

“The Asset Price Meltdown and the
Wealth of the Middle Class”

22nd Minsky Conference, Ford Foundation

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April 17, 2013

The Great Recession, 2007-2010

- 1. Housing prices fall by 24% in real terms.
- 2. Stock prices down by 26% in real terms.

What Is Wealth?

- My Standard Definition. Assets:
- (1) the gross value of owner-occupied housing.
- (2) other real estate owned by the household.
- (3) cash and demand deposits.
- (4) time and savings deposits, certificates of deposit, and money market accounts;

What Is Wealth (cont.)?

- (5) government bonds, corporate bonds, foreign bonds, and other financial securities.
- (6) the cash surrender value of life insurance plans.
- (7) the cash surrender value of pension plans, including IRAs, Keogh, and 401(k) plans.

What Is Wealth (cont.)?

- (8) corporate stock and mutual funds.
- (9) net equity in unincorporated businesses.
- and (10) equity in trust funds.
- Total liabilities are the sum of.
 - (1) mortgage debt.
 - (2) consumer debt, including auto loans.
 - and (3) other debt, including educational loans.

What Is Wealth (cont.)?

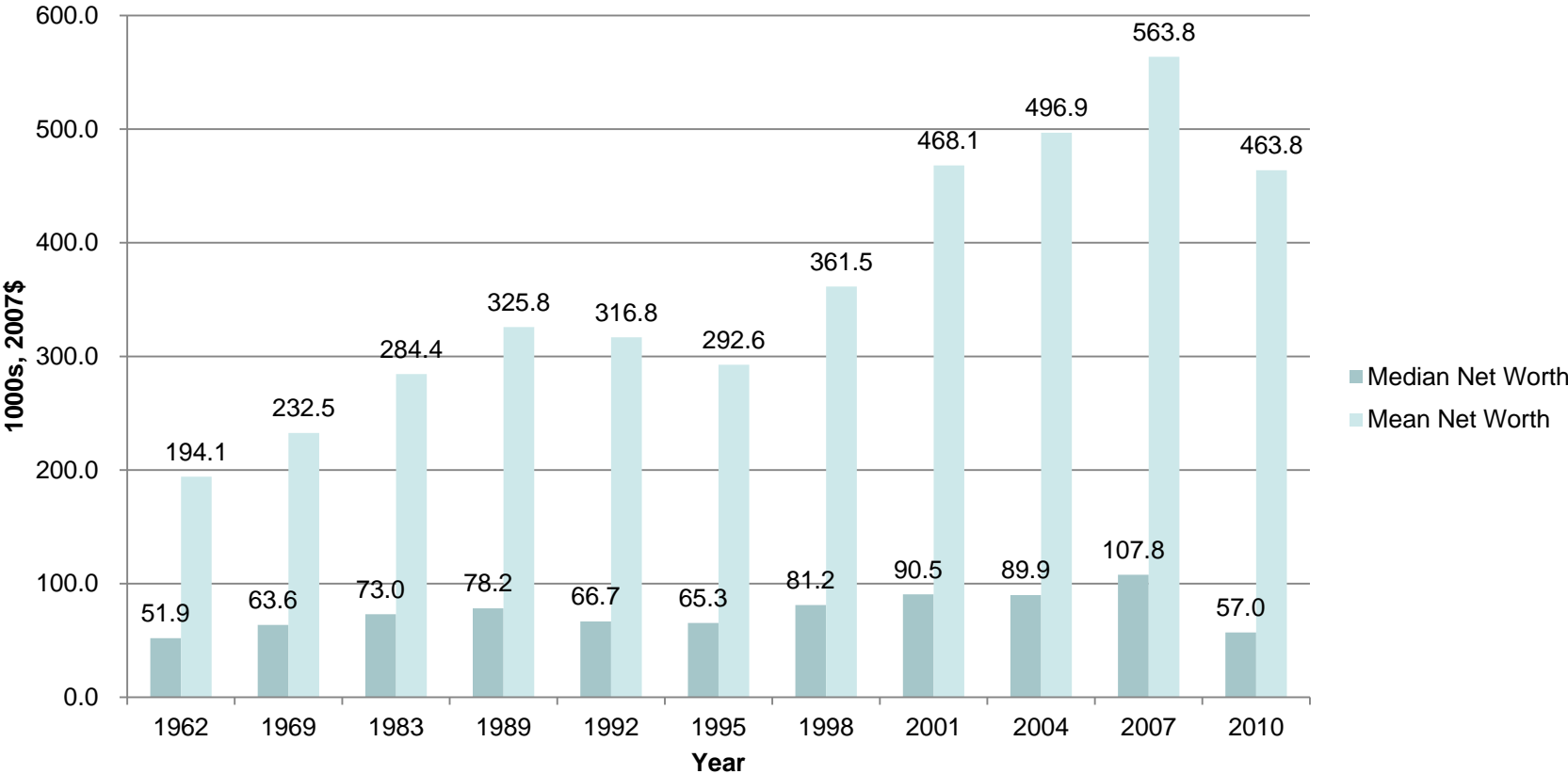
- NOT INCLUDED:
- 1. Value of vehicles (standard FRB tables INCLUDE this).
- 2. Other consumer durables.
- 3. The value of future social security benefits the family may receive upon retirement (usually referred to as "social security wealth"), as well as the value of retirement benefits from private pension plans ("pension wealth").

