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DYNAMISM OF U.S. ECONOMY IS REFLECTED IN INCOME MOBILITY

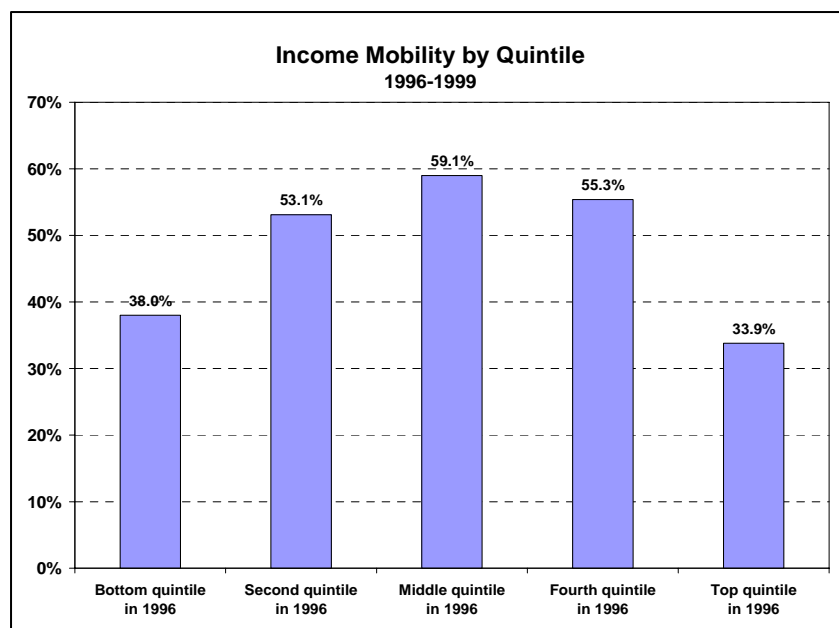
The flexible, dynamic, and resilient U.S. market economy is characterized by continuous economic change. New technologies, industries, and products are constantly emerging to upset the status quo. This process of economic growth creates new jobs and opportunities resulting in a greater degree of income dynamics than is apparent in some summary income measures.

For example, in considering trends in income, or the impact of tax policy over time, the dispersion of income among households or other units is often of interest to analysts. Under one common approach, families, households, individuals, or tax filers may be ranked by income from highest to lowest, and then subdivided into fifths (quintiles), from the top fifth to the bottom fifth. The average income and tax liability of each fifth can then be estimated, and differences in the averages observed over time. However, there are a number of important data limitations that must be considered. One limitation is that the composition of these groups is not static, and that income mobility is often not taken into account.

For example, in considering changes in the income of actual families or

households, many standard measures of income are problematic, because they do not directly measure the incomes of groups consisting of the same people over time. As the Census Bureau itself has noted: “Data from the Current Population Survey are recommended when looking at changes in the overall income distribution, but are not useful for looking at changes for the same households over time, as there is no attempt to follow households if they move, nor are any households in the CPS for more than two consecutive years.”¹

Income mobility is the movement of families, households, or persons from one income group to another over time. The income mobility of specific households from one fifth to another is important for the interpretation of income and some tax data.



If all households remained within a given fifth over extended periods of time, then changes in the average income of this fifth could roughly approximate the changes in income experienced by actual households in the group. However, the greater the tendency of households to exit a given quintile over time, the less representative changes in income or taxes would be.

Census data from the Survey of Income and Program Participation (SIPP) show the extent of income mobility for the 1996 to 1999 time period.² These data demonstrate that the extent of income mobility is considerable. In the middle three fifths, more than half of all households moved to a different income group over a relatively short period. Although the degree of income mobility varies, even the top and bottom quintiles reflect income mobility rates exceeding one-third of households.

Overall, 47.9 percent, or nearly half, of all U.S. households moved to a different quintile between 1996 and 1999. The graph shows the extent of mobility for each quintile during this period. Of the households in the bottom quintile, 38.0 percent had moved upward by 1999. In each of the three middle quintiles, over half of the households had moved. By 1999, 33.9 percent of the households in the top quintile had fallen to a lower income quintile.

Income mobility can affect the interpretation of a variety of income data. As the Census Bureau has noted of changes in median income over a specific time period, “It is not a picture of what has happened to the same households over that time period. Medians, like those from the CPS, can conceal an enormous amount of movement in the income of individual households.”³

For example, of the households in the middle quintile in 1996, 32.4 percent had moved to a higher quintile, and 26.7 percent to a lower quintile, by 1999. Only 41 percent of the households in the middle quintile in 1996 remained by 1999.

Conclusion

The point here is not that income mobility has increased greatly or now is especially high, but simply that the membership of various income groups changes significantly over time.

As a previous JEC study noted, “Quintiles may be a convenient way of presenting snapshots of income data for a group of people at a certain point in time. Nonetheless, the notion of a quintile as a fixed economic class or social reality is a statistical mirage.”⁴ Thus changes in the average income levels of various quintiles over time need not correspond to changes in the incomes of actual persons or households who are members of a given group only temporarily.

Although there is more stability in the bottom and top quintiles, the dynamism and flexibility of the U.S. economy is reflected in a considerable amount of overall income mobility.

¹ Hisnanick, John J., and Walker, Katherine G., U.S. Census Bureau, *Dynamics of Economic Well-Being: Movements in the U.S. Income Distribution, 1996-1999*, Current Population Report P70-95 (July 2004), 2.

² *Ibid.*, 3.

³ *Ibid.*, 1.

⁴ U.S. Congress, Joint Economic Committee, *Income Mobility and Economic Opportunity* (June 1992), 2.