspirational adages are not there to fill up the page. They are making a very specific point: Success is available to everyone. Opportunity is equal. And the difference between success and failure is effort. You too can become a billionaire, if you dream big and work hard. "That's the American Dream, that anything here is possible," according to Ellison.

This story, and thousands of others like it, encapsulates and caricatures a dominant narrative in the U.S. that is so prevalent that we are often not aware that it's there: Success is determined by individual effort, something everyone can achieve. But the narrative is not only about the sufficiency of individual effort to success. The individual must have the opportunity to exert effort for just

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[1] Wood, Laura 2017. "10 billionaires like Oprah Winfrey who grew up poor," CNBC *make it*, September 11. https://www.cnbc.com/2017/09/11/10-billionaires-who-grew-up-dirt-poor.html

compensation. Thus a key component of the narrative is that we truly are the land of opportunity, in which the opportunity to succeed is available to everyone. And not only is opportunity universally available, but the reward to taking the opportunity and working hard is just compensation—otherwise, why do all the work? Put differently, we live in a meritocracy—a system in which people get what they deserve, where all workers from CEOs to maintenance workers are paid according to their true value to the economy.

So far, the narrative focuses on individuals' opportunity, effort and reward. But there are other key actors who complete this view of the world: Businesses and government. And this narrative has a very specific view on the way businesses and government are best structured to allow individual achievement to flourish. As for businesses, they do best for everyone when they obey the categorical imperative for firms, as articulated by Milton Friedman in his 1970 *New York Times* essay: maximize shareholder value, and nothing else.[2] In Friedman's view, other foci--"social conscience," taking responsibility for providing employment, eliminating discrimination, avoiding pollution—are distractions and worse, are tantamount to socialism. As for government's role: Its job is to promote the free operation of markets, and more generally to minimize its interventions in the economy—to get out of the way of individual achievement. Finally and critically, the narrative may acknowledge to some extent the racial injustices of the past, but embraces the belief that racism is now behind us, and today plays little role in determining economic outcomes. I'll call this collection of narrative components "The Myth" in what follows.

Note that while The Myth largely focuses on the individual, business and government ingredients for success, it also implies by its definition explanations for failure. Poor economic outcomes—the yawning class and racial inequities in income, wealth, education, criminal justice, health care—are best explained by lack of effort by individuals, or by inappropriate government interference that does not allow markets to operate freely and efficiently.

In my view, this view of the world is corrosive, disrespectful to those millions in our country who cannot achieve success (disproportionately people of color), and grossly inaccurate. Other than that, I'm okay with it.

This narrative and its constituent components play two important roles in our economy. First, the narrative is used to explain and justify the array of outcomes that are documented in chapter 1 of this book. We trust free-market capitalist economies with minimal government

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[2] Milton Friedman, "The Social Responsibility of Business is to Increase its Profits," *The New York Times Magazine*, September 13, 1970.

intervention to produce the best economic outcomes, so the outcomes we observe must be the best we can achieve. Tinkering with them (especially via government policy) is dangerous!

Second, the narrative is used to shape the economy so as to perpetuate and augment the disparate outcomes that it has produced to date, by advocating for government policy, and by structuring the workplace. As was made clear in chapter 1, the system works really well for a small subset of the population. As a consequence, there is strong financial and political interest among the powerful in keeping it that way. Both roles are important if we are to understand how our economy came to be the way it is. They are also important in providing hope that we can change the way the economy works.

I propose an alternative narrative that challenges the premises underlying the individual-effort narrative. We do not live in the land of opportunity, as opportunity is far from equally available to all. As an obvious corollary, most simply cannot achieve anything they dream. Differences in outcomes are not best explained by differences in individual effort. There is no such thing as a "free" market that operates without significant government support and/or intervention. Decades of systemic racism have indeed caused the enormous gaps in wealth (and other outcomes) that we observe across races and ethnicities. CEOs do not merit the vast multiples of their employees' salaries that they are paid. A slavish devotion to shareholder value is the hobgoblin of the small-minded firm, and has likely caused tremendous damage to the welfare of the average low- to moderate-income worker in the economy. I'll call this narrative "The Reality" in what follows.

Perhaps most importantly to The Reality, we have consciously created this particular capitalist, free-market economy, designing it to deliver outlandish returns to the few, and a teetering economic existence to the many. It did not happen because that's the way capitalist free-market economies have to work.[3] It happened because we chose to make it that way. Looking on the bright side, this implies a glimmer of hope: We broke it, we can fix it.

Why do we use narratives?

Narrative (n): "a way of presenting or understanding a situation or series of events that reflects and promotes a particular point of view or set of values" [Merriam-Webster]
Narrative (n): "a story that connects and explains a carefully selected set of supposedly true events, experiences, or the like, intended to support a particular viewpoint or thesis" [Dictionary.com]

[3] Chapter 3 provides evidence by way of international comparisons to show that many other democratic, free market, capitalist countries produce far better outcomes in a variety of dimensions.

The real world is complicated. That's true for the physical world we inhabit, and for the more abstract world of thoughts, ideas, philosophies, politics, art and economics. To make sense of and make our way through the world, we constantly rely on simplifications that strip away the inessential and focus on the essential. Whether we're riding a bike, playing pool, or making judgments about what's good or bad economic policy, we use simplified renderings of more-complex realities to navigate and to make decisions.

Narratives are one way in which we do this. In making complex choices across options for how to conduct our business, whether to augment or reduce government safety net programs, and whether the current degree of inequality is acceptable or not, we often fall back on our underlying narratives.

Consider how one might frame choices from the perspectives of narratives 1 (and 2). Will a new business venture increase shareholder value (force us to reduce wages and/or benefits for our employees)? Will a new safety net reduce the incentive to work (afford greater economic stability to workers in volatile industries)? Will increased regulation reduce the efficiency of free markets (address a market imperfection that we believe markets cannot rectify)? In these simple examples, one could imagine making an argument on either side, and making decisions about what direction to take, shaped in part by adherence to The Myth or The Reality.

Narratives and the Broken Economy

The data presented in chapter 1 say what is. One can of course debate any one of the statistics cited there, as they are all subject to difficulties in measurement and interpretation. But the qualitative picture that they draw is much harder to argue with. In terms of both inequality and absolute outcomes, many in the economy have been left behind. Our economy produces vast differences in outcomes.

But this doesn't answer the question of why our country looks this way. That's where our narratives come in. They boil down the complex to the simple. Our country is providing the opportunity it should, or it isn't. Differences in outcome reflect (primarily) differences in effort, or they don't.

I will begin by going into more depth on the narratives, especially The Myth, providing more detail on its components, tracing some of its origins, and presenting a number of examples of its use in a wide array of contexts. Following the citation of popular culture examples, I will summarize the results of a survey by the Pew Charitable Trusts, conducted in the wake of the Great Recession and

Financial Crisis of 2007-9. The survey provides a useful window into the resilience of The Myth in the face of a crisis that might have shaken one's faith in the narrative's underpinnings.

The elements of The Myth

Success is determined by individual effort.

This nostrum is so embedded in our country's thinking that it's easy to overlook it. It is closely related to the notion that our economy may be described as a meritocracy—people earn what they deserve and "merit," and more generally receive the resources and benefits that they deserve. The best rise to the top. Hard work gets the job done.

This principle can be employed in a particularly pernicious way to re-interpret the effects of systemic racism on economic outcomes for families of color. Rather than admit the ways in which our country as a matter of policy has barred all non-white people from equal opportunity to success, the individual effort narrative instead asserts that racial and ethnic differences in economic outcomes reflect defects in individuals' efforts, as well as their choices about education, housing, and criminal activity. Differences between affluent and poor white families can be attributed to the same differences in effort and choices, although in many cases they are also seen as the result of government interference in free-market practice.

Chapter 3 will discuss the empirical evidence in favor of elements of The Myth. However, there are some logical issues with the individual effort element of the Narrative. First, attribution of success often ignores a particular form of selection bias inherent in doing so: The issue of survivorship bias. Those who we observe today as successful are the *ex post* winners in our economic system. Focusing only on those individuals who have already achieved success in the system obviously ignores those who did not succeed. By doing so, one could falsely conclude that anyone can succeed, or make false linkages between starting conditions among the winners and ultimate success, as in the parables of the self-made man. Hard work is still of course required to succeed from any initial conditions, but hard work is quite clearly not sufficient to ensure success.

A second issue is that the hard-work-begets-success element of the narrative is often stood on its head in two ways to draw inferences, often inappropriate, about successful and less-successful people. The first is that anyone who accrues the outward trappings of success (homes, cars, boats, etc.) must have (a) worked very hard, and (b) be brilliant. In many cases, both are true (although it appears that at least 20% of people fall into the top 1% of the IQ distribution). But many arrive at

their advantaged circumstances at least in part through good fortune, which takes many forms. They are born to the right parents, in the right neighborhood, with access to good schools where they may make vital business connections, taken on board by a key mentor, beat out a competitor with a similar product idea by a week due to a fluke of marketing or finance—the list goes on and on. Because of the role that chance plays in determining economic outcomes, it is hazardous to infer that success implies previous hard work and brilliance, or more simply, that success is always earned.[4]

This is nowhere more true than in the financial sector, which pays enormous salaries and accounts for a surprisingly large fraction of overall US compensation and profits. As of mid-2021, the financial sector accounted for 22% of profits (it had peaked at 38% in 2002 in the lead-up to the financial crisis) and 7.9% of compensation paid, for an industry that has accounted for a steady 4 to 4.5% of employment for decades.[5] Imputations of genius and social worth are made freely. And yet, the actual value added to society for some financial sector activities is highly suspect, often in the form of marginally higher returns for high net worth individuals. Of course, a good portion of what financial markets do is essential to nonfinancial activity—providing credit to businesses for productive investment, lending to households for stable (and affordable) housing, for educational opportunity, and providing depository and payments vehicles for households and businesses. But much has less direct connection to the essential functions of the mainstream economy.[6]

More damaging than these suspect deductions are the implications that the hard work narrative bears for the less successful. The hard work narrative imputes to the less-successful personal deficiencies that account for their lack of success. They are lazy, or have not persevered, or made poor decisions.[7] An alternative is that they did not enjoy the same accidents of birth and life that the successful did. While I know of no hard data to support this conclusion, I will assert the following postulate:

Laziness is uniformly distributed across income deciles.

