Economics in Context
Update April 2015
Designed for use with the Global Development And Environment Institute's *In Context* textbooks

The Great Recession's Impact on Wealth Inequality in the United States

The Great Recession clearly reduced overall wealth in the United States. According to analysis by economist Edward Wolff, median net worth in the U.S. declined by 44% from 2007 to 2010. But how did the Great Recession, and subsequent recovery, impact the distribution of wealth? Wolff's analysis provides the first detailed estimates of how the assets of different groups were affected by the financial crisis.

One of Wolff's main findings is that during the Great Recession (2007-2010) wealth inequality increased significantly in the United States. During this period the share of all wealth held by the richest 20% rose from 85% to 89%, and the Gini coefficient based on wealth increased from 0.834 to 0.866. The assets of the middle class were particularly hard-hit by the Great Recession. The main reason is that middle-class households tend to have a disproportionately high share of their assets in the equity value of their homes. When median home prices declined by 24% during the Great Recession, many households saw the positive equity in their homes become a net liability as the market price of their homes fell below their remaining mortgage balance. As Wolff writes:

> The key to understanding the plight of the middle class over the Great Recession was their high degree of leverage and the high concentration of assets in their home. The steep decline in median net worth between 2007 and 2010 was primarily due to the very high negative rate of return on net worth of the middle three wealth quintiles (-10.6 percent per year). This, in turn, was attributable to the precipitous fall in home prices and their very high degree of leverage. (p. 43)

Wolff also found that wealth inequality based on race and ethnicity increased during the Great Recession. In 2007 median wealth among black households stood at only 19% of median wealth among white households. By 2010 this percentage had fallen to 14%. The relative impact of the Great Recession on Hispanic households was even more severe, with their median net worth plummeting from 26% to 15% of white households. For both groups, the primary explanation again seems to be found in the fact that a disproportionate share of their net assets were reduced (or became negative) as a result of the decline in home values.

Surprisingly, median assets in the U.S. did not recover over the period 2010-2013, despite rising home values and stock market prices. Wolff concludes that this is a result of the high dissavings of the middle class. So while the good news is that the outstanding debt of middle-class households fell during this period, it appears

Note: This update specifically relates to *Microeconomics in Context* Chapter 10, *Macroeconomics in Context* Chapter 15, *Principles of Economics in Context* Chapters 11 and 30.
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many drew down their assets to pay debts and finance consumption. With wages stagnating for many households, they were able to maintain existing consumption levels and reduce debt only by selling off some of their assets.

Overall, there was little change in wealth inequality from 2010 to 2013, with the Gini coefficient increasing from 0.866 to 0.871. Wealth inequality on the basis of race also remained about the same over this time period. Wolff's data indicate that black and Hispanic households had relatively high rates of return on their assets over 2010-2013, but that this was offset by particularly high dissavings rates.

As of 2013, median net worth among those in the top 1% stood at over $18 million, an increase of 82% compared to 1983, even after adjusting for inflation. For those in the middle wealth quintile, their median net assets fell from about $79,000 to $68,000 over 1983-2013. But poorer households fared even worse. Those in the bottom 40% saw their median worth fall from about positive $7,000 in 1983 to negative $11,000 in 2013.

Note:
The wealth data presented above are all median values. The Wolff paper also documents trends in mean wealth. While real median wealth in the U.S. fell from $78,000 to $64,000 between 1983 and 2013, real mean wealth increased from $304,000 to $509,000. Given that the median value decreased while the mean value increased, we can conclude that wealth inequality increased during this time period.

Source:
Wolff, Edward N. 2014. "Household Wealth Trends in the United States, 1962-2013: What Happened over the Great Recession?" *National Bureau of Economic Research Working Paper 20733*, December 2014.