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Robert M. La Follette School of Public Affairs
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"Social and Economic Mobility in an Era of Extreme Inequality: Who Owns the Robots?"

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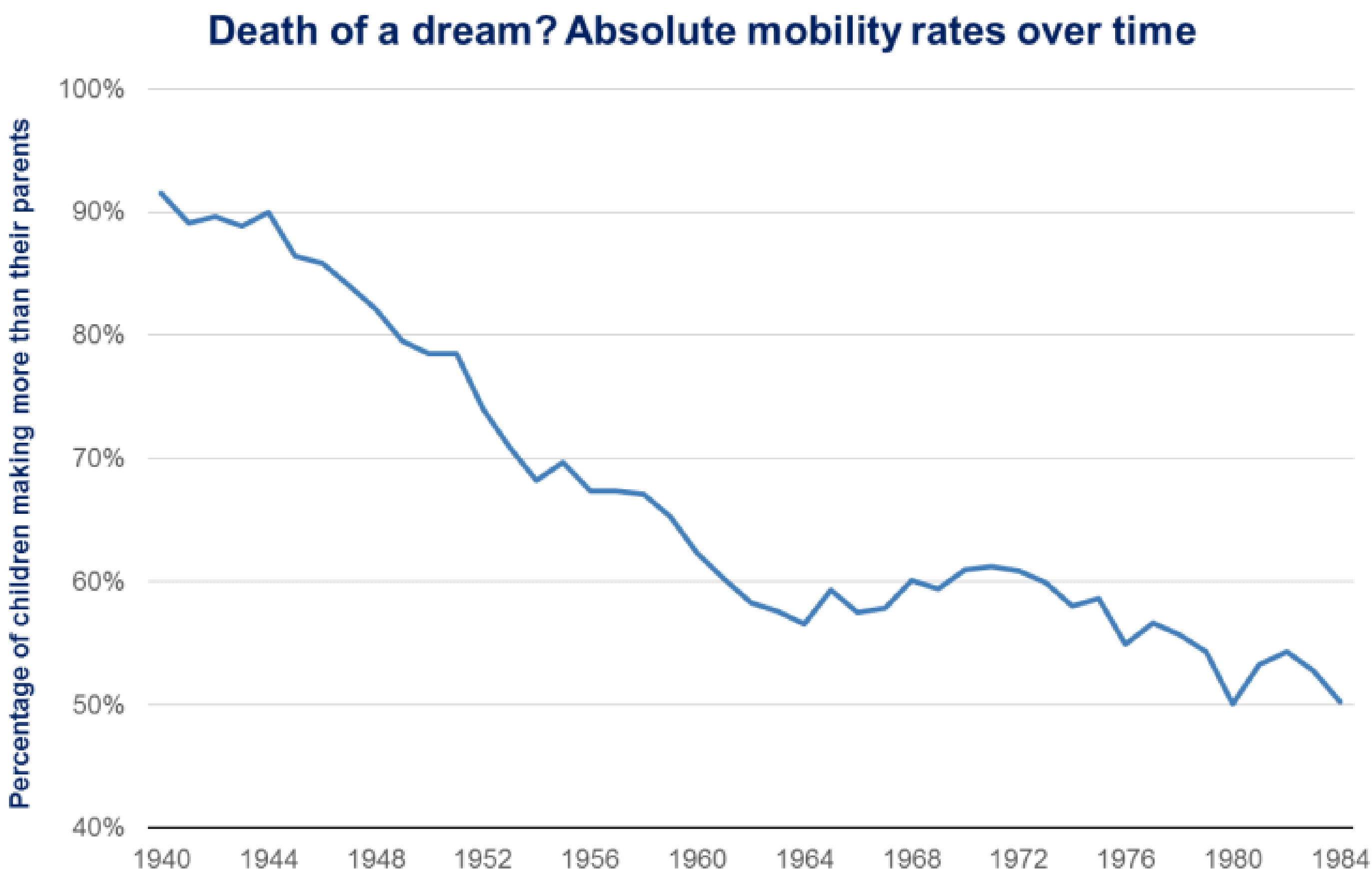
Abstract

Americans used to believe that we lived in a land of opportunity with a good chance for everyone and their children to do well. But America is near the bottom of nations where everyone has fair chance of reaching the American Dream. This lecture considers mobility at the bottom, top and middle of the distribution, both over time and across generations in a nation where capital income (who owns the robots) dominates labor income, where public policy increases extreme inequality and where the future of work is increasingly dim for those without a college education and without good opportunities to make use of that investment.

The American Dream in decline



Source: Chetty et al., "The Fading American Dream: Trends in Absolute Income Mobility Since 1940."

BROOKINGS

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The Era of Extreme Inequality: Who Owns the Robots?"

A. INEQUALITY

1. "Capital" , wealth and capital income, is the most important source of inequality
2. The owners of the robots are winning; labor– working and middle class as well as poor -- is losing
3. Inequalities in Y, C and W are rising in tandem and are corrosive

What does this do to social an economic mobility ?

B. MOBILITY

1. Life course approach— where and how you grow up affects where you end up
2. Given trends in key parameters for child mobility, are we making progress ? (NO)
3. Except for the children of the wealthy

C. POLICY

What an be done about inequality and mobility ?

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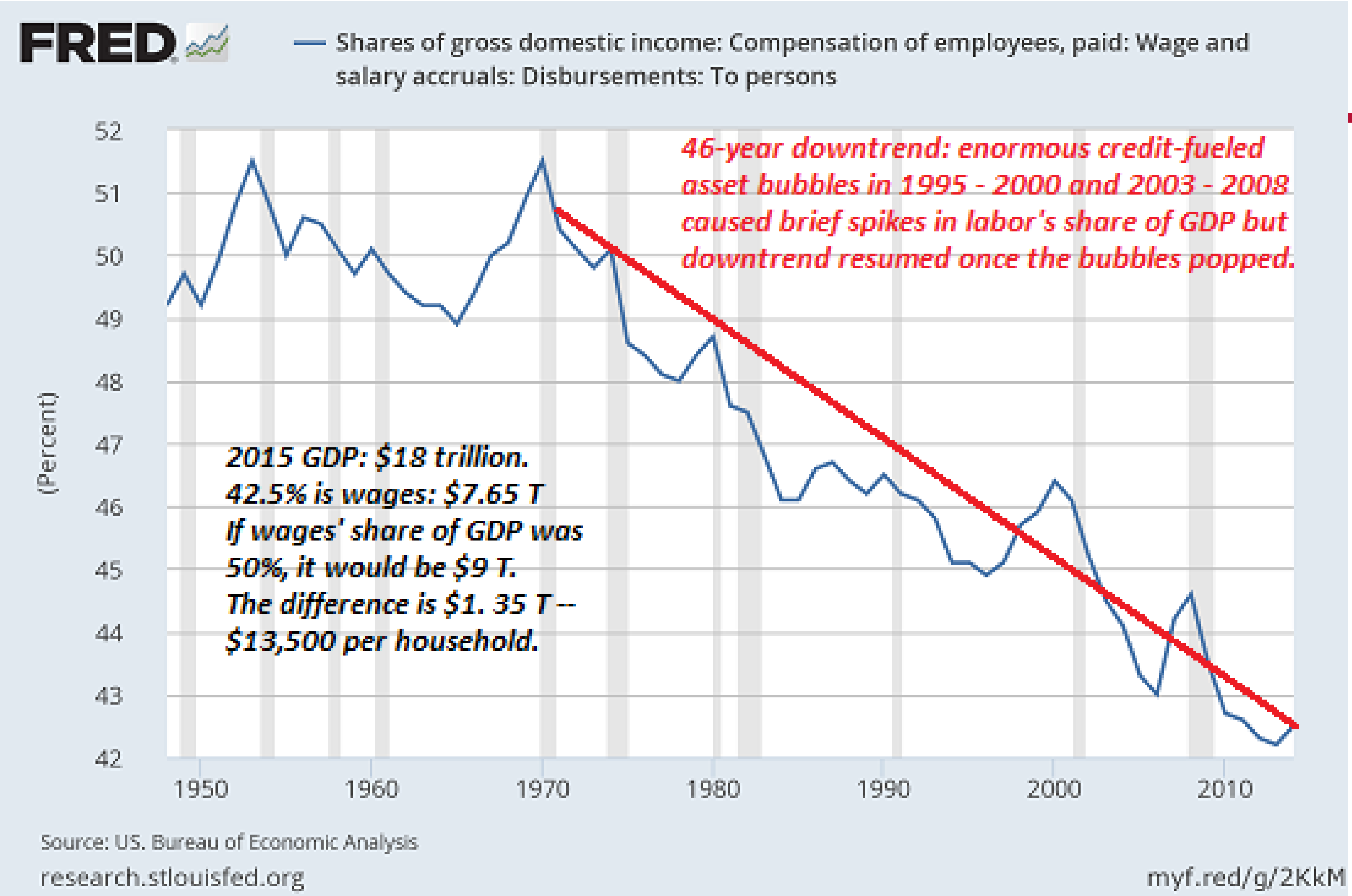
INEQUALITY
Start with *sources* of income

- Functional "sources" side of income (Y) , adding together income from labor/earnings (E), & income from capital (KI, including capital gains plus other income from wealth), plus net transfers (NT, those received minus those paid out which we ignore)

  Y = E + KI + NT

- If we ignore NT, divide self-employment income into income from labor and capital, we are left with the macroeconomists' "functional distribution" of income.
- **So what can we learn here for distributional analyses from the sources side ?**

Sources side : Y = E + K



Factor Shares—E (labor share of national income) falling in USA : more than 50 % in 1970's, now 42%

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Why is capital (K) share up ?

