Would **Baby Bonds Reduce** Racial **Inequality in Retirement** Wealth?

Pension Research Council

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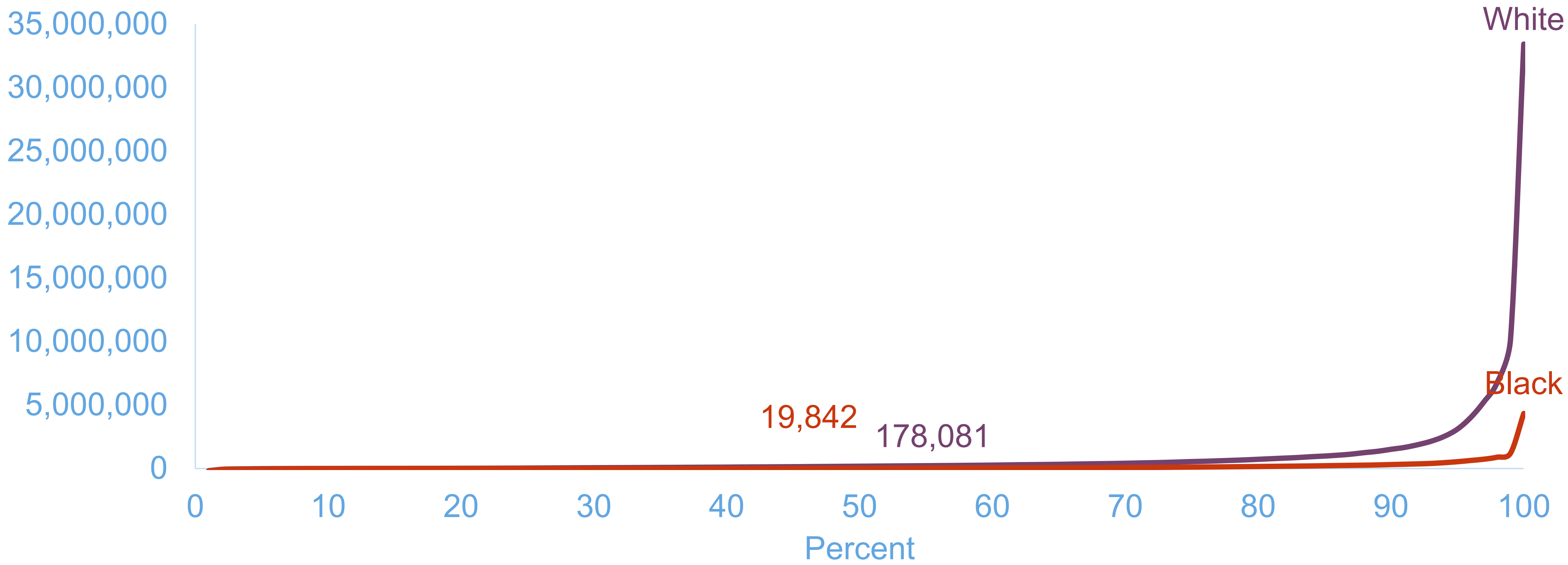
Two wealth inequality problems



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Source: Calculations from Survey of Consumer Finances, 2019

Wealth provides stability, growth, and power

Hard to save while poor, despite existing incentives

- 529s depend on parental participation, regressive tax breaks
- Individual Development Accounts are difficult to stick to

Baby Bonds designed to redress these issues (Hamilton and Darity 2010)

- Federally funded, progressively seeded, $500 to $50,000
- Parents and kids cannot access until early adulthood
- Universal and feasible total cost of $80 billion

Could the program make headway on big wealth issues?

