Joint Economic Committee
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REPUBLICAN STAFF COMMENTARY

Economic Inequality and Mobility

A Dynamic Picture

June 19, 2012

Annual income is a snapshot, but life is a motion picture.
– Alan Reynolds, *Income and Wealth*[1]

As was made apparent in the initial commentary of the series, there are many factors affecting the distribution of income and wealth among U.S. households over time. A critical component of the analysis of income inequality is a comprehensive picture of income and wealth *mobility*; this facet of the analysis provides more than just a snapshot of the income and wealth distribution at any particular moment. As economist Scott Winship mentions in his testimony before the Senate Budget Committee on income inequality and income mobility, the evidence that rising inequality has hurt the middle class and the poor is very thin at best.[2] Furthermore, policies to address income inequality are poorly targeted and may actually create a barrier to income mobility.

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Absolute and Relative Mobility

As defined in the collaborative *Economic Mobility Project* report of the Pew Charitable Trusts and Brookings Institution, there are two types of economic mobility to consider that differ from the changes in income resulting from rising or falling economic inequality: absolute mobility and relative mobility. *Absolute mobility* is a result of economic growth that enriches all groups of society. In the report, the economy is likened to a ladder that grows taller and all the ladder rungs are rising. At the same time, the rungs on the ladder may be getting closer together or farther apart as the ladder grows, demonstrating the degree of income inequality. In turn, *relative mobility* can be described as the ability of individuals to move from one rung to another dependent upon opportunity.[3]

Absolute mobility is a result of the economic growth that enriches all income levels. Relative mobility is the ability to move between income levels.

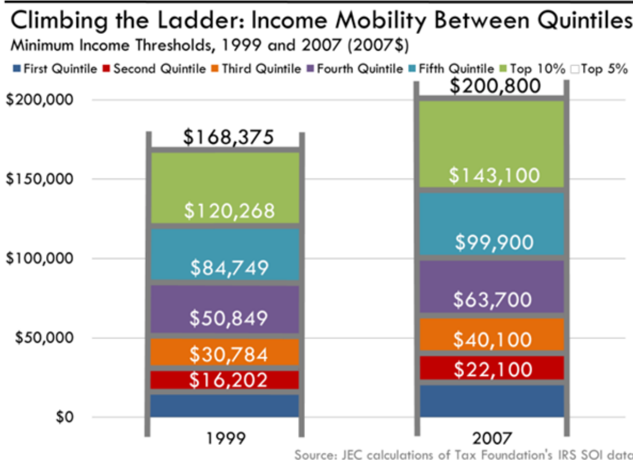


Figure 1 – The overall ladder has increased over time in real dollars, changing the spacing of the 'rungs' in the ladder even before mobility is accounted for over time.

Mobility within One's Lifetime

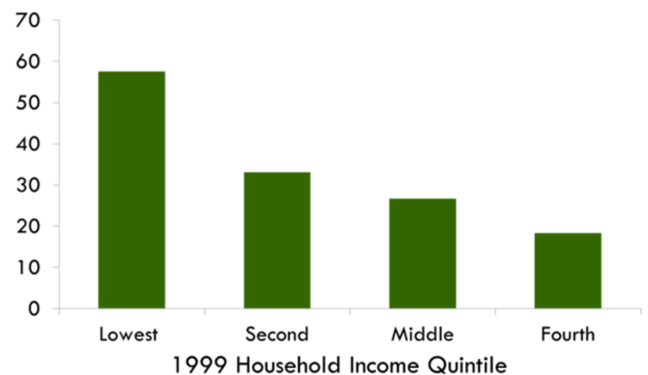
In Figure 1, showing figures from a Tax Foundation study using Internal Revenue

(Continued on the next page …)

Service (IRS) data, notably the 'rungs' of the 'ladder' between minimum income thresholds have increased in inflation-adjusted 2007 dollars between 1999 and 2007.

Approximately 60 percent of households that were in the lowest income quintile in 1999 were in a higher quintile in 2007.

