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Income mobility – curse or blessing?

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The description and explanation of the income of people, households, and families has a long tradition in economics as income and its distribution are seen as a main aspect of the wealth of nations. In this context the distribution and its changes over time are of great interest from a theoretical as well as from an empirical point of view and a lot of research has been done to answer questions such as how the distribution is forming out or what the underlying process is which creates the distribution. Younger people are joining the distribution, older people are leaving – therefore the inequality may change but the underlying process about the development of individual income is unclear. If one can answer those questions, one can also give solutions for economic policy measures concerning the income distribution and therefore the wealth of nations.

In the context of economic insecurity and well-being the relevance of income mobility is manifold. One assumption in economic theory is that people normally are risk averse. Therefore they are interested in a steady income stream. This can be called the *security aspect* of income mobility: The higher the mobility, the lower ceteris paribus the wealth of people. The expectation of future income is relevant for planning of expenditures and savings: The

less stable an income stream is, the more people are concerned with the arrangement of spending and saving money. A lot of goods and services have to be paid permanently such as rent, contributions for insurances or redemption of credits. An unsteady income stream bears the risk of not being able to fulfil the expectations and therefore may hinder e.g. long term financial commitments.

Another facet of income mobility from an economic point of view is the *incentive aspect*. Upward income mobility provides incentives for economic activities as it is possible to be successful and move up the income ladder as a reward, enjoying a higher social standing. Downward mobility delivers the “sticks” for economic activities as if one is not successful, he will move down in the income distribution – in the worst case getting stigmatized as a failure. Additionally, income mobility is seen as an aspect which can offset the inequality of an income distribution. It is seen as there exists a general possibility of moving up the ladder of wealth – often called the American Dream or the Horatio Alger Myth. In other words income mobility therefore is considered to be an equalizer of opportunities. Mobility characterises an open society, where everyone has a chance to climb the ladder of success, which is to some extent documented in the income position.

Last but not least, in a more technical view, income mobility can be regarded as just another form of redistribution – albeit a stochastic one.

In most empirical analyses, the time period covered by the data is relatively short. Therefore special aspects of the life cycle theory could not be analysed. As we can use data of workers covering their whole working life, we are able to shed some light on the income mobility over their entire employment careers. We examine wage mobility in Germany, using Social Security Earnings Data from the Research Data Centre of the German Federal Pension Insurance (FDZ-RV). This will result in more information about the adequacy of some assumptions of the life cycle theory concerning the development of income over time – especially about the inverted-U-shape assumption of income profiles.

Furthermore, we will fill some gap in the knowledge as in Germany, income mobility is mainly neglected in the area of distributional and social policy analysis. Virtually nothing is known for example about earnings mobility and its impact on earnings inequality. Has earnings mobility increased along with earnings dispersion? Is it now easier than before the transition to move up the earnings ladder? Has earnings mobility offset the increase in earnings inequality? Which worker groups are likely to see their earnings status to improve, and which to worsen?