



Real Time Economics

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WHY WEALTH INEQUALITY IS WAY MORE COMPLICATED THAN JUST RICH AND POOR

By Josh Zumbrun
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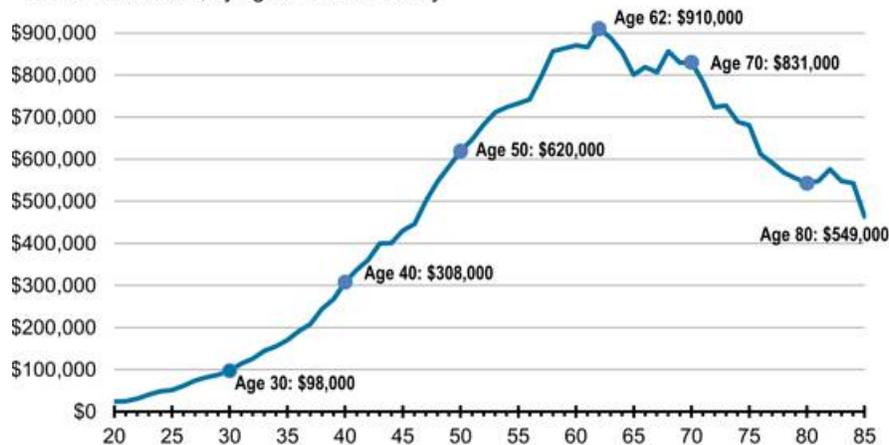
When economists talk about wealth inequality, they often focus on the gap between the rich and the poor. But to understand what's really happening in the U.S., they ought to talk more often about the gap between the young and the old, and between different races.

A new paper from Federal Reserve economists Jeffrey Thompson and Gustavo Suarez provides a detailed look at patterns of wealth in America. Anyone who's thought much about wealth in the U.S. probably has realized that the old are richer than the young and whites are richer than blacks and Hispanics, but the extent of the discrepancies uncovered by Mr. Thompson and Mr. Suarez's research could be startling.

First, consider this anxiety-inducing chart that shows the average net worth of people at every age.

Asset Building

Average family net worth, defined as the value of all assets like cash, stock and homes minus all liabilities, by age of head of family*



*Three-year moving average. Source: Federal Reserve | WSJ.com

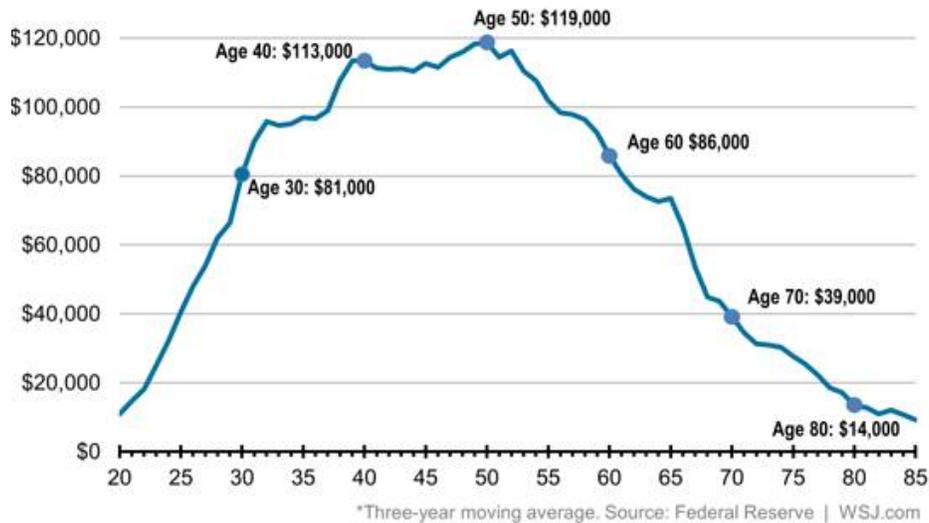
On average, wealth climbs with age. The average 20-something doesn't have much in terms of assets. The average 62-year-old is nearly a millionaire. These are averages, and so they are skewed by the very rich, but the underlying point remains: For the most part, people don't start out rich, they become that way over time.

