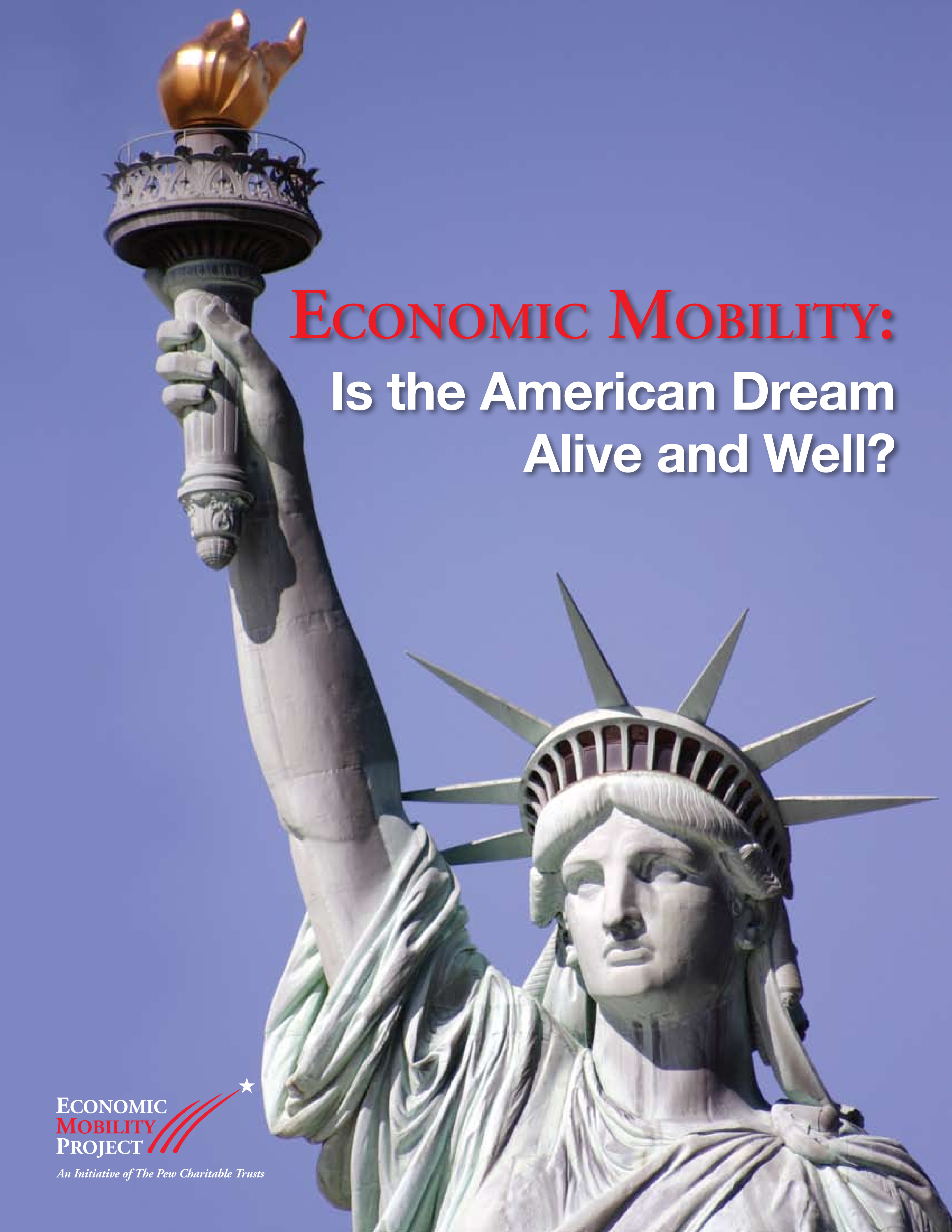


Economic Mobility:

Is the American Dream Alive and Well?

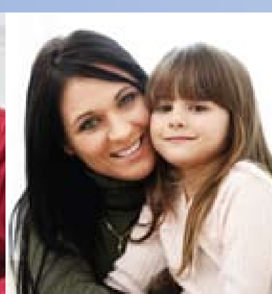
Economic Mobility Project
An Initiative of The Pew Charitable Trusts

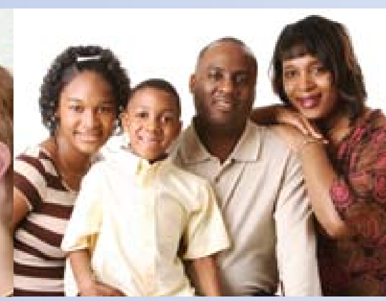
About the Economic Mobility Project

With the convergence of a presidential election cycle, income inequalities last seen nearly a century ago, and emerging new data on the state of mobility in America, the present moment provides a unique opportunity to refocus attention and debate on the question of economic mobility and the American Dream.