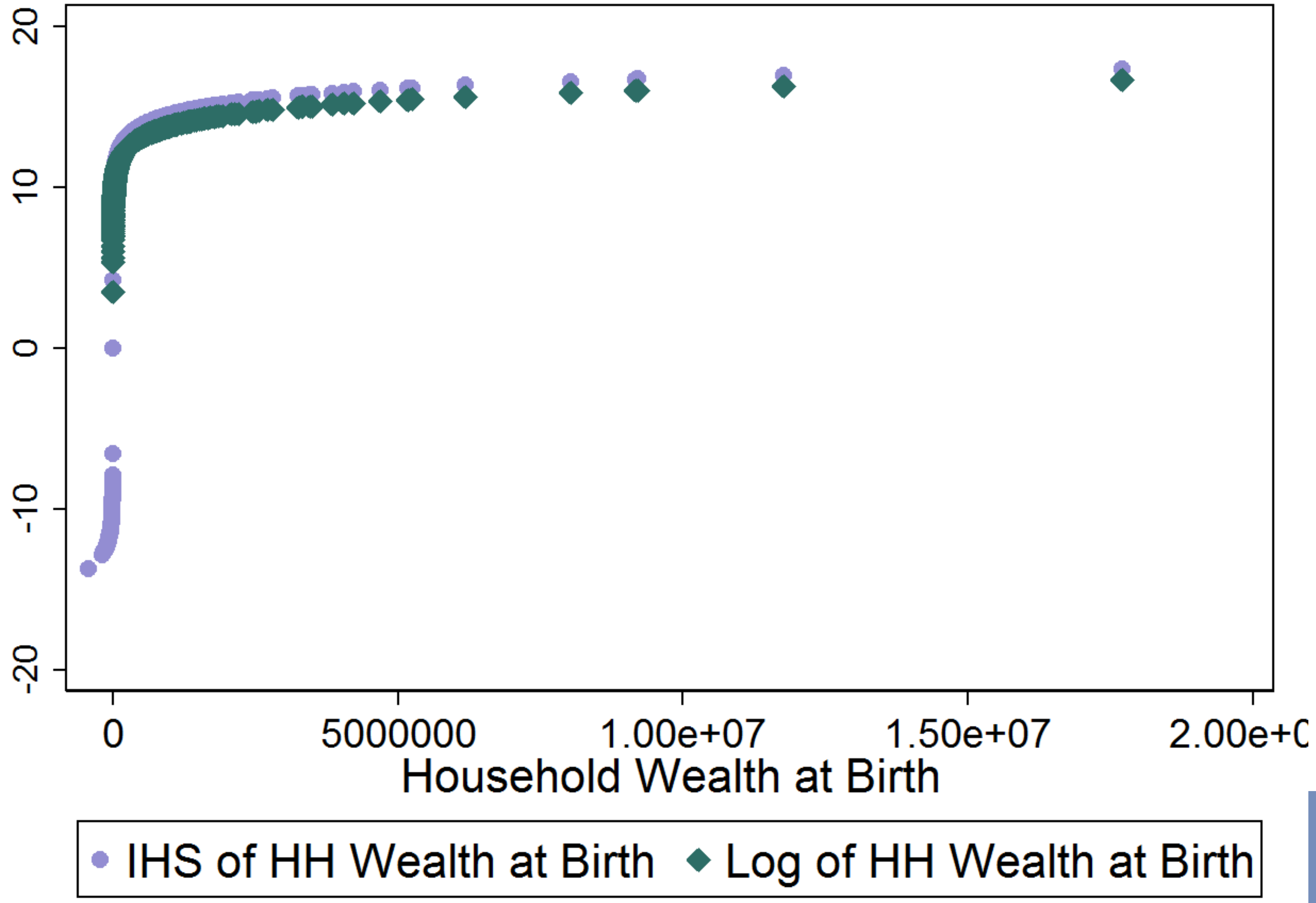
Longitudinal wealth data from birth through Young adulthood

- Young Adults in 2015 PSID, ages 18-25
- Household net worth at birth and in 2015
- Match to 1989 wave if born between ‘89 and ‘91, 1994 wave for ‘92-’96
- All inflated to 2015 USD (Zewde 2020)