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[4] Adam Smith laments in The Theory of Moral Sentiments this "…disposition to admire, and almost to worship, the rich and powerful, and to despise, or, at least, to neglect persons of poor and mean condition…", and deems it "…the most universal cause of the corruption of our moral sentiments." He goes on to despair "That wealth and greatness are often regarded with the respect and admiration which are due only to wisdom and virtue…" and that "…the contempt, of which vice and folly are the only proper objects, is often most unjustly bestowed upon poverty and weakness…". Part 1, section 3, chapter 3.

[5] National Income and Product Accounts, 2021.

[6] See Ben Friedman's "Is our financial system serving us well?", *Daedalus*, Fall 2010, for more on this topic.

[7] The results from the Pew survey cited later in this chapter bear this out as a widely-held perception among the general populace.

The incidence of laziness among the rich is the same as that among the poor.

A third error of inference that is very commonly employed is the "I know a person" retort. In support of the notion that hard work can overcome any initial conditions, no matter how bad, some will point to a person they know who has succeeded despite objectively poor initial conditions. Therefore, one can succeed if one works hard. You only need one counter-example to rebut the claim that hard work is not enough.

But of course, this is almost always misleading, for two reasons. First, upon further examination, it often turns out that this person had the benefit of a mentor or other benefactor, an unusual schooling or employment opportunity, or some other "leg up" that helped them, despite the odds, to succeed.[8] Those advantages are great for that individual, but they are not scalable to the larger population that this book is concerned with.

Second, the points that this book are trying to make pertain to the bulk of the population, not to the few outliers from the norm, the exceptions that prove the rule. We will always delight in those who can be successful despite a difficult start. But it is a mistake to generalize from those rare examples to the plight of the far larger population. There are tens of millions who are finding it difficult to succeed in our economy. It's great that there are a few hundred who make it from such starts, but this highlights the scale of the problem, it does not reveal a hidden solution.

The rewards to work justify the effort: Workers are paid according to their true value to the business

Economic theory would suggest (loosely) that factors of production (workers, capital equipment) are paid according to their marginal productivity, which is to say that if the addition of a worker to a firm's rolls contributes $1000 of value-added to the firm's output, in a perfectly competitive world, the worker would receive something like $1000 (in total compensation) for her effort. This element of the narrative bears implications on both the low and the high end of the compensation scale.

On the low end, this principle can be used to justify whatever workers are currently paid. Low wages must reflect a relatively low contribution to the firm's product or service. That contribution may be low because (given current technology) the position occupied by the worker is inherently a low value-added position. Or it could be because the specific worker brings relatively

[8] The section later in this chapter on Horatio Alger stories and more recent "rags-to-riches" stories provides many examples of this point. Very few succeed on their own, without any good luck or Divine Intervention.

low skills and experience to the job, and thus will contribute relatively less to the firm's welfare. There should of course be some truth to both explanations. Jobs that require fewer skills and less training will on average pay less than those that require more skills and training, a prediction that has been borne out in numerous studies of actual earnings.[9] And within a specific job type, workers who bring lower skills and training to the job will over time likely accrue less pay, as they add less to the value of the firm.

A problem with this component of The Myth is that is very difficult to verify, or to falsify. It is hard to measure the productivity for many types of workers, in part because it is hard to measure their output (recall that productivity here is defined as output produced per hour worked). How do we measure the output of a lawyer? Or a health care aide? Or a secretary? Or a teacher? We can certainly measure the hours spent on a task, but that tells us nothing about the output produced during those hours, and is of course hopelessly circular when it comes to measuring output per hour. You can't measure both hours and output via hours! For any worker involved in providing a service—legal, health, educational, professional—the measurement of output and thus of (output per hour or) productivity is notoriously difficult.[10]

Assuming we can clear the hurdle of output measurement, can we clearly attribute increases in the output of a firm or institution to a particular worker, or a particular class of workers? In some cases—think simple manufacturing operations or assembly lines—one may be able to measure a specific worker's productivity. But for other categories of jobs, attribution can be extremely difficult. You may know how many hours a health aide spent with a patient. But how much did he contribute to the medical output—improvements to the health of the patient? The point is that knowing when wages are in or out of line with productivity is extremely difficult, for the individual worker, or for whole classes of jobs. This allows a lot of leeway and subjectivity in assessing whether workers are under- or over-paid. [11]

[Citing a "shortage of skilled workers" is so common among business gatherings that it has become a boilerplate of PowerPoint presentations about the workforce.[12] But foundational to the

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[9] The research dates back at least to Mincer (1958), and includes novel empirical approaches such as that in Ashenfelter and Krueger (1994).

[10] Robert J. Gordon has led the way in highlighting difficulties in productivity measurement. See Gordon (1995), Gordon (2015).

[11] In an interesting development, some companies have raised wages for entry-level and lower-skilled workers in the wake of the pandemic. Paul Krugman has called this the "The Revolt of the American Worker," a make-up for many years of low wages for workers in such jobs. See Krugman (2021a), *New York Times*.

[12] For one more thoughtful example, see Sarah Chamberlain (Forbes Magazine, Aug. 21 2019) "Addressing the Skilled Labor Shortage in America."

accumulation of skills are primary and secondary education. Children do not choose their schooling options. If one is born to a rich family, the family may have some private-school choices. But in low- and middle-class families, schooling is a function of where you live, plain and simple. Rarely is the solution to raise wages—a fairly typical Econ 101 response in the face of a shortage, although that may be changing for some positions in the wake of the COVID-19 pandemic.]

On the high end of the compensation scale, the same basic argument is often applied, with some embellishments. Sky-high CEO compensation is justified by reference to the value-added principle: It must be that CEOs contribute great multiples of value-added to their firms relative to the average worker. If they did not, no firm would pay them the salaries they receive, often in the tens of millions of dollars. It wouldn't be "rational." Recent estimates of CEO pay show an increasing spread between CEO and average worker compensation. A series of studies by the Economic Policy Institute, for example shows top executive pay increasing from a multiple of 20-30 in 1965 to over 350 in 2020.[13]

Theoretical arguments that seek to justify huge gaps include the value of CEO's "rolodexes" or professional networks (as in Engelberg, Gao and Parsons 2009); the increasing importance of digital platform companies who have typically paid their CEO's higher, perhaps due to importance of the vast customer networks that form the basis of their business models; the increasing array of complex skills now required to function as a CEO, including an understanding of financial markets, public relations, and navigating a globalized marketplace and supply chain (see Tyler Cowen 2019); and the effect of increasing firm size on CEO compensation (Gabaix and Landier (2008)). To oversimplify this last argument, even if the CEO's contributions make a difference of as little as .01% to the value of the firm, for a firm with market value of $350B, that could justify a $35M salary. Other research that blends theory and practice notes that the actual link between CEO compensation and firm performance is weak, and that CEO compensation may be better explained by the "social psychology of the boardroom" (see O'Reilly and Main 2010). That is, relationships among board members lead to cross-confirmation of CEO's compensation via common board participation.

To me, these stories reflect the economics and business profession's strong desire to rationalize outcomes that most would view as simply outlandish. As a good friend of mine quipped, "do you think that Mark Zuckerberg would have abandoned his Facebook project if he knew that

[13] See Mishel and Kandra, Economic Policy Institute, August 10, 2021.

his compensation would be a mere $100 million, instead of $100 billion?" CEO compensation seems well out of proportion with any true value-added, either to the company in question or to society.

We live in a "post-racial" economy.

With the Supreme Court's ruling on *Brown versus Board of Education* in 1954, the passage of the Civil Rights Act in 1964, the Fair Housing Act of 1968, and the Executive Orders that spurred the use of Affirmative Action in employment and university admissions, many believed we were entering a "post-racial" era of U.S. history. These landmark pieces of legislation and Administration leadership made anti-discrimination the law of the land. Mission accomplished.

Because it has been more than 50 years since the passage of this legislation, any effects of previous discrimination should have been reversed, this narrative might say. The laws should remain on the books, but the use of Affirmative Action for employment or educational goals is no longer necessary. The election of Barack Obama in 2008 further bolstered adherents to this narrative. The *Wall Street Journal*, for example, in a 2008 editorial averred "One promise of his victory is that perhaps can put to rest the myth of racism as a barrier to achievement in this splendid country."[14] [15]

That the *Journal* might be optimistic about moving into a post-racial economy seems less controversial. That they call racism as a barrier to achievement up to that date in 2008 a "myth" is stunning, and reflects an underlying pillar to The Myth that has operated for some time. Racism has <u>not</u> been a barrier to economic success—that is a myth. Therefore, something or someone else must be to blame. It would be nearly impossible to conclude that racial and ethnic (and gender!) disparities in economic outcomes no longer exist, as the wealth of data in chapter one show. This critical element of The Myth says that racism, personal or structural, is not to blame.

Government's role: Stay out of the way.

Unfettered capitalism with free markets does the best job of allocating the nation's resources among its people. The genius of markets is that they provide a mechanism for allocating economic resources without the need for Soviet-style government interference. Relative scarcities produce increased prices (for goods, services, labor, financial assets), enticing suppliers to produce more of the scarce goods, easing the scarcity and lowering the price. In the long run, those goods and

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[14] "President-Elect Obama: The voters rebuke Republicans for economic failure," *Wall Street Journal*, November 5, 2008.
[15] Love and Tosolt (2010) provide a fascinating take on President Obama's place in the racial and political landscape.

services that yield the greatest benefit to society will be in highest demand, yield the most profit, and draw the most resources, producing the most beneficial outcome. Government policies that restrict unfettered capitalism will distort the price signals needed to clear markets, and lead to worse outcomes overall.

To be clear, I am not taking the position that capitalism *per se* is a problem. Capitalism and (relatively) free markets—more on that below—can work well in many circumstances. A brief discussion of what capitalism does well is presented in chapter 1. The problem lies in our particular brand of capitalism, a brand we have worked hard to create and sustain.