The Economic Mobility Project is a unique nonpartisan collaborative effort of The Pew Charitable Trusts and respected thinkers from four leading policy institutes — The American Enterprise Institute, The Brookings Institution, The Heritage Foundation and The Urban Institute. While as individuals they may not necessarily agree on the solutions or policy prescriptions for action, each believes that economic mobility plays a central role in defining the American experience and that more attention must be paid to understanding the status and health of the American Dream.

In the months to come, the project will develop new findings, tackle difficult questions such as the role of education, race, gender, and immigration in mobility, and analyze the effects of wealth accumulation and the extent to which short-run fluctuations in income may be affecting mobility. Our purpose is to provoke a more rigorous discussion about the role and strength of economic mobility in American society.

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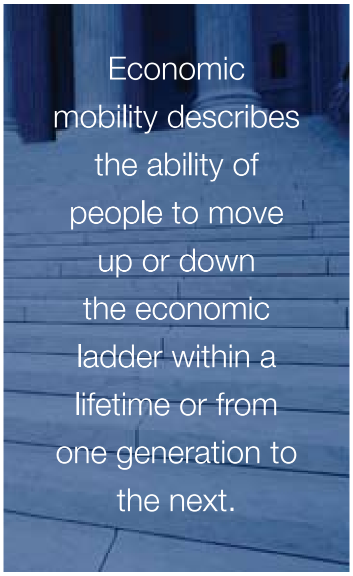
Economic Mobility:
Is the American Dream Alive and Well?

For more than two centuries, economic opportunity and the prospect of upward mobility have formed the bedrock upon which the American story has been anchored — inspiring people in distant lands to seek our shores and sustaining the unwavering optimism of Americans at home. From the hopes of the earliest settlers to the aspirations of today's diverse population, the American Dream unites us in a common quest for individual and national success. But new data suggest that this once solid ground may well be shifting. This raises provocative questions about the continuing ability of all Americans to move up the economic ladder and calls into question whether the American economic meritocracy is still alive and well.

Recent studies suggest that there is less economic mobility in the United States than has long been presumed. The last thirty years has seen a considerable drop-off in median household income growth compared to earlier generations. And, by some measurements, we are actually a less mobile society than many other nations, including Canada, France, Germany and most Scandinavian countries. This challenges the notion of America as the land of opportunity.



Despite these potentially troubling findings, the current national economic debate remains focused too narrowly on the issue of inequality, leaving aside the more important core question of whether the foundation of opportunity, economic mobility, remains intact. As Federal Reserve chairman Ben Bernanke recently noted:

Although we Americans strive to provide equality of economic opportunity, we do not guarantee equality of economic outcomes, nor should we. Indeed, without the possibility of unequal outcomes tied to differences in effort and skill, the economic incentive for productive behavior would be eliminated, and our market-based economy — which encourages productive activity primarily through the promise of financial reward — would function far less effectively. [1]

Why should Americans care about economic mobility? How should citizens and policy makers alike understand economic mobility? This report addresses these questions in the same way Americans think about their lives and imagine the future for their children: it looks at how a family's standard of living improves from one generation to the next. Further, it asks whether a rising tide of economic growth lifts all ships, whether individual effort and talent allow a particular family's boat to move ahead of others in the fleet, or whether there is some combination of both.

This report also discusses the implications of new analysis showing that the strength of America's rising economic tide has not benefited significant segments of our citizenry. Gone are the days when a stable, single income was enough to launch the next generation toward growing prosperity. In modern America, upward mobility is increasingly a family enterprise. And during a time of rapidly shifting household structure, this has significant repercussions for the economic mobility prospects of millions of Americans.

"Among aristocratic nations... families remain for centuries in the same condition. ... Among democratic nations, new families are constantly springing up, others are constantly falling away, and all that remain change their condition."

– Alexis de Tocqueville,
Individualism in Democratic Countries

What is Economic Mobility?

There are many ways to define *economic mobility*. For simplicity's sake, and because it best captures what people care most about, this report measures economic mobility by trends in personal or family incomes.

Economic mobility also has a time dimension. One can talk about mobility over a lifetime, between generations, or over a short period such as a year or two. Unlike analyses that investigate shorter-term fluctuations or volatility in incomes, this report focuses mainly on ***intergenerational mobility*** — the extent to which children move up or down the income spectrum relative to their parents' generation. This intergenerational analysis is perhaps most in keeping with the spirit of the American Dream, in which each generation is meant to do better than the one that came before.

