Parental Wealth and Early Labor Market Outcomes

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Introduction

– Why do some young adults thrive in the labor market while others struggle, even when they share similar educational backgrounds and skills?

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- Why do some young adults thrive in the labor market while others struggle, even when they share similar educational backgrounds and skills?
- We study the role of family wealth for early career outcomes focusing on young adults with similar characteristics

What our paper does

- We use rich administrative data on the universe of individuals in Sweden
  - Collect parental wealth information when children are age 16
  - Focus on early labor market outcomes (first five years after entry)
- Document novel facts and, in particular, the role of firms in propagating wealth differences (using MEE data)
- Develop a parsimonious model to explain the empirical facts and use it for policy simulations

Data

Data description

Population wide data from Sweden (16–74 y.o., 1990–2019)
$\Rightarrow$ our main sample is individuals who turn 18 between 2000–2007

1. Wealth registers (real, net and financial wealth), 2000–2007
   - → Liquid wealth (financial wealth and positive housing equity)
2. Matched employer-employee data (16–74 y.o., 1990–2019)
   - Focus on the first five years after labor market entry
3. Intergenerational registers linking children to their parents (biological/adoptive)

Summary statistics by wealth decile

	Family wealth at age 16, deciles									%ile
	1–2	3	4	5	6	7	8	9	10	100
Median w.	0	5.6	32.4	88.2	165.5	183.2	258.9	461.7	1226.9	5810.5
Mean w.	0.6	10.5	37.3	91.4	165.9	233.4	333.0	558.5	2913.6	16752.2
Edu. years	12.2	12.6	13.0	13.2	13.3	13.4	13.6	13.9	14.3	14.5
Bachelor (%)	18.6	23.7	28.	32.7	35.3	37.4	41.3	46.6	54.6	59.6
Age grad.	22.3	22.6	22.9	23.1	23.2	23.3	23.6	23.9	24.3	24.6
Emp. rate (%)	77.2	83.5	86.5	87.8	88.0	88.3	89.6	90.3	90.4	88.6
Self-emp. (%)	0.8	0.8	0.9	1.0	1.1	1.2	1.2	1.4	2.1	3.3
Obs.	172335	86554	86760	86738	86714	86715	86749	86779	86855	8657

Table 1: Summary statistics by wealth decile.
Note: Wealth (w) is measured as liquid wealth owned by children and their parents when the child is 18 years old, in thousands of Swedish krona at 2010 prices. Bachelor (%) is the share graduating with at least a bachelors degree.

Early career labor market outcomes

Early career labor market outcomes

We look at outcome variables averaged over the first five years after entry and residualized as follows:

$$y_{ixt} = \phi_{xt} + f(earn_p) + \epsilon_{it}$$

For example, the log earnings of worker i, belonging to group x, in year t, where groups are defined using interacted fixed effects

- "Raw": age and birth year cohort
- "Edu": + years of education
- "Major": + degree major
- "Residualized": + municipality and a polynomial in parental earnings

Average earnings

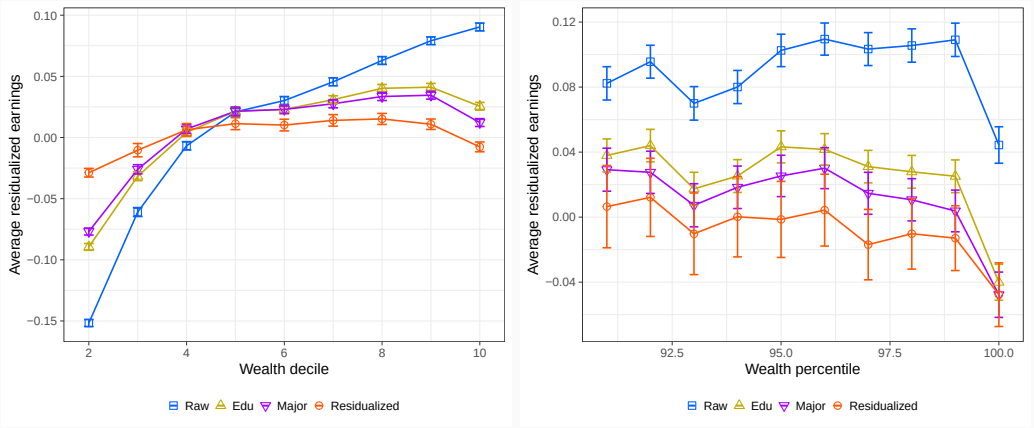

Figure 1: Average residualized log earnings for all wealth groups (left) and the top 10%. Variance