- Technological change, global trade--- and policy --

-'Regulatory' policy : rising concentration of industry, less competition & more profit

-Pro-capital tax policy, eg stock buy backs

-'Rent capture': sheltered markets, limited enforcement, protected market niches , and political power

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Why is labor share down ?

- Rising monopsony power and policy, global competition from cheap labor, insecurity of work —*not* just decline of unions but broader malaise

- "non–compete clauses";
- workplace inflexibility;
- spatial immobility of workers;
- rise of "gig" economy
- declining real federal and WI minimum wages

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Measuring "uses" of income and effects of inequality: Y,C,W

- "the most pertinent measures of the distribution of material living standards are probably based on jointly considering the income, consumption, and wealth position of households or individuals."

Commission on the Measurement of Economic Performance and Social Progress (Fitoussi, Stiglitz et al.,2009):

- Income(Y), consumption(C), and wealth (W,NW)
- all three together *for the same households*
- Start with aggregate accounting again

Flows and stocks: Income (Y); Consumption (C); Net Worth (NW)

- Haig and Simons definition, income (Y) is equal to consumption (C) plus the ***change in net worth*** (ΔNW) realized over an income accounting period.
- So defined, Y , H-S income, is a measure of potential consumption : amount one could consume or transfer without changing total net worth (one's stock of assets or debts)
- Thus according to a **"uses " of income definition:**

$$Y = C + \Delta NW$$

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On the uses of income side--

- The hardest thing to measure is the real change in net worth (ΔNW) as much of it is not realized or distributed and hence not captured in surveys or registers —but it is behaviorally VERY important
- It would also let us determine consumption in a much more accurate way $C = Y +/- \Delta NW$
- The thing we can measure much better is the stock – W (NW) alone using proper samples like the Survey of Consumer Sciences (SCF) which lines up well with SNA

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Why care about ΔNW ?

- Changes in financial wealth have cyclical elements (eg GR, Trump tariff talk) but stronger upward trends when smoothed
- Most stocks and financial wealth, including defined contribution pension plans, are owned by the top decile (about 75 % in USA)in a period when capital is winning on the sources side
- E.g, 2017, a "very good year" for top decile wealth and pension holders in USA (financial wealth with 25-30% return vs. your academic salary?)

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Turn to Wealth or Net Worth as key

- The stock , NW can replace the flows, Y and C , multiple times over
- from the SCF comes the distribution of wealth
- from panel data , we see dynastic wealth mobility across three generations or more now in PSID
- Key: role of intergenerational transfers in improving off-spring economic position

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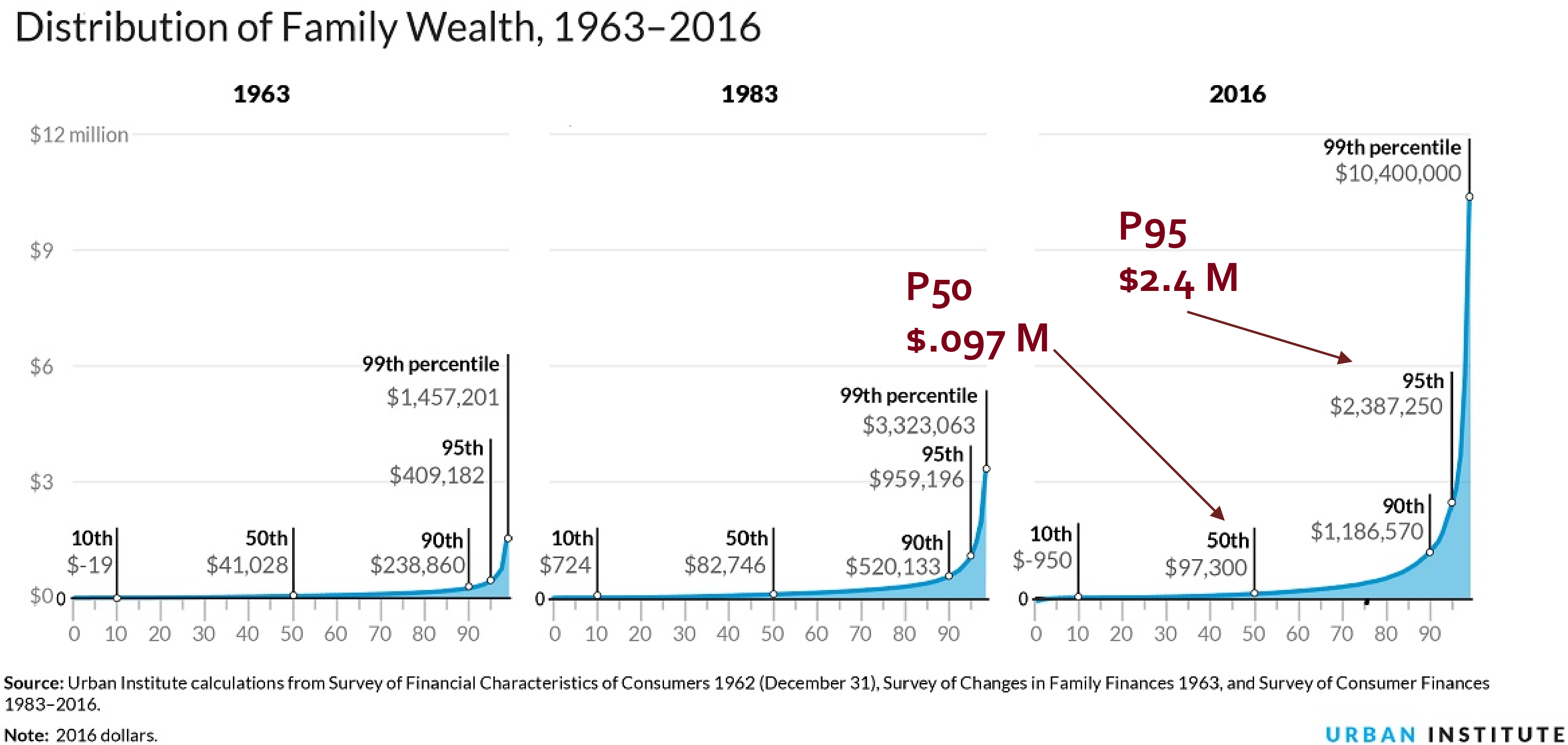
The distribution of family wealth: USA 1963-2016 (*before 2017-18*)



Source : SCF at http://apps.urban.org/features/wealth-inequality-charts/

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After the Great Recession wealth inequality explodes

Growth in Household Wealth, 1950-2016

Notes: Lines show growth rates for different wealth groups, with blue for the bottom 50 percent,
for the middle class (50th percentile to 90th percentile), and orange for the top 10 percent. All ti
series are indexed to 1 in 1971. Vertical line indicates financial crisis.
Source: Authors' calculations

https://www.minneapolisfed.org/institute/working-papers-institute/iwp9.pdf

Y, C and W(NW)-- USA, 1989-2016

- Consider C, Y and NW , *all three for the same persons based SCF with some CEX imputes*
- Findings------measures of one-dimensional inequality understate the level of inequality and the growth in inequality :

-inequality in income (Y), consumption (C)and wealth (or net worth, NW) all rising *separately*

-inequality *in any two dimensions increased faster than in any one dimension over this period*

