Redistribution and Social Preferences: Explaining Trends in Inequality

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Abstract

Since the mid 1990s, we have observed an interesting trend in many advanced economies: despite rising income inequality over the past three decades, government redistribution has either stagnated or declined. Traditional political economy models, such as Meltzer and Richard (1981), would predict increased redistribution in response to growing inequality. However, empirical data show that more unequal countries often redistribute less. I propose a novel explanation grounded in the political economy of skill-biased technological change (SBTC), whereby high-skilled individuals—who disproportionately benefit from automation—acquire greater political influence and shape redistributive policies in their favor.

To formalize this mechanism, I develop a stylized general equilibrium model where automation replaces routine labor and amplifies wage inequality. A centralized planner sets the progressivity of the tax system to finance government spending, but political weights in the planner's objective function are endogenous and proportional to group income shares. As automation deepens, high-skilled workers' income rises, increasing their political weight. This shift leads to a lower optimal progressivity level, as pre-tax inequality increases. The model's calibration and simulation exercises confirm that greater automation results in reduced redistribution, providing a theoretical explanation for the empirical redistribution-inequality disconnect.

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1 Introduction

Over the past three decades, advanced economies have experienced two parallel and seemingly contradictory trends. On the one hand, income inequality has been steadily increasing. This phenomenon has been documented extensively by the OECD OECD (2011, 2015, 2016, 2020), which highlights that the income gap between high and low-skilled workers has widened substantially in most developed countries since the early 1990s. On the other hand, contrary to the standard predictions of political economy theory, the level of government redistribution, through taxes and social transfers, has not risen in tandem. In fact, OECD data from 2017 show that redistribution has either stagnated or declined across many member countries since the mid-1990s.

This pattern is surprising when considered through the lens of classical political economy models such as those proposed by Meltzer & Richard (1981) and Benabou (2002). These models predict that rising inequality should result in increased political pressure for redistribution, as the median voter becomes relatively poorer and therefore more likely to support redistributive policies. Under the assumption of universal suffrage and equal political representation, greater inequality should translate into a stronger electoral demand for redistribution, leading to more progressive taxation and expanded transfer programs.

Table 1: Correlation with Market Inequality

Variable	**Correlation with Market Inequality**
Tax Progressivity	-0.2012
Social Security Transfers	-0.1608
Private Transfers	-0.0907
Employment Transfers	-0.1415

However, empirical evidence contradicts this prediction. Cross-country comparisons indicate that countries with higher levels of income inequality often implement less redistribution, not more. Furthermore, recent survey data from the OECD's "Risk That Matters" project reveal that demand for redistribution—measured as the proportion of people who believe the government should do more to redistribute income—is frequently higher in countries where actual redistribution is lower. There appears to be a genuine rise in public demand for increased redistribution as inequality reaches high levels; however, this demand often fails to translate into effective policy action. This paradox motivates the central research question of this thesis: why has redistribution declined or remained stagnant in many advanced economies despite the rise in income inequality?

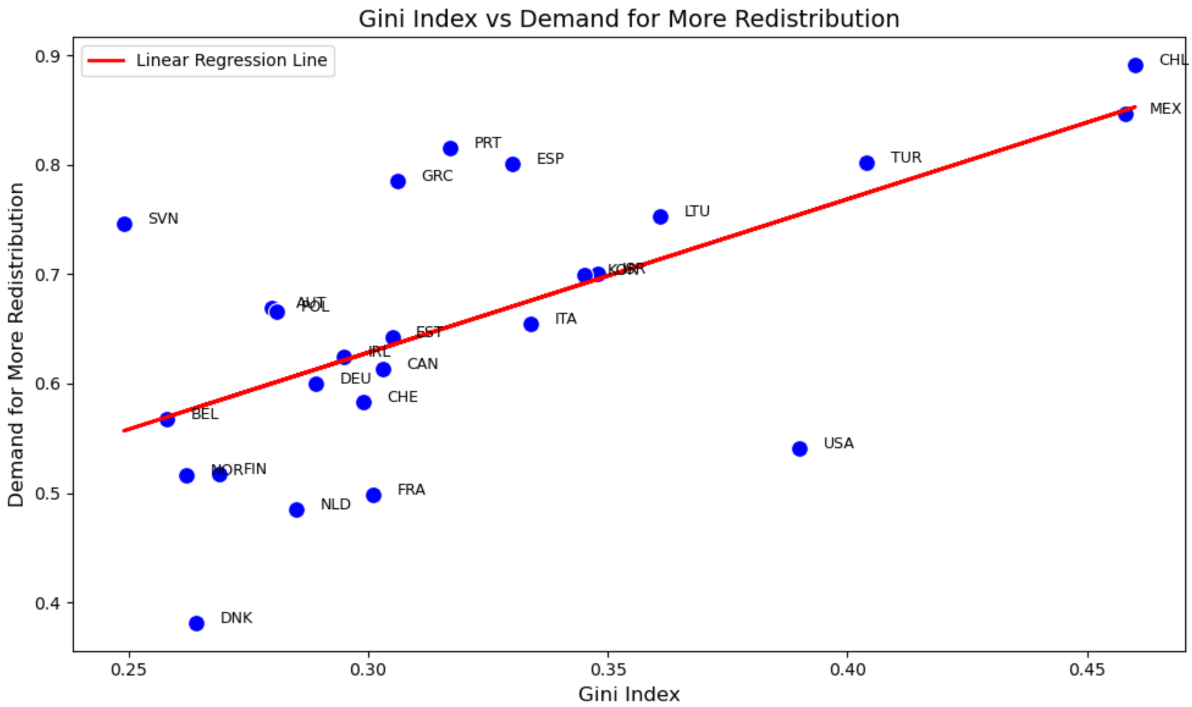

Figure 1: Demand for redistribution is defined as the proportion of people that answered "more" or "much more" to question: "Do you think the government should implement more/about the same/less redistribution?"

To address this puzzle, I propose a theoretical explanation grounded in the political economy of technological change. In particular, I focus on the role of skill-biased technological change (SBTC), which has been identified as one of the key drivers of inequality in recent decades. As documented by Acemoglu & Restrepo (2019) and **?** (among the others) in many influential papers, SBTC has led to the automation and routinization of tasks formerly performed by medium-skilled workers, thereby displacing them into lower-paid jobs while simultaneously enhancing the productivity and wages of high-skilled workers. The net result has been an increase in the wage gap between routine and non-routine workers and a growing concentration of income in high-skilled sectors. Moreover, the displacement of medium-skilled workers into lower-skilled and lower-paid sectors due to technological change has effectively shifted the median voter further down the income distribution. This shift, in theory, should strengthen electoral support for redistributive policies.

Standard economic reasoning would suggest that this rise in market inequality should increase the political demand for redistribution. However, I argue that SBTC also alters the political landscape by changing the distribution of political influence. As high-skilled workers accumulate a larger share of income, they gain disproportionate influence over policy-making—either through higher political participation, greater lobbying power, or more compact and effective political organization. All these facts are well documented in recent elections and political landscape in the US. Consequently, the political weights in the social welfare function used by policy-makers become increasingly tilted in favor of the rich. Redistribution, therefore, becomes a function not only of inequality but also of the political power structure.

To formalize this mechanism, I develop a stylized general equilibrium model in which automation replaces routine labor and raises inequality. A centralized planner chooses the optimal level of tax progressivity to finance a fixed level of government spending. However, unlike classical models where each citizen counts equally, I assume that the planner's objective function assigns political weights that are endogenous and proportional to each group's income. As automation intensifies and high-skilled incomes rise, so does their political influence, leading to lower levels of redistribution—even as inequality increases.

The model provides a theoretical framework that can reconcile the empirical disconnect between inequality and redistribution. It highlights that the relationship between economic and political inequality is endogenous and mutually reinforcing. Moreover, it underscores the importance of understanding how technological change shapes not only labor market outcomes but also the political process itself.

2 SBTC and its role in shaping inequality

Skill-biased technological change (SBTC) has emerged as one of the leading explanations for the rise in wage inequality and labor market polarization observed in advanced economies since the 1980s. In their seminal survey, Acemoglu & Autor (2011) provide a comprehensive framework linking technological advances to changes in the relative demand for skills. SBTC refers to technological progress that disproportionately enhances the productivity of high-skilled workers relative to low- and medium-skilled workers, thereby increasing the wage premium on skills.

Historically, technological improvements have always influenced the labor market by altering the demand for various types of skills. What distinguishes SBTC is the particular nature of recent innovations—especially the introduction and diffusion of information and communication technologies (ICT)—which automate routine tasks primarily performed by middle-skill workers, such as clerical and manufacturing jobs, while complementing non-routine cognitive and manual tasks typically done by high-skilled workers. This dynamic has led to a hollowing out of middle-skill employment and a marked increase in wage dispersion across skill groups Autor et al. (2003).

