Economic Mobility and the American Dream

Robert Manduca
NCSL Annual Meeting
8/9/17
What is the American Dream?
What is the American Dream?

Let’s ask some Presidents...
What is the American Dream?

“They tell us we must learn to live with less, and teach our children that their lives will be less full and prosperous than ours have been; that the America of the coming years will be a place where — because of our past excesses — it will be impossible to dream and make those dreams come true. I don't believe that. And, I don't believe you do either. That is why I am seeking the presidency”

—Ronald Reagan, Announcement of Presidential Candidacy, 1979
What is the American Dream?

“We'll think of the faith of our parents that was instilled in us here in America, the idea that if you work hard and play by the rules, you'll be rewarded with a good life for yourself and a better chance for your children... Many of us can remember our own parents working long hours on their jobs and then coming home and helping us with our homework. The American dream has always been a better life for people who are willing to work for it.”

–Bill Clinton, Labor Day Address, 1993
What is the American Dream?

“[W]e know that people’s frustrations run deeper than these most recent political battles. Their frustration is rooted in their own daily battles -- to make ends meet, to pay for college, buy a home, save for retirement...And it’s rooted in the fear that their kids won’t be better off than they were. They may not follow the constant back-and-forth in Washington or all the policy details, but they experience in a very personal way the...lack of upward mobility that has jeopardized middle-class America’s basic bargain -- that if you work hard, you have a chance to get ahead”

–Barack Obama, Remarks on Economic Mobility, 2013
Economic mobility is central to the American Dream

Republican and Democratic presidents agree:

• The US is a place where everyone has or should have the chance to move up economically, if you work for it
• Your kids should grow up to be materially better off than you were
• Americans expect equal opportunity, not necessarily equal results
• “The Land of Opportunity”
• “A better life for your children”
## Two types of economic mobility

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- Relative Mobility:
  - Mobility in rank
  - Can poor children grow up to be rich?
  - Measures how open or fluid a society is
  - Zero-sum
Two types of economic mobility

Relative Mobility
• Mobility in rank
• Can poor children grow up to be rich?
• Measures how open or fluid a society is
• Zero-sum

Absolute Mobility
• Mobility in dollars
• Are kids better off than their parents?
• Measures whether a society is becoming more prosperous
• Not zero-sum
Two types of economic mobility

Relative Mobility

Absolute Mobility
Two types of economic mobility

Relative Mobility

Absolute Mobility
Societies with higher absolute mobility are more:

- Open
- Generous
- Pragmatic
- Committed to fairness
- Tolerant
- Committed to democracy

Study 1: Trends in US Absolute Mobility Over Time

RESEARCH ARTICLE

The fading American dream: Trends in absolute income mobility since 1940

Raj Chetty¹*, David Grusky²*, Maximilian Hell², Nathaniel Hendren³*, Robert Manduca⁴, Ji...
+ See all authors and affiliations

Science 24 Apr 2017:
eaal4617
DOI: 10.1126/science.aal4617
Percent of Children Earning More than their Parents
By Parent Income Percentile

Parent Income Percentile (conditional on positive income)
Pct. of Children Earning more than their Parents

1940
1950
Percent of Children Earning More than their Parents
By Parent Income Percentile

Pct. of Children Earning more than their Parents
Percent of Children Earning More than their Parents
By Parent Income Percentile

Pct. of Children Earning more than their Parents vs. Parent Income Percentile (conditional on positive income)
Mean rates of upward absolute mobility over time: Percentage of children who grow up to earn more than their parents did.
Sensitivity Analysis

Result that absolute mobility has declined sharply since 1940 is robust to key specification choices:

1. Alternative measures of inflation
2. Using post-tax and transfer incomes
3. Measuring income at age 40 rather than 30
4. Using individual rather than family income
5. Adjusting for changes in household size
What is behind the decline in absolute mobility?

- The decline in absolute mobility is primarily due to wage stagnation since the 1970s
- About 30% due to slower growth, 70% due to incomes not keeping up with growth (inequality)
- Can revisit during Q&A
Our Broken Economy, in One Simple Chart

By DAVID LEONHARDT
AUG. 7, 2017

The poor and middle class used to see the largest income growth.

But now, the very affluent (the 99.999th percentile) see the largest income growth.

Note: Inflation-adjusted annual average growth using income after taxes, transfers and non-cash benefits.
The poor and middle class used to see the largest income growth.

But now, the very affluent (the 99.999th percentile) see the largest income growth.

Note: Inflation-adjusted annual average growth using income after taxes, transfers and non-cash benefits.
Takeaways from study 1

• Rates of upward absolute income mobility have fallen from approximately 90% for the 1940 birth cohort to roughly 50% for young adults today

• This is primarily due to wage stagnation since the 1970s
Study 2: The Geography of Relative Mobility

THE QUARTERLY JOURNAL OF ECONOMICS

EDITOR'S CHOICE

Where is the land of Opportunity? The Geography of Intergenerational Mobility in the United States

Raj Chetty, Nathaniel Hendren, Patrick Kline, Emmanuel Saez

Published: 14 September 2014
Relative Mobility in the United States, 1980-82 cohorts

Rank-Rank Slope (U.S) = 0.341 (0.0003)
Relative Mobility varies across regions of the country

Salt Lake City: \( Y_{100} - Y_0 = 26.4 \)

Charlotte: \( Y_{100} - Y_0 = 39.7 \)
Places have childhood exposure effects: the longer you live there, the closer your outcome becomes to those of permanent residents, until about age 24.

Coefficient on Predicted Rank in Destination

Slope: -0.038 (0.002)
Slope: -0.002 (0.011)
Geographic variation in upward mobility: Predicted effects of growing up in different parts of the country on income at age 26

Note: Estimates represent % change in earnings from growing up from birth (i.e. 20 years of childhood exposure) in Commuting Zone for children with parents at the 25th percentile of the national income distribution.
Thank you!

