



Australian Government
Productivity Commission

Effects of wealth transfers on wealth inequality and intergenerational wealth persistence

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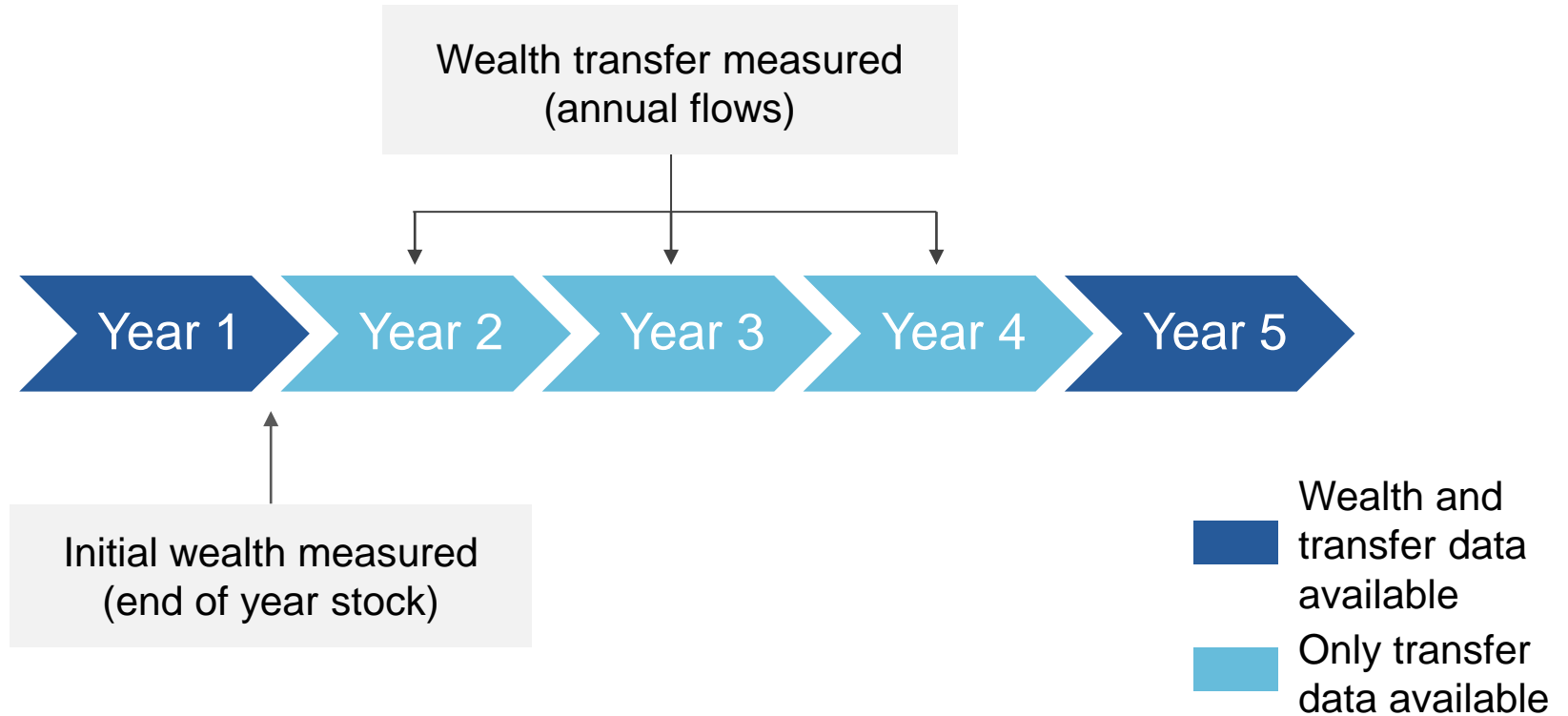
Inequality and intergenerational persistence

- Effects of wealth transfers on wealth inequality
 - Large existing literature
 - Few studies of Australia
- Effects of inheritances on intergenerational wealth persistence
 - Small existing literature
 - No studies of Australia