Breaking away from the ladder imagery, as shown in the graphs in Figure 2, the study identified that nearly 60 percent of households that were in the lowest income quintile in 1999 were in a higher quintile in 2007; well over 30 percent of the second quintile in 1999 were in a higher quintile by 2007; nearly 27 percent in the middle quintile moved up at least one or higher; and 18 percent in the fourth quintile moved to the top quintile. As many households move up, many also move down. Another almost 40 percent of households in the top quintile fell at least one quintile over the same nine-year period. Nearly the same percentage of households fell from the top one percent as those that moved from the lowest quintile into a higher income group. Almost half fell from the top 5 percent, and just over 45 percent fell from the top 10 percent.[4]



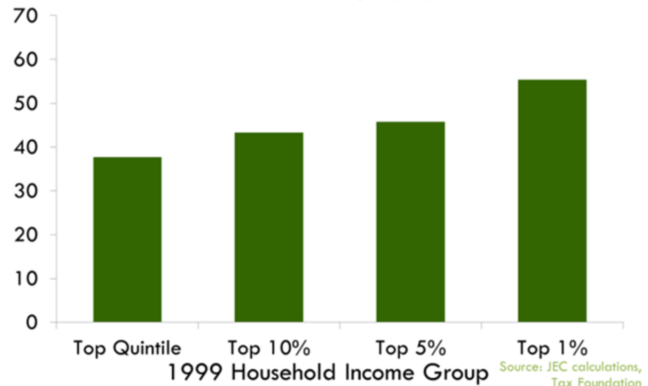


Figure 2 – The percent of lowest quintile households moving into a higher income quintile reaches nearly 60 percent 1999-2007. The highest percentiles experience nearly as much movement into a lower percentile.

The Federal Reserve Bank of Minneapolis has also demonstrated earnings mobility of U.S. households using income data from the Panel Study of Income Dynamics (PSID) that followed the same households from 2001 to 2007. The empirical results demonstrate that 44 percent of those in the lowest quintile moved up at least one quintile by 2007, and 34 percent in the highest quintile moved down at least one quintile over the same time period.[5]

The 400 highest earning tax returns filed between 1992 and 2008 included only four people who appeared in the top 400 filers continuously; however, one-timers abounded: 39 percent of the top 400 filers appeared in that category only once over the 17-year period.

In another examination of IRS data, the 400 highest earning tax returns filed between 1992 and 2008 included only four people who appeared in the top 400 filers continuously; however, one-timers abounded: 39 percent of the top 400 filers appeared in that category only once over the 17-year period.[6]

Addressing the Top One Percent and Income Mobility

As a measure of adjusted gross income (AGI), shown in Figure 3, the income share of the top one percent in the United States fell from nearly 25 percent in 2007 to 17 percent in 2009. The income share of the top 0.1 percent experienced a drop from just over 12 percent to eight percent of the income earned in 2009, the lowest it has been since 2003.[7] This adds complexity to the fact that not many stay in the top one percent for an extended period of time; the share of wealth among the top one percent fluctuates over any given period of time as well. The recent spikes shown in Figure 3 in the late 1990s and through the 2000s similarly demonstrate the effects of the tech and housing bubbles, respectively.

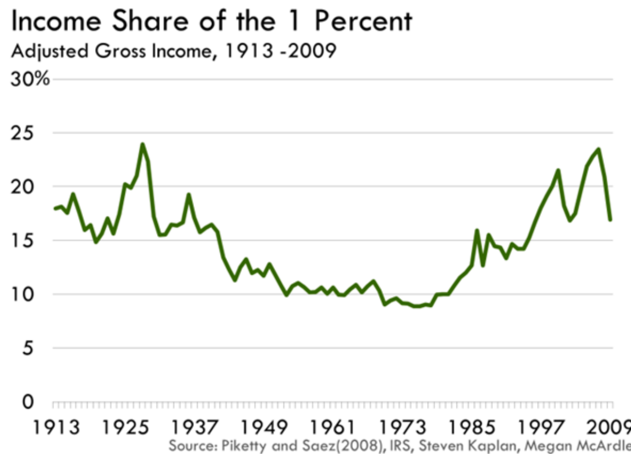


Figure 3 – The top one percent's share of adjusted gross income (AGI) demonstrates that the wealthy held 17 percent of AGI in 2009, similar to that of 1913.

