

# A Life-Cycle Perspective on the Great Recession's Effects on the Middle Class

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## **Paper Abstract:**

More than five years after the end of the 2007–2009 “Great Recession,” our understanding of the downturn’s immediate and longer-term consequences for families’ finances is still taking shape. Bricker et al. (2015), for example, show that the recession’s effects were far from uniform: though over half of U.S. households lost wealth between 2007 and 2009, about onethird of households experienced increases in wealth over this period. In addition, studies that have examined the roles of house price growth, mortgage originations, and mortgage delinquencies in the crisis have reached differing conclusions about the relative importance of mortgage lending to lower-income borrowers compared with lending to middle-income borrowers (Mian and Sufi, 2009; Adelino, Schoar, and Severino, 2016).

I use longitudinal data from the 2007–09 Survey of Consumer Finances (SCF) panel and from the 1989–2007 SCF cross-sections to examine the effects of the Great Recession on the finances of U.S. households, particularly on the finances of “middle-class” households. The paper’s definition of middle class reflects not only a household’s current wealth but also its expected wealth accumulation over the life cycle. To apply this definition, I estimate model household net worth, separately by race/ethnicity and education of the household head, as a function of age to calculate age-adjusted wealth levels.

I focus on a household’s age-adjusted wealth, rather than its current wealth, in defining the middle class because the set of households in a given range of the wealth distribution at a point in time likely includes households at different ages and life-cycle stages. The middle of the cross-sectional wealth distribution might include, for instance, both older households with relatively low lifetime income but who are near the peak of their lifetime wealth as well as high-income, younger households in the early stages of accumulating wealth. The longer-term consequences of the Great Recession for household wealth and wealth inequality, however, may differ depending on whether wealth losses for the middle class were, in this example, concentrated among younger, high-income households or older, low-income households. Younger households that lost wealth may, for example, delay homeownership but would have several years to potentially recover wealth losses. In contrast, the older households may be more heavily reliant on Social Security (government benefits for older households) than they otherwise would have been and would have limited opportunity to replace lost savings.

The building blocks of the analysis are the estimated age-wealth profiles. In modelling these relationships, the paper clearly highlights the differences in the level of wealth held by households by education and by race/ethnicity that have been noted elsewhere. I then take two approaches to calculating counterfactual, age-adjusted wealth at age 50 for households—one that assumes an age effect that is additive in a household’s rank in the net worth distribution and another the other assumes proportional increases in wealth as households age. I find that both of these approaches change the set of households classified as middle class, but they do not significantly shift the demographic characteristics of “middle-class” households. For both approaches, adjusting for life-

cycle patterns in wealth has almost no effect on conclusions about how the middle-class fared over the Great Recession. Instead estimates of the magnitude and distribution of changes in wealth, assets, and debt are essentially unchanged when using age- adjusted wealth rather than actual wealth to define a household's socioeconomic class.