Employment

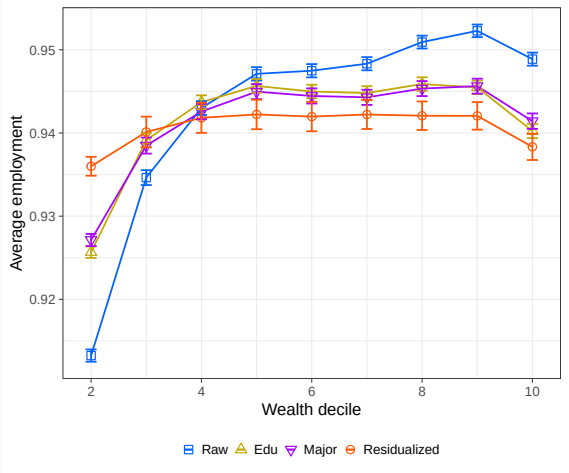

Figure 2: Employment rate by wealth decile. Labor market transitions

Within and between firm differences in earnings

– We decompose individual earnings into between and within firm contributions

- Between-firm – highlights the role played by the allocation of workers to firms
- Within-firm – highlights the potential differences in ability or labor supply
- We do a similar decomposition using 3-digit occupation codes as well

$$y_{ij} = \underbrace{\frac{\sum_{i \in j} y_{ij}}{N_{i \in j}}}_{\text{Between firm}} + \underbrace{y_{ij} - \frac{\sum_{i \in j} y_{ij}}{N_{i \in j}}}_{\text{Within firm}}.$$

The role of firms

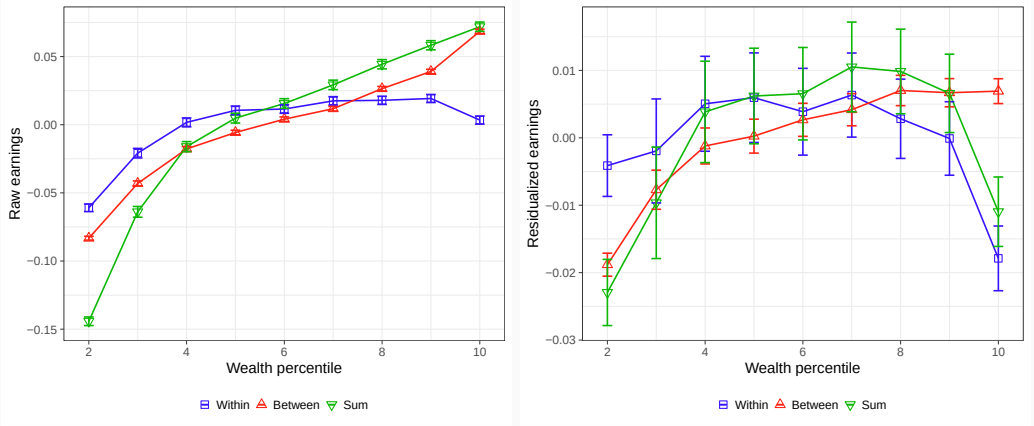

Figure 3: Within and between-firm components of log earnings using firms with at least 5 workers (raw series on the left and residualized on the right). Occupations

Model

Model

- Set up a parsimonious search model with savings (building on Lise 2013), heterogenous job destruction, and disutility from working
- Key mechanisms:
  - Wealth can be used to finance consumption when unemployed
  - Job destruction rate decreases in wages
  - Decreasing marginal utility from consumption
- Predictions:
  1. Earnings should converge over time due to the curvature of the utility function
  2. The safety net from parental wealth is more important when jobs are scarce
- Social networks provide an alternative explanation for the observed sorting. However, we don't find that this can explain the patterns in the data. Networks

Earnings convergence

- We run a matched regression[1] to test for earnings convergence
- Individuals from deciles 1 and 2 are considered treated and deciles 4–9 are potential controls

$$y_{itp} = \alpha_i + f(earn_p) + \sum_{\tau=0}^{10} \beta_\tau D_{i,\tau} + \theta_{p,t} + \gamma_m + \varepsilon_{itk} \tag{1}$$

- Controlling for individual FE α_i, parental earnings $f(earn_p)$, interacted matched pair and time FE $\theta_{p,t}$, and educational major FE γ_m

[1] We use coarsened exact matching (CEM) and match individuals based on year of entry, years of education, age at graduation, gender, municipality of residence, and earnings rank of parents.