Sources of Wealth Data

- 1. 1983, 1989, 1992, 1995, 1998, 2001, 2004, 2007, and 2010 Survey of Consumer Finances (SCF) conducted by the Federal Reserve Board.
- 2. Each survey consists of a core representative sample combined with a high-income supplement.

Trends in Mean and Median Wealth and Income

Figure 1. Mean and Median Net Worth, 1962-2010



Trends in Mean and Median Wealth and Income (cont.)

Figure 4. Mean and Median Household Income, 1962-2010

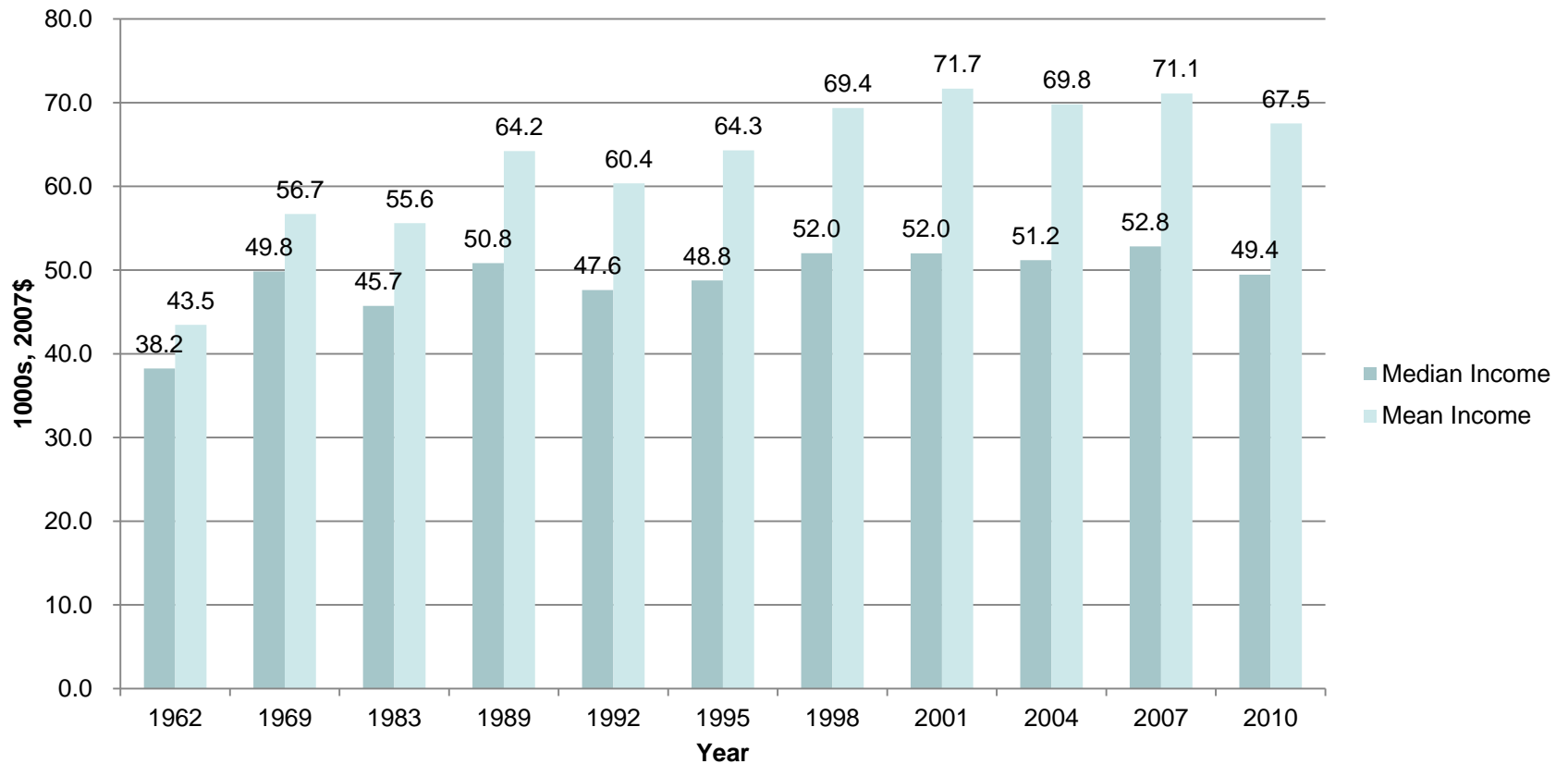


Table 1. Wealth and Income Trends
(1000s, 2010\$)

				% Chng	% Chng	% Chng
	<u>1983</u>	<u>2001</u>	<u>2007</u>	<u>1983- 2001</u>	<u>2001- 2007</u>	<u>1983- 2007</u>