A strong corollary to the free markets religion is that smaller government is better, <u>because the private sector does most things better than government can</u>. The private sector is of course better suited to the basic provision of many goods and services. No one today seriously advocates a move towards Soviet-era government control of resources.[16] A quote from President Reagan in remarks to the National Alliance of Business in 1981 sums up this position nicely:

> "There is a legitimate role for government, but we musn't forget: Before the idea got around that government was the principal vehicle of social change, it was understood that the real source of our progress as a people was the private sector. The private sector still offers creative, less expensive, and more efficient alternatives to solving our social problems. Now, we're not advocating private initiatives and voluntary activities as a halfhearted replacement for budget cuts. We advocate them because they're right in their own regard. They're a part of what we can proudly call ``the American personality."[17]

The argument over the size and appropriate role of government continues today, and it is not restricted to debate across party lines. There is significant disagreement within parties about that role, as evidenced by the difficulties within the Democratic party to pass the Biden Administration's historic (in size as well as reach) social programs bill in the fall of 2021.

Inequality is OK, maybe even beneficial, because riches accruing to the top will inevitably benefit the needy.

The phrase "trickle down" has been so widely-used that it is now an economics-specific entry in the dictionary:

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[16] As Galbraith puts it, in discussing the "Nor does the experience of the countries for whom public ownership became policy…suggest that it enlarges the liberties of the citizen. On the contrary. Accordingly, the principal case for socialism has dissolved. This is recognized." Galbraith (1996), p. 17.

[17] Remarks at the Annual Meeting of the National Alliance of Business, October 5, 1981. Ronald Reagan Presidential Library and Museum, Archives. https://www.reaganlibrary.gov/archives/speech/remarks-annual-meeting-national-alliance-business

> **trickle-down theory** (noun): a theory that financial benefits given to big business [and the wealthy] will in turn pass down to smaller businesses and consumers. (Merriam-Webster, online edition; bracketed text added from the *Investopedia* definition)

I will examine the evidence bearing on this theory later in the book. The phrase appears to have originated with comedian Will Rogers, who reportedly used it to berate President Herbert Hoover's economic stimulus efforts during the Great Depression. It was subsequently used by FDR in a speech that poked fun at the notion, and by detractors (John Kenneth Galbraith among them) to describe President Reagan's "supply-side" economic policies. While few conservatives would label their own policies "trickle-down," many would subscribe to the notion that less regulation, and tax cuts for corporations and the wealthy can be expected to raise output and create jobs.

This theory is used to this day to justify tax cuts for corporations and wealthy individuals—indeed, the Tax Cuts and Jobs Act of 2017 incorporates some elements of supply-side economics. The importance of this element of the narrative lies exactly in its power to motivate politicians to pursue specific policies that overtly benefit the already wealthy and successful in our economy. Without an appeal to the benefits such a policy might yield for the lower and middle classes, it might be very difficult to garner political backing. But if the supply side effects really do kick in, well then, it's a win-win proposition for the rich and the poor!

How business should operate in a free market system

Maximizing shareholder value is the ultimate overarching goal for the firm. Milton Friedman helped to elevate this maxim in his 1970 essay, cited above. A quote from that essay reveals the intensity with which Friedman held this view, and some of the ideological underpinnings that motivated his view:

> The businessmen believe that they are defending free enterprise when they declaim that business is not concerned "merely" with profit but also with promoting desirable "social" ends; that business has a "social conscience" and takes seriously its responsibilities for providing employment, eliminating discrimination, avoiding pollution and whatever else may be the catchwords of the contemporary crop of reformers. In fact they are—or would be if they or anyone else took them seriously—preaching pure and unadulterated socialism. Businessmen who talk this way are unwitting puppets of the intellectual forces that have been undermining the basis of a free society these past decades.[18]

[18] Friedman (1970), *op cit.*

Note the emphasis in this quote on "socialism," and on undermining a "free society." Maximizing shareholder value is not just a nice idea. Pursuing other goals undermines the basis of a free society. Them's fightin' words.[19]

Adherence to this element of The Myth has borne significant consequences. Note that increasing shareholder value is roughly equivalent to maximizing the stream of profits generated by a company—this generally raises stock prices, so is good for the shareholder. In fact, many models of stock prices posit exactly this linkage.

So how is a firm to raise profits? Well, profits are approximately equal to revenues minus0 costs, one can either (a) raise revenues, by increasing prices or expanding markets or market share, or (b) lower costs. Costs in turn may be lowered by finding new and more efficient ways to produce goods or offer services (an increase in productivity, economists would say), or by lowering the direct costs of the inputs to production—labor, machinery, utilities costs, and so on.

The US economy is already pretty productive. Finding ways to significantly increase productivity—innovating--is not easy, although companies are striving to do so all the time. However, keeping down the largest cost of producing most any good or service (about two-thirds of all cost)—labor—may be easier to achieve. It is fair to argue that the relentless drive to raise profits, in large part by keeping labor costs down, has much to do with the distribution of wages and income that we observe in the US today. That goal has been accomplished by dramatically reducing the penetration of unions,[20] nearly eliminating the provision of defined-benefit pensions, shifting the cost-sharing of health-care towards workers, keeping wages from rising quickly (data on wage gains in low- and middle-income over past decades)—all of which make the firm profitable, but do not particularly help the worker.

One way to summarize the impact of these decisions is this: While productivity (output produced per hour of labor effort) has continued to rise moderately over the past several decades (the green line), averaging two percent annually in recent years, and profits have increased significantly over the same period (the blue line), the share of income going to labor (the red line in the second chart) has declined significantly over the past 30 years, in part as a consequence of these conscious actions. Another way of putting this is that although businesses have increased their efficiency, and therefore increased profits, the benefits of increased efficiency have largely not gone

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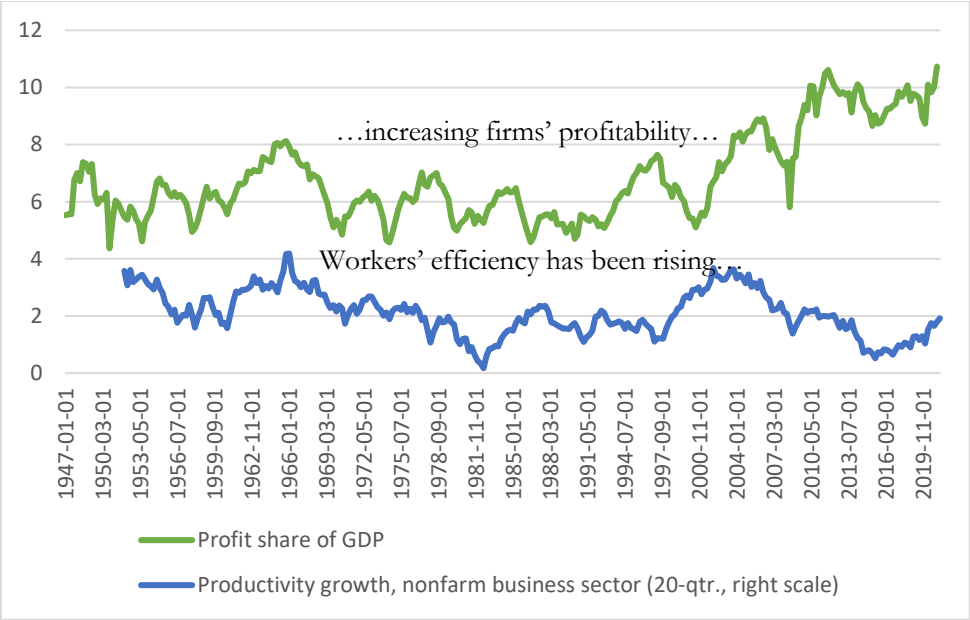
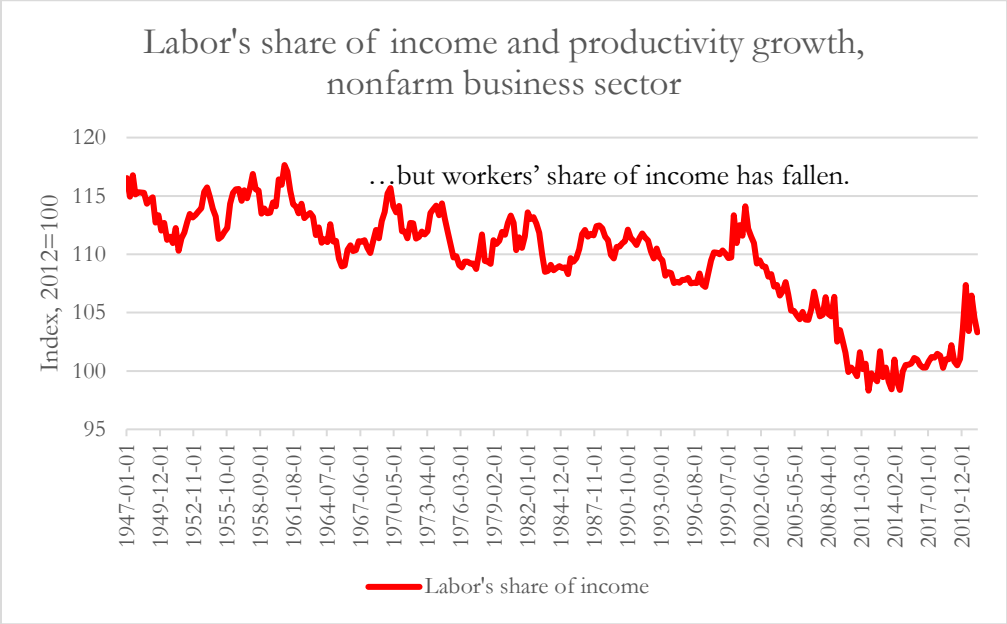
[19] Wartzman (2017), Stiglitz (2012), and Krugman (2021a), among others, highlight the damage done by strict adherence to Friedman's maxim. Krugman summarizes: "For America is a rich country that treats many of its workers remarkably badly. Wages are often low;…Hours are long…Work is also unstable…"

[20] See Kane (2016), pp. 30-33.

to workers. Shareholders, however have benefitted, as larger profits generally translate into higher stock prices. And shareowners are lopsidedly those in the highest income and wealth deciles.





