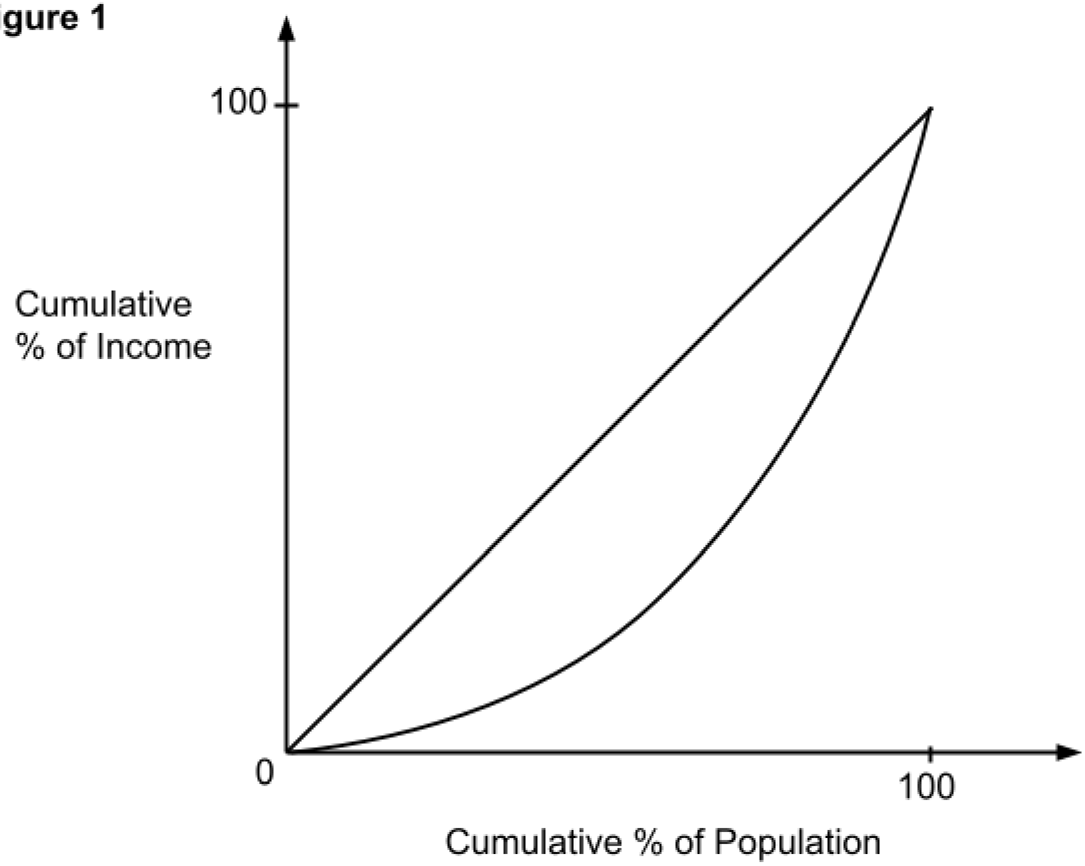
Inequality has been a forever present side effect of capitalism. Janet Yellen, the chairwoman of the Federal Reserve, is worried that the inequality issue is increasing, and that it might be an obstacle in the growth of America's economy. The Federal Reserve is America's central bank; central banks control the nation's money supply through monetary policy.

The graph in Figure 1 shows an approximate of the Lorenz Curve for America. The line of absolute equality shows everyone in the population earning the same income. The curved line, however, demonstrates the reality in which a smaller percentage of the population earns most of the money. The warning issued by Yellen suggests that the Lorenz Curve is going to get further away from the line of absolute equality.

Figure 1



The gini coefficient is the space between the line of absolute equality and the Lorenz Curve. Janet Yellen wants to attempt to decrease that by focusing on four areas: raising children, access to education, inheritance, and small business ownerships. By providing more goods and services to the public, the gap between the wealthy and the poor can be decreased.

Focusing on access to education would also help improve the unemployment rate. Structural unemployment, or the type of unemployment where people do not have a job because their skills are not needed in the economy, would decrease if more people had access to education. Frictional unemployment would also decrease, as frictional unemployment occurs when people are looking for jobs that require higher education.