A key contribution of the SBTC literature is the task-based framework introduced by Autor et al. (2003) and extended by Acemoglu & Autor (2011). Rather than classifying workers solely by formal education or occupation, this approach emphasizes the nature of the tasks performed on the job. Technological change affects labor demand not just by skill level, but by the routine or non-routine content of tasks:

- **Routine tasks**—tasks that follow explicit rules and procedures and are thus easily codifiable—are increasingly subject to automation.
- **Non-routine tasks**—which require problem-solving, creativity, and interpersonal skills—are complemented by new technologies and hence see increased labor demand.

This task-based model explains labor market polarization: middle-skill, routine-intensive jobs decline, while both low-skill manual jobs and high-skill cognitive jobs grow. The result is a U-shaped employment distribution with expanded low and high-wage job categories and a shrinking middle class, with a disproportional increase of low-skilled workers overall.

Mathematically, if we denote labor input by type $i \in \{\text{low}, \text{middle}, \text{high}\}$ with associated productivity A_i affected by technology, and wages w_i reflecting marginal productivity, the evolving technology induces a relative increase in A_{high} compared to A_{middle} and A_{low}. The wage premium for high-skilled workers then grows as

$$\frac{w_{\text{high}}}{w_{\text{middle}}} \approx \frac{A_{\text{high}}}{A_{\text{middle}}} \uparrow,$$

consistent with empirical wage data since the 1990s.

2.1 Empirical Evidence on SBTC and Inequality

The empirical literature robustly documents the rise of wage inequality attributable to SBTC across OECD countries. For example, Autor & Dorn (2013) show that routine-task automation explains a significant share of the decline in middle-skill employment in the United States. OECD reports OECD (2015, 2020) confirm a widening skill premium and growing income gaps correlated with the pace of technological adoption. The wage premium for college-educated workers relative to high school graduates rose substantially between 1980 and 2000, reflecting the strong demand for skilled labor in the US. According to Autor & Dorn (2013), the college–high school wage gap increased from approximately 30 percent in 1980 to over 50 percent by 2000, stabilizing around that level through 2020.

While SBTC is widely accepted as a fundamental driver of rising economic inequality, its political economy implications have received comparatively less attention. In the context of this thesis, SBTC offers a crucial link between technological progress and the puzzling divergence between rising inequality and stagnant or declining redistribution.

The key insight is that SBTC not only reshapes the distribution of income but also alters the political landscape by changing the relative economic power of different skill groups. As high-skilled workers accrue greater income shares due to skill-biased automa-

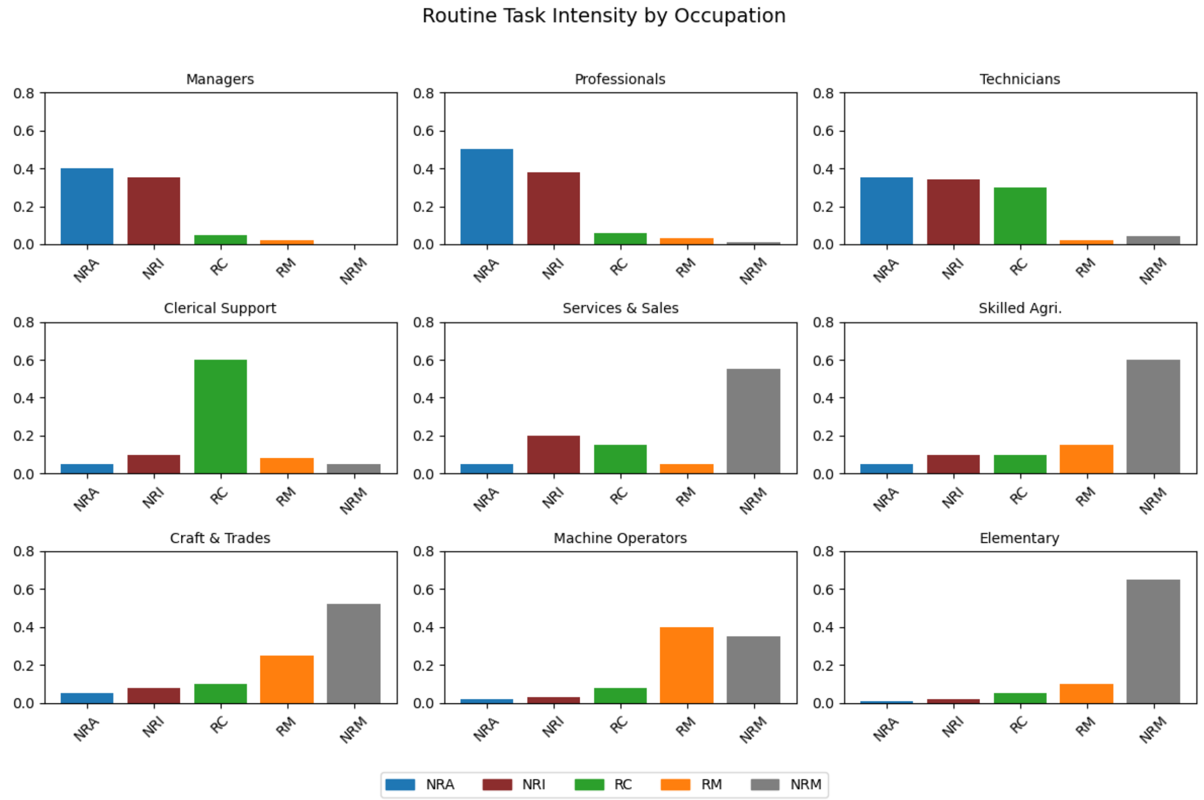

Figure 2: Task composition of different occupations.

tion, they also tend to increase their political influence through mechanisms such as higher voter turnout, greater lobbying capacity, and stronger representation in policy-making arenas through political campaign contributions. This amplification of political weight reinforces the preferences of the wealthy for lower redistribution and limited tax progressivity.

Formally, suppose a social planner maximizes a weighted social welfare function:

$$W = \sum_i \alpha_i U(c_i),$$

where c_i is consumption of group i, $U(\cdot)$ is a concave utility function reflecting diminishing marginal utility of consumption, and α_i is the political weight of group i. In classical models, α_i are equal across individuals, reflecting equal political representation. However, under SBTC-driven income shifts,

$$\alpha_i = \frac{Y_i}{\sum_j Y_j},$$

where Y_i is income of group i. As automation boosts Y_{high}, the planner's objective becomes skewed towards high-income groups, reducing the incentive to implement progressive redistribution despite rising income inequality.

In this thesis, the skill-biased technical change (SBTC) mechanism is embedded within a stylized general equilibrium model of taxation and redistribution. The model captures the key labor market consequences of technological change, particularly the displacement of routine tasks through automation and the resulting increase in wage dispersion. As high-skilled workers benefit disproportionately, their rising income shares translate into greater political influence, which is endogenously determined within the framework. This shift in political power affects the choice of tax progressivity, which is no longer driven solely by equity-efficiency trade-offs but is also constrained by the political preferences of those who gain from technological change.

This modeling approach reflects recent theoretical developments and provides a micro-founded explanation for the empirical puzzle introduced in the introduction: why increasing inequality has not been met with a corresponding rise in redistribution. By linking structural economic shifts to political realignments, the SBTC framework offers a compelling narrative in which the redistributional capacity of democratic institutions is increasingly shaped by the very forces that drive inequality. The following chapters develop this logic formally and explore the resulting policy implications in greater detail.

2.2 Technological Change and the Political Economy of Redistribution

A central argument of this thesis is that technological change does not only reshape the economic structure—it also transforms the political dynamics underlying redistribution. While past episodes of technological advancement, such as the Industrial Revolution, generated enormous shifts in labor markets and production, they did so within a markedly different institutional and political context. The present wave of skill-biased technical change (SBTC), driven by digital innovation and automation, has introduced a new layer of conflict over redistribution that is more deeply embedded in democratic political institutions and shaped by the concentration of technological power Acemoglu & Restrepo (2019); Korinek & Stiglitz (2021).

Unlike in the 19th century, when political influence was largely the preserve of elites by design—through limited suffrage and institutional exclusion—contemporary democracies formally grant equal political rights to all adult citizens. However, the move from elite to mass suffrage has not eliminated the capacity of economic elites to shape policy outcomes. Instead, it has redefined the mechanisms through which influence is exercised. In today's political economy, those who benefit disproportionately from technological progress—particularly high-skilled individuals and capital owners in leading technology sectors—can exert influence through campaign financing, lobbying, and control over key information channels Gilens & Page (2014); Zingales (2017). Political power is thus no longer allocated solely by legal privilege, but increasingly purchased through economic means. The implication is that redistribution becomes not just a matter of social preference or economic constraint, but also a function of how power is acquired and deployed within a democratic framework.