Median NW	73.0	90.5	107.8	23.9	19.1	47.5
Mean NW	284.4	468.1	563.8	64.6	20.4	98.2
Median Income	45.7	52.0	52.8	13.8	1.4	15.4

Table 1. Income and Wealth Trends (cont.)
 (1000s, 2010\$)

	<u>2007</u>	<u>2010</u>	<u>%Change</u>
Median NW	107.8	57.0	-47.1
Mean NW	563.8	463.8	-17.7
Median Income	52.8	49.4	-6.4
Mean Income	71.1	67.5	-5.0

Figure 5. Gini Coefficient and the Share of the Top One Percent for Net Worth, 1962-2010

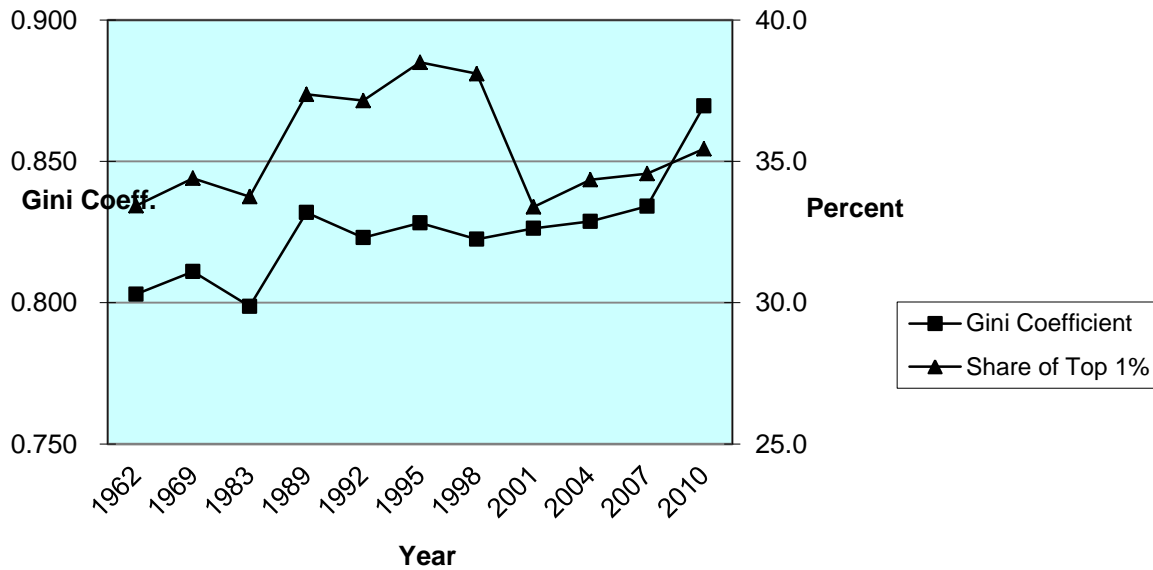


Table 2. Wealth Inequality Trends

<u>NW Shares</u>	<u>2007</u>	<u>2010</u>	<u>Change</u>
Top 20%	85.0	88.9	3.9
Next 20%	10.9	9.4	-1.5
Middle 20%	4.0	2.6	-1.4
Bottom 40%	0.2	-0.9	-1.1
Gini Coeff.	0.834	0.870	0.036