Figure 2

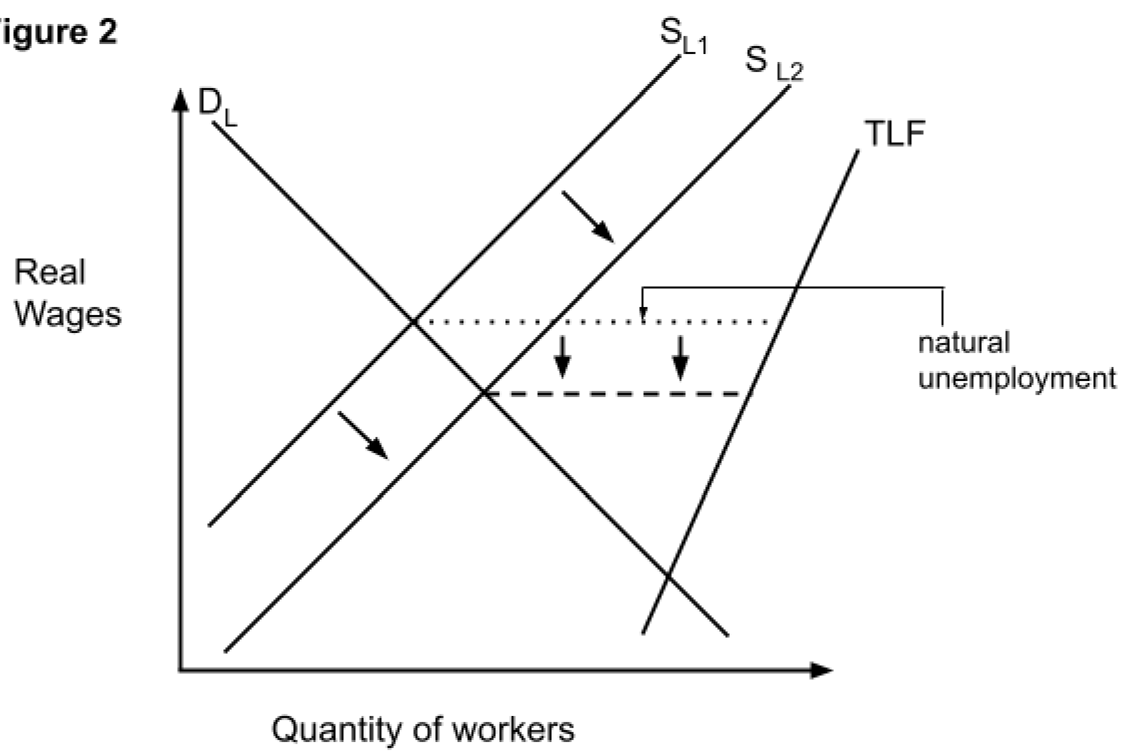


Figure 2 demonstrates the mismatch between the total labor force (TLF) and the demand of labor (D_L). As shown by the gap, which is natural unemployment, many potential workers are unemployed and not earning money. By decreasing the unemployment rate, the supply of labor is increased and shifts to the right from S_{L1} to S_{L2}. The percentage of income earned by a certain percentage of the population increases, helping decrease the inequality between the wealthy and the poor.

The inequality issue could also be addressed through more progressive taxation, which aims to reduce the inequality gap as opposed to regressive taxation, which would reduce the inequality gap. For example, sales taxes charge the same amount to everyone, taking a larger percentage of money from poor than wealthy, therefore increasing inequality. However, taxes like luxury taxes are progressive since they attempt to charge the wealthy only. A larger problem, perhaps, is tax evasion. Wealthy people have mastered techniques for tax evasion and enforcing better laws to ensure that this is less of a problem would be a larger part to the solution for the problem of increasing inequality.

Another way to decrease inequality is through transfer payments, which transfer money from the wealthy to the poor. Transfer payments, although balancing the spread of money, make earning money without doing work easy for people. Automatic stabilizers such as welfare, unemployment payments, and food stamps are government programs that could also play a role in decreasing inequality. However, both of these could become disincentives for people to work because they would receive money anyway.

A certain amount of inequality is necessary to the structure of the nation's economy. Inequality serves as an incentive for others to do better so that they can attain a higher standing in America's economy. Without inequality, people might not see the benefit in working hard and the economy would suffer from the lack of motivation of people.

The inequality issue could be left unaddressed. The wealthy are already paying taxes, and they buy more expensive goods with their money, putting it back into the system by consuming. However, tax evasion is a complication and wealthy people do not spend all of their money, often investing it elsewhere, or saving it. The inequality in America is alarming and needs to be addressed for the economy to advance. The working class is more likely to spend their money than the wealthy. For example, although a person may have more money, the person will still buy only one toothbrush and have money left unspent; other people may not have enough money to buy a toothbrush. Therefore, money that the working class could be spending is left unspent in the hands of the wealthy. Reducing unemployment would take care of the unused labor, and whenever there is unused labor, the economy is not working at the highest possible efficiency. For the economy to advance, inequality must be reduced through government programs for education, taxes or transfer payments.