Source: Bureau of Labor Statistics, FRED (St. Louis Federal Reserve Bank)

In an encouraging sign, some business leaders have called this principle into question of late. In 2019, the Business Roundtable issued the following proclamation:

> Americans deserve an economy that allows each person to succeed through hard work and creativity and to lead a life of meaning and dignity. We believe the free-market system is

> the best means of generating good jobs, a strong and sustainable economy, innovation, a healthy environment and economic opportunity for all…
>
> While each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders. We commit to:
>
> - Delivering value to our customers. We will further the tradition of American companies leading the way in meeting or exceeding customer expectations.
> - Investing in our employees. This starts with compensating them fairly and providing important benefits. It also includes supporting them through training and education that help develop new skills for a rapidly changing world. We foster diversity and inclusion, dignity and respect.
> - Dealing fairly and ethically with our suppliers. We are dedicated to serving as good partners to the other companies, large and small, that help us meet our missions.
> - Supporting the communities in which we work. We respect the people in our communities and protect the environment by embracing sustainable practices across our businesses.
> - Generating long-term value for shareholders, who provide the capital that allows companies to invest, grow and innovate. We are committed to transparency and effective engagement with shareholders.
>
> Each of our stakeholders is essential. We commit to deliver value to all of them, for the future success of our companies, our communities and our country.

Recent academic work has similarly revisited Friedman's maxim, notably a paper by Hart and Zingales (2017) that advocates "Companies should maximize shareholder welfare not market value". Jamie Dimon, in the same Business Roundtable report, suggests with a mix of understatement and hyperbole that:

> "**The American dream is alive, but fraying**," said Jamie Dimon, Chairman and CEO of JPMorgan Chase & Co. and Chairman of Business Roundtable. "**Major employers are investing in their workers and communities because they know it is the only way to be successful over the long term. These modernized principles reflect the business community's unwavering commitment to continue to push for an economy that serves all Americans.**"

These are indeed encouraging signs. But academic articles and business lobbying group proclamations do not immediately change the landscape. However, they indicate some awareness on the part of some larger business leaders that all is not right with the U.S. economy. Jamie Dimon might alternatively have said "The Myth is alive, but fraying."

<u>Stories of self-made success</u>: the parable of the self-made man in popular culture

I have suggested that the narrative of individual effort, like The Force, is strong in us. In this section, I cite a number of examples, both recent and older, that show how widely disseminated and admired is the parable of the self-made man in everyday culture. This may serve to demonstrate that, while elements of The Myth may be more closely aligned with a conservative than a liberal viewpoint (minimal government intervention, for example), this element crosses all ideological boundaries.

Horatio Alger's "rags-to-riches" stories

Stories of self-made men, often called "rags-to-riches" stories, were promulgated in the 19th century by Horatio Alger. A brief digression into these Alger stories may be of interest, as it will illustrate what Alger actually wrote, and how his writings have been adapted to fit The Myth, again reflecting our deep desire to believe that individual effort in a Land of Opportunity makes anything possible for anyone.

Alger wrote his stories, often in serial form, in the last third of the 19th century. While his novels for boys are often characterized as rags-to-riches stories, in fact they most often focused on the virtues of the protagonist, who usually began in disadvantaged circumstances. In most all of the stories, the protagonist benefitted from an intervention that boosted him out of his initial circumstances. Alger described these interventions as the result of Divine Providence—God had looked favorably on the person of high virtue, and rewarded him with material prosperity. Alger did not believe such Providence was likely to be available to the average person, so his wasn't in fact a self-help prescription for widespread economic success. Instead, it was a morality play that ended well for the virtuous protagonist, due to Divine intervention. Today, some might change the source of individuals' success from "Providence" to "luck." In short, hard work did not lead to wealth. Good luck—or good fortune—did.

Alger's novels came to popularity during the Gilded Age, but they subsequently fell out of favor as wealth inequality rose, and as labor unions and labor disputes became more prominent features of the economy. [21] Yet the distorted interpretation of his morality plays persists to this day. The Horatio Alger Society annually presents its "Strive and Succeed" award to "promising young people who emulate the ideals of Horatio Alger, Jr.", namely the spirit of "Strive and Succeed," "…the concept that success is earned and character is developed by following principles of honesty, integrity, hard work, industry, and good sportsmanship."[22] No one could fault the Society for

[21] See Nackenoff (1997) and Scharnhorst and Bales (1981).

[22] From the Horatio Alger Society's website ("Bylaws") as of October 19, 2021. https://www.horatioalgersociety.net/

promoting these virtues. But the link others have somewhat mistakenly drawn between Alger's novels and the notion that all individual effort is all that is required to succeed reveals our deep desire to believe that's how our economy works.

Interestingly, in Alger's preface to "Ragged Dick," first published as a serial and then collected into a single volume, he frames his stories as follows:

> The author hopes that, while the volumes in this series may prove interesting stories, they may also have the effect of enlisting the sympathies of his readers in behalf of the unfortunate children whose life is described, and of leading them to co-operate with the praiseworthy efforts now making by the Children's Aid Society and other organizations to ameliorate their condition.[23]

Rather than a self-help manual for the indigent, it was a plea for compassion—and aid—to the many who were born into poverty. Yet we have distorted Alger's meaning to suit our love of The Myth.

The popularity of such stories endures long after the demise of Alger and the Gilded Age. Stories of the type can be found across all forms of media, from newspapers to TV and cable news to online sites to films.

TV/Cable News Stories

You don't have to look far to find recent network and cable news stories that play up the rags-to-riches, hard work is all it takes meme. The start of this chapter cites the September 11, 2017 CNBC news story "10 billionaires like Oprah Winfrey who grew up poor." ABC News (12/13 2006) posted the story of Chris Gardner that was the basis of the Will Smith film "The Pursuit of Happyness". Gardner was born poor, black, abused, parents missing in action. He enlisted in the Navy for four years. By chance, he encountered a rich stockbroker driving a Ferrari. That chance meeting motivated him to take a training course on brokerage, which he could barely afford. During some personal troubles, he was helped by a local church that provided a place to sleep. He persevered, got his stockbroker's license, and made a lot of money. Actor Will Smith, who portrayed Gardner in the film, said of him: "Chris represents the American Dream." It's of course a great story, and Gardner's start was indeed tragic and difficult.

There are many such stories on Fox News, many with accompanying opinion and editorializing. One interesting example is the rags-to-riches story of Forrest Lucas, on the "Life, Liberty and Levin" show. Host Levin quickly decries the "Democrat Party," "Socialism," "The

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[23] Horatio Alger (1868), Ragged Dick; Or, Street Life in New York, (Digireads.com edtion, 2009.)

Green New Deal," and the "We've gotta get rid of fossil fuels" crowd in passing as he introduces Mr. Lucas, noting that "…most of these people have never created a single job in their lives." Mr. Lucas, he says, is someone who has "made it on his own." Born poor, right after the Depression, on a farm, Lucas did not attend college, but did get a good HS education. His father was a drinker, often absent. Lucas left home to work on another farm. While not his first choice, he went to work for a manufacturing firm on the night shift. He saved up, bought a semi truck, and started driving at age 21. On the road all the time, he continued to save enough to buy a small business, but his wife blew the money away. Over time, he bought more and more trucks, eventually moving to the West Coast, where he runs a large trucking company, and is quite wealthy.[24]

CBS News ran a story on March 12, 2015 entitled "Self-made Billionaires."[25] This brief reporting highlights that "Among the record 1,826 people on [Forbes' annual billionaires list] are plenty of people with very humble beginnings." Featured are Hong Kong business magnate Li Ka-shing (a high-school dropout), Starbucks CEO Howard Schultz (grew up in a New York housing project), real estate developer David Walentas ("grew up poor, shoveling manure at a farm"), canned-produce gian David Murdoch (never finished high school), and WhatsApp creator Jan Koum ("relied on food stamps before growing up").

Why are these news stories? To be sure, Lucas, Gardner, and the billionaires in CBS's story started off in tough circumstances, and they demonstrated grit, hard work, thrift and perseverance. But implicit in these stories is the message for the millions of others who also start off in disadvantaged circumstances: You too can achieve this kind of wealth, if you just work hard and stick to it. Sadly, that proposition has been tested millions of times, and it almost always fails. The few stories highlighted in the popular media are quite literally the exceptions that prove the rule.

Films

The movies' treatment of the rags-to-riches genre varies greatly. In some, like "Trading Places" (1983), "Pretty Woman" (1990), and "Slumdog Millionaire" (2008), the protagonist begins in economically challenging circumstances, but a twist of fate or the intervention of a kind stranger changes their lives, and the happy ending is affluence and/or wealth. In Citizen Kane (1941), the protagonist is plucked from poverty to attain great riches, through equal measures of hard work and conniving, but finds material success to be lacking. Kane ends up longing for the simple joy found in

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[24] "Forrest Lucas shares his rags to riches story," Life, Liberty & Levin, June 30, 2019.
[25] https://www.cbsnews.com/pictures/self-made-billionaires/

his childhood sled (spoiler alert). "The Pursuit of Happyness" (2006) depicts a struggling single father who takes a course in stock brokerage, begins trading, and ends up amassing significant wealth through his trading prowess.

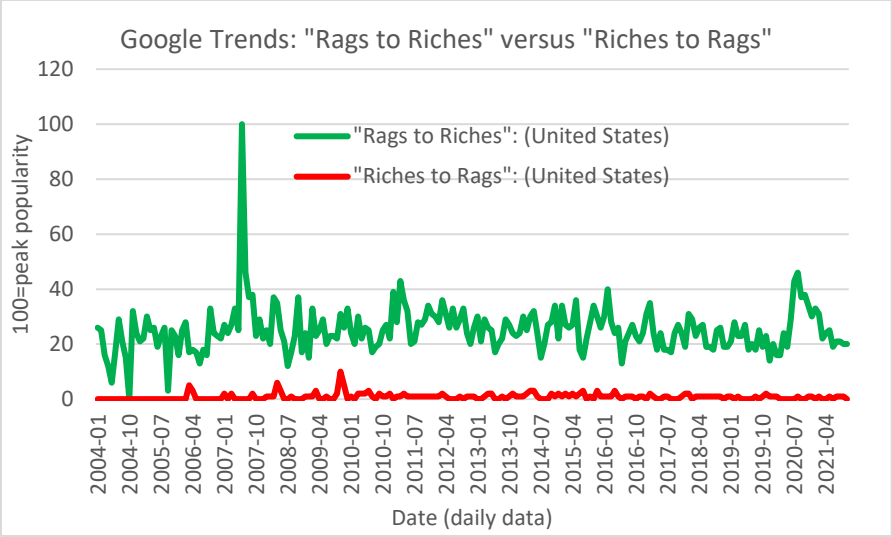
While the treatment of the rages-to-riches stories in film is more nuanced, studios bank on our attraction to the story of the economic and social underdog who wins in the end.