Results matched regression

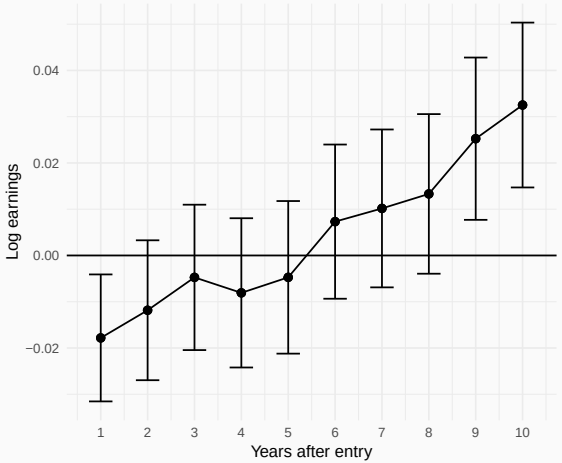

Figure 4: Earnings gap by years since graduation.

Local labor markets

– To test whether the role of parental wealth is more important when jobs are scarce, we use local variation in employment rates. We:

1. define local labor markets as municipality-year-age observation separating individuals with and without tertiary education
2. calculate the nonemployment rate for each LLM and the average wage earnings for different wealth deciles
3. compare the relative average earnings between wealth deciles

Local labor market results

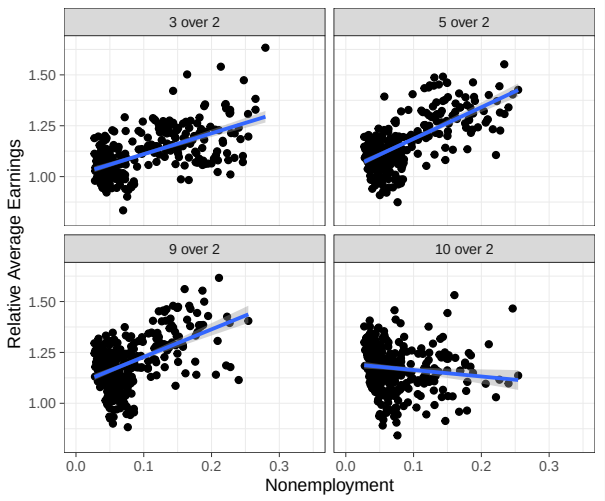

Figure 5: Relative local average earnings and local nonemployment rate. We restrict the analysis to observations with at least 100 individuals in each group. Employees only

Model vs data: earnings and job separations

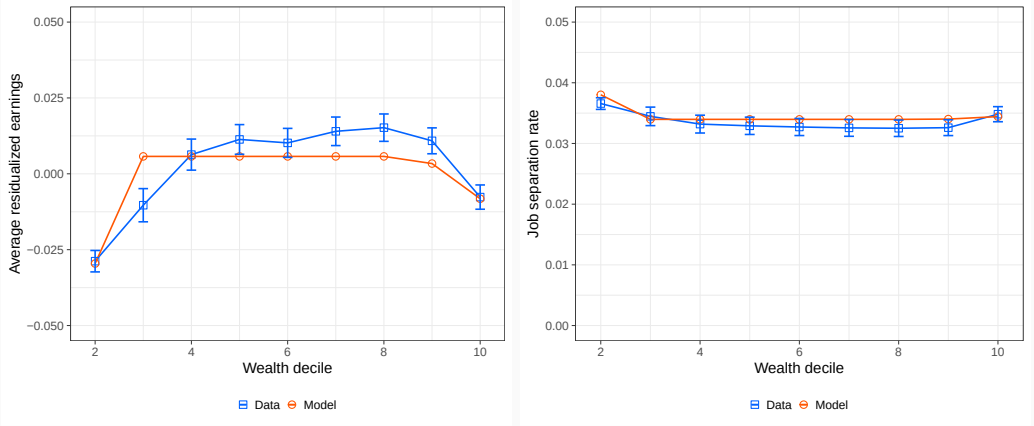

Figure 6: Average log earnings for different wealth groups, observed and simulated (left), and job separations (right).

