What is the source of the intergenerational correlation in earnings?

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The Context

- Parental earnings tend to be correlated with offspring earnings.

- Many studies: intergenerational earnings correlation in the US: 0.3-0.8.

- Not nearly as many studies that aim to understand the causal mechanisms behind the the persistence.

What does this paper do?

- This paper is one of the few papers to attempt this:

- Q: What are the causes of intergenerational persistence in earnings?

- This is important especially if we want to understand what fraction of the persistence in earnings can be 'corrected' by policy vs is inevitable.

Model

- Life-cycle model with intergenerational links through altruism.

- People are born at age 25 with a "type" = (education, skill, race, gender).

- Immediately, matched with a spouse via assortative matching.

- Each period they make joint, discrete decisions on fertility, labor supply, and time investment in offspring.

- Wage is a function of type, age, and experience.

Model

- A fraction of family income goes to monetary investment in children exogenously.

- Rest goes to family consumption: no borrowing or saving (bequests).

- An offspring's type (skill and education) is determined stochastically as a function of:

  - parental type,

  - time and monetary investments they receive,

  - number and timing of siblings.

- They estimate this model using 2 generations from PSID.

Results

- Model fit:

Table: Benchmark Calibration Procedure

Parameter	Data	Model
Fathers and sons	0.356	0.266
F and S (family earnings)	0.337	0.251
Mothers and daughters	-0.032	0.204
M and D (family earnings)	0.286	0.222

Average earnings between 30-40.

Results

Causes of intergenerational earnings persistence:

- Decompose the contributions of various channels to intergenerational persistence:

    - Assortative mating,

    - Age profile of earnings,

    - Effect of experience on earnings,

    - Non-linear returns to labor supply,

    - Dependence of monetary cost on parental education.

Discussion of Results

- The current decomposition exercise is not very policy relevant.

- Decomposition exercises that aim to understand what fraction of persistence is inevitable would be valuable:

  1. Force all parents to make identical monetary investment.

  2. Force all parents to make identical monetary and time investments.

- Adding policy to the model: monetary transfers or Head Start.

Other comments

- What if household decision making occurred via bargaining?

- Period discount factor is estimated to be 0.81. Too low if model period is a year.

- All siblings become adults at the same time in the model. That may have strange implications for when couples have children in the model. Is that true?

- Intergenerational transfers other than human capital investments are not allowed. This might overestimate the importance of human capital channel.