At the same time, the nature of contemporary growth further deepens the redistributional tension. While the Industrial Revolution was associated with broad-based increases in productivity and rising living standards over time, the recent trajectory of growth in advanced economies has been more uneven Piketty (2014); Gordon (2016). In many cases, real wage growth for the median worker has stagnated despite ongoing technological progress. This divergence between innovation and inclusion has intensified distributional conflict, as the gains from technological change accrue narrowly to a subset of the population. When economic growth no longer lifts all boats, the political stakes of redistribution become sharper, and the ability of winners to resist compensatory policies grows more consequential.

Finally, a distinctive feature of modern technological change is the degree of centralization in its production and diffusion. Innovation today is disproportionately driven by a small number of large firms—primarily in the digital and information sectors—that hold both the financial resources and technical capacity to shape the direction of technological progress ?Zuboff (2019). These firms often prioritize labor-replacing innovations, such as artificial intelligence and robotics, which substitute for routine and even non-routine human tasks. In contrast to earlier waves of mechanization that frequently complemented human labor (e.g., in manufacturing or transportation), the current trend is toward automation that displaces it Brynjolfsson & McAfee (2014). This focus on labor-substitution rather than labor-augmentation has not only economic but also political consequences: it reduces the bargaining power of workers and weakens the societal coalition that might otherwise demand redistribution.

In sum, the present technological era differs fundamentally from past episodes in how it redistributes both economic gains and political influence. The democratic context requires greater "effort" from elites to shape policy outcomes, yet the tools to do so—wealth, lobbying power, control over platforms—are increasingly effective. Meanwhile, the stagnation of inclusive growth and the labor-displacing character of dominant innovations amplify the social pressures for redistribution even as they reduce the political feasibility of delivering it. This dynamic tension lies at the heart of the analysis that follows.

3 The Model

3.1 Overview

This section presents a stylized general equilibrium model designed to study the political economy of redistribution in an economy affected by automation. The model consists of a representative firm, a government that redistributes income through taxation, and two types of heterogeneous households distinguished by their comparative advantage in performing either routine or non-routine tasks. Technological change—specifically, automation—endogenously alters the distribution of income, which in turn influences political power and the optimal degree of redistribution chosen by a social planner. The key departure from standard utilitarian frameworks is the assumption that political weights in the social welfare function are proportional to income shares, thereby endogenizing political influence.

3.2 Production Sector

We consider a representative firm that produces output using three inputs: non-routine labor (NR), routine labor (R), and automation capital (x). The firm operates under perfect competition, taking input prices as given, and chooses input levels to maximize profits. The production function exhibits constant returns to scale and is given by:

$$Y = NR^{\alpha}(R + x)^{1-\alpha},$$

where $0 < \alpha < 1$ determines the output elasticity of non-routine labor, while routine labor and automation capital are perfect substitutes in production. This assumption captures the idea that routine tasks can be performed either by human workers or by machines.

The firm's profit maximization problem is:

$$\max_{NR,R,x} \ \Pi = NR^{\alpha}(R + x)^{1-\alpha} - w_{NR} \cdot NR - w_R \cdot R - \theta x,$$

where w_{NR} and w_R are the wages paid to non-routine and routine workers, respectively, and θ is the per-unit cost of automation capital.

Under perfect competition, firms make zero profits in equilibrium, and the price of each input equals its marginal productivity. We derive the first-order conditions for each input as follows:

For non-routine labor:

$$\frac{\partial \Pi}{\partial NR} = \alpha NR^{\alpha-1}(R + x)^{1-\alpha} - w_{NR} = 0 \quad \Rightarrow \quad w_{NR} = \alpha \cdot \frac{Y}{NR}.$$

For routine labor:

$$\frac{\partial \Pi}{\partial R} = (1 - \alpha)NR^{\alpha}(R + x)^{-\alpha} - w_R = 0 \quad \Rightarrow \quad w_R = (1 - \alpha) \cdot \frac{Y}{R + x}.$$

For automation capital:

$$\frac{\partial \Pi}{\partial x} = (1-\alpha) N R^{\alpha} (R+x)^{-\alpha} - \theta = 0 \quad \Rightarrow \quad \theta = (1-\alpha) \cdot \frac{Y}{R+x}.$$

The first-order conditions for R and x yield an important implication. Specifically, they imply:

$$w_R = \theta.$$

That is, the wage paid to routine workers equals the cost of automation per unit. This equality reflects a central implication of perfect competition in a setting where routine labor and automation are perfect substitutes: the firm is indifferent at the margin between employing a human worker or installing a machine to perform the same task. If, for example, the cost of automation θ were to fall below w_R, the firm would replace routine workers with machines until the equality is restored. Conversely, if $w_R < \theta$, firms would prefer employing human workers for routine tasks.

This mechanism highlights how technological progress, by reducing the cost of automation θ, can depress the demand for routine labor and ultimately reduce routine wages. In equilibrium, the routine wage is pinned down not by bargaining or policy but by the cost of its closest technological substitute.

Meanwhile, the wage of non-routine workers is:

$$w_{NR} = \alpha \cdot \frac{Y}{NR},$$

which is increasing in output and decreasing in the supply of non-routine labor. Unlike routine workers, non-routine workers do not compete directly with automation. Their wage is determined by their marginal productivity, which remains protected as long as their tasks are not replicable by machines.

We define wage inequality as the ratio of the wage of non-routine labor to that of routine labor. From the first-order conditions and the equilibrium relationships, we can write:

$$w_{NR} = \alpha \cdot \frac{Y}{NR}, \quad w_R = (1 - \alpha) \cdot \frac{Y}{R + x} = \theta.$$

Combining these, we obtain:

$$\frac{w_{NR}}{w_R} = \frac{\alpha \cdot \frac{Y}{NR}}{(1 - \alpha) \cdot \frac{Y}{R+x}} = \frac{\alpha}{1 - \alpha} \cdot \frac{R + x}{NR}.$$

Thus, wage inequality depends positively on the intensity of routine tasks (whether performed by humans or machines) relative to non-routine labor.

This expression has intuitive economic implications:

- A decline in θ, the cost of automation, increases the firm's use of x to replace routine labor. This raises x, and hence $R + x$, increasing the numerator of the inequality ratio. Since NR is unchanged in the short run, inequality rises.
- If the supply of non-routine labor NR falls, then, holding everything else constant, w_{NR} rises due to scarcity, and the inequality ratio increases.
- An increase in the productivity of capital or automation (e.g., via a fall in θ or higher x) causes routine labor to be replaced more rapidly. This compresses w_R toward θ, and the gap between w_{NR} and w_R widens.

This model provides a clear prediction: wage inequality increases when automation becomes cheaper, i.e., when θ falls. This happens because routine labor is a direct substitute for capital, while non-routine labor is complementary. As a result, technological change that favors automation boosts the relative productivity and remuneration of non-routine tasks.

This theoretical framework suggests that unless non-routine labor supply expands, through training or education, technological progress in the form of cheaper automation will increase inequality.

3.2.1 Feasibility and Full Employment Conditions

The economy's resource feasibility constraint requires that total demand for consumption goods, public spending, and the cost of automation investment must not exceed the total output produced by firms. Formally, this is expressed as:

$$\sum_i m_i c_i + G + \theta x \leq NR^{\alpha}(R + x)^{1-\alpha},$$

where m_i denotes the mass of agents with skill type i, c_i is their individual consumption, G is the fixed level of government spending, θ is the unit cost of automation, and x represents the automation input. The right-hand side corresponds to aggregate output produced by the firm using a Cobb-Douglas technology that combines non-routine labor NR and the sum of routine labor R and automation x as inputs.

This constraint ensures that the economy's total resource use—private consumption, government expenditure, and automation investment—cannot exceed the output available, thereby imposing a fundamental balance between production and aggregate demand.

The full employment condition requires that labor markets clear for both non-routine and routine labor types. Assuming all individuals within each group are identical, the total labor input L_i demanded by firms must equal the aggregate labor supply of that group:

$$L_i = m_i h_i, \quad \text{for } i \in \{NR, R\},$$

where h_i denotes the uniform labor supply decision made by each individual of skill type i, and m_i is the number of such individuals. This condition ensures that the total labor supplied by agents in each skill group exactly matches the labor demanded by firms, guaranteeing full employment within the economy.

3.3 Government Sector

The government finances a fixed amount of public expenditure, denoted by G, entirely through labor income taxation. To capture real-world features of tax systems, we assume that the tax schedule is nonlinear and parameterized by two key parameters: $\lambda \in [0, 1]$ and $\gamma \leq 1$. The tax function applied to individual labor income y_i is given by:

$$T(y_i) = y_i - \lambda y_i^{1-\gamma}.$$

This formulation implies that each individual pays taxes equal to their income minus a function that depends on both income and the parameters λ and γ. Several points are worth noting about this tax function:

- When $\gamma = 0$, the tax becomes linear: $T(y_i) = (1 - \lambda)y_i$, which corresponds to a flat tax rate of $1 - \lambda$.
- As γ increases, the tax schedule becomes more progressive. That is, higher-income individuals pay a larger fraction of their income in taxes. The marginal tax rate, given by $T'(y_i) = 1 - \lambda(1 - \gamma)y_i^{-\gamma}$, increases in income when $\gamma > 0$.
- For values of $\gamma < 0$, the tax becomes regressive, with marginal tax rates decreasing in income—a case generally not pursued in realistic policy modeling.