Table 2 (cont.). Income Inequality Trends

<u>Income Shares</u>	<u>2006</u>	<u>2009</u>	<u>Change</u>
Top 20%	61.4	59.1	-2.3
Next 20%	17.8	18.7	0.9
Middle 20%	11.1	14.9	3.8
Bottom 40%	9.6	7.3	-2.3
Gini Coeff.	0.574	0.549	-0.025

**Figure 7. Composition of Household Wealth, 1983 and 2010
(percent of gross assets)**

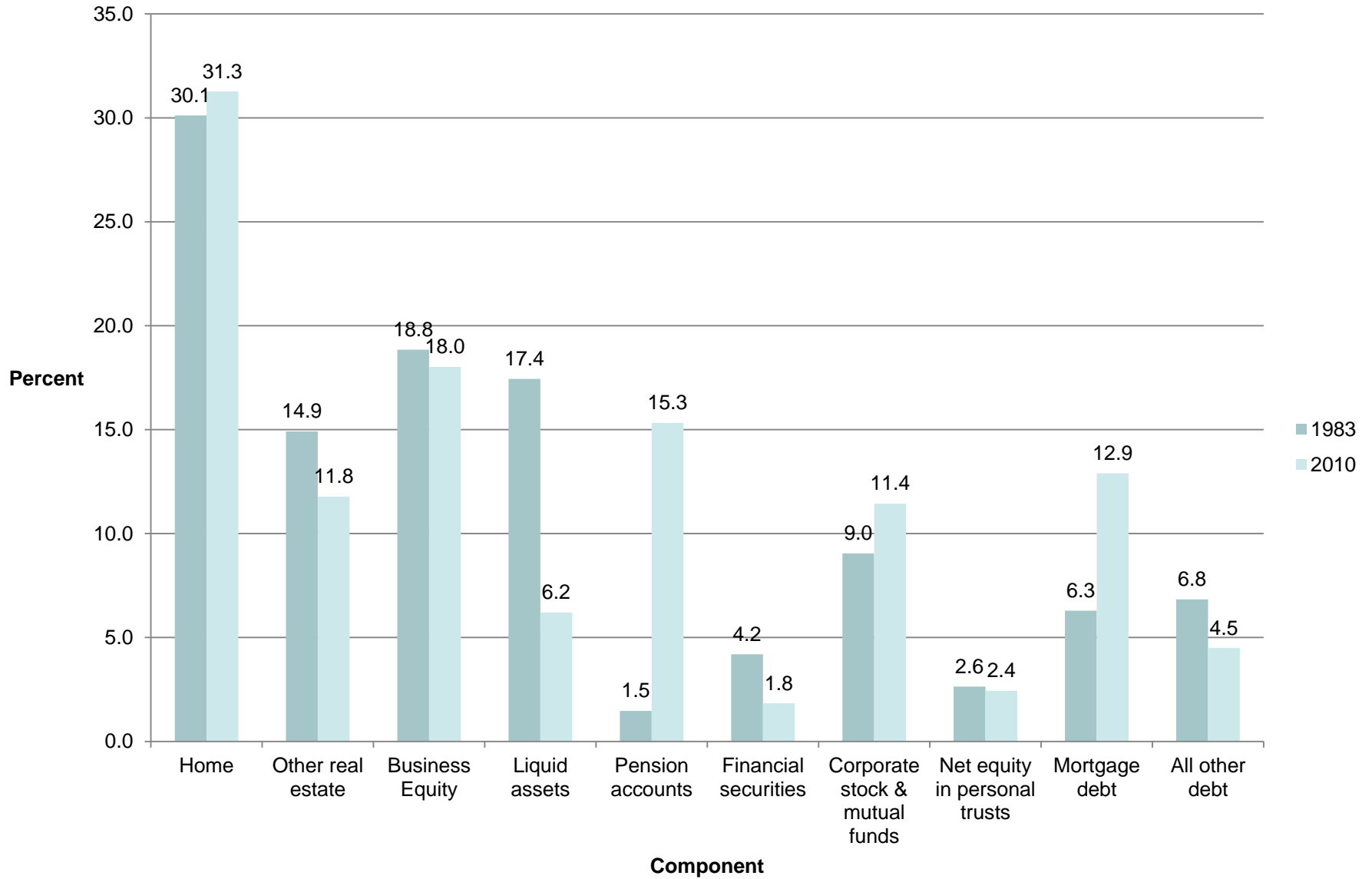


Figure 8. Composition of Household Wealth by Wealth Class, 2010 (percent of gross assets)