Online media

Celebrities are a favorite subject for rags-to-riches tales. They are highly visible, often beautiful, and fabulously wealthy. And some started off in truly difficult circumstances. An article in The Business Insider from January 10, 2021, entitled "21 rags-to-riches stories that will inspire you," is one recent example. It tallies a number of celebrities who started off with quite modest means—Dolly Parton, Leo DiCaprio, Halle Berry, Oprah Winfrey—and are now worth millions or billions. Their stories cite the importance of perseverance, hard work, and frugality—they slept in homeless shelters, delivered newspapers, tended bar, went without telephone and electricity. All of these represent true hardships, but as the title indicates, their millions/billions are meant to inspire us to work hard, persevere, dream. A similar story in the same publication about 17 billionaires begins with the advice: "These 17 rags-to-riches stories remind us that through determination, grit, and a little bit of luck anyone can overcome their circumstances and achieve extraordinary success."

It would be easy to produce dozens more of these stories. They clearly entertain readers and viewers, or they wouldn't be produced with such regularity. Their explicit premise, however, is dangerous. If anyone can succeed—not just to comfort, but to unbelievable riches—then there is no need to change the way the economy works. This is indeed the Land of Opportunity, equally available to all. The markets are working just fine. Nothing to see here.

While the rags-to-riches stories are incredibly popular, the riches-to-rags, or more commonly the rags-to-rags stories garner much less attention. As a fun but hardly scientific demonstration of this, the next chart shows the prevalence of rags-to-riches versus riches-to-rags in a Google Trend analysis performed in October of 2021. It's pretty clear where the money is.



What explains success?

The Pew Trust survey on Economic Mobility and The American Dream

A more scientific approach to assessing how the general public has assimilated the elements of The Myth may be found in this fascinating 2009 survey.[26] These data were collected in the midst of the Great Recession and Financial Crisis, an episode that highlighted some of the perils of a slavish adherence to The Myth (this episode will be discussed in more detail in Chapter 3). The build-up to the crisis featured cyclical narratives that Robert Shiller has shown often propel economic crises—in this case, housing will always be a good investment; house prices have never fallen nationally; you can't prove that these double-digit house price increases represent a "bubble;" financial entities know what they're doing with mortgage-related securities; too much financial regulation will stall economic progress.[27]

The summary that accompanies the survey report demonstrates the resilience of The Myth to onslaughts from severe economic circumstances that could plausibly have shaken its foundations:

> "In the midst of an historic economic crisis, Americans insist that despite the recession it is still possible for people to improve their economic standing, and most believe that they control their economic destiny. Americans believe ambition, hard work and education primarily drive mobility, rather than outside forces like the current state of the economy."

[26] The Pew Charitable Trusts, 2009. "Findings from a National Survey & Focus Groups on Economic Mobility." Note that for the Pew surveys cited in this chapter, the sample draws from the American Trends Panel, with over 10,000 respondents. The margin of sampling error for the full sample is plus or minus 1.5 percentage points, so that all of the differences highlighted in the text are statistically significant.

[27] See Shiller (2019), Narrative Economics: How Stories Go Viral and Drive Major Economic Events

That is some sticking power! Some of the specific findings of the survey are germaine to this discussion:

- 71% of respondents believe that "personal attributes, like hard work and drive, are more important to economic mobility than external conditions, like the economy and economic circumstances growing up," versus 21% who believe otherwise.
- There is a distinct (and disturbing, to me) symmetry in respondents' beliefs about what determines outcomes: The most common explanation for downward mobility in the survey was "personal attributes such as poor life choices and too much debt."
- Sadly, very few attributed differences in economic mobility to race and gender (15 and 16 percent, respectively).
- It is more important to give people "a fair chance to succeed" than it is to reduce inequality, by a 71 to 21% margin.
- In strong contradiction to the evidence on economic mobility, 55% percent of respondents disagreed with the statement: "In the US, a child's chances of achieving financial success is tied to the income of his or her parent."
- In confirmation of the individual effort aspect of The Myth, one respondent, a male parent aged 35-49 offered "People manage to pull themselves up from their bootstraps all the time". If only.

There is some evidence in the survey that runs counter to the strict version of The Myth. Most believe that there are some government policies that might help: "And while many believe the government hurts more than helps people move up the economic ladder, a majority say that a number of government policies would be effective at encouraging economic mobility."

Overall, this survey demonstrates the remarkable resilience of The Myth among the general public despite an ongoing crisis in which circumstances well beyond individuals' control had mightily disrupted their economic lives. Homeowners who had paid their mortgages regularly lost their homes when the price of their homes fell below the value of debt they owed, and their incomes were disrupted when they lost their jobs due to the recession. Bootstraps clearly provided insufficient lift for many during this episode, yet belief in self-made success persisted. On top of this, the priorities of economic policymakers were made quite clear: Financial institutions were quickly rescued, while ordinary households suffered for many years after 2009. We will return to this pivotal episode in chapter 3.

A more recent read on perceptions about the sources of success comes from a 2019 Pew survey: Sixty percent of respondents agree with the statement "Most people who want to get ahead can make it if they're willing to work hard." That is The Myth in a nutshell, and it has adherents among both Democrats (45%) and Republicans (78%). However, equally powerful is the split over whether poor families "have it easy, hard." This one splits strongly along partisan lines, with 74% of

Republican/Leaning Republican respondents agreeing with the statement "Poor people today have it easy because they can get government benefits without doing anything in return." Yikes. On the other side of the Great Divide, 72% of Democrats/Leaning Democratic agree with the statement "Poor people have hard lives because government benefits don't go far enough to help them live decently." That view has hardened among Democratic respondents over the past quarter-century: Less than 50 percent held the "hard lives" view in 1994. Republicans have stayed fairly steady, with around 25 percent agreeing with that statement since 1994.[28]

Respondents differed widely on their assessments of the contributors to economic inequality, as summarized in the table below, reproduced from the Pew Center's 2020 report.

Major contributors to economic inequality	
Explanation	**Percent saying "contributes a great deal"**
Outsourcing of jobs to other countries	45
The tax system	45
Problems with the educational system	44
The different life choices people make	42
Some people start out with more opportunity	40
Not enough regulation of major corporations	37
Some people work harder than others	34
Discrimination against racial minorities	32
Automation of jobs	30
Current US trade policies	29
The growing number of legal immigrants working in the US	23
Too much regulation of major corporations	15
Pew Research Center, January 9, 2020. Data collected Sep. 16-29, 2019.	

Regulation of companies was either too light (37%) or too burdensome (15%). Individual initiative--the "different life choices that people make," and "some people work harder than others" registered 42% and 34% acceptance respectively. Forty percent believed that "some people start out with more

[28] Pew Research Center 2019, "Views of the economic system and social safety net," December 17. https://www.pewresearch.org/politics/2019/12/17/views-of-the-economic-system-and-social-safety-net/

opportunities than others," a contributor for which there is ample research evidence. Just under one-third attributed inequality to "discrimination against racial and ethnic minorities."[29]

An interesting counterpoint may be found in a 2020 Pew survey that asks respondents why people are rich or poor. The survey finds that almost two-thirds believe that rich people are rich because "They have had more advantages in life than most other people," with one-third believing "They have worked harder than most other people." With respect to why people are poor, the responses are similar, with 71 percent believing "They have faced more obstacles in life than most other people," versus "They have not worked as hard as most other people."[30]

As with many issues of late, these results vary quite significantly by political affiliation. Among those self-reported as Republican or "leaning" Republican, 53 percent attribute success of the rich to working harder, and 42 percent believe the source of poverty is not working as hard as most other people. Both Republicans and Democrats are more likely now to attribute the source of richness to advantages than they were in 2014, with the Republican share so responding rising from 35 to 45 percent, and the Democratic share rising from 62 to 82 percent from 2014 to 2020. Almost all of that increase occurred between the 2019 and 2020 surveys. Just a couple of years prior to 2020, as many as 71 percent of Republicans believed that hard work explained rich people's success. The volatility of these responses over the past several years, the possible (temporary?) effect of the COVID pandemic and recession on responses, the relatively recent shift in responses, and the contradiction to the results of the 2009 survey tempers my optimism about these results. On this last point, the fact that 71 percent of respondents in the 2009 survey found that "personal attributes, like hard work and drive, are more important to economic mobility than external conditions, like the economy and economic circumstances growing up" seems to partially contradict the results in the 2020 survey.

There are of course nuanced differences between the questions in 2009, 2019 and 2020, but it's difficult to see all of these results as perfectly consistent. In 2009 and 2019 results, you can get ahead if you work hard. People pull themselves up by their bootstraps all the time. But the 2020

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[29] Pew Research Center 2020a, "Most Americans Say There is Too Much Economic Inequality in the U.S., but Fewer than Half Call it a Top Priority", January 9. https://www.pewresearch.org/social-trends/2020/01/09/most-americans-say-there-is-too-much-economic-inequality-in-the-u-s-but-fewer-than-half-call-it-a-top-priority/
Detail on contributors to economic inequality, https://www.pewresearch.org/social-trends/2020/01/09/what-americans-see-as-contributors-to-economic-inequality/

[30] Pew Research 2020. "Most Americans Point to Circumstances, Not Work Ethic, for Why People are Rich or Poor," March 2. https://www.pewresearch.org/politics/2020/03/02/most-americans-point-to-circumstances-not-work-ethic-as-reasons-people-are-rich-or-poor/

survey sees rich and poor significantly affected by external circumstances—"more advantages" for the rich and "more obstacles" for the poor.