This tax specification has been widely adopted in the macroeconomics and public finance literature because of its tractability and its ability to closely match empirical tax and transfer systems. Notably, it has been used in quantitative heterogeneous-agent models, such as those in Benabou (2002), Heathcote et al. (2017), and **?**, to study the effects of taxation on labor supply, income inequality, and redistribution. The advantage of this specification is that it allows for flexible calibration of both the average and marginal tax rates across the income distribution with just two parameters.

The parameter λ primarily governs the average tax burden: higher values of λ correspond to lower average taxes (i.e., higher post-tax incomes). Importantly, λ is adjusted endogenously to ensure that the government satisfies its balanced-budget condition in every period:

$$\sum_i T(y_i) = G.$$

This constraint implies that total tax revenue collected from households must exactly cover the government's exogenous public spending G. In equilibrium, λ is solved for such that this identity holds, given the distribution of pre-tax incomes $\{y_i\}$.

This formulation ensures internal consistency between the tax structure and government financing, and allows for straightforward comparative statics regarding the effects of changing progressivity (through γ) on labor supply, redistribution, and inequality.

Importantly, the public spending G is treated as exogenous and does not directly enter the utility function of households, nor is it redistributed back to them in the form of transfers or public goods. In this sense, the government is modeled as a revenue-absorbing agent: it collects taxes and spends the resources in a way that does not affect private agents' utility or budget constraints. One can think of G as a metaphorical "money-burning" activity—resources are taxed away from households and disappear from the private economy.

Of course, one could enrich the model by allowing G to fund public goods or provide utility-enhancing transfers. However, as long as such goods or transfers are uniform and non-rival, the qualitative results of the model would be largely unchanged. The simplifying assumption of treating G as utility-irrelevant enables us to isolate the effects of taxation on labor supply and income inequality without conflating them with indirect benefits from government services.

3.4 Households

The economy is populated by a continuum of households indexed by their comparative advantage in either routine or non-routine work. Each household supplies labor h_i inelastically in the labor market at a wage w_i and earns income $y_i = w_i h_i$. After taxes, disposable income is given by

$$c_i = y_i - T(y_i) = \lambda y_i^{1-\gamma}.$$

Households derive utility from consumption and suffer disutility from labor. Preferences are given by

$$U_i = \ln(c_i) - \chi \frac{h_i^{1+\frac{1}{\phi}}}{1+\frac{1}{\phi}},$$

where $\chi > 0$ governs the intensity of labor disutility, and $\phi > 0$ denotes the Frisch elasticity of labor supply.

Each household chooses labor supply to maximize utility, taking wages and taxes as given:

$$\max_{h_i} \left\{ \ln\left(\lambda (w_i h_i)^{1-\gamma}\right) - \chi \frac{h_i^{1+\frac{1}{\phi}}}{1+\frac{1}{\phi}} \right\}.$$

The first-order condition for optimal labor supply yields:

$$h_i^* = \left(\frac{1-\gamma}{\chi}\right)^{\frac{\phi}{1+\phi}}.$$

A striking feature of this expression is that the optimal labor supply h_i^* does not depend on the wage w_i. This result emerges due to the specific functional forms assumed for preferences. In particular, the utility function is logarithmic in consumption, $u(c) = \log c$, which implies a unitary income elasticity of consumption demand. At the same time, disutility from labor takes the constant elasticity of substitution (CES) form, $v(h) = \chi \frac{h_i^{1+\frac{1}{\phi}}}{1+\frac{1}{\phi}}$, where ϕ denotes the Frisch elasticity of labor supply.

Under these conditions, the income and substitution effects of a change in the wage exactly offset each other in the labor-leisure choice. An increase in the wage raises the marginal benefit of working (substitution effect), but it also increases income and thus the demand for leisure (income effect). Because of the log utility, these two forces are exactly balanced, leading to a labor supply decision that is entirely independent of the wage. Instead, h_i^* depends only on parameters capturing tax progressivity (γ), labor preferences (χ), and the Frisch elasticity (ϕ). This functional form greatly simplifies the aggregation of individual decisions and ensures that both groups of households with different level of skills react equally with a change of tax parameters.

Substituting back, the disposable income of household i becomes:

$$\tilde{y}_i = \lambda w_i^{1-\gamma} \left(\frac{1-\gamma}{\chi} \right)^{\frac{\phi(1-\gamma)}{1+\phi}} .$$

Note that disposable income depends on wages, tax progressivity, and preferences. For a given γ, higher-wage households retain a larger share of their income. Conversely, a rise in γ compresses post-tax income inequality but also reduces total labor supply and thus output.

Given a choice of γ, one can solve for the value of λ that satisfies the government's budget constraint in equilibrium. For instance, using the analytical form of labor supply and wage income derived earlier, the value of λ that ensures balanced public finances is:

$$\lambda^* = \left(\frac{1-\gamma}{\chi} \right)^{\frac{\phi\gamma}{1+\phi}} w_i^{\gamma} - G \left(\frac{1-\gamma}{\chi} \right)^{\frac{\phi(1-\gamma)}{1+\phi}} w_i^{\gamma-1}.$$

This expression makes clear that λ adjusts to ensure the tax revenues exactly match the fixed level of public spending G for any given level of progressivity γ.

An important modeling insight concerns the distinct roles of the parameters λ and γ. In this framework, γ is interpreted as a political choice variable. It captures society's preference over the degree of redistribution: higher values of γ imply stronger redistribution through a more progressive tax system, which benefits low-income households at the cost of higher distortions to labor supply.

In contrast, λ serves only a technical role—it adjusts mechanically to ensure that the government's budget constraint is satisfied for a given level of γ and economic fundamentals such as G, wages, and preferences. Therefore, the relevant optimization problem for a benevolent planner or political process is to choose the degree of progressivity γ that maximizes a social welfare function (SWF), while λ is determined residually to balance the government budget:

$$\begin{aligned} \max_{\gamma} \quad & \text{SWF}(\gamma), \\ \text{s.t.} \quad & \sum_i T(y_i; \lambda(\gamma), \gamma) = G. \end{aligned}$$

This decomposition allows us to focus on the normative implications of different progressivity levels without worrying about feasibility, since the model ensures that any γ is implementable via a corresponding λ.

3.5 Planner's Problem

The central feature of the model lies in the structure of the planner's objective function. Departing from a purely utilitarian benchmark that assigns equal welfare weights to all individuals, we consider a politically constrained planner whose preferences reflect the relative economic influence of different social groups. This formulation captures the empirical reality that political decisions are often shaped not only by equity concerns, but also by the lobbying power, campaign financing, and mobilization capacity of economically dominant constituencies.

Formally, the planner maximizes a weighted social welfare function (SWF) of the form:

$$SWF = \omega_{NR} U_{NR} + \omega_R U_R,$$

where U_i denotes the indirect utility of an agent of type $i \in \{NR, R\}$, and the political weights ω_i are endogenously determined as:

$$\omega_{NR} = \frac{m_{NR} y_{NR}}{m_{NR} y_{NR} + m_R y_R}, \quad \omega_R = \frac{m_R y_R}{m_{NR} y_{NR} + m_R y_R}.$$

Here, m_i denotes the mass (or measure) of individuals of type i, and y_i is their individual labor income. As a result, the political weight assigned to each group is proportional to its total income, reflecting a reduced-form approach to modeling political power through economic resources. This specification embodies the idea that groups with greater aggregate income wield more influence over redistributive policy.

The planner selects the progressivity parameter γ in the tax schedule—recall $T(y_i) = y_i - \lambda y_i^{1-\gamma}$—to maximize the politically weighted SWF, taking into account both individual responses to taxation and the government's balanced budget constraint. Since the tax schedule is fully characterized by the pair (λ, γ), and λ adjusts endogenously to balance the budget for any choice of γ, the planner's problem can be written as:

$$\max_{\gamma} \sum_{i \in \{NR, R\}} \omega_i \cdot U_i(\lambda(\gamma), \gamma, w_i),$$

where each individual's utility is given by:

$$U_i = \ln(\lambda) + (1-\gamma)\ln(w_i) + \frac{\phi(1-\gamma)}{1+\phi}\ln\left(\frac{1-\gamma}{\chi}\right) - \frac{1-\gamma}{1+\frac{1}{\phi}}.$$

A crucial insight of the model is that political weights ω_i are endogenous and depend directly on each group's aggregate income. As automation progresses, it tends to raise the income of non-routine workers while lowering that of routine workers—either by reducing their wages or substituting them entirely. This shift in income distribution mechanically increases ω_{NR} and decreases ω_R, transferring political influence toward the richer, non-routine group.