-*inequality in all three dimensions together rose by the most*

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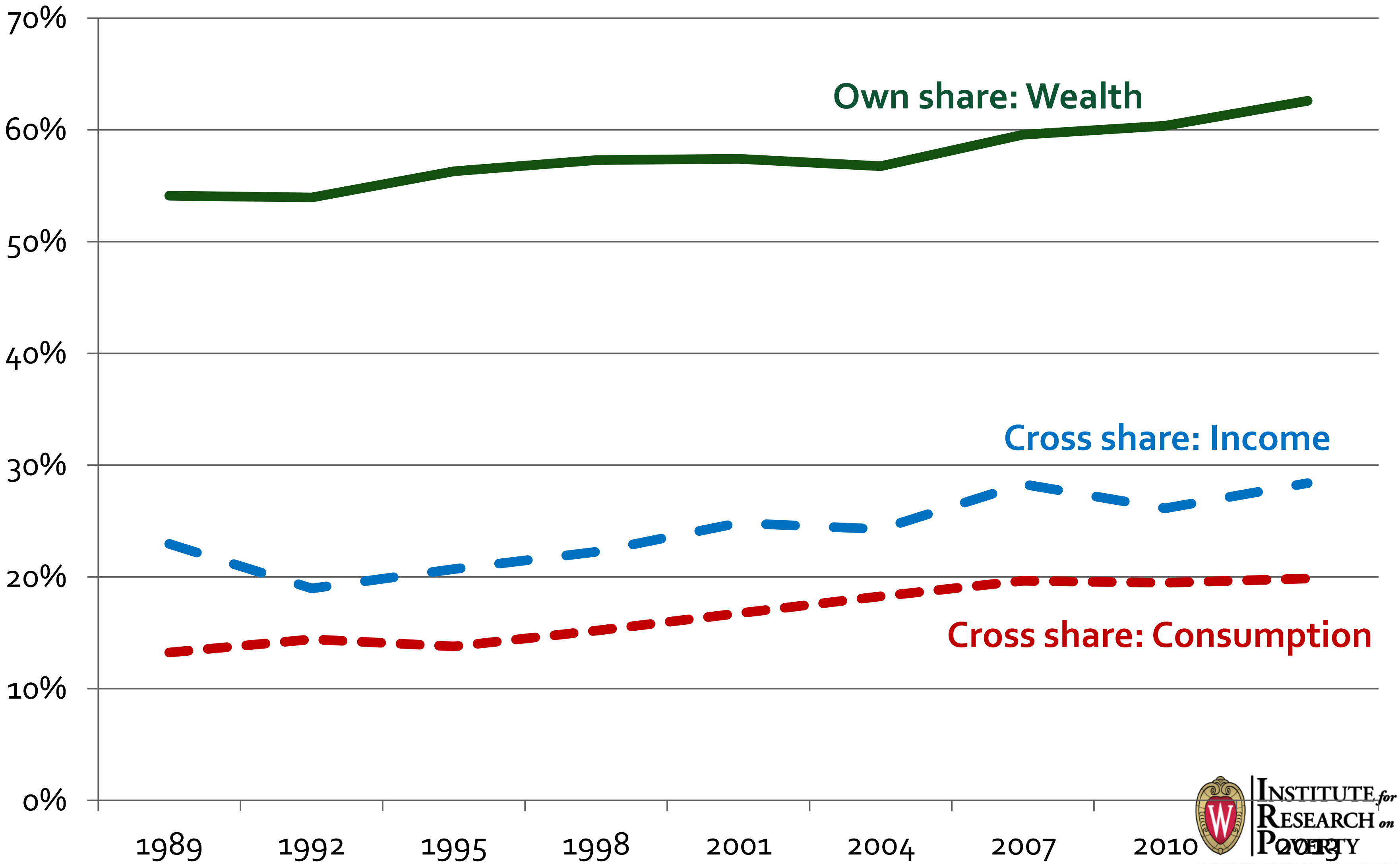
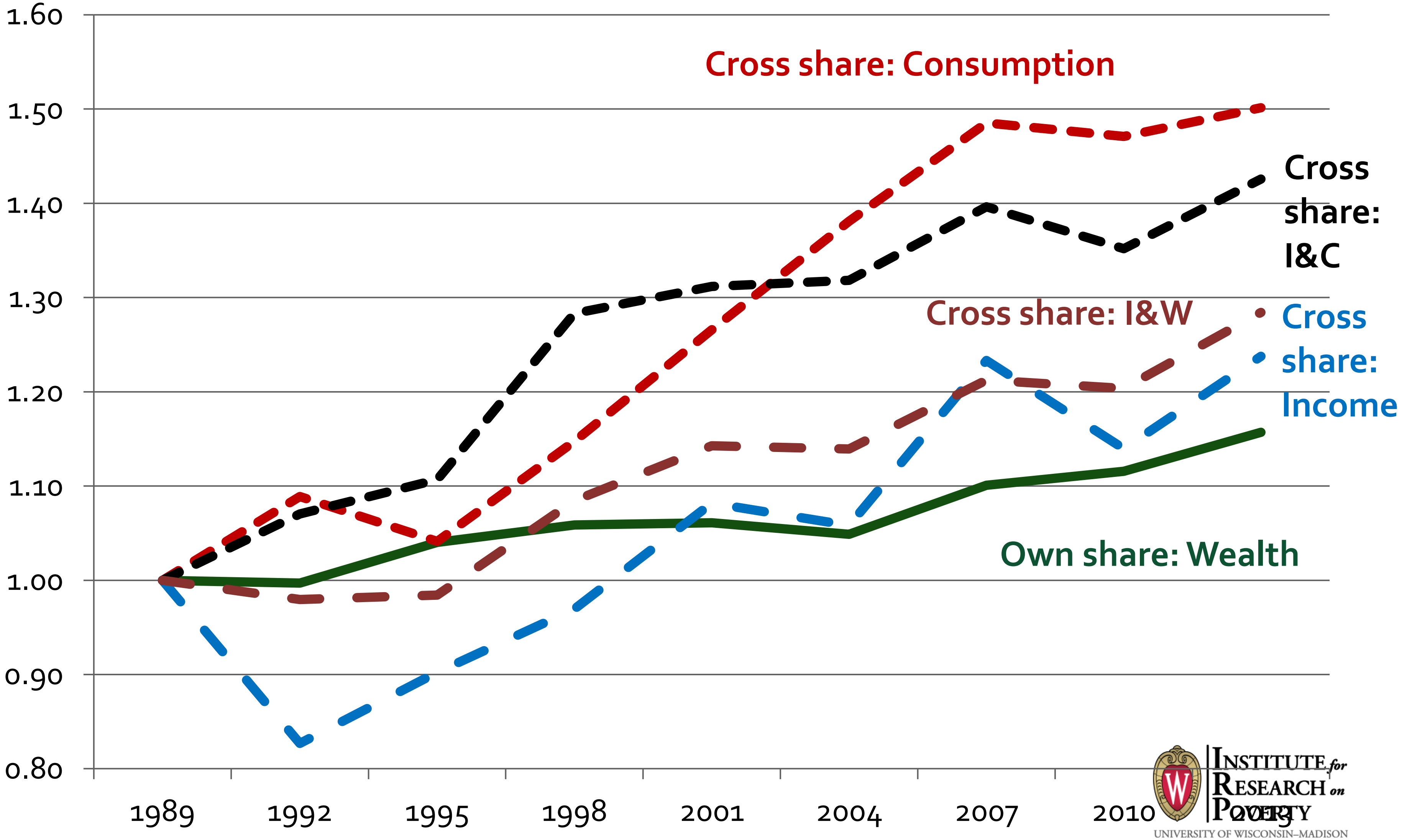
One dimensional(1D)--Wealth Shares (own and cross) for top 5% of Wealth, Income, and Consumption