A Gallup poll that asks about "the most important problem facing the country today" found that only one percent of respondents believed the "gap between rich and poor" to be the most important problem. Economic problems in general registered much lower than non-economic problems, by a margin of 85 percent (non-economic) to 16 percent (economic) in September 2021. But even within economic problems, the "economy in general," unemployment, and the federal budget deficit/debt ranked ahead of the gap between rich and poor.[31] Social issues such as poor government leadership, immigration, the judicial system, and race relations/racism (fortunately!) ranked well ahead of the rich/poor gap, with percentages ranging from 19 to 5 percent, respectively for these categories.

Are workers paid what they are worth?

A 2021 McKinsey study surveyed 25,000 residents about the state of economic opportunity. Only one-third of respondents agreed that "most people are fairly recognized and rewarded for their work." Only one-quarter of women agreed with this statement. There were only small differences across responses by race and ethnicity. When asked if they agree with the statement "the pay that most people receive allows them a good quality of life," just under one-third agreed, again with one-quarter of women agreeing, and more than a third of men. Racial and ethnic responses differed very little from the average. The lowest responses for both of these questions were from low-income workers: About 30 percent of those with earnings under $75,000 agreed with the statement, versus 42 to 47 percent for workers with earnings of $100,000 or greater.[32]

Employers may well believe that they are paying workers their value to the firm, given competition and cost pressures. Their workers feel differently.[33] Even more importantly, most workers believe they are not paid enough to afford a good quality of life. This represents another tension in adherence to The Myth: The ones in control (employers) believe it. The ones receiving the compensation aren't so sure.

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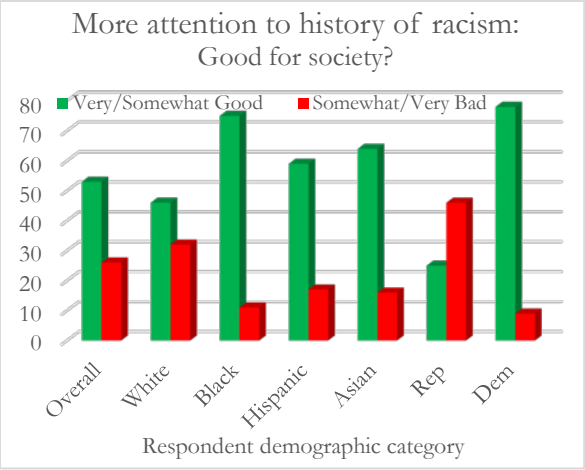
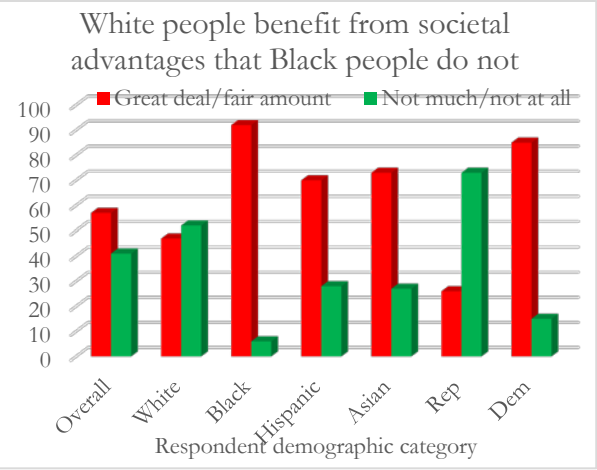
[31] Gallup Poll, "Most Important Problem," https://news.gallup.com/poll/1675/most-important-problem.aspx, November 5, 2021.
[32] McKinsey (2021), "Unequal America: Ten insights on the state of economic opportunity."
[33] Note that surveys of employees often find that employees believe they are paid below market rates, even when they may be above the prevailing market wage (see Smith, *Harvard Business Review* (2015)). Of course this is not the same as being paid fairly, if market wages undervalue many professions in the low end of the wage scale.

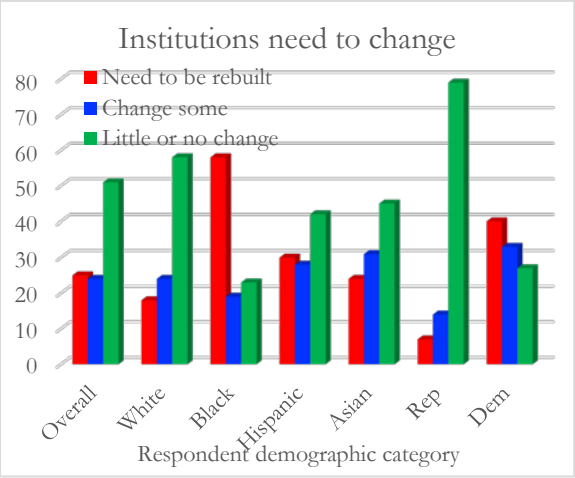
Post-racist/sexist/homophobic?

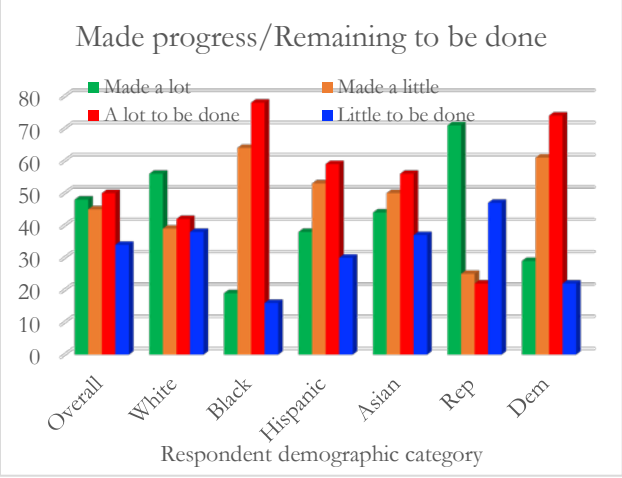
The same McKinsey survey finds that individuals' identities are perceived as negatively affecting their careers for some demographics. Whites and males appear to be doing okay, not surprisingly. More than one-third of women with family obligations felt that their job prospects were negatively affected by these aspects of their identity. Forty-one percent and 35 percent of Blacks felt that job prospects and compensation, respectively, were negatively affected by their identity. About 30 percent of LGBT men and women felt their identify had negatively affected job prospects and compensation.

The country more broadly disagrees on whether we are a Post-Racist nation or not, with opinions dividing by racial, ethnic, and partisan lines, as the following charts from a Pew survey focusing on racial divisions show.[34]









[34] Pew Trust (2021b).

Republicans stand out as feeling that attention to the history of racism is bad for society; Democrats and ethnic minorities line up reasonably well. Republicans stand out again in accepting or rejecting the notion of "white privilege," and again Democrats and ethinic minorities line up well, with modest differences between Blacks and Hispanics and Asians. Republicans clearly would prefer to leave institutions alone, but here they align more closely with whites, and Blacks feel the strongest about the need for institutional change (note that "change some" refers to making change, but working within existing institutions). Finally, whites and Republicans believe that a lot of change has already been made. That is far less true among Black and Democratic respondents. Most categories feel that much remains to be done, with the strong exception of Republicans and, to a lesser extent, whites.

Thus as to whether we are a post-racist nation, it depends on who you ask. Minorities and Democrats believe white privilege is real, and many believe institutions need to change. The same categories (not necessarily most people) believe that a lot remains to be done, so those groups clearly do not believe we are a post-racist country. But many white survey respondents and many Republicans (there is of course overlap) believe we are essentially post-Racist—no good will come from focusing more on the history of slavery and racism, no need to change institutions, and little work remaining to be done, given the progress already made.

What do people believe the role of government should be?

According to a 2020 Pew Trust survey, trust in government is at near-record lows, although it has been near its current reading repeatedly since 1980. This view is shared by Democrats and Republicans, although Republicans have a modestly more optimistic assessment (28%) than Democrats (12%) at the end of the Trump presidency.[35]

The appropriate role for the government also varies by partisan affiliation, but some broad patterns are consistent across parties. Respondents believe strongly that government should play a "major role" in addressing threats to public health (not surprising given the survey was conducted in the midst of a pandemic), responding to natural disasters, ensuring safe food and medicine, managing immigration, keeping the country safe from terrorism, and strengthening the economy (the item with the lowest gap between Republicans and Democrats).

[35] Pew Trust (2020b). The mistrust of the government is echoed in Gallup polls, see "Five Questions about Views of Business and Industry Sectors," question 5, https://news.gallup.com/opinion/polling-matters/354929/five-questions-views-business-industry-sectors.aspx , September 24, 2021.

Considerably lower numbers of respondents felt the federal government should play a "major role" in ensuring access to health care, protecting the environment, and "helping people get out of poverty," although the partisan split is also widest for these three categories. Republicans score the poverty and health care categories the lowest of all options. Democrats score the poverty category second lowest, but still evince considerable support for government's role (74%). Only 18 percent of Democrats believe the government is doing a very or somewhat good job in helping people escape poverty. Democrats and Republicans disagree strongly on whether government should be bigger and provide more services (76% of Democrats, 25% of Republicans) or smaller and provide fewer services (21% of Democrats, 72% of Republicans).

But views of some specific government programs tend to be quite positive—Social Security, the military, and Medicare, for example. Three-quarters of respondents to a 2019 survey wished no reductions to Social Security benefits should be made, and responses varied only a bit between Democrats and Republicans. Providing high-quality, affordable health care was viewed as a top priority for government by more than two-thirds of respondents, although most did not favor increasing spending on Social Security, Medicare and Medicaid.[36] Support for this objective was moderate (about one-half) among Republicans, and very strong (83 percent) among Democrats.

The American public holds conflicting views about the appropriate role of government, and not just across party lines. As a recent Gallup summary suggests:

> They tend to see the way the government works as a major problem facing the nation, they evaluate the government negatively, and they express little confidence in the government's broad ability to address domestic issues. Yet, Americans increasingly say the government should do more to solve, and take on a major role in addressing, the nation's problems.[37]

Sounds like an internal battle between The Myth and The Reality.

What do people believe the role of business should be?

That depends on which people you ask. CEOs and business writers are actively debating the role that maximizing shareholder value, à la Friedman (1970), should play versus maximizing stakeholder value, or practicing Corporate Social Responsibility. The citations of the Business Roundtable and associated discussions above reflect the growing awareness that shareholder value may not be the be-all-and-end-all of business objectives. By and large, this is a discussion among the

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[36] Pew Research Center, (2019b), sections 2 and 4.