Indeed, in the wake of the recent recession, the number of individuals making a million dollars or more per year fell by 40 percent to 236,883, and their combined incomes fell by nearly 50 percent. In the 1990-91 and 2001 recessions, the richest five percent of Americans experienced the largest declines in wealth. By contrast, the effect was much broader in 2009, with the richest 20 percent encountering the greatest loss in average wealth of any other quintile. For all three recessions, the top one percent of earners experienced the largest income shocks in percentage terms of any U.S. income group, and the measured gap between the top and bottom quintiles shrank during recessions.[8]

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Wealth Mobility and the One Percent

As a measure of total wealth, since the Great Depression, top wealth shares have increased only modestly during the stock market booms of the 1960s and 1990s. Prior to the Depression, the top one percent held 35 to 40 percent of total wealth in the United States, but over the last three decades leading up to 2000 that share has declined to between 20 and 25 percent.[9] In 2009, Wojciech Kopczuk restated there was no compelling evidence that wealth concentration has much changed since the early 1980s.[10]

According to a paper published with the National Bureau of Economic Research by authors Emmanuel Saez and Wojciech Kopczuk, the shocks of the Great Depression, the New Deal, and World War II radically reduced the share of wealth held by the top of the wealth distribution.[11] The aftermath of the recent recession has and continues to affect wealth mobility of the once most-affluent. In recent research from the Federal Reserve using the cross-sectional Survey of Consumer Finances, among the wealthiest one percent of households in 2007, 33 percent fell from that group by 2009; among households in the top one percent of income in 2007, 43 percent fell from that highest category by 2009.[12]

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Intergenerational Mobility

Another facet of the discussion of income mobility concerns not just the movement of an individual or household between "rungs" on the "ladder" over time, but the degree of mobility between generations of the same family over time.

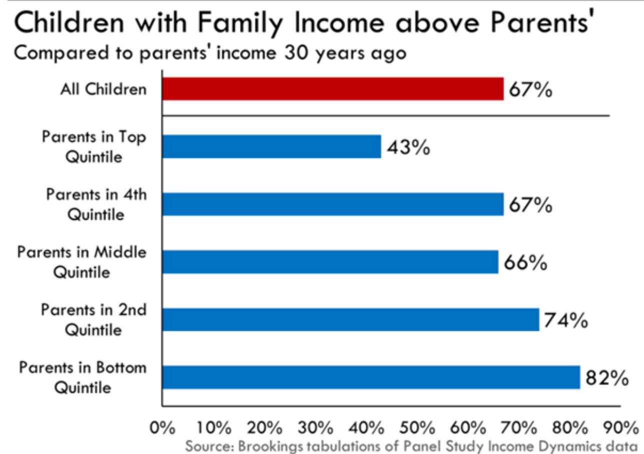

Figure 4 – The percent of the children with family income above their parents by parents' income ranking shows that 67 percent of all children will achieve income above that of their parents.

Over two out of three Americans have higher absolute family incomes today than their own parents had approximately 30 years ago.

Median family income increased by 29 percent between the two generations, from an inflation-adjusted $55,600 to $71,600. Mean income grew a much faster 43 percent, from $61,600 to $88,000.