2D Wealth Shares increase more than 1D own Wealth Shares



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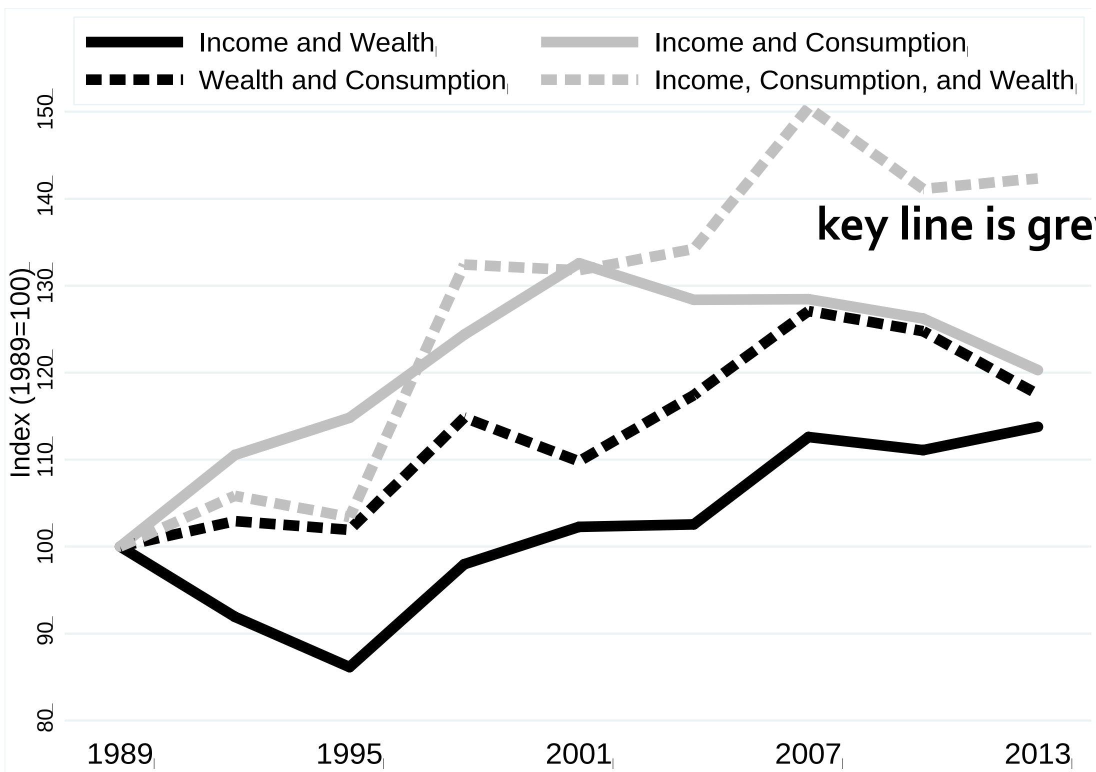
Inequality in 3 D --Percent of Households in Top 5% of Two or Three Measures (1989-2013)



key line is grey dotted one

C,Y & W together for same families-Question:

What fraction of all households that were in the top 5% of the income (Y) distribution, were also in the top 5% of the consumption (C) distribution and the top 5% of the wealth (NW) distribution year by year , 1989,2007, 2016 ?

C,Y & W together for same families

Answers :

1989-- 32 %

2007 -- 49 %

2016 -- 44% *

* **March 2016 (SCF)- January 2018, stock markets rose more than 30 % in USA, suggesting that the answer is now more than 50%**

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B. MOBILITY

1. Life course approach— where and how you grow up affects where you end up
2. Americans care much more about inequalities in opportunity—chances for the poor to move up—than inequalities in outcomes (income, wealth), even if they think the result unfair
3. Given trends in key parameters for child mobility, are we making progress ?

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Figure 1: A Model of Intergenerational Transmission of Advantage by Life Stage

*It is implicit in the model that outcomes at any life stage can be associated with outcomes at any subsequent life stage.

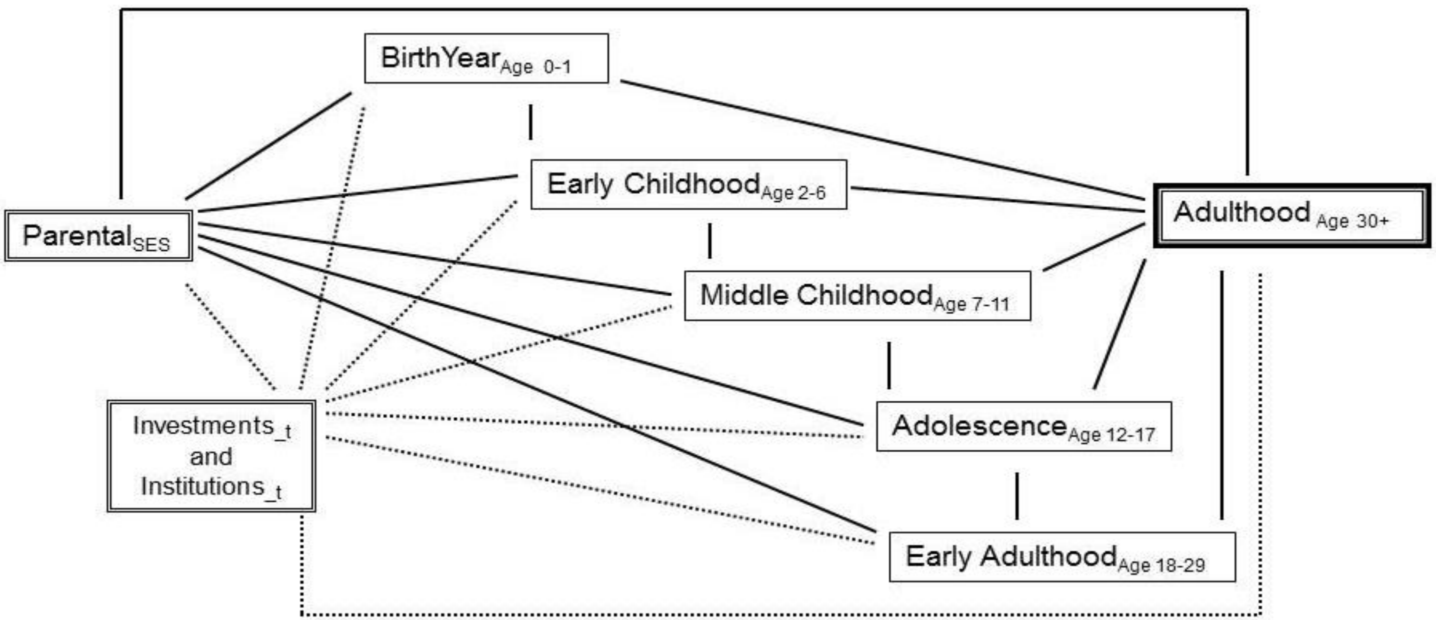

Table A. Variable Definitions and Examples of Proposed Measures at Different Points in the Life Course

Parental SocioEconomic Variables (Parental$_{SES}$) *Measures*: Education, Income, Earnings, SES, Occupation, Wealth, Employment	**Childhood/Early Adulthood Life Stages** BirthYear (age 0-1), Early Childhood (age 2-6) Middle Childhood (age 7-11), Adolescence (age 12-17), Early Adulthood (age 18-29) *Measures*: Educational attainment, cognitive measures, socio-emotional behavior, employment/labor market, health/physical	**Investments$_{_t}$ and Institutions$_{_t}$** Are assumed to be different public and private investments and institutions contributing to children's development that vary by country.	**Adulthood (Age 30+)** *Measures*: Child SES, Income, Education, Employment, Labor Market Attachment

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what are the key factors in child development based on these approaches ?

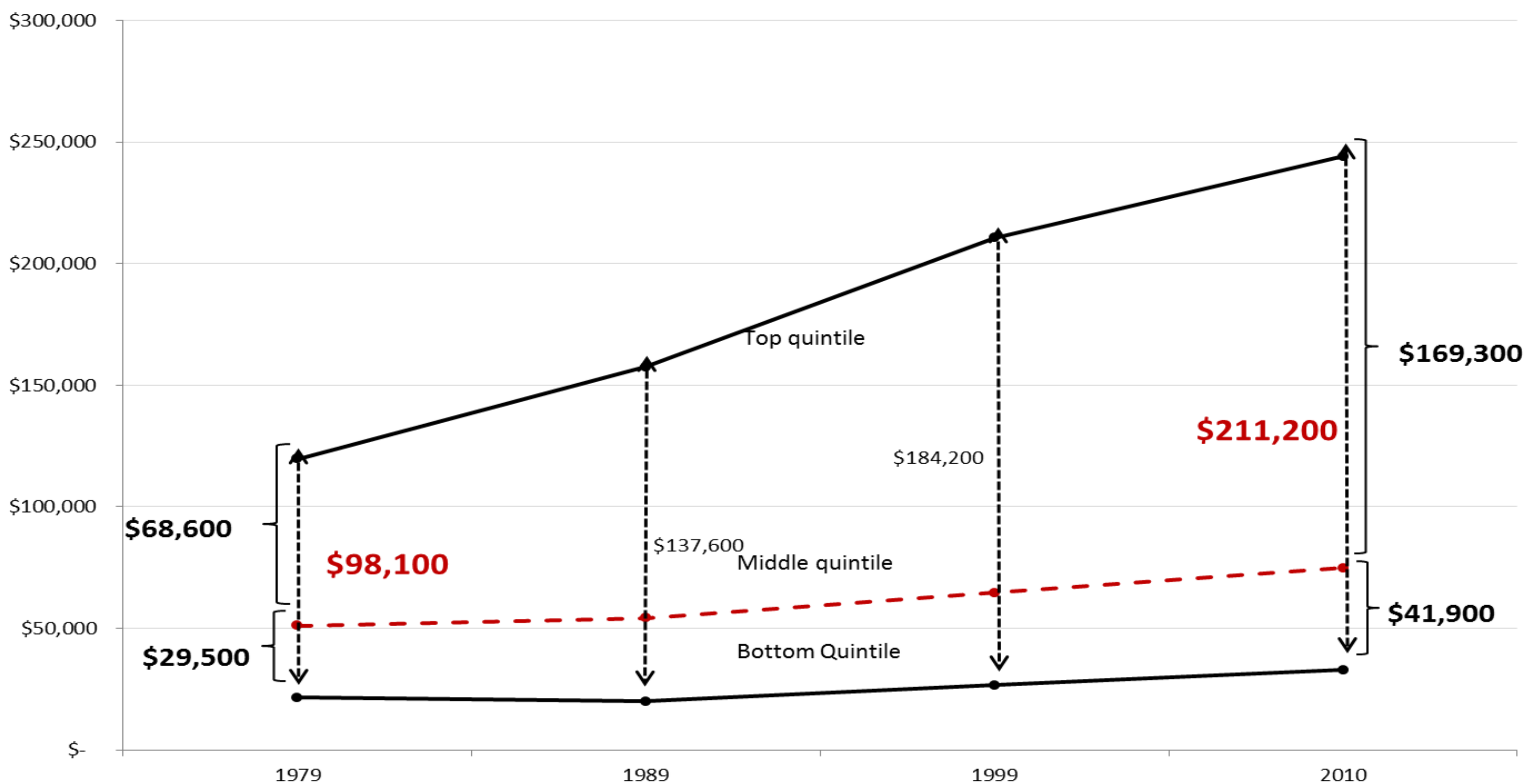
1. **Family status** early in life: ’diverging destinies hypothesis’ ,birth conditions, age and education of mom
2. **Parents and parenting:** stability of family; human and material resources available for kids
3. **Money: economic status of families (and growing inequality)**: differences in human capital returns mean big differences in financial ability to raise children and provide a private safety net (W and the “glass floor”)
4. **Social Institutions** : pay setting, education, health care
5. **Role of place**: amplifies parenting differences and money differences