[37] Gallup Polling Matters (2020), "Americans and the Role of Government," October 9. https://news.gallup.com/opinion/polling-matters/321767/americans-role-government.aspx

very largest business owners, who have the overhead and profit margins—the luxury, really—to consider new business objectives.

Michael Porter sees hope for businesses that expand their horizons beyond the shareholder value yolk, embracing the goal of creating "shared value," which creates economic value "by creating societal value". [38] Some of Porter's suggestions amount to means of improving productivity by involving new voices in the design and production of products, taking into account the variety of impacts that a company's products and production processes may have on the communities it operates in. But they also include investing in employee well-being and engagement, which have been shown to improve productivity. "Not all profit is equal" in Porter and Kramer's view. "Profits involving a social purpose represent a higher form of capitalism—one that will enable society to advance more rapidly while allowing companies to grow even more. The result is a positive cycle of company and community prosperity, which leads to profits that endure."[39]

Forbes Magazine (2019) points out the difficulty in implementing a new paradigm like this—how does one trade off the competing objectives inherent in a shared value or multiple stakeholder approach? The simplicity and clarity of shareholder value, which is (relatively) easy to measure, means that this maxim continues to dominate business thinking.[40] Porter's goal is laudable, but it is not yet clear that it has pulled business away from the overwhelmingly shiny object of profit maximization. Despite the talk, it remains uncertain how in practice businesses might realign to a new guiding star, much as we might wish they could. One nagging question that arises in reading through Porter's works: How do we get most or all businesses to agree to coordinate on a new set of objectives? Will they do it themselves, especially if it involves meeting newer, less-easily measured goals? Or does it require some form of government coordination?

Evidently, some business leaders are grappling with how they might move away from the Friedman (1970) rule. As for the public, to begin with, their trust in business is only a bit higher than their trust in government, as both Gallup and Pew surveys confirm.[41] The Pew survey asked respondents if they had a great deal or a fair amount of confidence that a given institution would act in the best interest of the public. Less than half (46 percent) of the "medium trusters" among respondents placed that level of trust in business leaders. Thirty-nine percent placed that same level

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[38] Porter and Kramer (2011).
[39] Porter and Kramer, *op cit.* p. 75.
[40] Neil Malhotra, "Should Corporations Simply Maximize Shareholder Value?" *Forbes*, April 16, 2019. https://www.forbes.com/sites/neilmalhotra/2019/04/16/should-corporations-simply-maximize-shareholder-value/?sh=46ec3a5227b7
[41] Pew Research Center (2019c), Gallup Polls (2021b).

of trust in elected officials. The Gallup poll has asked similar questions for four decades, and the responses are similar. Eighteen percent placed "a great deal or quite a lot" of confidence in "big business", versus twelve percent for government. The leaders in these surveys were consistently the military, with well almost 60 percent expressing high confidence in 2021, along with scientists, religious leaders, school teachers and the police. Small business, in contrast to the big business results, received among the highest scores in the Gallup polls, peaking recently at 70-75 percent with a "great deal/quite a lot" confidence rating. So it would be wise not to lump all businesses together in thinking about how business fits into the public's narrative about the economy.[42]

Part of the dichotomy in opinions likely revolves around the difference between publicly-traded and privately-held or -owned companies. Publicly-traded companies may be more likely to follow the "maximize shareholder value" maxim—after all, they have shareholders—and as a consequence may over time have become less trusted by the general public. Thus while large business executives, Boards and stockholders still hold on to much of the Friedman doctrine, to the chagrin of employees and the general public, smaller businesses are perhaps viewed as "one of us." Proximity and relation to the community likely also matter. Large corporations are distant and abstract, while small businesses operate in your town, owned by your neighbors. It's easier to trust your local hair salon than it is to trust Alphabet, or Meta, whatever those companies are really about.

Thus the relationship between the public and business is nuanced. But trust or not, most still feel that businesses should be left alone to do what they do best. Since 1994, the Pew Trust has tracked views on whether government regulation of business is necessary "to protect the public interest" or that it "usually does more harm than good." Both shares hovered near 50 percent from 1994-2017, the last time this question was asked, with a small rise in the "protects public interest" share from 41 to 50 percent over that period, and a correspondingly modest decline in the "does more harm than good" share from 54 to 45 percent. The split between Democrats and Republicans is more pronounced, and always has been, with about one-third of Republicans seeing regulation as necessary, versus two-thirds of Democrats.[43] In the most recent Gallup poll on the subject (September 2021), 43 percent of respondents said there was "too much" government regulation of business, one-quarter said there was too little, and 30 percent thought there was just the right

[42] Gallup's data on small business confidence extends only back to 1997.
[43] Pew Trust (2017), section 2.

amount, implying that three-quarters would oppose any increase in business regulations.[44] However it is measured, a substantial share of the population is generally opposed to business regulations.[45]

To attempt a reconciliation on these views on business:

- People do not trust Big Business, and they never have. The only institution with lower trust is government.
- People really trust small businesses, and they always have.
- People on balance would prefer the same or less regulation of businesses.
- It seems likely they are thinking primarily of small businesses when they vote to maintain or reduce regulation.
- This might suggest the door is open for a bipartisan agreement to keep regulation on small business light, but to tighten regulation on larger businesses where necessary (as validation of this proposal, see the note above on polling results that report calls for greater regulation of large tech and social media companies).
- A fly in this ointment is that people don't trust government, so it's unclear whether they would trust government to effectively regulate big businesses.

To conclude, from the perspective of those who control businesses, while well-intentioned academics and CEOs have begun to think about whether shareholder value might not be the best North Star, there has yet to be a sea change in the orientation of businesses, as there was in the other direction following Friedman's article. It may be that such a change requires coordination. It may be that it will just take time. But to date, it has not changed the outcomes for the millions who continue to labor under conditions that maximize both profits and worker misery.

From the workers' perspective, distrust of big business is significant and persistent. While survey respondents generally prefer no more or even less regulation, they might well make exceptions for the largest businesses, especially massive tech businesses.

<u>What the many stories that embed The Myth reveal about us</u>

It should by now be clear that this narrative resonates deeply with us—we want to believe in the efficacy of individual effort, meritocracy, the Land of Opportunity, and the American Dream. But rarely do stories of self-made success make clear that these are far and away the <u>exceptions</u> to the most common experience—starting in poor circumstances usually leads to poor outcomes later in life. Economic mobility is low. Thus these stories strongly reveal a triumph of belief over reality for the average citizen. For those on the top of the economic pyramid, they may reveal a desire to

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[44] Gallup Poll (2021c), "Big Business."

[45] One exception to the opposition to regulation is the recent rise in calls for regulation of large tech and social media companies. This concern is shared by members of both political parties. See Pew Trust (2021).

perpetuate the current hierarchy through continuous promulgation of the myth of self-determination. Chapter 4 will explore this linkage in more detail.

The Reality

The alternative narrative is in part the negation of some of the elements of The Myth: Free markets don't always deliver the best outcomes. People are not always paid what they're worth, on both ends of the pay spectrum. Individual effort is necessary but not sufficient for economic success. Maximizing shareholder value may not be the best or only objective for businesses. Opportunity is not equal for all.

But The Reality is more complicated than that, in ways that are central to this book's thesis. While free markets and capitalism in the abstract can be an excellent frame on which to hang our economic structure, our particular brand of free-market capitalism is only one of many possible ways for a capitalist economy to work. And our flavor of capitalism did not arise by accident. It has been tailored to benefit a select few. In short, we made it this way. "American Inequality didn't just happen. It was created." (Stiglitz, 2012, chapter 2).

A 2017 publication by the Center for Health Progress puts it this way: "The big lie of the American Dream is that with hard work, anyone can achieve great success. While it does happen, it's rare; and, it fails to account for the immense barriers we actively construct to make the journey more difficult for some than others."[46] A very similar sentiment is expressed in the Martin Luther King, Jr. quote at the beginning of this book. To reiterate a key part of that quote: "…capitalism has often left a gulf between superfluous wealth and abject poverty, has created conditions permitting necessities to be taken from the many to give luxuries to the few…" (author's emphasis). King recognized clearly in 1967 the extent to which we had consciously created barriers that caused disparate outcomes.

The Land of Opportunity: Our system denies opportunity to many, often intentionally

Many of those barriers were created to explicitly prevent families of color from achieving the economic success of their white peers. Chapter 3 cites the vast historical evidence documenting the litany of government policies and programs that by statute and implementation excluded all but whites from the roads to prosperity and wealth-building. The *New York Times's* 1619 Project work is

[46] See McAfee, Sarah, 2017. "Immigrant Rights Issues are Health Issues," *Center for Health Progress,* December 1.

one of the latest to painstakingly document the foundations of our country in slavery, and the long-lasting effects that history has had on outcomes through the present day. While I would prefer to avoid overtly political diatribes, it mystifies me that there are those in our country who wish to ignore this part of our nation's history, reacting strongly (sometimes violently) to the notion that it should be taught to our school children. To ignore it is to ignore some of the fundamental forces that have always been at work in our nation. Doing so is not only a failure of historical pedagogy, it is a moral failure to come to a reckoning with who we have been, to take responsibility for it, and consequently to work towards repairing the damage we have done.[47]

As suggested earlier, people hold different views about our turbulent racial history, and these narratives shape our explanations for persistent racial and ethnic gaps in income, wealth, education, health care, and incarceration. Those who believe we are post-racist, or that institutional racism was a small or insignificant factor in our history, will be less inclined to entertain significant remedies for the gaps today. That will be especially true if they couple this interpretation of history with the "individual effort" narrative, as they can attribute differential outcomes to differences in individual effort. But a key element of The Reality is that it embraces the rather considerable evidence to the contrary—that we are not post-racist, that our history is replete with stories of systemic and institutional racism, and that such racism has dramatically lowered the opportunities for people of color to succeed in so many ways.