Policy experiment

- We observe big differences in family wealth, and that this affects labor market outcomes
- Could providing a subsidy similar to unemployment insurance upon initial labor market entry reduce the importance of family background?
- In the model, workers who enter the labor market receive basic social insurance (b_{min})
  - → Polycy experiment: Increase b_{min} and finance it through labor taxes on all workers

Providing more benefits upon entry (preliminary)

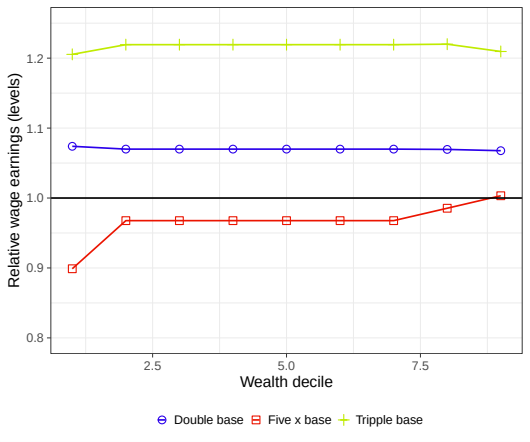

Figure 7: Simulated increase in benefits: the effect on average net-of-tax wages

Conclusion

Conclusion

- Parental wealth is important for early labor market outcomes:
  - Wealthier individuals earn more, have a higher employment rate, lower variance of earnings and a lower probability to separate from their jobs
  - This relationship holds after we control for a wide range of observables, with the exception of workers from the top 10%
- We find evidence of wealthier individuals sorting into higher-paying firms (controlling for observables, along the whole spectrum)
- We interpret these results through the lens of a job search model and show that increasing UIB at entry can increase average wages for young adults

References

Kramarz, F., & Nordström Skans, O. (2014). When strong ties are strong: Networks and youth labour market entry. *Review of Economic Studies*, 1164–1200.

San, S. (2022). The role of social connections in the labor market: A new model and evidence from israel. *mimeo*.

Eliason, M., Hensvik, L., Kramarz, F., & Nordström Skans, O. (2023). Social connections and the sorting of workers to firms. *Journal of Econometrics*.

Staiger, M. (2021). The intergenerational transmission of employers and the earnings of young workers. *Washington Center for Equitable Growth Working Paper. https://equitablegrowth.org/working-papers/the-intergenerational-transmission-of-employers-and-the-earnings-of-young-workers/[Accessed 22 June 2022]*.

Appendix: Variance of earnings

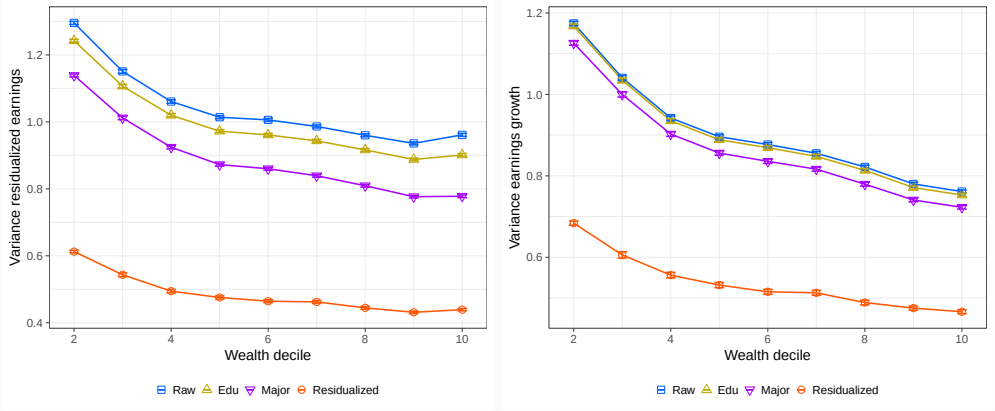

Figure 8: The variance of earnings (left) and the variance of log growth rate and wealth (right) by family wealth decile. Back