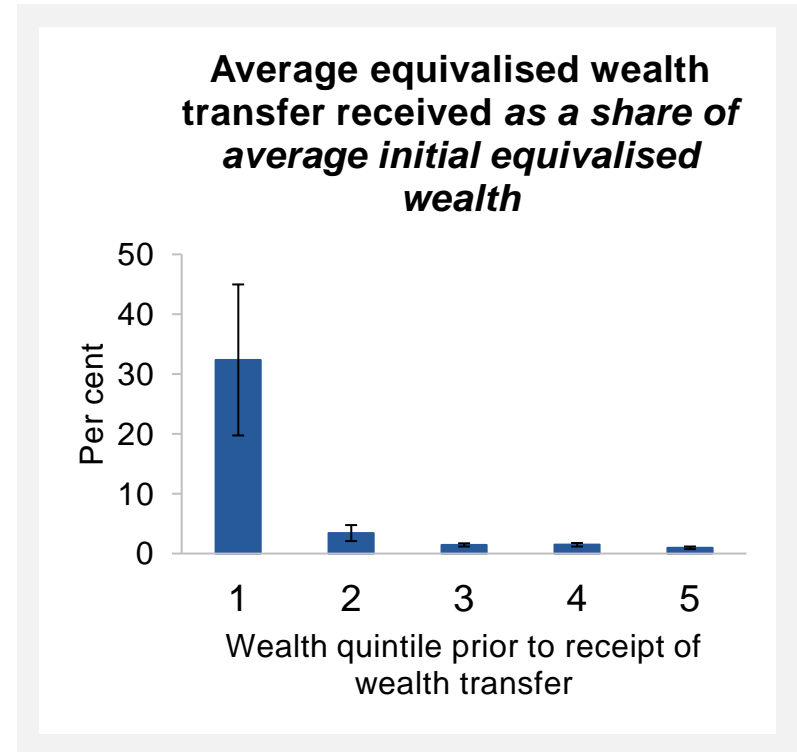
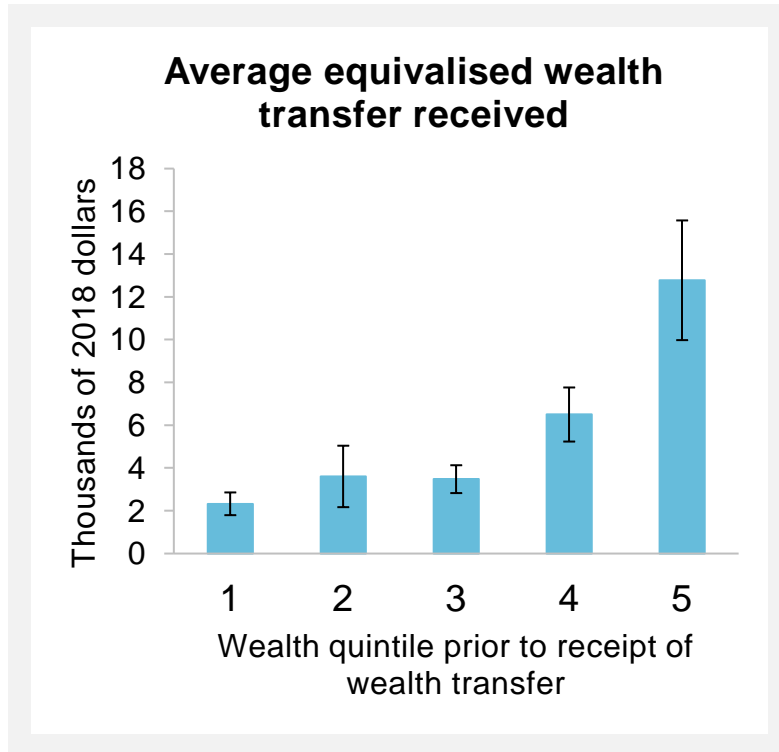
Absolute or relative inequality?

- **Absolute** wealth inequality: inequality in the level of wealth
 - Everyone gets \$5 – unchanged
 - Everyone gets 5% – increases
- **Relative** wealth inequality: inequality in the share of wealth
 - Everyone gets \$5 – decreases
 - Everyone gets 5% – unchanged