The role of changing economic well being

- Incomes
- Wages
- Earnings (says incomes) of men vs earlier generations (fathers)
- Earnings of children vs their parents : percent kids who earn more
- Finally earnings and marriage

Mean CBO incomes for top, bottom , middle income US kids: 1979-2010

CBO after-tax income mean of bottom, middle, and top quintiles and gap in 2010 dollars, households with children



Source: http://www.cbo.gov/sites/default/files/cbofiles/attachments/44604-AverageTaxRates_Supplemental.xlsx

Gaps: middle vs. top income gap exceeds middle vs. bottom gap

- Middle (median family with children) is losing more ground vs. top than is bottom !
- Absolute & relative mobility are both important to the middle class their incomes have been flat or falling since 2008 (hence calls for 'inclusive growth', 'shared prosperity', etc.)
- Only top 5% or at most 20 % are winning
- 'Beyond BA' education wins big in the labor market

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Why? wages have diverged markedly by education level (*plus assortative mating*)

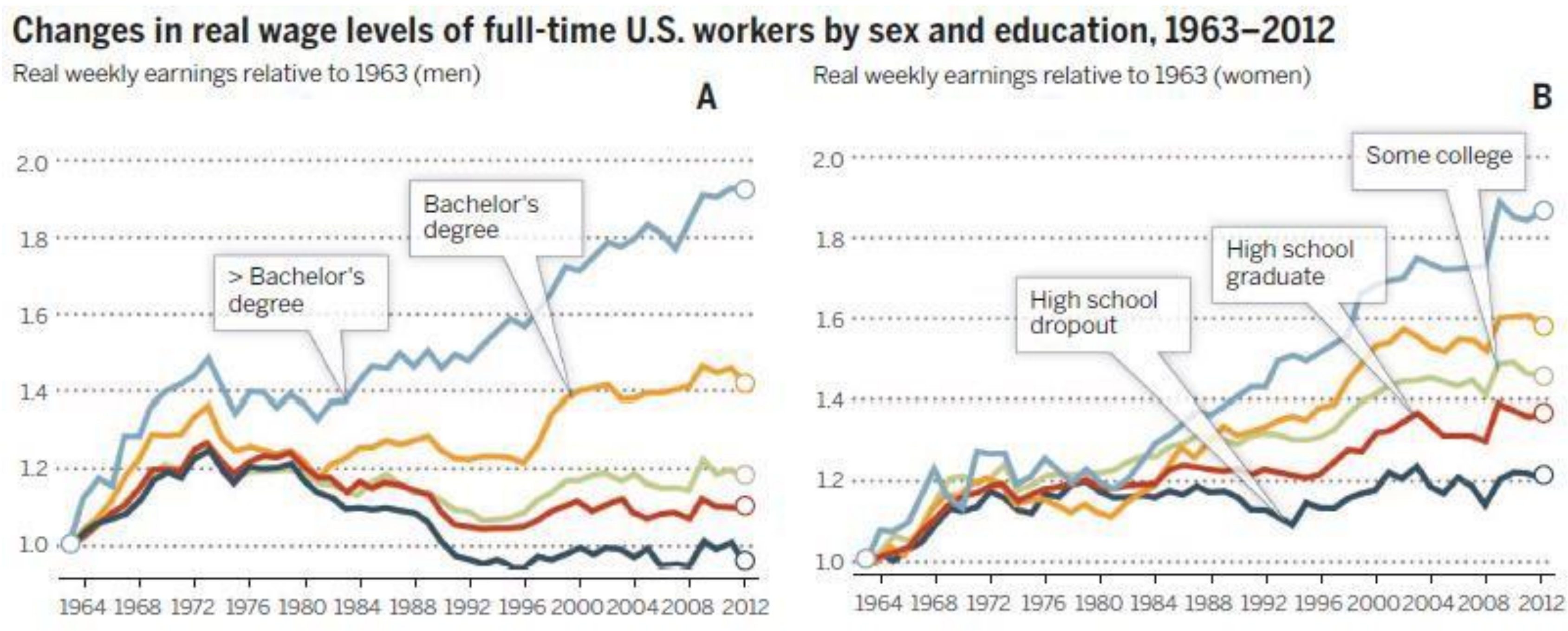
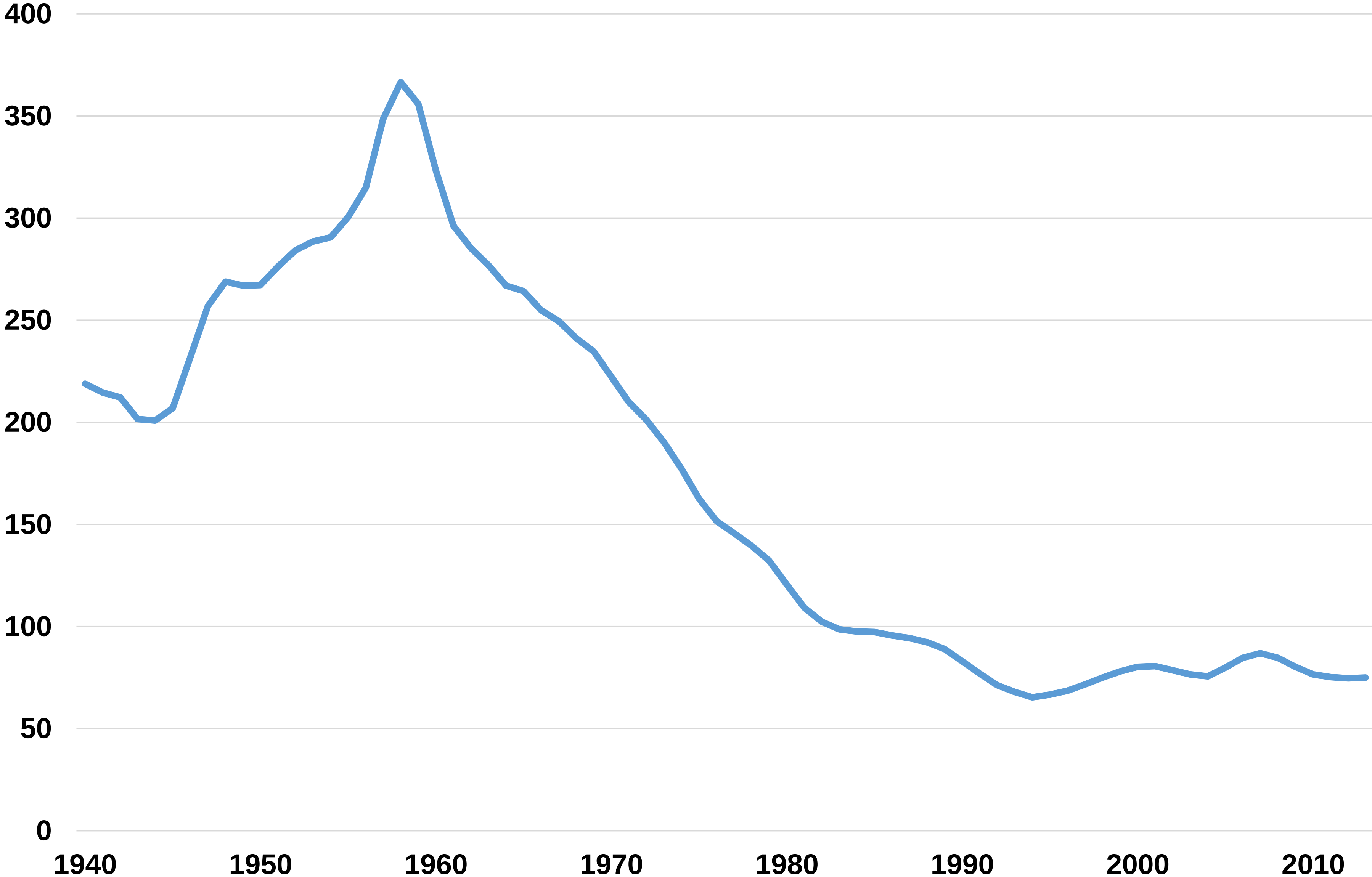


