US rich get richer on stock market investments while modest investors are left behind

June 26 2014

In a new study, researchers from Imperial College Business School, Columbia University and the University of Maryland found that wealthy individuals in the US can get in relative terms up to 70 per cent times greater returns on their investments than those with modest wealth, when the yields on assets such as stocks and bonds are calculated. The team say that this further widens the income gap between rich and poor and potentially creates disparities in society.

Income inequality in the US has been steadily rising. According to a report by Oxfam International released earlier this year, the wealthiest one per cent has captured 95 per cent of post-financial crisis growth since 2009, while the bottom 90 per cent became poorer in the US.

The research is the first to offer a consistent explanation of income inequality generated from financial markets.

In particular, the team suggest that rich investors have better access to resources and advice from professionals such as asset managers. This enables them to better determine where to invest their money on the stock exchange. In contrast, investors with a modest income are unable to afford the same access to information and expertise and they're also wary of being exploited by rich investors. This means that they're less likely to invest in riskier stocks and bonds that could provide them with a higher return on investments.

Professor Marcin Kacperczyk, co-author of the report from Imperial College Business School, said:

"Understanding how income from stock market activity can add to income inequality is something that has never been fully explored by economists before. Our research shows that some wealthy individuals are making substantial profits on stock markets because they have tools at their disposal that individuals from modest incomes don't. This further creates a widening income gap between rich and poor, which is bad for society, making it difficult to have equality of opportunity. "

Typically, economists have focused on inequality originating in labour markets by calculating the difference between the highest and lowest salaries of workers in the US. They also measure income inequality by determining the value of a range of different assets held by workers including homes, automobiles, personal valuables, businesses, savings and investments such as art and wine.

In the study, the researchers determine income inequality in the US, using data from Thomson Reuters that measured the income investors received from their stock market activity. They used this calculation to measure the income inequality between those from higher and lower wealth backgrounds.

In the future, the team aim to use the formula to shed more light on income inequality in the UK.

Provided by Imperial College London