In order to keep up with the average, you need to accumulate about \$100,000 in your 20s, an additional \$200,000 in your 30s, and then top it off with \$300,000 more in both your 40s and 50s. American net worth peaks at age 62 and declines as people retire and start to live off their savings.

The average American has a distinct debt cycle based on their age, too.

Borrowing Years

Average family's total debt, by age of head of family*

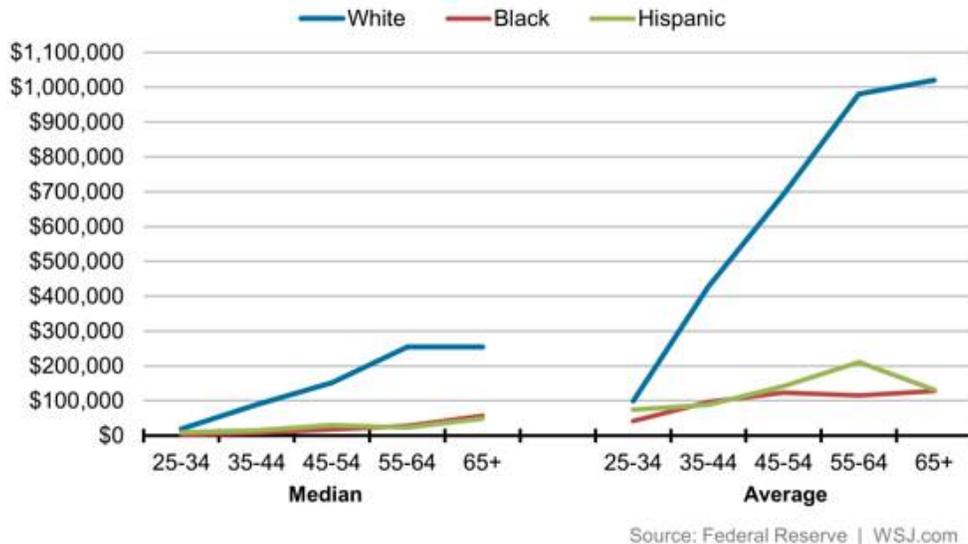


People accumulate debt rapidly in their 20s and 30s. But debt peaks at age 50, and declines, mostly as people pay off their mortgages.

But if you instantly suspected that many people don't follow this pattern, you're right. Wealth accumulation in the U.S. is driven, for the most part, by a handful of people.

Wealth Gap

Average and median net worth, by race and age of head of family

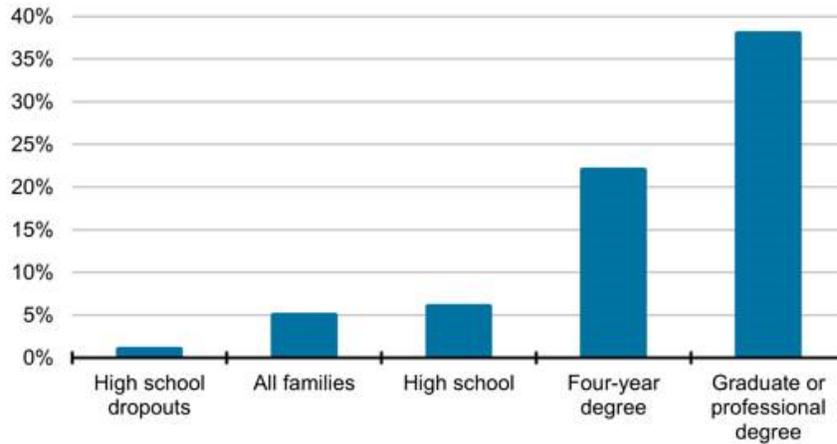


The median white person and the average black or Hispanic person, are not nearly so wealthy. Earlier this year, economists at the St. Louis Federal Reserve parsed the population along lines of race, age and education. They found that this wealth accumulation process primarily works for white and Asian, middle-aged or older families, with a college education or higher. That's just under a quarter of U.S. families, but they own over two-thirds of the U.S. economy's wealth.