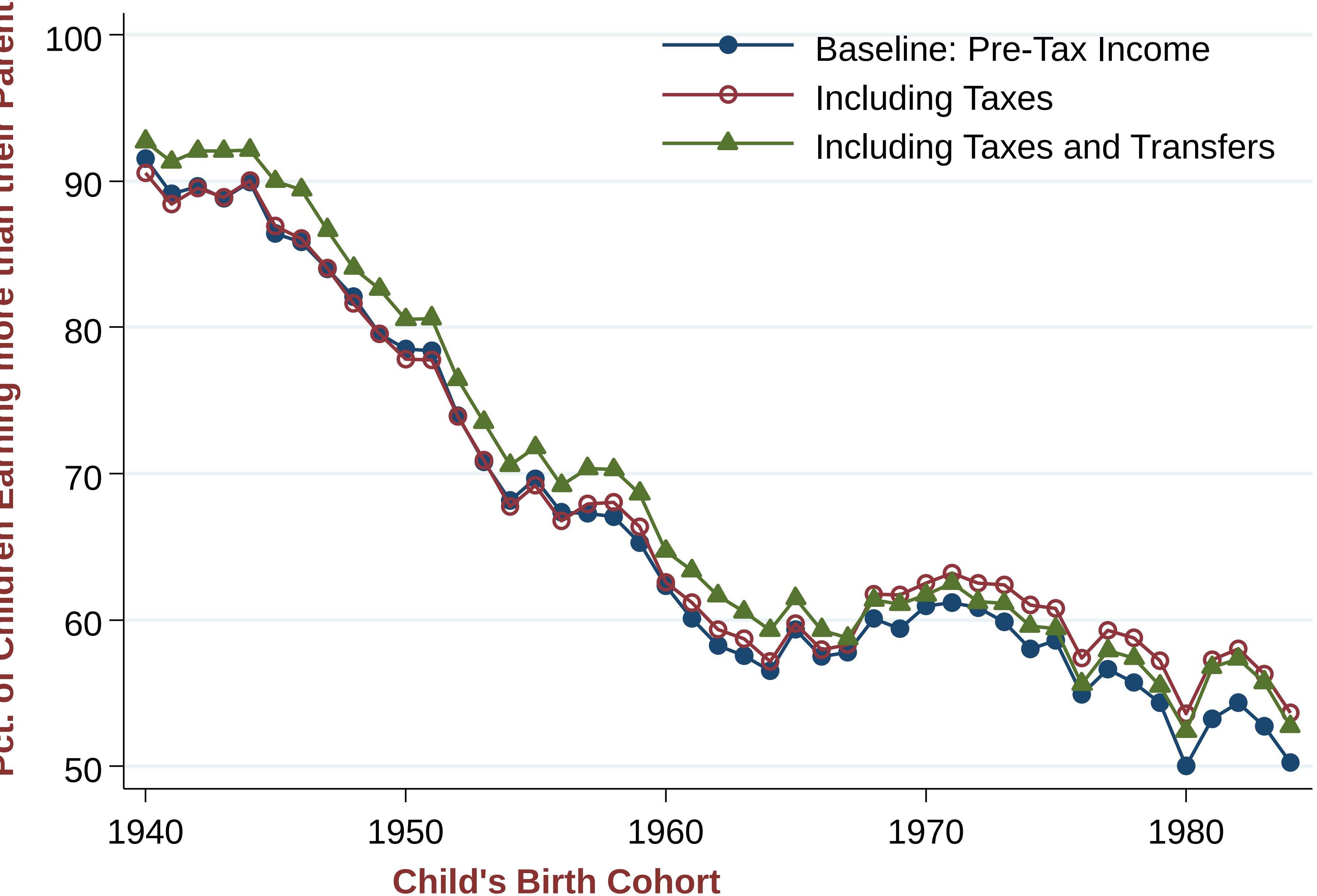
Fig. 6. Change in real wage levels of full-time workers by education, 1963–2012. (**A**) Male workers, (**B**) female workers. Data and sample construction are as in Fig. 3.

Autor, David H. 2014. "Skills, education, and the rise of earnings inequality among the 'other 99 percent'". *Science* 344(6186), pp. 843-851. Source is CPS

FALLING LIVING STANDARDS--Median income as a % of median income in previous generation (25 years before): US men age 25-29, 1940-2013

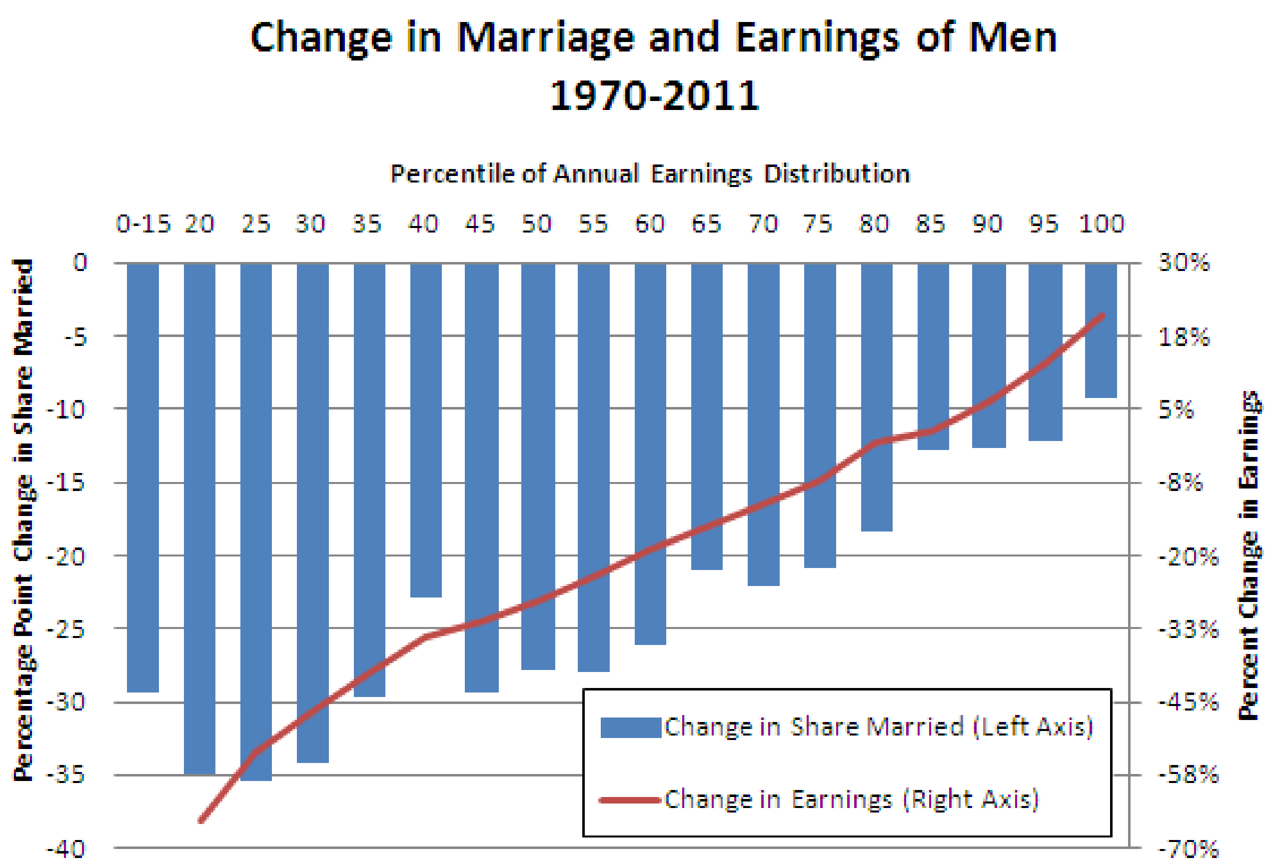


Trends in Children's Earnings vs. Their Parents



Source: Chetty et al "The Fading American Dream Trends in Absolute Income Mobility Since 1940

When Men's Earnings Fall, Marriage Falls



Sample includes non-institutionalized men, ages 30-50. The first income category on the x-axis includes all men with no earnings in 2010.
Source: IPUMS-CPS 1971,2011.