According to a recent study by Pew Charitable Trusts and the Brookings Institute which used data tracking a nationally representative sample of children between the ages of 0 and 18 in 1968 through the Panel Study Income Dynamics (PSID) found, as shown in Figure 4, just over two out of three Americans have higher absolute family incomes today than their own parents had approximately 30 years ago. Children born to parents in the bottom quintile are more likely to surpass their parents' income than children from any other quintile. While the higher the parents' income, the higher their children's income, it was also noteworthy that the amount by which children exceeded their parents' income decreased the higher the parents' income was. In addition, median family income increased by 29 percent between the two generations, from an inflation-adjusted $55,600 to $71,600. Mean income grew a much faster 43 percent, from $61,600 to $88,000. The study also made a point to highlight that (1) the incomes and income growth of those in the study were taken during prime earning ages of native-born adults; (2) a shrinking family size accompanied this growth in family incomes over time; (3) women in the workforce have heavily influenced the growth in family income, and women's average earnings have particularly increased; and (4) non-cash contributions might affect upward mobility as well. While children's chances of getting ahead by parents' family income from the bottom to top quintile is infrequent (6 percent did in the survey), there remains a fair amount of mobility, with 61 percent of those born at the top no longer remaining there.[13]

Addressing Gender Inequality and Mobility

Often discussion of an income gap and immobility turns attention to more specific socioeconomic differences, such as the wage gap between men and women. However, the differentiation between men and women's earnings has also been changing over time, both intergenerational and intra-generational. The most commonly cited statistic originates from Census data, showing that women earn 77 cents on the dollar compared to men's earnings. However, like the omission of household demographics in the income inequality discussion, this statistic fails to account for differences in education, job type, experience, and hours worked.

The Labor Department, which defines a full-time job as 35 hours per week or more, finds that nearly 55 percent of workers that achieve more than 35 hours per week are men, with 25 percent working 41 hours or more per week compared to 14 percent of women working as long. The most significant reason for this is not gender discrimination—it pertains to career changes by women for children. According to a study from the American Association for University Women, of the women who graduated from college in the 1992-3 academic year, 23 percent who became mothers were out of the workforce in 2003; another 17 percent were working part-time. Furthermore, women comprise two-thirds of part-time workers in the United States.[14] As for stay-at-home dads, there is currently no comprehensive data available to determine if dads working part-time, if at all, have taken a similar reduction in pay as stay-at-home and part-time working mothers do.

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Comparing men and women by earnings of full-time wage and salary workers 25 years and older, women are set on a trajectory to earn more than men; between 1979 and 2010, women with a bachelor's degree and higher experienced a 33.4 percent gain in constant-dollar median usual weekly earnings compared to a 19.9 percent gain for men, as shown in Figure 5.[15] Additionally, single, childless women between the ages of 22 and 30 have been out-earning their male counterparts in most U.S. cities by 8 percent on average since 2008, according to an analysis of Census Bureau data by Reach Advisers. The largest earnings gap between men and women was in Atlanta, where young women without children were earning 121 percent of male counterparts.[16]

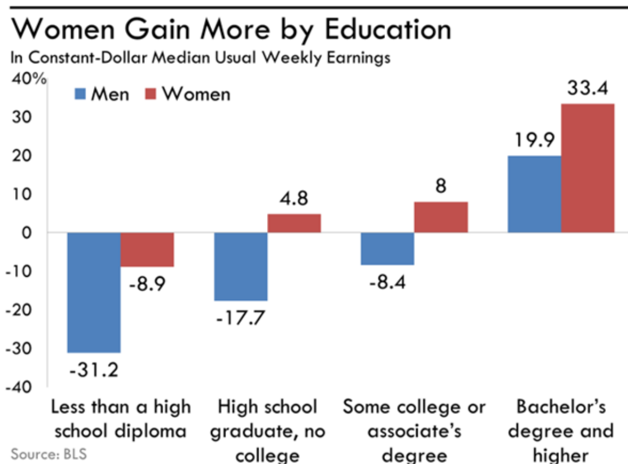

Figure 5 – Women with a bachelor's degree and higher have gained more than men as a percent change of constant-dollar median usual weekly earnings.