“Demography may not be destiny, but it is powerful in predicting family wealth,” wrote researchers Ray Boshara, William Emmons and Bryan Noeth. (The Fed’s Survey of Consumer Finances, on which all this data is based, uses families as its unit of measurement. Education levels, age and race are all those of the head of the family. There are some obvious drawbacks to this approach, but, then again, this is already some of the most complicated and difficult-to-compile data in economics. How much more complicated would you want to make it?)

Who Wants to Be a Millionaire?

Share of families headed by someone over age 40 with a net worth above one million dollars, by highest level of educational attainment

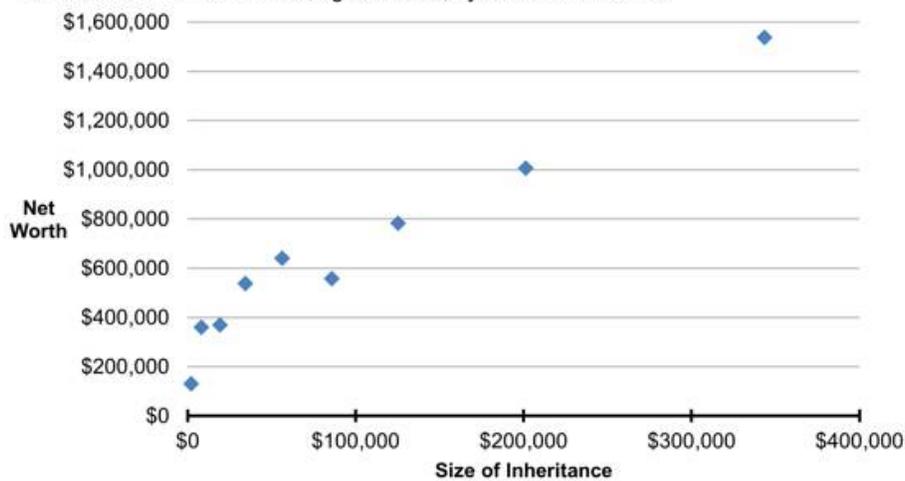


Source: Federal Reserve Bank of St. Louis | WSJ.com

The St. Louis Fed study contained some striking data on how much difference there is for people of different education levels. By the age of 40 and over, about 5 percent of families have become millionaires. But among families with college degrees, that’s about 22 percent—more than one in five—and among those with a graduate or professional degrees, that’s about 38 percent. Among high school dropouts, less than 1 percent are millionaires.

A Little Inheritance Goes a Long Way

Net worth of inheritor families, age 30 to 59, by size of inheritance



Source: Federal Reserve | WSJ.com

Of course, there is one more way that people get rich: inheritance. Even families who receive fairly modest inheritances end up quite a bit wealthier. For this chart, the Fed's economists divided inheritances into 10 buckets. The bottom 10 percent of inheritors received an inheritance averaging only about \$2,000. Families receiving this much inheritance aren't that wealthy.

But among families that received a \$35,000 inheritance, their net worth is over half a million. Families that received a \$125,000 inheritance are worth \$780,000 on average and those that receive a \$200,000 inheritance are, on average, millionaires. (The top 10 percent of inheritors, not pictured in this chart, inherit \$1.6 million on average and have a net worth of \$4.2 million.)

This data raises tons of uncomfortable questions with no easy answers. One question that Mr. Thompson and Mr. Suarez wanted to answer was why the racial wealth gaps in the U.S. are so large. This might sound straightforward—maybe the wealthy simply earned and inherited more money. But that's not what the data shows. Even after accounting for different incomes, inheritances, education and other factors, these gaps between families of different races remain, especially among the wealthy. It turns out that documenting the gaps is only the first step.