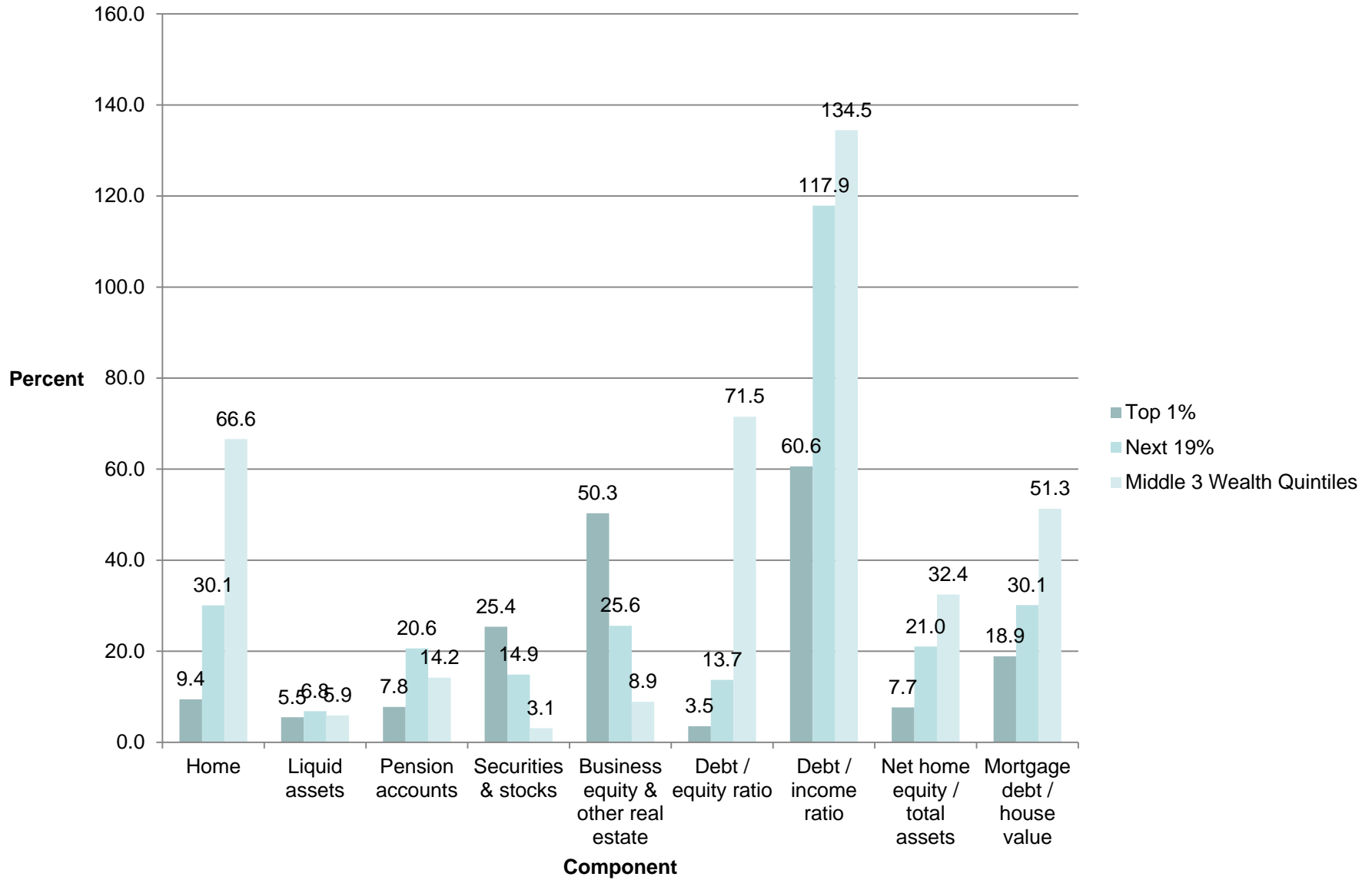


Table 6. Composition of Wealth of Middle 3 Wealth Quintiles

<u>Ratio</u>	<u>1983</u>	<u>2007</u>
Debt/Equity	37.4	61.1
Debt/Income	66.9	156.7
Net Home Equity/Total Assets	43.8	34.8
Principal Residence Debt/House Value	28.8	46.6