This creates a powerful feedback loop between inequality and redistribution: as automation increases inequality, it also reduces the political demand for redistribution by changing the composition of political power. In particular, because the richer group tends to prefer lower values of γ, reflecting less redistribution, rising automation leads to a lower equilibrium choice of γ.

Thus, even if the social welfare function allows for redistribution in principle, the endogeneity of political weights implies that rising inequality can itself constrain redistributive policy. This political channel distinguishes our framework from standard optimal taxation models, where redistribution is mechanically increased in response to rising inequality.

3.6 Technological Change in the Model

Consider a decline in the cost of automation, captured by a reduction in the parameter θ. As automation becomes cheaper, firms optimally substitute routine labor with capital, leading to an increase in the level of automation x. This substitution reduces the demand for routine workers, thereby depressing their wages and employment prospects. In contrast, non-routine workers—whose tasks are complementary to automation—experience rising relative wages and labor demand.

At the aggregate level, this technological shock leads to a rise in market income inequality. However, contrary to the predictions of the classical median voter framework—where rising inequality typically strengthens the political demand for redistribution—the opposite occurs in our setting. Because political weights are tied to income shares, the income gains of non-routine workers translate directly into greater political influence. Formally, their political weight ω_{NR} increases relative to that of routine workers.

Given that non-routine workers are richer and thus have lower marginal utility from redistributive transfers, their increased influence shifts the planner's preferences toward policies favoring less redistribution. As a result, the planner endogenously chooses a lower value of the progressivity parameter γ, even though inequality has increased.

This mechanism gives rise to what we term an "automation bias": a political feedback loop whereby a technological shock that increases inequality simultaneously reduces redistributive pressure, due to the shifting composition of political power. The model thus underscores how the interaction between technological change and endogenous political influence can lead to regressive policy responses, fundamentally altering the normative implications of automation.

4 Results

This section presents the quantitative results of the model, emphasizing how a decline in the cost of automation affects the equilibrium level of redistribution through the endogenous political process. The central mechanism at play is the feedback loop between technological change, income distribution, and political influence. The model is solved using an iterative algorithm that captures the dynamics of political weight redistribution induced by changes in income shares across heterogeneous worker groups.

4.1 Solution Algorithm

To characterize the equilibrium redistribution policy in the presence of endogenous political weights and automation, we follow a step-by-step iterative algorithm. This algorithm simulates how technological change—in particular, a decline in the cost of automation—affects the planner's redistributive choice via political feedback. The steps of the solution are detailed as follows:

4.1.1 Step 1: Initialization

We begin by initializing the economy in a baseline steady state with no automation, i.e., we set the level of the automation input to zero: $x = 0$. This implies that production is entirely dependent on labor inputs from routine and non-routine workers. At this stage, the pre-tax income distribution reflects only the underlying productivity and the share of each type of labor in the production process.

The political weights are initialized as exogenous and symmetric:

$$\omega_{NR}^{(0)} = \omega_{R}^{(0)} = 0.5.$$

This assumption captures an egalitarian political system where both groups initially have equal influence on policy. These weights are used in the planner's objective function to determine the optimal degree of tax progressivity.

4.1.2 Step 2: Solving the Planner's Problem

For some initial parameters, and given the initial political weights and the absence of automation, we solve the planner's problem by choosing the value of the progressivity parameter γ that maximizes the social welfare function:

$$SWF = \sum_{i \in \{NR,R\}} \omega_i U_i.$$

The utility U_i for each group incorporates consumption, pre-tax income, labor effort, and disutility from working, taking into account the effect of taxes. The government budget constraint is satisfied by adjusting λ accordingly, for any chosen value of γ.

Thus, in this step, γ is the only policy variable over which the planner optimizes, while λ is endogenously determined to ensure fiscal balance.

4.1.3 Step 3: Updating Political Weights and Iteration

Once the optimal γ is determined in Step 2, we compute the corresponding equilibrium incomes y_{NR} and y_R. These are used to update the political weights endogenously based on the income shares of each group:

$$\omega_{NR} = \frac{m_{NR}y_{NR}}{m_{NR}y_{NR} + m_R y_R}, \quad \omega_R = \frac{m_R y_R}{m_{NR}y_{NR} + m_R y_R}.$$

This reflects the idea that political influence is proportional to a group's total market income, capturing mechanisms such as lobbying capacity, campaign financing, or voter mobilization tied to economic power.

With these new political weights, we re-solve the planner's problem by repeating Step 2. This process continues iteratively until convergence is reached, i.e., until the political weights and the associated optimal policy γ stabilize. This fixed point defines the initial steady state of the economy with no automation but endogenous political weights.

4.1.4 Step 4: Introducing Technological Change

Having established the initial steady state, we introduce a technological shock by simulating a decline in the price of the automation input, θ. A lower θ makes automation more attractive to firms, leading to an increase in the use of automation x. As automation rises, routine workers experience a decline in labor demand, depressing their wages. Conversely, non-routine workers see an increase in their relative wages.

This change alters the pre-tax income distribution, increasing market income inequality. We then compute the new equilibrium incomes and update the political weights accordingly. The planner re-optimizes the redistribution policy γ in response to these new weights.

Importantly, due to the endogenous nature of political power, the increase in income among non-routine workers also increases their political influence. Since this group has lower marginal utility from redistribution, the planner chooses a less progressive tax system.

4.2 Model Calibration

To solve the model numerically, we calibrate a set of structural parameters using values consistent with empirical evidence and commonly adopted in the macroeconomic literature. These parameters are considered to be externally given, rather than estimated within the model, and are chosen to ensure that the initial steady state reflects a balanced labor market prior to the introduction of automation.

Table 2: Parameters Chosen Outside the Model

Parameter	Description	Value
α	Production elasticity with respect to labor	0.66
ϕ	Frisch elasticity of labor supply	1
χ	Disutility of labor	0.03
m_{NR}	Mass of non-routine workers	0.4
m_R	Mass of routine workers (Restrepo, 2022)	0.6
G	Government expenditure as a share of output	0.3 of Y

The labor share parameter $\alpha = 0.66$ is consistent with standard Cobb-Douglas production functions calibrated to U.S. data. The Frisch elasticity $\phi = 1$ reflects moderate responsiveness of labor supply to wage changes, in line with estimates from labor supply studies. The disutility of labor parameter $\chi = 0.03$ is calibrated to ensure plausible equilibrium labor supply levels.

The population shares of routine and non-routine workers are taken from **?**, reflecting observed occupational distributions in US economy. Finally, government spending is fixed at 30% of total output, which is broadly consistent with empirical averages in US economy as well.

This calibration allows the model to reproduce a reasonable pre-automation baseline against which the effects of technological change can be evaluated. As demonstrated in the subsequent figures, the interaction between economic structure and political feedback is critical to understanding how automation impacts income inequality and the design of redistributive policies.

4.3 Analysis of the key mechanisms

Figure 3 illustrates the evolution of the optimal tax parameters as a function of the political influence exerted by non-routine (high-skilled) workers. This visualization is central to understanding how political economy considerations mediate the relationship between technological change and redistributive policy design.