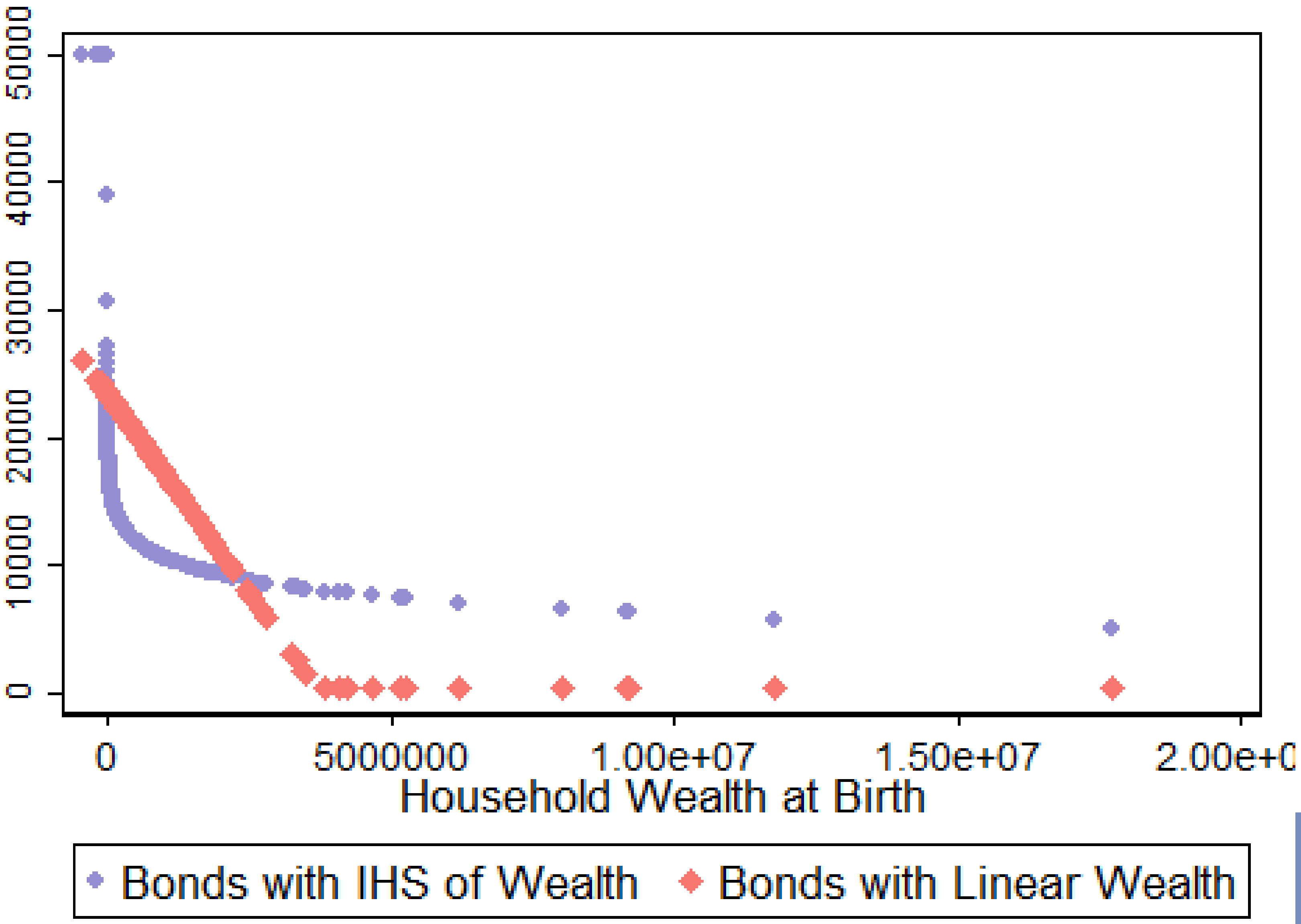
Progressive Distribution of funds

- Assigned categorical values by quintiles of wealth
- Smoothed out discrete values by regressing on IHS-transformed wealth
  - Log(birthwealth + sqrt(birthwealth^2 +1))