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Papers and data are available at www.equality-of-opportunity.org
Copula Robustness
Bounds on Absolute Mobility Across All Copulas

Pct. of Children Earning more than their Parents

Child's Birth Cohort

Copula Observed
Explaining mechanics of absolute mobility
Household Income Distributions of Parents and Children at Age 30
For Children in 1940 Birth Cohort

- 14th percentile of children's distribution
- 80th percentile of parents distribution

Income (Measured in Real 2014$)
Household Income Distributions of Parents and Children at Age 30
For Children in 1980 Birth Cohort

- 74th percentile of children's distribution
- 80th percentile of parents distribution

Income (Measured in Real 2014$)
Child Rank Required to Earn More Than Parents

- 1940
- 1980
- (80, 14)
- (80, 74)
Note: Darker colors represent higher density in copula.
Counterfactuals
What policies can reverse the decline in absolute mobility?

• Two key macroeconomic changes since 1940: lower GDP growth rates and less equal distribution of growth

• Consider two counterfactual scenarios for children born in 1980:
  1. **Higher growth**: growth rate since birth corresponding to 1940 cohort, with GDP distributed across households as it is today
  2. **More equal growth**: Same GDP growth as today, but GDP distributed across income percentiles as in the 1940 cohort
What has driven the decline in upward mobility?

Two key macroeconomic changes in the US since 1940:
  • Lower GDP/productivity growth
  • Decoupling of productivity and wages (higher inequality)
What has driven the decline in upward mobility?

Source: Economic Policy Institute, “Understanding the Historic Divergence Between Productivity and a Typical Worker’s Pay”, 9/2/15
What has driven the decline in upward mobility?

Two key macroeconomic changes since 1940:

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Counterfactual Rates of Absolute Mobility by Parent Income Percentile

Pct. of Children Earning more than their Parents

Parent Income Percentile (conditional on positive income)
Counterfactual Rates of Absolute Mobility by Parent Income Percentile

Pct. of Children Earning more than their Parents

Parent Income Percentile (conditional on positive income)

1940 Empirical
Mean AM: 91.5%

1980 Empirical
Mean AM: 61.9%

1940 GDP/family growth rate (2.5%), 1980 income shares

Mean AM: 50.0%

1980 GDP/family growth rate (2.5%), 1980 income shares
Counterfactual Rates of Absolute Mobility by Parent Income Percentile

Pct. of Children Earning more than their Parents

Parent Income Percentile (conditional on positive income)

Mean AM: 91.5%
Mean AM: 79.6%
Mean AM: 61.9%
Mean AM: 50.0%

1940 Empirical
1980 Empirical

1980 GDP/family growth rate (1.5%), 1940 income shares
1940 GDP/family growth rate (2.5%), 1980 income shares
Absolute Mobility Under Counterfactual Growth Rates
Growth Distributed According to GDP Shares for 1980 Cohort
Sensitivity Analysis
Result that absolute mobility has declined sharply since 1940 is robust to key specification choices

1. Using alternative price deflators
2. Using post-tax and transfer incomes
3. Measuring incomes at age 40 instead of 30
4. Using individual income instead of family income
5. Adjusting for changes in household size
6. Accounting for fringe benefits and income under-reporting
Trends in Absolute Mobility: Alternative Price Deflators

Pct. of Children Earning more than their Parents

- Baseline: CPI-U-RS
- CPI-U-RS minus 0.8%
- CPI-U-RS minus 2%

Child's Birth Cohort


Baseline: CPI-U-RS
CPI-U-RS minus 0.8%
CPI-U-RS minus 2%
Trends in Absolute Mobility: Alternative Price Deflators

- Baseline: CPI-U-RS
- GDP Deflator
- PCEPI
- CPI-U

Pct. of Children Earning more than their Parents

Child's Birth Cohort

Trends in Absolute Mobility: Including Taxes and Transfers

Pct. of Children Earning more than their Parents

Baseline: Pre-Tax Income
Including Taxes
Including Taxes and Transfers

Child's Birth Cohort

Trends in Absolute Mobility: Income Measured at Age 40

- **Baseline:** Children Age 30, Parents 25-35
- **Children Age 40, Parents 35-45**

<table>
<thead>
<tr>
<th>Year</th>
<th>Pct. of Children Earning more than their Parents</th>
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<tbody>
<tr>
<td>1940</td>
<td>90</td>
</tr>
<tr>
<td>1950</td>
<td>80</td>
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<tr>
<td>1960</td>
<td>70</td>
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<tr>
<td>1970</td>
<td>60</td>
</tr>
<tr>
<td>1980</td>
<td>50</td>
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Trends in Absolute Mobility: Individual Income, Sons vs. Fathers

- Pct. of Children Earning more than their Parents
- Child's Birth Cohort
- Baseline
- Son vs. Father Individual Income

Graph showing trends in absolute mobility from 1940 to 1980.
Trends in Absolute Mobility: Adjusting for Family Size

- Baseline: No Adjustment
- Divide by Family Size
- Divide by Sqrt(Family Size)

Pct. of Children Earning more than their Parents

Children's Birth Cohort:
- 1940
- 1950
- 1960
- 1970
- 1980
Why does absolute mobility matter?

• Measures whether people’s lives are improving materially
• Societies with high rates of absolute mobility tend to be nicer places to live:
  • More open
  • More generous
  • More committed to fairness
  • More tolerant
  • More pragmatic
  • More committed to democracy, the environment, worker safety...


• Intuitively, it’s easier to be more generous if the pie is growing
  • If most people feel their lives are getting better, they can afford to care about others, society, higher ideals, etc.