Appendix: Labor market transitions

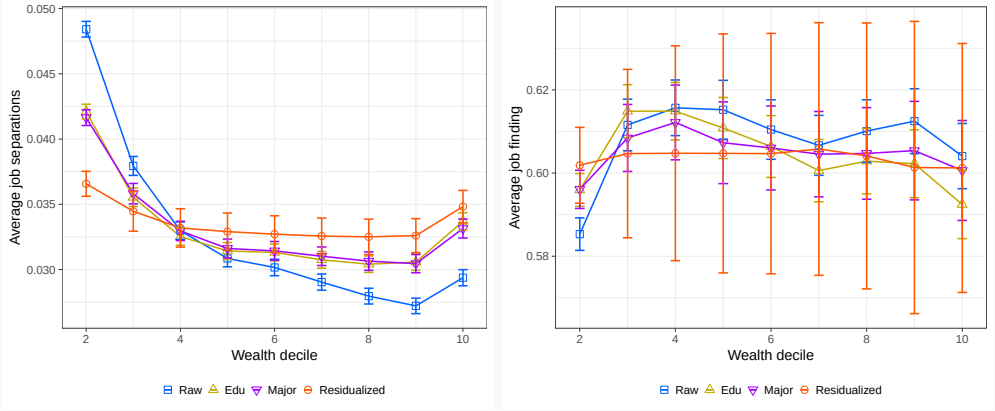

Figure 9: Transitions from employment to nonemployment (left), transitions from nonemployment to employment (right) by wealth decile. Back

Appendix: Job change rate

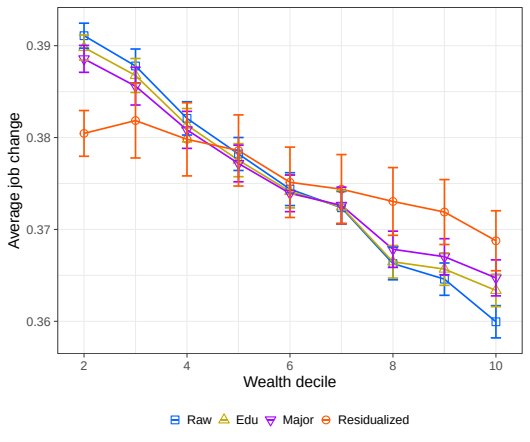

Figure 10: Job change rates by wealth decile. Back

Appendix: The role of occupations

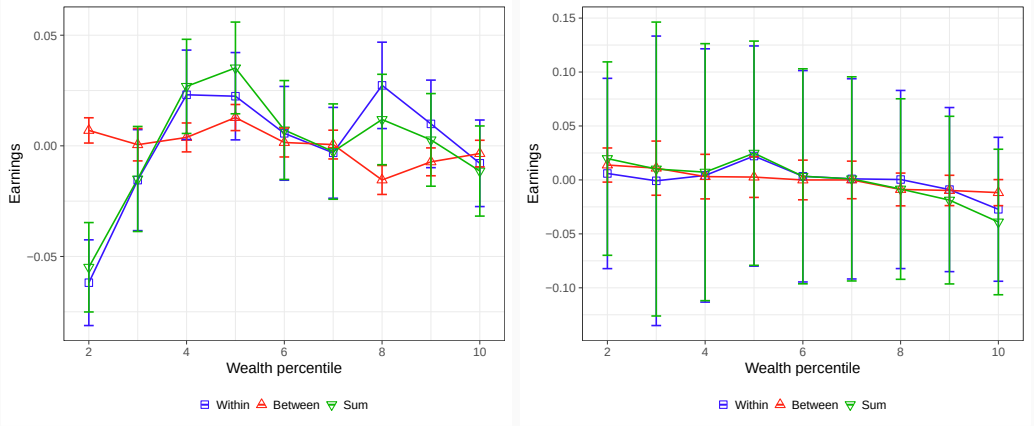

Figure 11: Within and between-occupation components of log earnings using individuals with observed and up-to-date occupation codes (raw series on the left and residualized on the right). Back