IHS: similar to log, but allows negatives



More progressive than a linear regression



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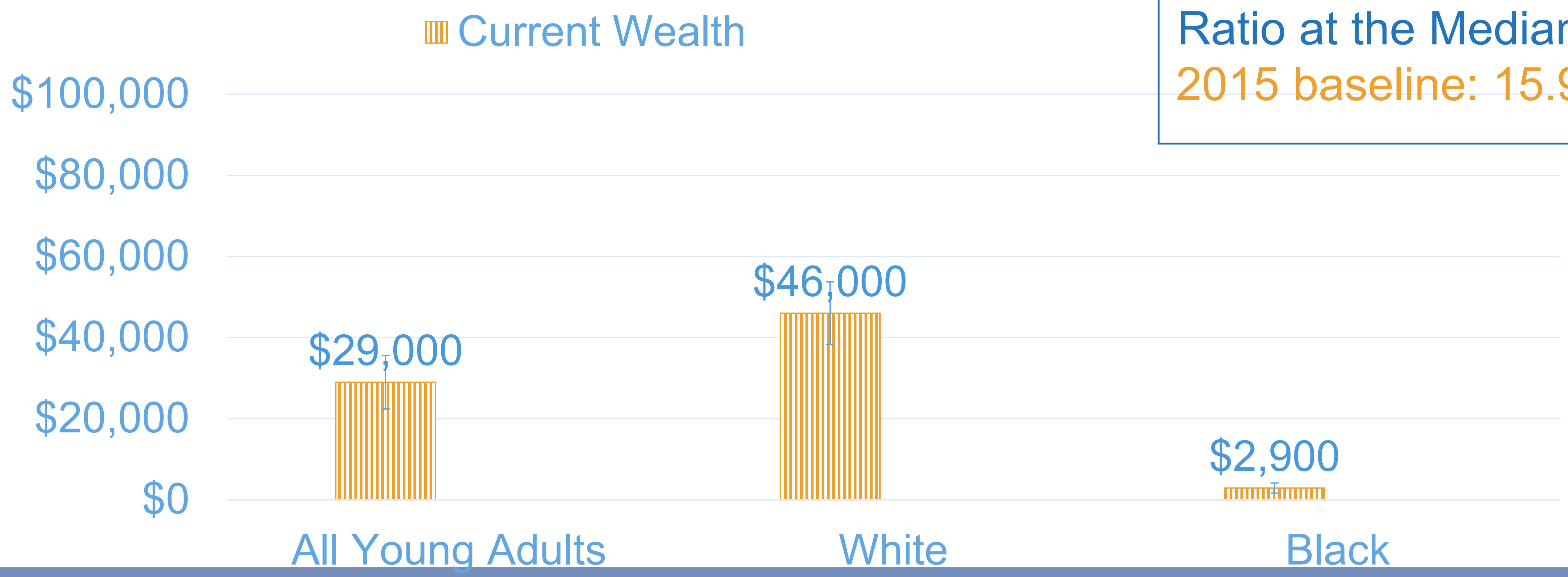
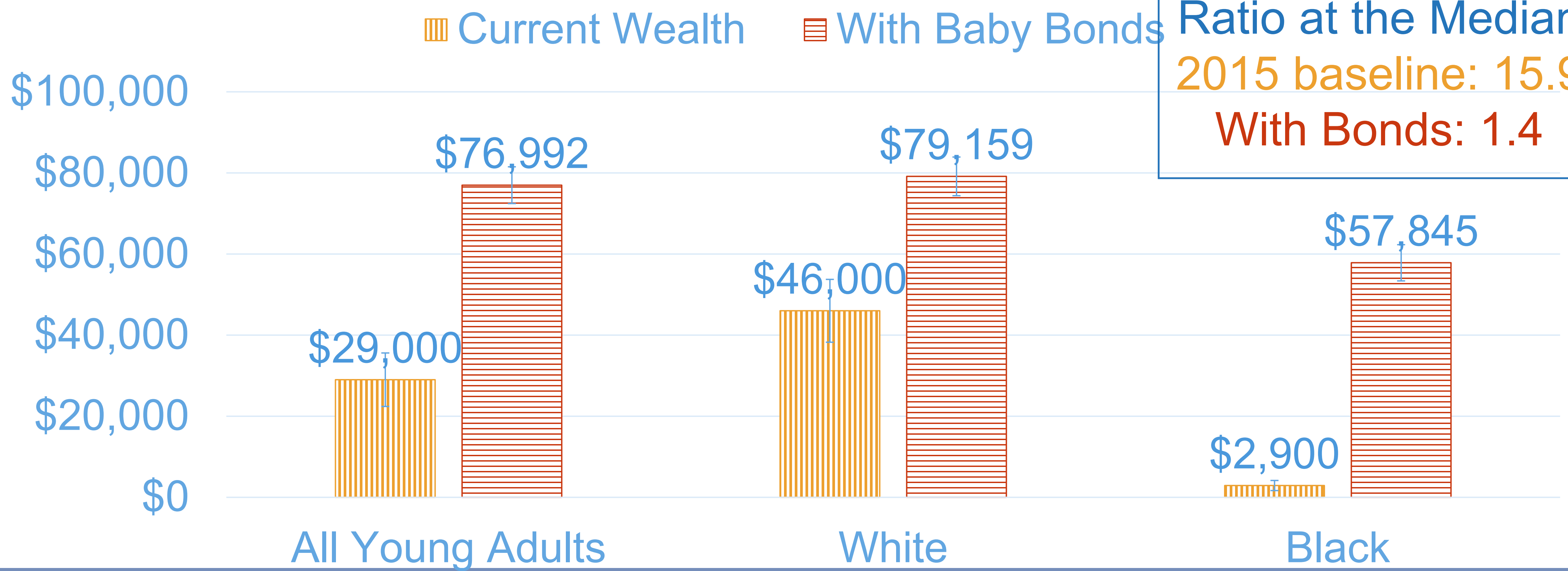
Universal Baby Bonds Reduce Median Racial Wealth Gap