THE HAMILTON PROJECT

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So, what does poverty mean for intergenerational mobility, IGM ?

- If you are born into poverty, what helps you rise up and get out– to middle class ?

-- stable families (two married parents best)

-- smart parenting

-- avoid incarceration

-- stable job and rising earned income

-- good pre-school and schooling

-- safe neighborhoods and stable housing

- Nationally what do we find about mobility up from poverty ?

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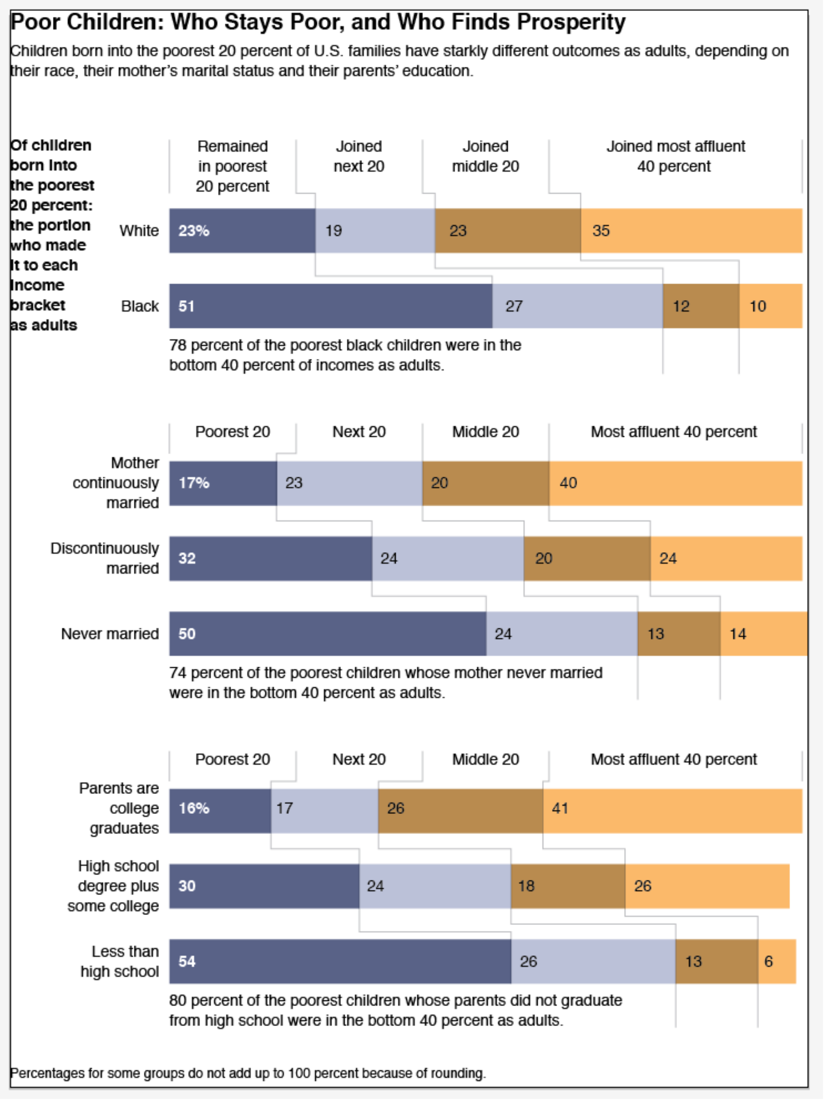
Who is stuck at the bottom ?



"Separated at Birth "
at http://nyti.ms/1WGfRD3

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Who is stuck at the top ? the corrosive effect of W on intergenerational mobility

- **Wealth is passed generation to generation in two forms :**
- **Inheritance -- only at death of oldest parent, so late in life**
- **In-vivos-- at key stages in life course, earlier on through key periods of human and physical capital formation**

(-note the **"glass floor"** at the top : child's neighborhood; education; co-sign mortgage ; free rent; subsidized internships; and often lifetime job in family firm)

So what? the "glass floor-rich kid " safety net-- inter-vivos "strategic transfers"

1. Parents buy an expensive home in a good safe school district with other amenities
2. Children graduate college and often post-grad degrees, with no debt
3. Children intern free or at Min wage in expensive cities & overcome high end spatial job mismatch
4. Parents help buy a first home at favorable interest rates by co-signing the mortgage
5. Plus direct lifetime jobs for kids (US,DK, and CN evidence on top 5 percent)

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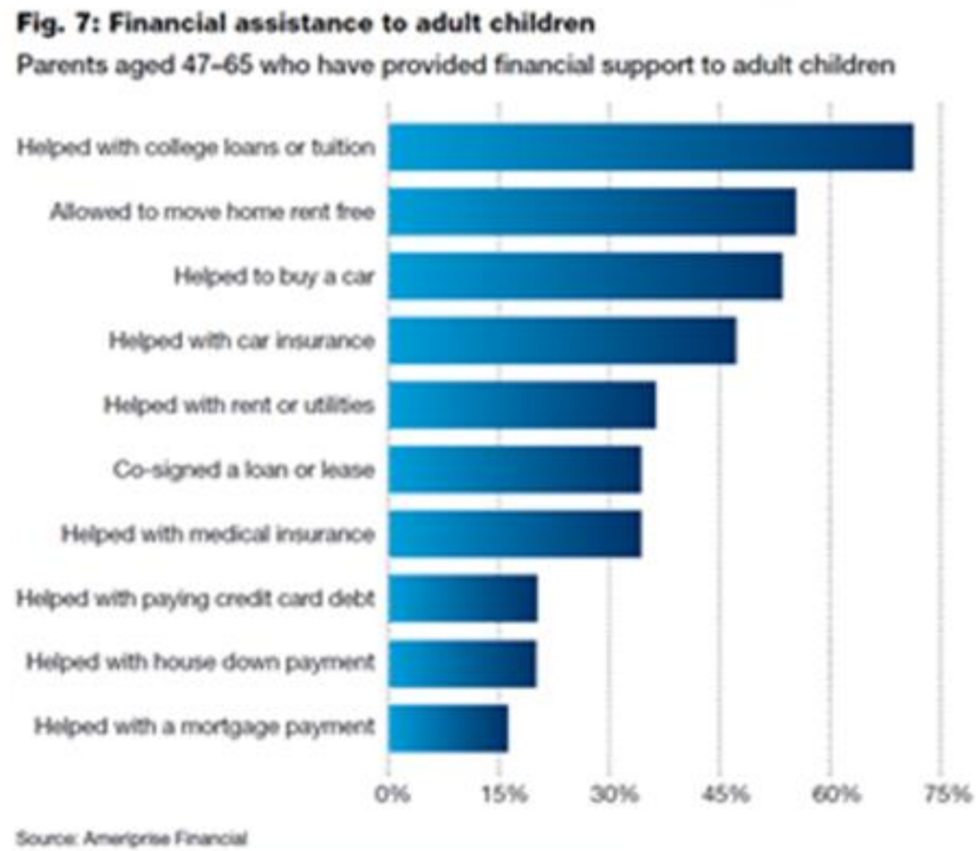
Intergenerational transfers and frequent and large and make a difference

Consider the source– but- see the numbers too



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C. POLICY -- what to do about IGM policy lessons-- modesty?

- It is *possible* to provide more equal life chances than is the case in the USA in ways that do not violate family autonomy.
- But there are also *limits* to such policies as parental influences are evident at every stage of the life course (rich 'buy out' of public goods, and are subsidized to do so in USA !!)
- Self-interested parents have reason to fight *against* such policies to give their children better advantages ; and so such polices are difficult to establish and after that, they will be difficult to sustain

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Policies to promote equality of opportunity face Fishkin's "trilemma"

Balance three widely supported values/principles:

1. **principle of merit** –society believes in procedural fairness in evaluating qualifications for school or jobs or other prizes (a "meritocracy", if you will)
2. **equality of life chances-** life chances or prospects for children should not vary systematically with any native characteristics (parental advantages ,SES, race, ethnicity)
3. **autonomy of the family** – one should not coercively interfere with parents except to ensure prerequisites for adult life and to provide safety for children

- **NOW try to find polices to promote "equality of opportunity" that satisfy all , bottom up only ?**

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Parental autonomy—what to do ?

