Trends in Household Wealth-Adjusted Income in Australia

by

Alan Fenna and Alan Tapper

Stephen P. Jenkins
London School of Economics, ISER, and IZA
Outline: summary, then comments

1. Summary:
   - What and Why?
     - Research question(s) and motivation(s)
   - How?
     - Methods and data
   - Findings?
   - Implications?
     - Missing from paper

2. Comments
   - Overall: interesting and stimulating … but requires development
Research questions & motivations

• There is value and interest in looking more comprehensive measures of economic well-being (‘income’)
  
  \[
  \text{Wealth-adjusted income (WAI)} = \text{money income} + \text{annuitized value of net worth (ANW)}
  \]

• Incorporating flow-equivalent of a stock is a version of this idea
  
  ▪ Cf. adding in value of benefits-in-kind, leisure or home production

• AUS evidence updated
  
  ▪ Travers & Richardson (TR), OUP, 1993

• AUS evidence compared with USA
  
  ▪ Wolff & Zacharias (WZ), JEI 2009
Methods: different income definitions

Final income (FI)
• FI = disposable income + benefits-in-kind – indirect taxes

Wealth-adjusted final income (WAFI)
• WAFI = FI – money income from financial assets + ANW
  o avoiding double-counting

Equivalised WAFI (EWAFI)
• EWAFI = WAFI/household equivalence scale rate

Annualized net worth (ANW)
= (either, TR) \( r \times NW \) (fixed rate: 3%, 4%, 5%)
= (or, WZ) lifetime annuity rate = annuity such that exhaust NW at death
  o depends on estimated years left to live! (Person-specific)

• WZ used narrower income definitions than FI, did not equvalize, different treatment of home wealth
Data

- ABS Household Expenditure Survey
- 2003/04 ($n = 6957$) and 2009/10 ($n = 9774$)
- These are the “only ABS surveys that report household final income and net worth”
- $NW = \text{Assets} – \text{Liabilities}$, where
- Assets: tangible and intangible fixed assets + financial assets (including superannuation account balances)
- Liabilities: mortgage debt, HP and other card debt, etc.
Findings: (1) overall

1. Comparisons for DI, FI, NW, WAFI, EWAFI of means, quintile group shares, Gini
   - Tables 1, 2; Figs 1, 2
   - E.g. Means by q-groups (~ q-group shares in Table 1!)

![Graph 1: Three kinds of household income by quintile, 2003-04](image1)

![Graph 2: Three kinds of household income by quintile, 2009-10](image2)
Findings: (2) breakdowns by age group

- EWAFI and EFI by age group
  - Means

- Gini became more equal among elderly groups

- Range of other comparisons, e.g. components of EFI by age (and role of benefits in kind)
Headline Findings (AUS-USA)

- Comparisons between AUS and USA bedevilled by lack of harmonisation of definitions, different years
- Broadly harmonised data leads to similar age-related patterns [?]
Tighten up the RQ and motivation

- More than simply re-doing TR and especially WZ?
- New methods?
  - Not really? Minor variations, and don’t make a big difference
- Different picture of the distribution of economic well-being in AUS?
  - Not really? No real surprises, e.g. hump-shaped relationship with age
- Different picture about trends over time in AUS?
  - Not really? No AUS context provided, including no trends data using conventional OECD/‘Canberra Group’ type definitions (cf. Wilkins EcRec 2014)
- AUS differs from the USA?
  - Hard to draw detailed conclusions using existing materials
- Interest in more comprehensive income definitions in general or wealth-adjustment per se? Paper mixes these (part 2)
Importance of housing (home wealth)

- Needs more detailed attention
- Very important in AUS (can’t see from Table 1 since only shows net value)
- How much is it driving things? Or is it other components?
  - NB a decomposition by income sources analysis à la WZ is missing here
- Clarification please (page 4)!
  - ZW: flow from home wealth = “imputed rent”
  - Authors: deduct imputed rent from FI, and treat full value of housing as an asset to be annuitized
  - But fixed rate annuity method is one way in which researchers have done imputed rent estimation, so just capturing difference between this and how ABS does it (which is??)
Conceptual: should we combine flows and stocks like this?

- Simply assumed here that we should
- But much of wealth not immediately fungible except maybe in lumps (think houses and pensions)
- Yes, wealth and income are important, but why not simply look at their joint distribution?
  - E.g. ‘transition matrices’ summarising fraction at top (or bottom) of both income and NW distributions; or fractions who are “asset rich but cash poor”
  - Jäntti, Sierminska, Van Kerm: REI forthcoming
- In any case, more information about marginal distributions as a whole, e.g. density comparisons
Tell us much more about data quality

• ABS household surveys notorious for changes in methodology over time: what about HES?
• Is “income” well measured in the HES, e.g. compared to (say) Survey of Income and Housing
• Many components of “final income” are estimated
  ▪ Imputed rental income from owner-occupation
  ▪ Benefits in kind (education, health services, …)
  ▪ Indirect taxes
• How is “remaining life years” estimated? Reliable?
• Why not use HILDA?
  ▪ Has more NW data: 2002(4)2014
  ▪ Does it really matter that has DI not FI?
  ▪ Consistent definitions over time (Wilkins EconRec 2014)
Assorted clarifications required

- Income is “per household per week”: hh is sharing-unit, but what is the unit of analysis?
- Equivalence scale used – what is it?
- Should the same equivalence scale rates be applied to DI, FI, and WAFI totals?
  - Implausible that there are the same economies of scale in each of the components added in going to the next broader definition?
Think more about policy implications

[Related to remarks about RQ and motivations]

• Are there any policy implications, including for ABS?
• Related literature: asset tests in addition to income tests for assessing benefit and programme eligibility
• Related literature: whether to incorporate imputed rental income in ‘official’ income measures, including how to deal with ‘asset rich, cash poor’ households (mainly elderly)