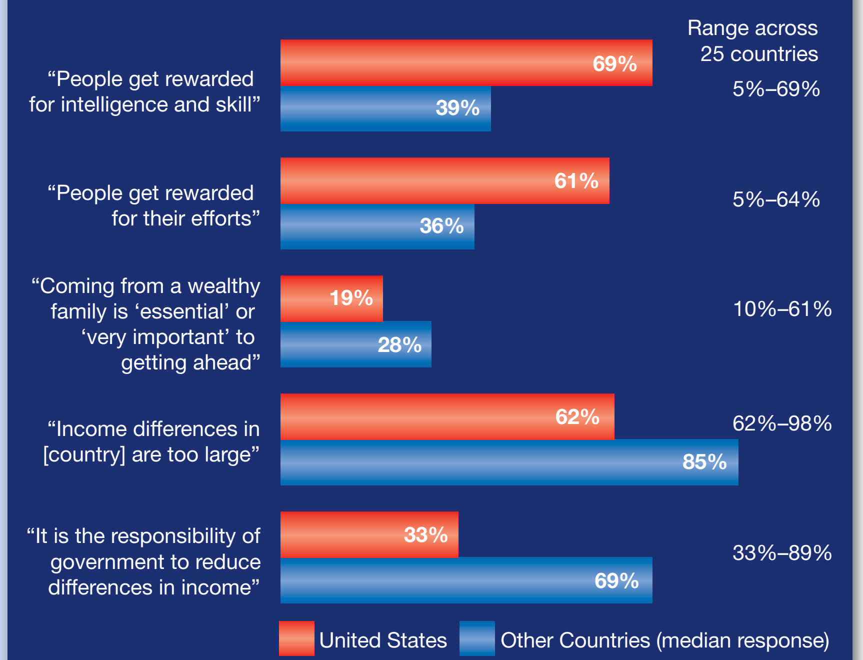
Finally, economic mobility can be measured in *absolute* or *relative* terms. The distinction between the two is very important and any analysis that focuses on one measure to the exclusion of the other misses a significant piece of the larger mobility story. ***Absolute mobility*** refers to a dynamic in which a rising tide is lifting all boats, but it does not capture the likelihood that boats are changing places in the harbor. ***Relative mobility***, by contrast, suggests that boats are changing places, but says nothing about the strength of the tide. In other words, the health and promise of the American Dream depends on some combination of both relative and absolute mobility.

A National Belief in Mobility

"A bedrock American principle is the idea that all individuals should have the opportunity to succeed on the basis of their own effort, skill, and ingenuity."

– Federal Reserve Chairman Ben Bernanke [2]

Figure 1. Percentage of Citizens Agreeing with Belief that...



Source: Brookings Institution tabulations of data from International Social Survey Program, 1999.

Historically, Americans have believed that hard work and talent bring a just reward, and that our society is, and should be, constructed to provide equality of opportunity, not to guarantee equality of outcomes.

The belief in America as a land of opportunity may also explain why rising inequality in the United States has yielded so little in terms of responsiveness from policy makers: if the American Dream is alive and well, then there is little need for government intervention to smooth the rough edges of capitalism. Diligence and skill, the argument goes, will yield a fair distribution of rewards.

The underlying belief in the fluidity of class and economic status has differentiated Americans from citizens in the majority of other developed nations. As the data in Figure 1 suggest, compared to their global counterparts, Americans have tended to be far more optimistic about their ability to control their own economic destinies through hard work, less likely to believe that coming from a wealthy family is important to getting ahead, less likely to think that differences in income within their country are too large, and less likely to favor the government's taking responsibility to reduce those differences.

Most observers attribute the optimism captured in this data to the conviction that what Americans lack in equality of outcomes, they make up for in economic mobility. But what happens if the public begins to question its prospects for upward mobility?