- Reeves, *Dream Hoarders* ,

(see https://www.amazon.com/Dream-Hoarders-American-Leaving-Everyone/dp/081572912X , or watch https://seminarsatsteamboat.org/video-audio/ or wait till September for IRP presentation)

- **What comes to mind to try ?**

1. **Exclusionary zoning and housing access**
2. **BIG push on higher ed. –eg graduation rates**
3. **Paid internships for all– better access ?**
4. **Tax policy– or too European ?**

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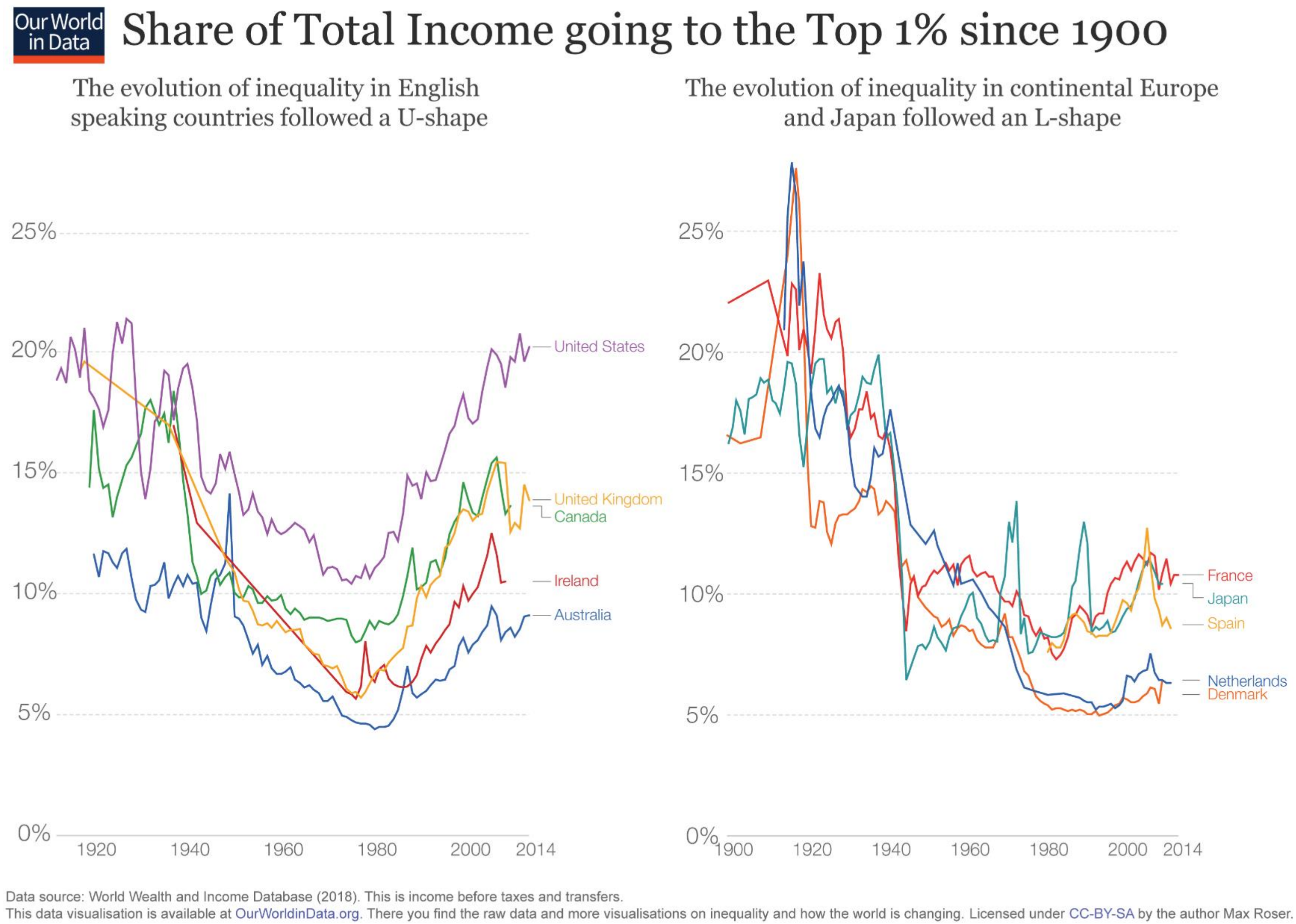
Lessons from cross-country data -ever growing top 1% share is *not* inevitable



C. POLICY—inequality, we can do better

Institutions matter:

- Public investment in human capital, especially for kids (health, education, upward mobility) ,how countries treat children is key
- Tax capital income (no K gains roll-over) same as labor income
- More widely shared profits –how owners treat valued workers will be important , esp. if scarce and highly productive
- Mandatory defined contribution pensions to all workers managed by third party (Australia and Denmark)
- Employer labor partnerships, post secondary education & training (eg German work sharing; Danish and EU 'ALMPs')
- Promote shared prosperity and inclusive growth, value firms for more than the bottom line (dignity of work, environment)
- Give labor a voice in political discourse

Some of my recent work—research on upward mobility

- **" How the Other Fifth Lives " at http://nyti.ms/1MYpeuy**
- Smeeding, Timothy. 2014. "Gates, Gaps, and Inter-Generational Mobility (IGM): The Importance of an Even Start" , in The Dynamics of Opportunity in America, pp. 255-295 at **http://link.springer.com/chapter/10.1007%2F978-3-319-25991-8_8**
- **"Separated at Birth " at http://nyti.ms/1WGfRD3**
- Smeeding, Timothy.2016. "Multiple Barriers to Economic Opportunity for the 'Truly' Disadvantaged and Vulnerable", *Russell Sage Foundation, Journal of the Social Sciences*, Volume: 2, Issue: 2, pp. 98-122 at http://www.rsfjournal.org/doi/full/10.7758/RSF.2016.2.2.04
- Brighouse, M . Harry , David O'Brien, Isabel Pike, and Timothy Smeeding . 2017 ." The costs of a well raised child", in preparation

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Some New anti-poverty policy papers

- **CA--** Shaefer, H. Luke, Greg Duncan. Kathryn Edin. Irv Garfinkel, David Harris, Tim Smeeding, Jane Waldfogel ,Chris Wimer, and Hiro Yoshikawa. 2016. "*Transforming the Child Tax Credit into a Universal Child Allowance (CA) for American Children"* (February 2017 Draft)
- **MBP--** Herd, Pamela, Melissa Favreault, Madonna Harrington Meyer and Timothy M Smeeding . 2016. "*Targeted Minimum Benefit Plan :A New Proposal to Reduce Poverty among the Elderly"* (February 2017 Draft)
- **Hard to Employ--** Smeeding, Tim. 2016. "How to Help the Hard to Employ: A Focus on Young Men, Especially the Ex- Incarcerated," in Michael R. Strain, ed. *The US Labor Market: Questions and Challenges for Public Policy,* American Enterprise Institute, Washington, October: pp 221-245
- **WOP** -Haveman, Robert, Rebecca Blank, Robert Moffitt, Timothy Smeeding, and Geoffrey Wallace. 2015. "The War on Poverty: Measurement, Trends, and Policy", *Journal of Policy Analysis and Management*, Summer, Volume 34, 3: 593–638

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Final set-- inequality in 3-D

- Fisher, Johnson, Latner, Smeeding, and Thompson, "Inequality and Mobility using Income, Consumption, and Wealth for the Same Individuals," in *Russell Sage Foundation Journal of the Social Sciences*, 2016-- uses PSID http://www.rsfjournal.org/doi/pdfplus/10.7758/RSF.2016.2.6.03
- Fisher, Johnson, Smeeding and Thompson, "Synergies in the Distributions of Income, Consumption and Wealth," Presented at the Washington Center for Equitable Growth Grantees Conference and PSID User Conference, Sept 2016. ---*shows how MPC differs by wealth*
- Fisher, Johnson, Smeeding and Thompson, ""The Demography of Inequality: Income, Consumption, and Wealth, 1989-2013" Presented at PAA 2016-- *and uses SCF and CE*
- Fisher, Johnson, Smeeding and Thompson, "Inequality in 3D: Income, Consumption, and Wealth" March, 2017 —*uses SCF and CE under review at QJE*

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