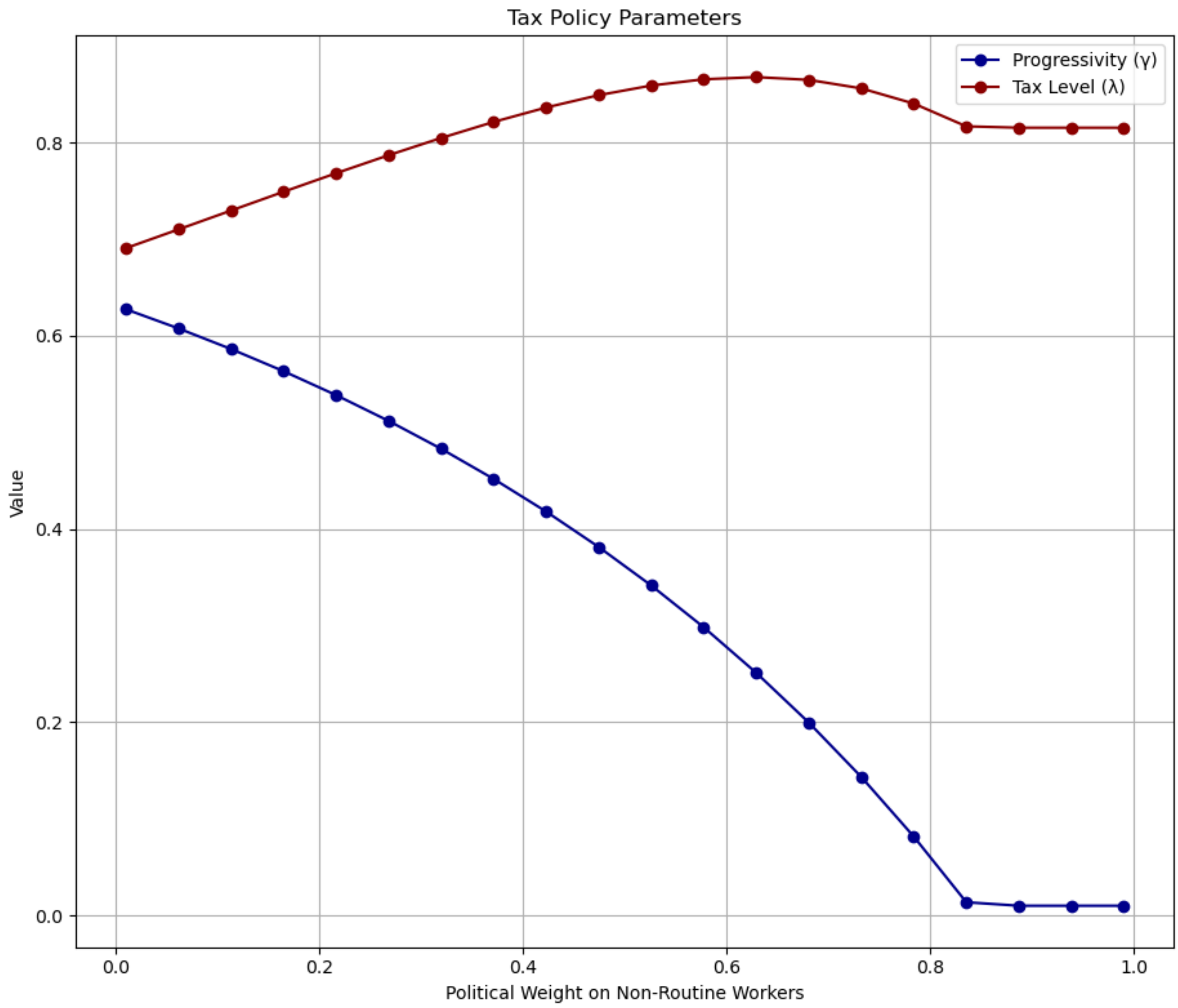

Figure 3: Optimal Tax Policy Parameters as a Function of Political Weight on Non-Routine Workers

The horizontal axis captures the increasing political weight assigned to non-routine workers, denoted ω_{NR}. In the model, this political weight is endogenously linked to the relative income share of non-routine workers, which itself rises as the cost of automation (θ) declines.

The blue line in Figure 3 represents the evolution of the optimal progressivity parameter γ. The relationship is strongly negative and monotonic: as ω_{NR} increases, the optimal value of γ declines sharply. This finding is central to the theoretical contribution of the model. It demonstrates that when individuals who disproportionately benefit from SBTC acquire more political power, the resulting tax system becomes markedly less progressive. A lower value of γ implies that the marginal tax rate rises more slowly with income, thereby reducing the redistributive effectiveness of the tax schedule. This decline in progressivity is a direct reflection of the planner's shifting political objective, increasingly shaped by the preferences of high-income agents.

The red line depicts the behavior of the tax level parameter λ in the tax function $T(y_i) = y_i - \lambda y_i^{1-\gamma}$. A higher value of λ implies a lower average tax burden for a given income level, holding γ constant. The graph reveals a generally increasing pattern in λ as the political weight of high-skilled workers rises, with a plateau or mild decline at higher levels of ω_{NR}. Remember that is always essential to raise a certain level of taxes to finance the exogenous government expenditure. This indicates that the politically dominant group is able to steer policy toward lower overall taxation, given the fact that lower progressivity will also allow output to increase significantly.

Taken together, the dynamics of γ and λ as shown in Figure 3 underscore a key mechanism of the model: economic gains from automation translate into political influence, which in turn leads to policy choices favoring the beneficiaries of technological change. The resulting tax policy is simultaneously less redistributive and lighter in average burden.

Figure 4 presents the evolution of aggregate output as a function of the political weight assigned to non-routine (high-skilled) workers. The graph reveals a clear upward trend: as the influence of non-routine workers increases within the social welfare function, total output in the economy also rises.

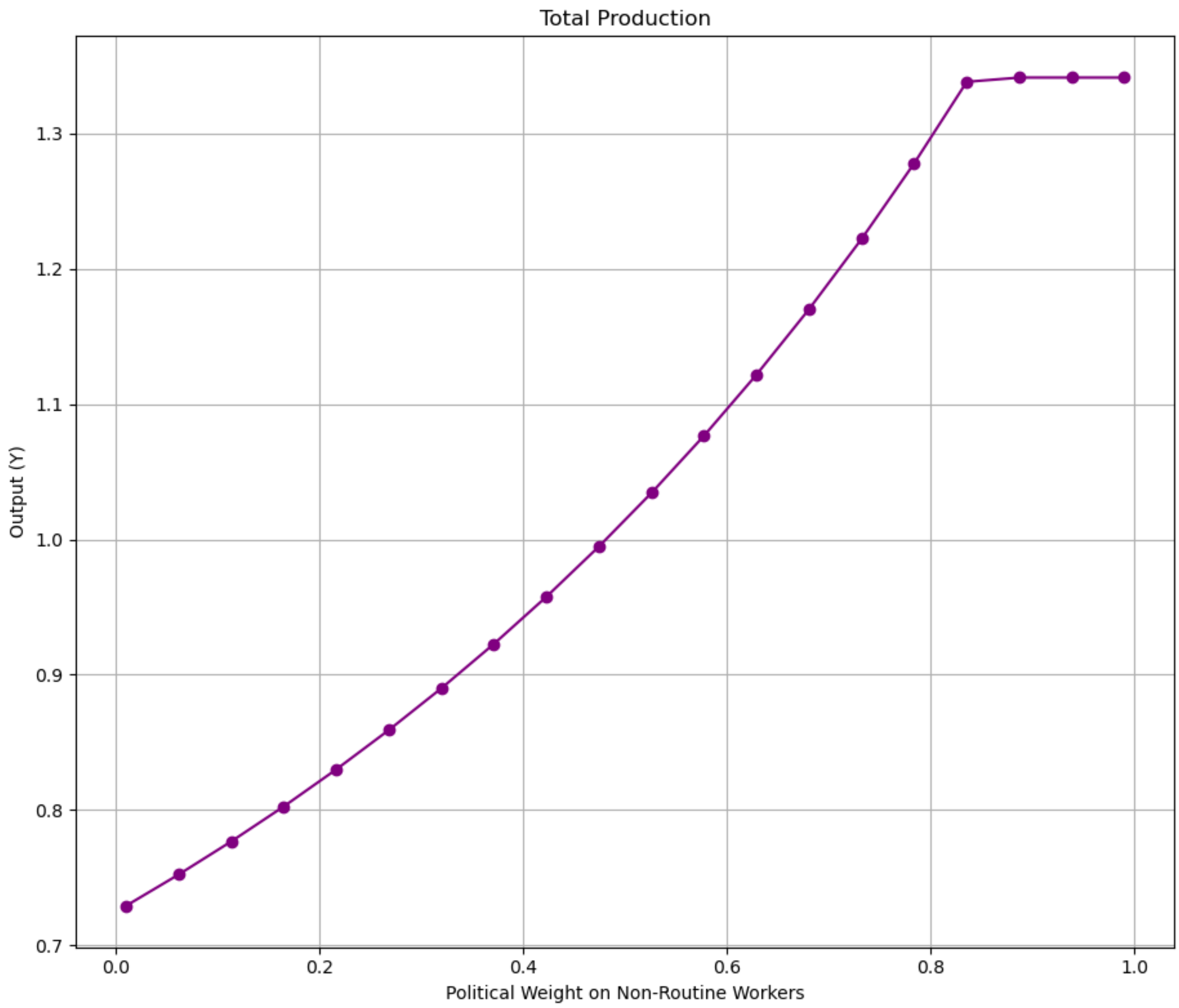

Figure 4: Total Production as a Function of Political Weight on Non-Routine Workers

This positive association between political weight and output is a direct consequence of the decline in the progressivity of the tax system. As previously illustrated in Figure 3, the social planner, under the increasing influence of high-skilled individuals, chooses a lower value for the progressivity parameter γ. A less progressive tax system reduces distortions in labor supply, particularly for high-productivity individuals. As a result, aggregate economic activity expands, leading to higher output.

The mechanism driving this result is rooted in the heterogeneous preferences over redistribution across different worker types. High-skilled, non-routine workers—who benefit more from automation and earn a disproportionately larger share of total income—have a strong preference for flatter tax schedules. This is confirmed in Figure 5, which displays the preferred level of the progressivity parameter γ separately for routine and non-routine groups.