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Addressing Income Immobility

Focusing on the economic problems of the very poor requires addressing obstacles on opportunities for low-income, income immobile individuals. According to an analysis by economist Scott Winship, mobility from the very bottom for young men in particular, is an area in which the United States falls behind internationally. Additionally, in a recent study from the Federal Reserve Board, it was found that over the period from 1987 to 2006 both before and after taxes, the increase in inequality was permanent for male earnings, and predominantly permanent for household income. Though the tax system was shown to reduce inequality, it did not significantly affect the increasing trend in inequality.[17]

Only 17 percent of children raised in the bottom fifth are expected to reach the top two-fifths of the income distribution. As Scott Winship points out, existing programs may provide a floor but also create a ceiling: though these

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programs lift the poor out of destitution, they can also discourage the upward mobility of poor children. Winship argues most policies intended to help the poor are poorly targeted, instead pricing the poor out of assets (such as higher education) that promote mobility, thus leaving a diminishing amount of money to reduce barriers to upward mobility for the poor.[18]

International Comparisons

Assessing how the United States compares in income inequality and degree of mobility can help to distinguish if the trend is unique to America, as Winship noted of young men in the preceding section. However, there are also reasons why international comparisons can be difficult when discussing income inequality and mobility.

Even if the focus is between the 99 percent and the top one percent, while inequality has grown considerably between these two categories, this phenomenon is not unique to the United States.

Even if the focus is between the 99 percent and the top one percent, while inequality has grown considerably between these two categories (or even between the 99.5 percent and the top 0.5 percent, which accounts for 16 percent of all income[19]), this phenomenon is not unique to the United States; in fact, there is very little evidence to suggest that this disparity is a result of the top gaining at the expense of the 99 percent. This is possible because the economic pie can grow in size that benefits the top one percent immensely while everyone else enjoys a bigger slice as well.[20] Economist Allan Meltzer confirms that the change between the top one percent and the 99 percent is a change occurring across all developed countries.[21] As a final comparison of note, Winship demonstrates that when the post-1986 U.S. trend of the top one percent is corrected for the changes made in the 1986 tax reform, the U.S. is rather consistent with the rest of the modern world over the past century (1916-2006).[22]

As highlighted by Jim Manzi, potential reasons for differences in the intergenerational earnings elasticity (IGE) amongst countries could include population size as countries with larger populations tend to have greater income variety, and thus higher IGE. Other variables Manzi mentions include degree of specialization of a given country and religious fractionalization. As Manzi states,

> *The real drivers of social mobility in America are a lot more complicated... This is why Winship was able to point out that various responsible estimates for the mobility-inequality correlations range from .87 to -.15. That is, the various versions of mobility-inequality curves predict everything from extreme social stratification to greater social mobility in the America of 2035. What we see in this case is exactly what statistical theory says we should in the presence of rampant omitted variable bias: wildly unstable parameter estimates.*[23]

The OECD also highlights skill-biased technological change (SBTC) and globalization (such as trade-induced innovation) as causes of income inequality in recent decades.[24] As highlighted in a former JEC paper of the same subject, if the demand shifts for non-routine, high-skilled labor is not offset by equal shifts in supply, then SBTC exacerbated income inequality by reducing the earnings or employment of low-skilled labor or those with skills that are less in demand.[25]

Conclusion

It is dishonest to discuss income inequality without giving consideration to the dynamic degree of mobility, both in absolute and relative terms, over time between generations and within generations. As with discussions of economic inequality, economic mobility can be measured both in terms of income and wealth. Economic opportunity allows people both by measure of individuals and households to move up and down the "rungs" of the "ladder." Relative to other countries, the United States falls in line with the current trend in income inequality and intergenerational mobility.

Rather than remain concerned with "concentrations" of income and wealth among the one percent, which is a constantly changing set of individuals, it is important to identify barriers to economic mobility. As aforementioned, Scott Winship points out many existing programs intended to help those currently in the lowest quintile are poorly targeted and can actually create a barrier to economic mobility. Ensuring that these programs don't end up pricing the poor out of opportunities can be a great place to start removing barriers to economic mobility.

Upcoming

In the third and final commentary, a look at causes and prescriptions for economic inequality will be covered, with regard to education and "wage premiums," skills-based technological change, and trade and globalization.

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