Four Puzzles

- 1. Why median wealth was down so much from 2007-2010 – much more than median income and more than housing prices.
- 2. Why wealth inequality spiked from 2007-2010 even though income inequality was down and stock and housing prices declined at about the same rate.

Four Puzzles (cont.)

- 3. Why median wealth surges from 2001-2007 while median income is sluggish.
- 4. Why wealth inequality is flat from 2001-2007 when income inequality grows.

Effects of Leverage: Arithmetic

Example 1a

	<u>Year 1</u>	<u>Year 2</u>	<u>% Change</u>
Assets	50	60	
Debt	0	0	
Net Worth	50	60	20
% Increase in Asset Prices			20

Effects of Leverage: Arithmetic

Example 1b

	<u>Year 1</u>	<u>Year 2</u>	<u>% Change</u>
Assets	50	60	
Debt	40	40	
Net Worth	10	20	100
% Increase in Asset Prices			20

Effects of Differential Leverage: Arithmetic

Example 2a

<u>The Rich</u>	<u>Year 1</u>	<u>Year 2</u>	<u>% Change</u>
Stocks	50	40	
Other Assets	50	50	
Debt	0	0	
Net Worth	100	90	-10
% Change in Stock Prices			-20

Effects of Differential Leverage: Arithmetic

Example 2b

<u>The Middle Class</u>	<u>Year 1</u>	<u>Year 2</u>	<u>% Change</u>
Housing	60	48	
Other Assets	10	10	
Debt	30	30	
Net Worth	40	28	-30
% Change in House Prices			-20

Table 12. Ratios of NW, Income, and Home Ownership between Blacks and Whites

	<u>Mean NW</u>	<u>Median NW</u>	<u>Median Income</u>	<u>Home Ownership Rate</u>
1983	0.19	0.07	0.56	0.65
2001	0.14	0.10	0.57	0.64
2007	0.19	0.06	0.60	0.65
2010	0.14	0.05	0.59	0.64

Table 13. Ratios of NW, Income, and Homes between Hispanics and (Non-Hisp.) Whites

	<u>Mean NW</u>	<u>Median NW</u>	<u>Median Income</u>	<u>Home Ownership Rate</u>
1983	0.16	0.04	0.66	0.48
2001	0.17	0.03	0.55	0.60
2007	0.26	0.06	0.70	0.66
2010	0.15	0.01	0.67	0.63

Table 14. Composition of Household Wealth by Race and Ethnicity, 2007
(Percent of gross assets)

Asset	Non-Hispanic Whites	African-Americans	Hispanics
Principal residence	30.8	54.0	52.5
Liquid assets (bank deposits, money market funds, and cash surrender value of life insurance)	6.6	7.6	3.9
Pension accounts	12.5	12.3	7.7
Corporate stock, financial securities, mutual funds, and personal trusts	17.1	3.4	2.5
Unincorporated business equity other real estate	31.3	20.9	32.9
Miscellaneous assets	1.7	1.8	0.4
Total assets	100.0	100.0	100.0
<u>Memo (selected ratios in percent):</u>			
Debt / equity ratio	15.4	55.3	51.1
Debt / income ratio	109.0	152.2	187.9
Net home equity / total assets ^a	20.8	27.3	28.8
Principal residence debt / house value	32.4	49.4	45.2
All stocks / total assets ^b	18.3	5.0	5.1