White-Black Wealth Ratio at the Median
2015 baseline: 15.9



Universal Baby Bonds Reduce Median Racial Wealth Gap

White-Black Wealth Ratio at the Median
2015 baseline: 15.9
With Bonds: 1.4



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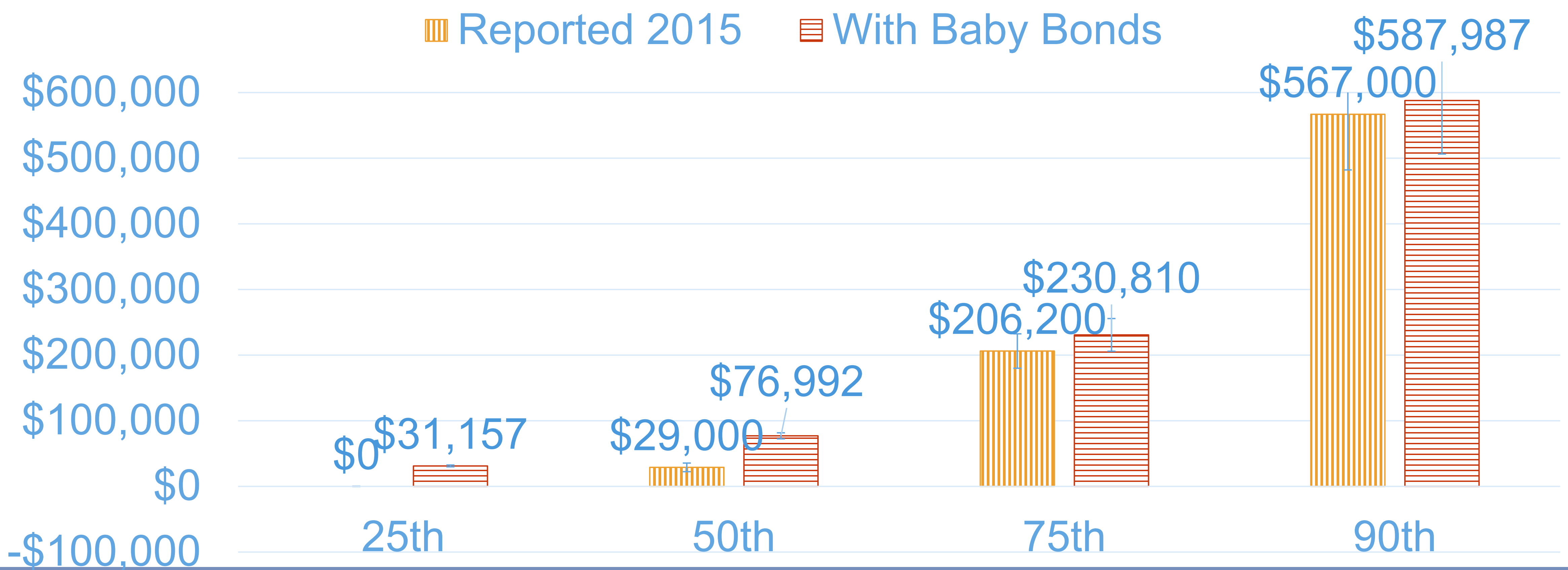
Greater Wealth Increase at Bottom and Middle



