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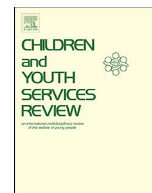

Unequal returns: Intragenerational asset accumulation differs by net worth in early adulthood

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ABSTRACT

We use quantile regression models of Panel Study of Income Dynamics (PSID) data to assess whether initial net worth moderates the relationship between initial economic standing (net worth and income) and later net worth (measured in 2011). Conditional quantile regression results suggest the returns to an increase in 1989 net worth or income vary substantially between the 25th, 50th, and 75th percentiles of 1989 net worth, with higher returns among those with higher initial net worth. Thus, financial improvement appears to generate different outcomes depending on initial net worth. These results suggest that helping families build an asset foundation may increase the efficacy of interventions that increase family income.

1. Introduction

Deeply rooted in the fabric of American culture, the American dream is something research suggests Americans of all socioeconomic classes believe is within reach (Samuel, 2012; Smith, 2017). In its simplest form, the American dream is the belief that success—sometimes operationalized as financial well-being—is a result of effort and hard work, coupled with ability (Rank, Hirschl, & Foster, 2014). The American Dream further holds that every American has an equal opportunity to secure this financial outcome. The American dream has a powerful hold over our social welfare policies, particularly those which undergird the U.S. economic mobility budget (i.e., the money spent to help people climb from one income level to the next).

Research conducted by the Pew Charitable Trusts (2013) finds that 45% of Americans who are born into the bottom income quintile remain stuck there as adults; 70% never make it to the middle income quintile. Similarly, Chetty, Friedman, Saez, Turner, and Yagan (2017) find that an American born in 1980 has only about a 50% chance of out-earning his/her parents, which is far less than an American born in 1940 (Chetty et al., 2017). Maybe even more concerning, some regions of the country seem to be trending toward downward mobility, giving young people in these communities little chance at the American Dream (Chetty et al., 2017). This raises questions about the reality of the American dream for children born into low-income families. Why is there so little economic mobility? While educational (Brown, Buchholz, Davis, & Gonzalez, 2016; Chetty et al., 2017) and employment (Hanushek & Woessman, 2017) policies have been given a lot of attention in economic mobility research, policies that facilitate wealth accumulation among low-income families have been given much less attention (Piketty, 2014).

Wealth accumulation—and the lack thereof—may be a significant part of the story of economic mobility in America today. According to the Pew Charitable Trusts (2013), families with liquid savings or other assets such as stocks are more likely to move out of the bottom income quintile than those without fungible assets (i.e., assets that are easy to turn into cash). Coupled with earlier evidence of less intergenerational mobility at the top and bottom of the socioeconomic ladder (Featherman & Hauser, 1978), these findings suggest wealth might be an important, understudied, factor for understanding economic mobility in America (Piketty, 2014; Shapiro, 2017).

In this study we use longitudinal data from the Panel Study of Income Dynamics (PSID) to examine whether initial net worth held by families headed by younger adults is associated with net worth held in later adulthood. We also examine whether the ability of income to generate future wealth is moderated by initial net worth. If initial net worth is positively associated with future net worth and income's power to generate future wealth is explained by initial net worth holdings, low-income families might be more likely to move out of poverty if they also had access to policies that facilitate wealth accumulation, even if their incomes remain low enough to keep them 'officially' poor. Evidence of this would suggest that wealth accumulation facilitates economic security, even for those with relatively constrained earning

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potential. These questions are increasingly salient in an economy where many low-income households find themselves constrained in income earnings by trends that have eroded the value of labor and led to stagnation of wages for all but the wealthiest Americans (Mishel & Shierholz, 2013).

2. Low-income families and the income maintenance welfare system

America's reliance on an income maintenance model of welfare, where one's well-being is tied to the income available to secure consumption, appears to align well with the notion that effort and ability determines outcomes. This is because there is a commonly held notion that the amount of income a person earns is a sign of the amount of hard work and ability the individual has put into his or her work (i.e., people who earn more must work harder and have more ability than those who earn less) (e.g., Attanasio, Hurst, & Pistaferri, 2013). Therefore, by definition, poor people are not hard-working and/or have limited ability while wealthy people are hardworking and have the necessary ability. Therefore, if poor people are provided with any more than a subsistence level of goods and services, this intervention is seen as providing them with a disincentive to seek out work, potentially dooming them to an endless cycle of poverty. These beliefs persist despite evidence to refute them (Porter, 2015: Widerquist, 2005). Maybe one reason these beliefs persist despite evidence refuting them is that the understanding of poverty and welfare in America is intimately intertwined with their racialization of them (e.g., Gilens, 1999). As such, it is less about facts, and more about the historically legacy of race in America that makes them particularly resistant to evidence.