Table 15. Age-Wealth Profiles and Homeownership Rates by Age, 1983-2010

Age	1983	1989	1992	1995	1998	2001	2004	2007	2010
<u>A. Mean Net Worth (Ratio to Overall Mean)</u>									
Overall	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Under 35	0.21	0.29	0.20	0.16	0.22	0.19	0.14	0.17	0.10
35-44	0.71	0.72	0.71	0.65	0.68	0.64	0.65	0.58	0.41
45-54	1.53	1.50	1.42	1.39	1.27	1.25	1.21	1.19	1.14
55-64	1.67	1.58	1.82	1.81	1.91	1.86	1.91	1.69	1.81
65-74	1.93	1.61	1.59	1.71	1.68	1.72	1.57	1.86	1.74
75 & over	1.05	1.26	1.20	1.32	1.12	1.20	1.19	1.16	1.36
<u>B. Homeownership Rate (in Percent)</u>									
Overall	63.4	62.8	64.1	64.7	66.3	67.7	69.1	68.6	67.2
Under 35	38.7	36.3	36.8	37.9	39.2	40.2	41.5	40.8	37.5
35-44	68.4	64.1	64.4	64.7	66.7	67.6	68.6	66.1	63.8
45-54	78.2	75.1	75.5	75.4	74.5	76.1	77.3	77.3	75.2
55-64	77.0	79.2	77.9	82.3	80.6	83.2	79.1	80.9	78.1
65-74	78.3	78.1	78.8	79.4	81.7	82.5	81.2	85.5	82.5
75 & over	69.4	70.2	78.1	72.5	76.9	76.2	85.1	77.0	81.3

Table 16. Composition of Household Wealth by Age Class, 2007

(Percent of gross assets)

Asset	All	Under 35	35-44	45-54	55-64	65-74	75 & over
Principal residence	32.8	54.3	43.7	33.8	25.6	28.2	30.2
Liquid assets (bank deposits, money market funds, and cash surrender value of life insurance)	6.6	5.7	5.4	6.4	6.3	6.1	10.5
Pension accounts	12.1	6.0	10.7	13.0	15.8	12.9	5.0
Corporate stock, financial securities, mutual funds, and personal trusts	15.5	4.2	8.6	13.1	16.4	20.5	25.6
Unincorporated business equity other real estate	31.3	28.7	30.1	32.0	34.4	30.2	27.1
Miscellaneous assets	1.7	1.2	1.5	1.7	1.5	2.1	1.6
Total assets	100.0	100.0	100.0	100.0	100.0	100.0	100.0
<u>Memo (selected ratios in percent):</u>							
Debt / equity ratio	18.1	92.7	41.3	20.2	11.9	7.1	2.1
Debt / income ratio	118.7	167.5	156.5	118.2	100.0	79.7	29.9
Net home equity / total assets ^a	21.4	18.8	21.3	20.9	18.1	23.4	28.7
Principal residence debt / house value	34.9	65.4	51.4	38.3	29.2	16.9	4.9
All stocks / total assets ^b	16.8	5.9	11.2	15.1	19.4	21.5	20.0

Table 17. Ratio of Mean NW between Age Group and Overall Mean

	<u>Under 35</u>	<u>Ages 35-44</u>	<u>Ages 55-64</u>	<u>Ages 65-74</u>
1983	0.21	0.71	1.67	1.93
2001	0.19	0.64	1.86	1.72
2007	0.17	0.58	1.69	1.86
2010	0.10	0.41	1.81	1.74

Principal Findings for the Great Recession, 2007-2010

- 1. Housing prices fall by 24% in real terms.
- 2. Stock prices down by 26% in real terms.
- 3. Median wealth plummets by 47% in real terms (with vehicles by 39%).
- 4. Mean wealth down by “only” 18%.
- 5. Median income falls by 6.4 percent.
- 6. Mean income down by 5.0 percent.

Principal Findings (cont.)

- 7. Wealth inequality spikes upward: (a) Gini coefficient rises from 0.834 to 0.870.
- (b) Share of top 20 percent up from 85 to 89 percent.
- 8. Income inequality falls: (a) Gini coefficient falls from 0.574 to 0.549.
- (b) Share of top 1% down from 21.3 to 17.2 percent.

Principal Findings (cont.)

- 9. Racial disparity in wealth holdings spikes upward, with the ratio of mean wealth between blacks and whites dropping from 0.19 to 0.14.
- 10. Hispanic families get hammered by the Great Recession, with the ratio of mean wealth plunging from 0.26 to 0.15.

Principal Findings (cont.)

- 11. Young families also get pummeled by the Great Recession, with the ratio of mean wealth between household under age 35 and all households plunging from 0.17 to 0.10, and that between age group 35-44 and all from 0.58 to 0.41.
- 12. Trends are explained by leverage and differential leverage between groups.