Local labor market results

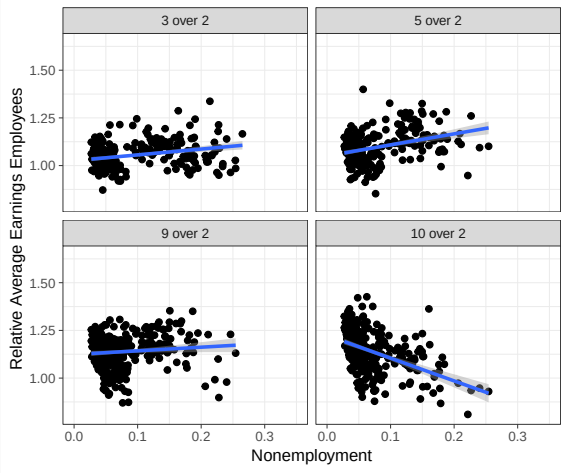

Figure 12: Relative local average earnings of employee and local nonemployment rate. We restrict the analysis to observations with at least 100 individuals in each group.

Back

Appendix: Networks

- Social networks is one possible explanation for the sorting across wealth groups.
  - Social networks have been found to be important for hiring and employment (e.g., Kramarz & Nordström Skans, 2014; San, 2022; Eliason et al., 2023), and wages (e.g., Staiger, 2021).
- To get a notion of the interaction between social networks and wealth, we construct 10-year rolling windows with parental workplaces and colleagues.
  - We categorize young adults who at any point during the first five years on the labor market:
    - works at their parents' current or former workplace (Parent workplace).
    - works with any former co-worker of a parent (Co-worker).
    - never works within their parents' social network (Outside).

Fraction of young adults working within parents' network

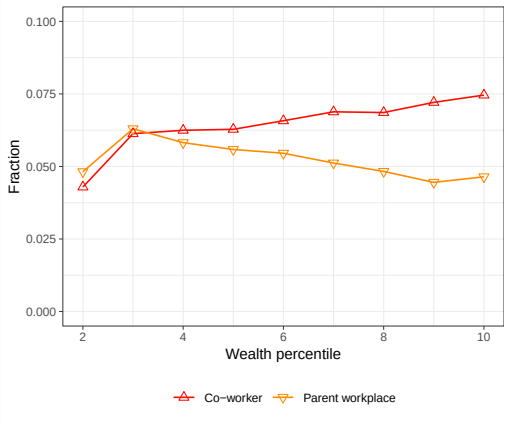

Figure 13: The fraction of young adults working within their parents network by wealth group.

Average earnings across wealth groups

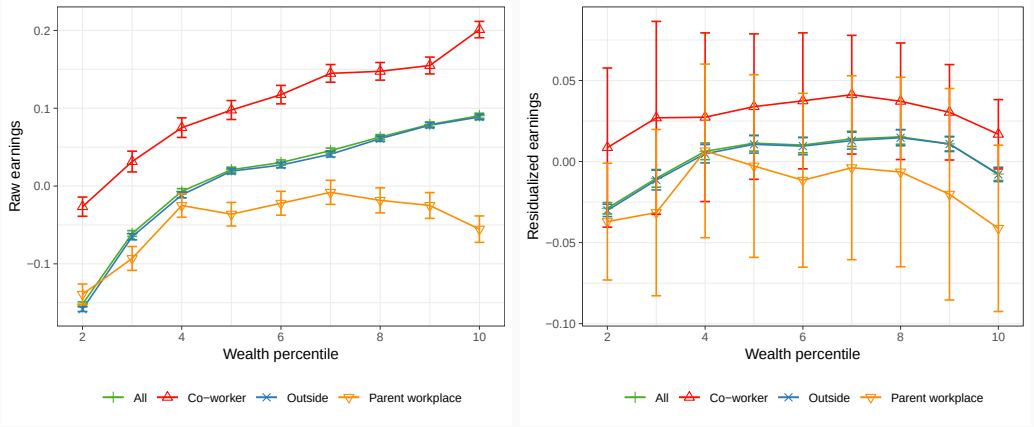

Figure 14: The average earnings by network and wealth group raw (left) and residualized (right). Back