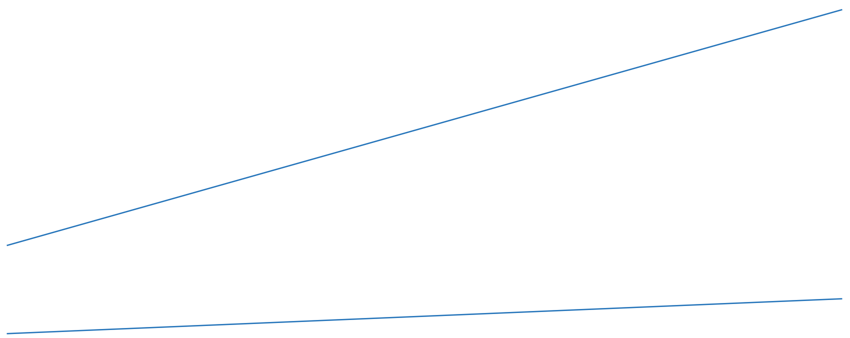
What will then happen over the life course?

- Would we observe an impact 5, 10, 40 years later?

Inequality tends to widen over life course

- Cumulative Dis/Advantage: Individuals or cohorts grow further apart with time
- Dubbed the Matthew Effect (Merton 1968)
- Attenuated by equitable institutions (Zewde & Crystal 2022)

Even small early differences

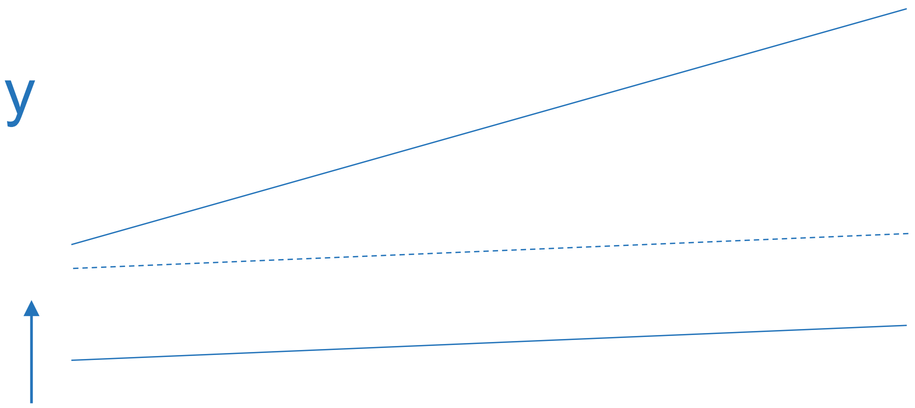


Can generate large differences over the life course

Long term observable impact requires at least:

1. Enough to invest in something
2. Consistent returns to investments

(1) Smaller early differences



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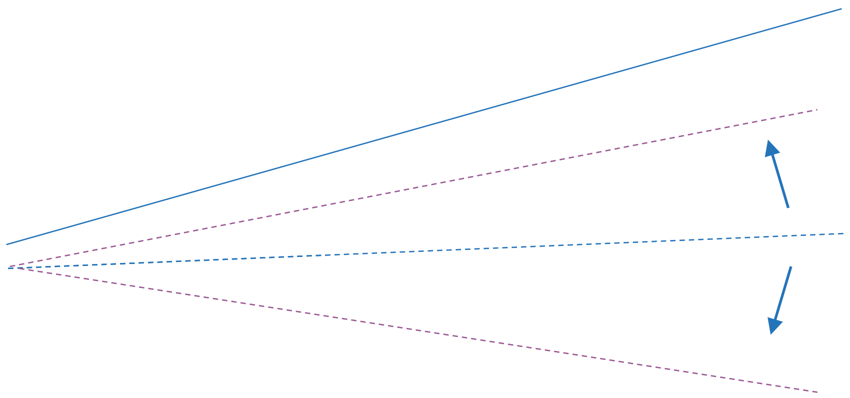