There is also the perception that people should not be rewarded for their failures. Therefore, the way out of poverty is through providing incentives to increase the poor's incomes by working harder and increasing their 'ability' (through human capital development). The welfare system for the poor reflects this approach, consisting of such means-tested programs[1] as the Temporary Assistance for Needy Families (TANF), Supplemental Nutrition Assistance Program (SNAP), Medicaid, and the Earned Income Tax Credit (EITC). The eligibility criteria for these programs typically prohibit significant wealth accumulation, viewing wealth as a source of potential consumption, rather than a store distinct from income flows. However, it is also important to point out, that these policies increasingly include not only work participation requirements (recently ruled admissible even in Medicaid, where they were previously denied), but also rules that specifically define 'work' as not including educational attainment thereby undermining the human capital development route out of poverty.

Asset limits require poor families to keep their financial (i.e., types of liquid assets) and vehicle (i.e., a type of illiquid asset) assets below limits set by federal or state governments in order to qualify for welfare benefits. These limits are viewed as not only morally appropriate, because aid should be reserved only for the most destitute, but also pragmatic, since poor households are assumed to be unable to save anyway, since their 'left over' or 'discretionary' income is very limited, after meeting subsistence requirements. Indeed, saving could theoretically be harmful to individuals in poverty, since any money they might take for building wealth results in them having to neglect purchasing goods and services required to meet vital subsistence needs. In this way, asset limits might be seen as both paternalistic and punitive, establishing very different expectations for how low-income households will accumulate wealth than what policy assumes for higher earners.

Research suggests, however, that this belief may reflect a misunderstanding about saving and poor households. The asset limits themselves shape asset accumulation (e.g., Nam, 2008). More liberal asset limits encourage greater wealth accumulation while stricter asset limits discourage asset accumulation (Nam, 2008). Therefore, asset limits may provide a disincentive to save (Nam, 2008). Additionally, asset limits may also discourage families who own assets but are income poor from taking advantage of much needed income maintenance programs such as SNAP. Huang, Nam, and Wikoff (2012) find that owning a home, vehicle or a bank account is negatively associated to participation in SNAP despite being eligible for the program. In multiple ways, then, low-income families may receive a message that wealth accumulation is potentially against their economic best interests.

Since saving, or more broadly wealth accumulation, is a potentially key component to moving out of poverty (Pew Charitable Trusts, 2013; Piketty, 2014; Shapiro, 2017), the structure of the income maintenance welfare system may, in itself, serve to prevent economic mobility among those poor enough to depend on it. And while the purpose of the welfare system designed for the poor is to provide them with assistance that allows them to meet basic subsistence needs, a different welfare system exists for middle- and upper-income families. In contrast to that which serves low-income households, this system is focused on economic mobility and social development through asset accumulation, preservation, and transfer.

3. Middle- and upper-income families and the asset-maintenance welfare system

There is a bifurcated welfare system in the U.S.: one branch primarily focuses on the ability of the poor to consume goods, while the other primarily focuses on the ability of middle- and upper-income families to accumulate wealth (Howard, 1997; Sherraden, 1991). In contrast to direct appropriations for means-tested programs, the asset-based welfare system is largely based on tax expenditures (e.g., tax deductions, tax credits, and preferential tax rates). Unlike income, which is a flow of money usually, assets are resources kept through time. In talking about why wealth matter, Oliver and Shapiro (2006) state, "the reality for most families is that income supplies the necessities of life; while wealth represents a kind of 'surplus' resource available for improving life chances, providing further opportunities, securing prestige, passing status along to one's family, and influencing the political process" (p. 32). Empirical research has suggested that wealth may be important for children's early social and emotional development (Huang, Kim, & Sherraden, 2016; Huang, Kim, Sherraden, & Clancy, 2017; Huang, Sherraden, Kim, & Clancy, 2014) and educational attainment (Elliott, 2013a; Zhan & Sherraden, 2011), as well as for other outcomes that influence long-term well-being. Therefore, we suggest that access to an income maintenance welfare system or an asset maintenance welfare system may yield widely diverging family trajectories.

3.1. Some ways that middle- and upper-income families have benefited

Accumulating wealth is not purely an individual act determined solely by human capital or even social background; it also requires access to the capabilities financial institutions provide (Sherraden, 1991). The primary way people gain access to financial institutions is through social policies. Prominent examples in the U.S. include the policies of the Federal Housing Administration (FHA) during the 1960s, which changed the rules of the game for buying a home (outside of redlined neighborhoods) by lowering the amount of down payment (from 90% of the price of the home to 10%), thereby facilitating wealth accumulation in the form of real property. Similarly, the GI Bill made mortgages available to some World War II veterans with no down payment and provided them with money for college. However, crucially, these and other policies provide varying levels of access to institutions and the opportunities they afford (Katznelson, 2005; Turner & Bound, 2003). Therefore, we suggest, that policy shapes individual

[1] Means-tested programs have income and asset limits as part of their eligibility requirements.

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