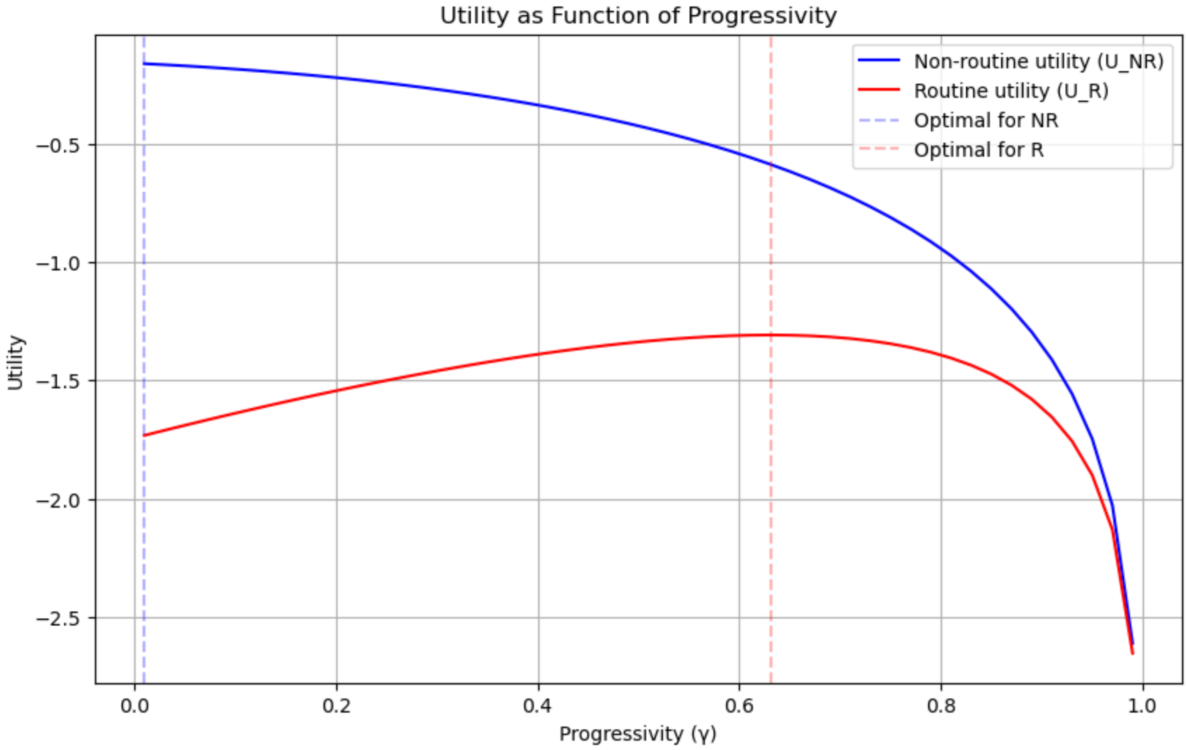

Figure 5: Preferred Progressivity Parameter by Group

The figure shows a pronounced difference in tax preferences across groups. Non-routine workers favor substantially lower values of γ, reflecting their economic incentives to minimize redistribution. Routine workers, in contrast, would prefer a much higher degree of tax progressivity, as they stand to gain from redistribution mechanisms that transfer resources from high to low earners.

The social planner's optimal policy thus reflects a weighted compromise between these divergent preferences. As the income share—and hence political weight—of non-routine workers increases, the planner places greater emphasis on their utility, resulting in a shift toward their preferred policy: lower progressivity and lighter taxation. This shift not only reduces redistribution but also leads to higher overall economic output by reducing efficiency losses associated with progressive taxation.

In summary, Figures 4 and 5 jointly illustrate a key political economy trade-off: while increasing political power of high-income groups leads to policies that enhance aggregate production, it also comes at the cost of diminished redistribution. This result highlights the tension between efficiency and equity in environments characterized by rising income concentration and endogenous political influence.

4.3.1 Disposable Income response

Figure 6 complements the preceding analysis by illustrating the differential effects of the endogenously determined tax policy on the disposable (after-tax) incomes of routine and non-routine workers. This figure plays a crucial role in elucidating the distributional consequences that arise from the evolving political influence within the model.

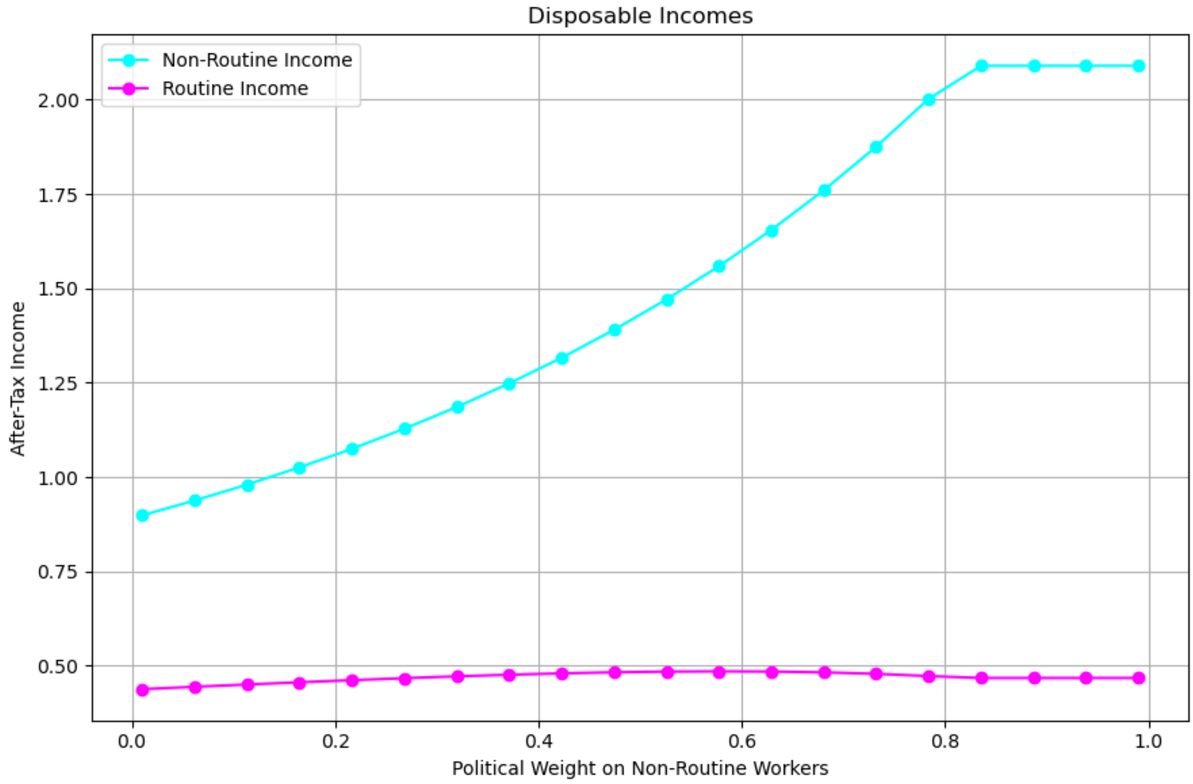

Figure 6: Disposable Incomes as a Function of Political Weight on Non-Routine Workers

The horizontal axis retains its central interpretive importance, as it captures the shifting balance of political power towards the high-skilled, non-routine labor group.

The cyan line, representing the after-tax income of non-routine workers, exhibits a clear and pronounced upward trajectory. As the political weight of this group increases, their disposable income rises steadily and substantially. This pattern results directly from the changes in tax policy documented in Figure 3, namely the progressive decline in the progressivity parameter γ and the corresponding rise in the tax level parameter λ, which effectively reduces the average tax burden. The enhanced political leverage of high-skilled workers enables them to influence the tax system in ways that disproportionately increase their post-tax earnings.

In contrast, the magenta line, which tracks the disposable income of routine workers, exhibits a modest increase but ultimately cannot prevent the widening gap with non-routine workers. This occurs because although routine workers supply more labor in response to the lower tax progressivity, the returns to their additional effort are scaled down by a smaller factor (W_R), limiting gains in their after-tax income relative to the high-skilled group.

Together with the earlier results on tax policy parameters, Figure 6 provides a comprehensive depiction of the model's political economy dynamics. It demonstrates how the ascendancy of high-skilled workers in the political arena not only drives a less redistributive tax structure but also generates widening disparities in after-tax income.

4.4 Evolution from the Steady State

Figure 7 presents the core economic implications of technological progress within the model. Technological improvement—specifically, skill-biased technological change (SBTC)—is captured through an exogenous reduction in the unit cost of automation capital, denoted by θ. A lower value of θ corresponds to more affordable and efficient automation technologies, enabling firms to substitute routine labor with machines at a lower cost.

The left panel depicts the equilibrium level of automation (x) as a function of the automation cost θ. As θ decreases (moving from right to left along the horizontal axis), the adoption of automation rises monotonically. This result aligns with the economic intuition that falling automation costs incentivize firms to invest more in capital that replaces routine labor. The model thus formalizes the first key channel through which SBTC affects the economy: technological advancement directly increases automation adoption.