Approach to measuring effect on wealth inequality

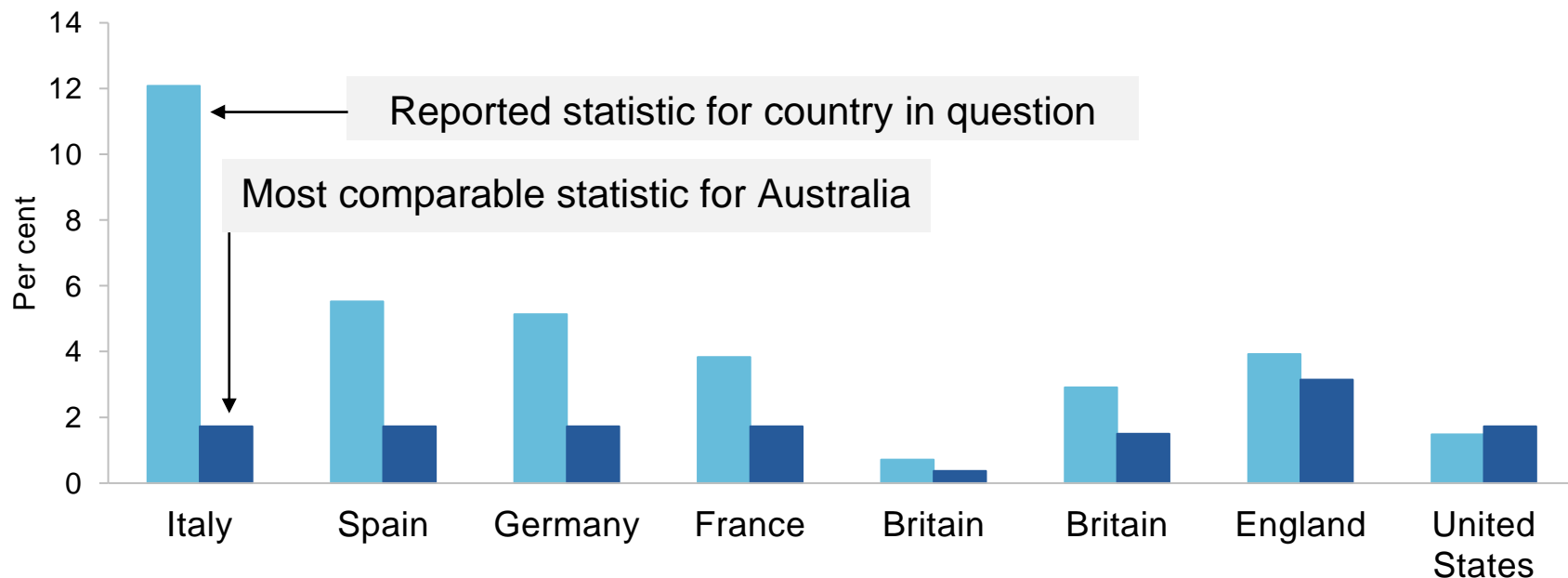


Transfers increased absolute inequality, decreased relative inequality



Same effect in other countries, but stronger

Decrease to relative wealth inequality due to wealth transfers



Sources: Crawford and Hood (2016),
Karagiannaki (2017), Nolan et al. (2021)

Do behavioural responses matter?

- Do behavioural responses to inheritance receipt change the results?
- Sweden: inheritances decreased relative inequality in the immediate term but increased relative inequality in the longer term (Nekoei and Seim 2021)
- No evidence of this in Australia

Intergenerational wealth persistence (IWP)

- Intergenerational persistence: correlation between parents' outcomes and their children's outcomes
 - High persistence implies low mobility
 - **Wealth** persistence, because inheritances contribute to wealth
- Intergenerational **wealth** persistence: correlation between parents' position in wealth distribution and their children's position in wealth distribution

Approach to measuring effect on IWP

- Approach loosely follows Adermon, Lindahl and Waldenström (2018)

- IWP ($\widehat{\beta}_1$):

*Child wealth (rank)*_{*i*,2018} =

$$\beta_0 + \beta_1 \text{Parent wealth (rank)}_{i,2002} + \mathbf{x}'_i \beta_4 + \varepsilon_i$$

- IWP in the absence of inheritances ($\widehat{\beta}_3$):

*Child wealth excluding inheritances (rank)*_{*i*,2018} =

$$\beta_2 + \beta_3 \text{Parent wealth (rank)}_{i,2002} + \mathbf{x}'_i \beta_5 + \delta_i$$

- Implied contribution of inheritances: $(1 - \widehat{\beta}_3 / \widehat{\beta}_1)$

Approach to imputing parent wealth rank

- Children need to be middle aged, but the data don't exist
- Imputed parents' wealth based on the size of the inheritances they left
 - First parent to die assumed to bequeath to second parent and/or children in equal shares (true in ~90% of cases)
 - Second parent to die assumed to bequeath to children in equal shares (true in ~80% of cases)

Estimator is somewhat robust to measurement error

- IWP estimate ($\widehat{\beta}_1$) is biased toward zero due to measurement error

*Child wealth (rank)*_{*i*,2018} =

$$\beta_0 + \beta_1 \text{Parent wealth (rank)}_{i,2002} + \mathbf{x}'_i \boldsymbol{\beta}_4 + \varepsilon_i$$

- IWP excluding inheritances estimate ($\widehat{\beta}_3$) is also biased toward zero due to measurement error

*Child wealth excluding inheritances (rank)*_{*i*,2018} =

$$\beta_2 + \beta_3 \text{Parent wealth (rank)}_{i,2002} + \mathbf{x}'_i \boldsymbol{\beta}_5 + \delta_i$$

- Estimated contribution of inheritances ($1 - \widehat{\beta}_3 / \widehat{\beta}_1$) is unbiased if parent wealth measurement error is not correlated with child wealth conditional on parent wealth

One third of IWP is due to inheritances

- 36% of IWP at child age 63-73 is due to inheritances
 - IWP at this age is mostly pre-inheritance (education, networks, attitudes, values, gifts etc)
- Wide range in studies of other countries
 - 35% in Denmark (but adapting our method to match theirs would suggest ~60% in Australia) (Boserup, Kopczuk and Kreiner 2017)
 - 50-60% in Sweden (Adermon, Lindahl and Waldenström 2018)
 - 65% in Sweden among adopted children (Black et al. 2017)



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