(2) Not *more* divergent than narrowing in (1)

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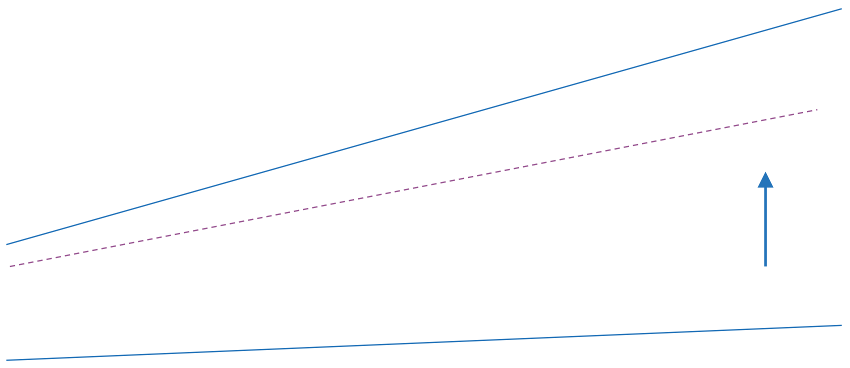

Not likely for a policy of cash infusion to only affect differential returns

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How might existing iterations affect future trajectories?

- $500 | $16,000 | $25,000 towards school, a home, a business, or retirement

Pennsylvania

- Passed | Universal eligibility | $500 max | Higher-ed

Connecticut

- Paused | Medicaid eligibility | $16,000 | 4 choices for use

Washington, DC

- Passed | Medicaid, income up to 300% FPL | $25,000 max | 4 choices for use

Higher ed tuition and fees

- $500 won’t go far
- 4 years at CSU campuses approximately $50k (enough for Assoc deg)
- 4 years at UDC costs about $25k, could cover this

Buying a home

- CT: need $12,400 down (median home $355k)
- DC: need $26,740 down (median home $764k)

First requirement within reach (not in PA)

- Enough to invest in some potentially appreciating assets
- Main threat is tuition and home price inflation outpacing Baby Bond accounts

Potential disparities in capacity to avoid consumption

- Say you need a life saving kidney transplant
- May withdraw early from IRA, or sell or refinance home in a couple of years

Potentially disparate investment vehicles

- If you already have down payment help, you can invest in financial assets
- Portfolio composition key driver of intergenerational correlation in wealth (Charles & Hurst 2003; Boulware & Kuttner 2020)

Potentially disparate returns to the same investment

- Racially disparate rates of home appreciation, returns to ed

Inconsistent returns likely, but hard to specify without a *huge* pilot

Can look to EITC

But small amounts relative to household needs,

Little evidence of savings or investment

(Smeeding, Phillips, & O'Connor 2000)

Table 2
Effect of Earned Income Tax Credit (EITC) Exposure on Education and Employment Outcomes (Reduced Form)

	Dependent Variable					
Variable	High School Graduate; Mean = .92 (1)	At Least Some College; Mean = .52 (2)	College Graduate; Mean = .31 (3)	Highest Grade Completed; Mean = 13.7 (4)	Employed; Mean = .817 (5)	Earnings (2013$); Mean = 25,391 (6)
EITC exposure between ages 0 and 5	−.005	−.000	−.007	−.024	.021	646.1
	(.005)	(.006)	(.019)	(.071)	(.022)	(818.3)
EITC exposure between ages 6 and 12	−.003	.002	.009	.008	−.002	42.4
	(.003)	(.005)	(.006)	(.022)	(.007)	(415.1)
EITC exposure between ages 13 and 18	.012***	.006	.013**	.081***	.008*	564.0**
	(.003)	(.007)	(.005)	(.025)	(.004)	(244.9)

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Baby Bonds improve net worth position for young adults

- Disproportionately for Black and low-wealth populations
- Expanded capability to own appreciating assets
- Potentially higher appreciation rates for the most well-off recipients
  - At the extreme could increase inequality at retirement

Policies that narrow divergence also those that increase equity broadly

- Maintain affordability of society’s building blocks: ed, homes, healthcare
- Increase impact of any working-age intervention on late-life wealth

Parsimonious direct approach: pair Baby Bonds with programs aimed squarely at retirement