In chapter VI, I will discuss some of the remedies that The Reality embraces. Because unequal opportunity has largely meant inability to build human and financial capital, they focus on changes that equalize opportunity to build both kinds of capital. And while people of color have suffered the most as a result of our economic system's design, women have also been denied opportunity, as the evidence in chapter 3 demonstrates. So too have many poor white families, often living in rural areas.[48] Whether or not you believe in The Reality, and many poor white families do not, that narrative believes it can explain why you are poor, and it does not boil down to your lack of effort.

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[47] The Southern Poverty Law Center's "Teaching Hard History: American Slavery" discusses this and related issues in depth, and provides a "comprehensive guide for teaching and learning this critical topic at all grade levels." https://www.learningforjustice.org/frameworks/teaching-hard-history/american-slavery?gclid=CjwKCAjw2bmLBhBREiwAZ6ugo0Mny_xSS4oXb_vN8ghSuodUPccHETP6ub11tNBKRI_fJC9U_-sa5BoChXUQAvD_BwE

[48] See the proceedings of the Federal Reserve Bank of Boston's Annual Economic Conference on "Geographic Disparities in Twenty-First Century America" for more on this topic. https://www.bostonfed.org/news-and-events/events/economic-research-conference-series/a-house-divided-geographic-disparities-in-twenty-first-century-america.aspx

Our disparities are not the unavoidable outcome of free markets and capitalism

This point is most readily made by comparing us to other advanced economies around the world, many of which are capitalist, free-market economies. But they produce very different results for their citizens. Chapter 3 provides a variety of comparisons across developed economies to make the point.

This is not to say that the solution is to adopt wholesale the economic framework of Sweden or France or Japan. The U.S. has a truly unique history, demographic makeup, and industrial structure that likely require a more equitable structure that differs from those of other capitalist economies. But it is to say that there is nothing inherent in capitalism and free markets *per se* that means we are forced to live with a lack of opportunity for millions of our residents.

Other aspects of our system that have been designed to produce disparate outcomes

The Reality believes—and chapter 3 will provide evidence to support—that in addition to systemic institutional racism, other key aspects of our system have been designed to slant opportunity towards white, affluent families and individuals. Key among these systems are:

Tax policy. While we have a progressive individual income tax system—which is to say that the rate per dollar earned increases with rising earnings—actual taxes paid look much less progressive than the statutory rates. While the top tax rate on individual income for married couples filing jointly with incomes over $628,300 is 37%, effective tax rates are lower. The effective tax rate—actual taxes paid divided by income earned—for the top quintile of filers in 2018 was about 15%. It has hovered near that level for the past 30 years, varying no more than one or two percentage points.[49] The effective tax rate across all filers has been about 10% for more than three decades. So-called "payroll taxes"—the taxes levied to pay into the Social Security and Medicare programs—are not calibrated to be progressive. As is well known, we are also not so progressive as some other advanced economies. Data to this effect are presented in Chapter 3.

Effective corporate tax rates are quite low. The current share of our national income that goes to corporate taxes is about 1% (as noted in chapter 1 and displayed in figure XX). At that effective rate—one-tenth the effective rate on personal income—corporate taxes generate about

[49] Historical CBO effective tax rates computed from their Tax Table Builder. Filers are ranked by income after taxes and transfers. See https://www.cbo.gov/publication/57061 .

one-ninth the revenue for the federal government yielded by individual income taxes[50]. Tax evasion, legal and illegal—for those who can afford it—is significant (witness the recent discussions about the Pandora Papers, and Secretary Treasury Yellen's efforts to get nations to agree on minimum corporate tax rates to avoid tax shopping), an important contributor to the low effective tax rates collected from high-income workers and larger corporations.

The structure of work. Over the past 50 years, we have constructed a set of conditions for workers in the lower earnings tiers that we did not accept earlier in our history. Low wages, poor benefits, unpredictable work schedules, poor chances for advancement (through "career ladders" or the like), poor "worker voice"—workers' way over the structure of their working conditions, insufficient flexibility for child and family care, poor access to child care together make life for the working poor a constant struggle.[51] In essence, we have arrived at a social norm in which many companies are quite comfortable sending their employees home with income and benefits that force them to accept government assistance—SNAP, TANF, housing assistance—to survive. This is often true even when households comprise multiple earners, or when workers toil at multiple jobs. I would contest that the arrival at this norm has been driven in part by the "maximize shareholder value" maxim, although it is difficult to prove this conclusively. The structure of work is discussed more fully in Chapter 1.

Redesigns of the Safety Net. The discussion of the Safety Net above shows that we have engaged in a constant dance between the implications of The Myth and The Reality for our safety net programs—SNAP, TANF, unemployment insurance, and others. The Myth consistently worries that programs that are too generous will reduce the incentive to work, to the detriment of recipients and the economy. The Reality sees this risk as less pronounced, although it could of course become an issue with extremely generous programs. The so-called "Welfare Reform Act" of 1996, passed with the backing of then-President Clinton, sought to reduce welfare benefits to non-working individuals. Welfare now includes a work requirement, which many view as problematic, as discussed in Chapter 1. Again, while The Myth and The Reality partition to some degree between Conservatives and Liberals, the Welfare Reform Act provides an example of the ways in which Democrats have also adopted some of the precepts of The Myth.

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[50] See the CBO's "Taxes" page at https://www.cbo.gov/topics/taxes.

[51] See Rick Wartzman (2017), The End of Loyalty: The Rise and Fall of Good Jobs in America. See also Chakrabarti and Fuhrer (2020) in Investing in America's Workforce: Improving Outcomes for Workers and Employers,

Ongoing policy debates. More recent debates about unemployment insurance (UI) in the wake of the COVID-19-induced economic coma reanimate the same arguments—will too much UI make work unattractive compared to receiving benefits? Did employment from 2020 to mid-2021 grow slowly because workers preferred to collect UI rather than work? The latest research suggests this is not the case, and adherents to The Reality generally favored generous UI benefits, but those adhering to The Myth were skeptical. A similar debate surrounds the potential for a "Universal Basic Income" (UBI) provision that would pay all (in the extreme case) or some means-tested (in the more moderate case) a no-questions-asked payment each year. A key concern that The Myth'ers might raise is how people might spend this money? Will it go to luxuries or vices, or to basic necessities? The Reality'ers overall may place more trust in the poor than The Myth'ers. Research on the UBI experiment in Chelsea, Massachusetts—a more targeted rather than a truly "universal" UBI program—suggests that participants in the pilot overwhelmingly spend the money on necessities, such as food and diapers. [52] It's OK to trust poor people to spend money wisely. They are making incredibly hard decisions with their resources every day, in a way that higher-income families never need to worry about.

<u>The two narratives hold some points in common</u>

Adherents to both narratives are likely aware to some extent of many of the outcomes for low-income and minority families. They differ in their assessments of why that has happened, and what to do about it. Likely points of agreement include:

- Hard work still matters in both narratives. There are very few who believe that economic success can or should be attained without individual effort. Whether it is <u>sufficient</u> for success or not is something else.
- Capitalism on the whole can be a great economic system. The alternative—state control of all economic activity—has been shown not to work well in many countries. Across both parties, most agree on this point.[53]
- Related to the previous point, there are obvious advantages to allowing markets and market signals to allocate scarce resources in most circumstances.

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[52] See Liebman *et al* (2021).

[53] A 2020 Gallup poll found that 45% would vote for a qualified socialist for president—"the lowest level of support for any of the groups Gallup examined." Bowman, Karlyn (2021), *Forbes*, July 1.

- In a Pew Research survey conducted in 2019, 61% of those surveyed agreed that there is "too much economic inequality in the country these days."

It is a good sign that the nation largely agrees on that last point. On what to do about it, not so much. Only 42% of all those surveyed said that reducing inequality should be a top priority. But among lower income respondents, 52% considered reducing inequality a top priority. Only 36% of upper income respondents held the same view.[54]

Finally, adherents to both narratives almost surely aspire to live in an economy in which there is equal opportunity to succeed, given effort. They differ on how close we are to that aspiration, and on how or whether we can improve.

How did The Myth Come to Be?

The aspiration to be a land of opportunity likely dates back to the country's founding documents—in which all are entitled to "Life, Liberty and the pursuit of Happiness." Entitlement and opportunity are not the same thing, however. And what happiness means appears to have evolved over the centuries.

Summing Up

My grandfather, Herbert Fuhrer, could well have been one of the stories cited above to support the self-made man element of The Myth. Born in 1906 to a family of quite modest means, he was high-school educated, graduating at age 16, a self-taught engineer who became the President of a pump company in New York. He designed a number of novel pump applications for military and private use , including fuel-handling pumps for oil companies. He received a patent for an articulated invalid bed in 1956. For a variety of reasons, he received no support from his family after the 1930s. He recounted to me stories of some of the difficult pumping tasks which he and his colleagues solved—pumping viscous liquids like toothpaste around factories, for example. He clearly had some natural engineering talent, and I'm quite sure he worked very hard. He did not become a billionaire, but he was well-off, with two houses and a comfortable life.

But despite my close connection to this "rags-to-riches" story, I now find it difficult to see this story as representative of the fate of many people who start off in challenged economic

[54] Pew Research Center (2020a).

circumstances. It simply is not borne out in the data. As alluring as that part of The Myth may be, it is critical that we not use it as a guide to interpreting our country's economic circumstances, nor as a benchmark against which to judge competing economic policies.

I frankly find The Myth, which to a large extent accepts the current economic setup as it exists, dispiriting. To my eye, it simply cannot be right that an economy as affluent as ours in the aggregate leaves so many hopelessly behind, without any real opportunity to succeed. A narrative that accepts that, to any degree, seems cold-hearted. Our country should be at the very least embarrassed by the outcomes detailed in chapter , and we should do more about it. Chapter 6 will discuss what that something might look like.

On the other hand, The Reality makes clear that we have constructed virtually all of this. Somewhat ironically, in the aggregate, our fate is not out of our control, even though for many individuals, it is. It is no small task to right this ship so that we look much more like the land of opportunity we aspire to. But as other countries have shown, and as <u>some</u> of our history suggests, we are capable of it. We abolished slavery. We offered the Marshall Plan to rebuild countries, including our former enemies, in the wake of World War II. We provided tremendous aid to Indonesia after the 2004 tsunami that killed 125,000 within one-half hour and devastated that country and several others. We need now to turn to our own citizens with that same degree of generosity, urgency and humanity.