The right panel displays the corresponding impact on the wage ratio between non-routine (W_{NR}) and routine (W_R) workers. As θ decreases, the wage ratio W_{NR}/W_R

increases steadily. This pattern arises because the wage of routine workers declines as their labor is increasingly substituted by automation, driving their marginal product closer to the cost of its technological substitute. Conversely, non-routine workers—whose labor is complementary to automation—maintain or even increase their marginal productivity and therefore experience wage gains. The result is a widening wage gap that reflects rising income inequality across skill groups.

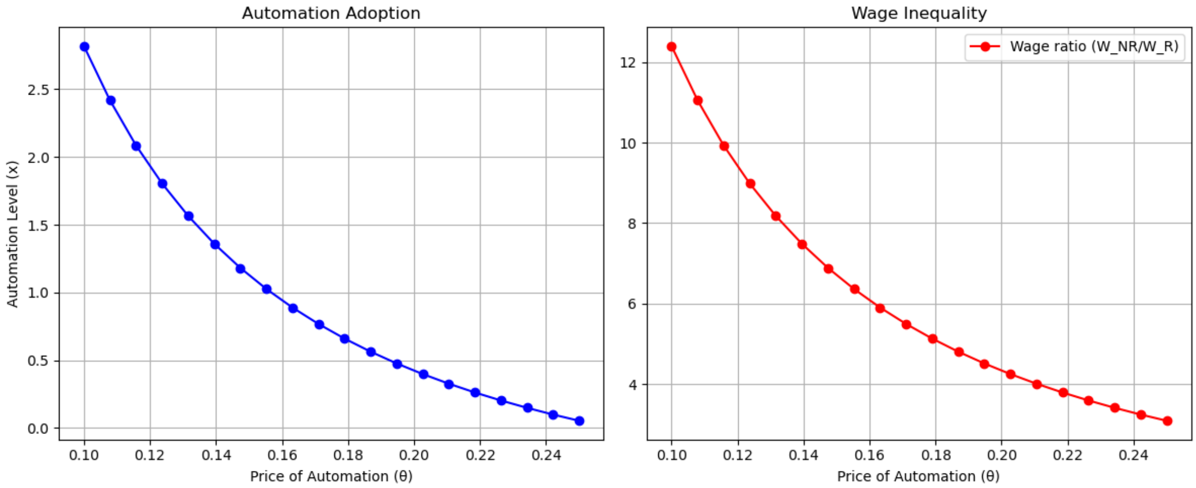

Figure 7: Automation adoption and wage inequality with cheaper technology

Together, the two panels in Figure 7 highlight the foundational economic mechanism in the model: exogenous technological progress, in the form of a reduction in θ, endogenously leads to increased automation and a pronounced rise in wage inequality.

4.4.1 The Political Response and Policy Outcome

Figure 8 illustrates the connection between the economic effects of automation and the resulting political and fiscal responses, thereby completing the core mechanism developed in this thesis.

The horizontal axis represents the endogenous adoption of automation technologies in the economy. As previously shown in Figure 7, higher values of x are associated with reductions in the price of automation (θ) and rising wage inequality between skill groups.

The dashed green line plots the political weight of non-routine workers, denoted ω_{NR}. This weight increases monotonically with x, indicating that the group benefiting most

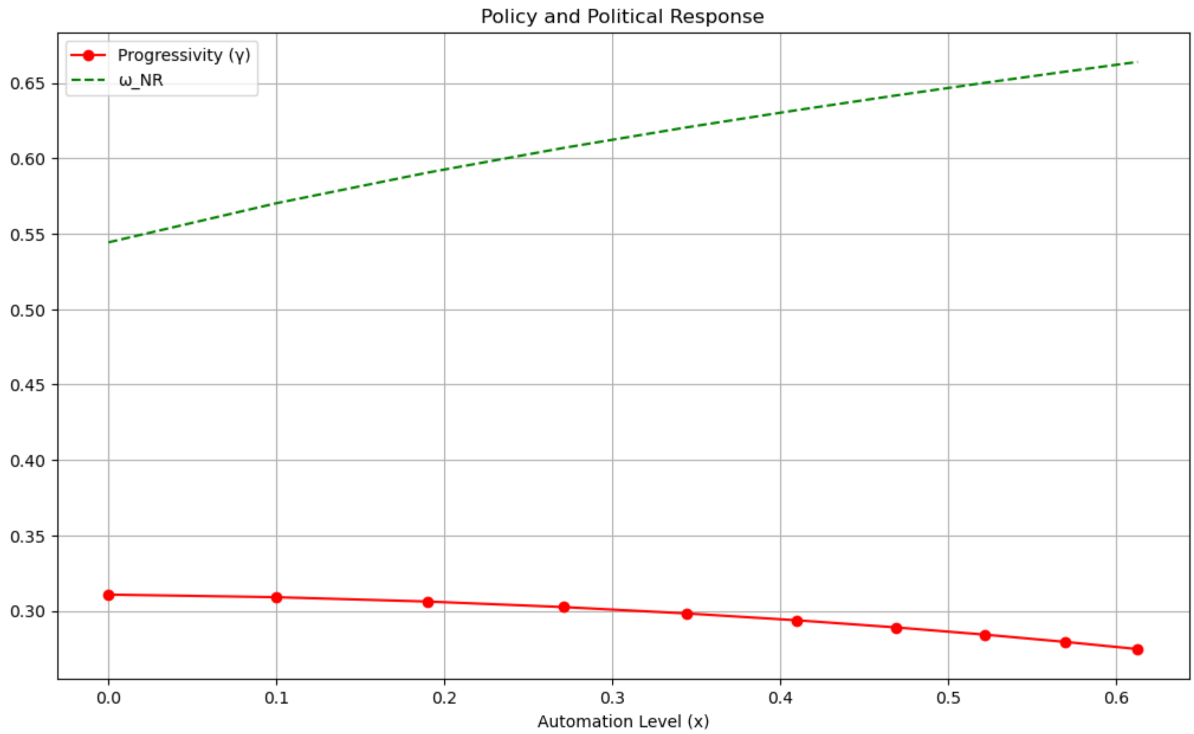

Figure 8: Tax progressivity and political weight as functions of the automation level

from automation—non-routine workers—gains greater influence in the social welfare function (SWF). The mechanism underlying this result is that political weights are proportional to pre-tax income shares; thus, as the income share of non-routine workers increases with automation, so does their political weight.

The solid red line shows the optimal tax progressivity parameter, γ, as chosen by a benevolent planner. As x increases, the progressivity of the tax system declines. This reflects the changing composition of political power: as the political weight of higher-income non-routine workers rises, the planner's preferred redistributive policy becomes less progressive. Non-routine workers, whose income rises with automation and who face higher marginal tax rates under a progressive system, prefer lower redistribution.

This figure formalizes the political economy feedback loop emphasized throughout the thesis. Automation drives inequality, which alters the political landscape by shifting influence toward high-income groups. In turn, these groups shape fiscal policy in a direction that reduces redistribution. Hence, rising inequality is accompanied by a decline in tax progressivity, even in a model with a benevolent planner, once political weights are allowed to respond endogenously to income distributions.

5 Conclusion

This thesis develops a unified framework to study the economic and political consequences of skill-biased technological change (SBTC) driven by automation. In contrast to much of the existing literature, which focuses on either economic inequality or political outcomes in isolation, the model presented here integrates both dimensions to uncover an endogenous feedback mechanism between technology, inequality, and redistribution policy.

The analysis begins with a formal model of the labor market in which automation reduces the cost of replacing routine labor with machines. As the cost of automation capital declines, firms substitute routine workers with capital, thereby increasing overall automation levels. This shift leads to a rising wage gap between routine and non-routine workers: while the wages of routine workers are compressed by the availability of cheap substitutes, non-routine workers—whose labor remains complementary to automation—see their wages rise. This mechanism generates an endogenous increase in income inequality.

The model then introduces a political economy dimension in which fiscal policy is determined by a benevolent planner who places weight on different income groups according to their relative pre-tax income shares. This feature captures the idea that political influence is tied to economic power. As automation-driven inequality increases, non-routine workers accrue a larger share of national income and, therefore, more political influence. Because they tend to prefer lower redistribution, their increased political weight leads to a decline in the optimal tax progressivity.

Quantitative simulations of the model confirm these dynamics. A reduction in the cost of automation capital induces a higher level of automation and a wider wage gap between skill groups. As a result, the political weight of non-routine workers increases and the planner responds by reducing the progressivity of the tax system. This leads to the key prediction of the model: rather than offsetting rising inequality, fiscal policy becomes less redistributive precisely when inequality is increasing. The decline in redistribution is not due to a change in preferences or policy constraints, but arises endogenously from shifts in political power caused by technological change.

These findings contribute to the growing literature on the political economy of inequality and automation. They suggest that the economic winners from automation not only benefit in terms of income, but also acquire greater influence over policy outcomes, reinforcing inequality. This dynamic highlights a potential political limit to redistribution in response to technological disruption and raises important questions for future research and policy design. Specifically, the results imply that mitigating inequality may require institutional arrangements that insulate redistribution policy from shifts in political power induced by changes in income distribution.

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