U.S. Income Inequality is Growing

The Stakes are High and the National Mood is Somber

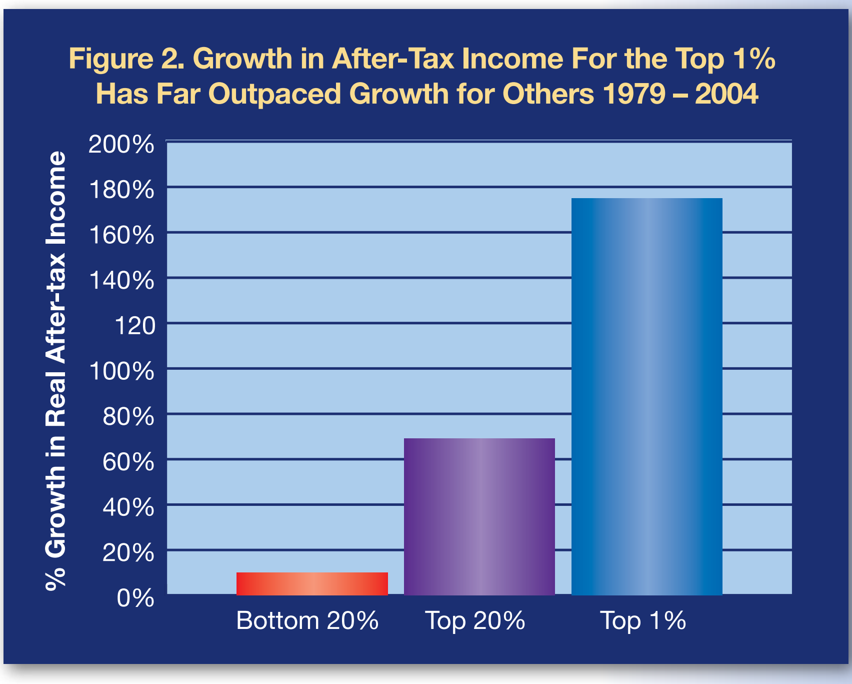
Income inequality has been widening for nearly three decades in the United States. Amidst a flurry of new data and media reports, President George W. Bush addressed the issue for the first time in January 2007 during remarks to Wall Street: "The fact is that income inequality is real — it's been rising for more than 25 years."[3] As the data in Figure 2 indicate, the Congressional Budget Office finds that between 1979 and 2004, the real after-tax income of the poorest one-fifth of Americans rose by 9 percent, that of the richest one-fifth by 69 percent, and that of the top 1 percent by 176 percent.

Focusing on the familiar story of rising inequalities between CEOs and their employees yields figures that are perhaps even more striking. Between 1978 and 2005, CEO pay increased from 35 times to nearly 262 times the average worker's pay.[4] Said another way, by 2005, the typical CEO made more in an hour than a minimum-wage worker made in a month.

In the high-stakes environment of a society with rapidly growing income inequality, it is ever more critical that society provides its citizens with a fair shot at competing for the economic rewards that come with success. And in today's economic game, the stakes are indubitably high. Widening income inequalities may be tolerable if everyone has a shot at the top. But is that the case in America today?

Perhaps driven by widening inequality and a concern about the fairness of the game, there is a tangible and growing sense of pessimism among the American public. In exit polls after the 2006 election, less than one- third of the voters said that they thought life would be better for the next generation.[5] In another poll, over half of Americans surveyed thought that the American Dream is no longer attainable for the majority of their fellow citizens.[6] Other polls suggest that Americans are increasingly worried that they will be able to maintain the standard of living they currently enjoy.[7]

The nation is ill at ease and seems to be wondering whether increasing inequality is affecting one's ability to get ahead. Although not definitive, some research suggests that greater inequality will produce less economic mobility in a society where the gaps between the rich and the poor are very wide.[8] In a March 2007 Pew Research Center poll, 73 percent of respondents — an 8 percentage increase since 2002 — agreed with the statement, "Today it's really true that the rich just get richer while the poor just get poorer."[9]



Source: Authors' calculations from CBO, 2006, Table 1C.

With an emerging public policy debate that is responding to an increasingly anxious public, an emphasis on economic mobility enables policymakers to focus on underlying causes of inequality. So long as the policy discussion remains focused on income inequality alone, a limited set of solutions may be on the table such as a more progressive tax code or enhanced government benefits. Likewise, economic growth alone will not solve the problem. While such solutions may or may not temper inequalities in the short-term, they do little to address the root causes. By looking at economic mobility we give greater attention to the underlying sources of opportunity in America, be they education, health care, family environments, culture, labor markets or other institutions or factors.

Absolute and Relative Mobility

Mobility can occur across generations in two ways, as mentioned earlier. First, upward *absolute mobility* occurs because of economic growth, which normally ensures that each generation is better off, or has a higher standard of living, on average, than the one before. With absolute mobility, children will usually do better than their parents.

Second, *relative mobility* can occur regardless of what is happening to the society as a whole. Individuals can change their position relative to others, moving up or down within the ranks as one would expect in a true meritocracy.

To illustrate the importance of relative mobility, consider three hypothetical societies with identical distributions of wealthy, poor, and middle-class citizens:[10]

- **The meritocratic society.** Those who work the hardest and have the greatest talent, regardless of class, gender, race, or other characteristics, have the highest income.

- **The "fortune cookie" society.** Where one ends up bears no relation to talent or energy, and is purely a matter of luck.

- **The class-stratified society.** Family background is all-important — children end up in the same relative position as their parents. Mobility between classes is little to nonexistent.

Given a choice between the three, most people would choose to live in a meritocracy, which is, by its nature, fairer and more just. In a meritocracy, success is dependent on individual action, whereas in a class-stratified or "fortune cookie" society, people are buffeted by forces beyond one's control. Even if the level of income inequality were identical in each of these societies, most people would judge them quite differently. In fact, most individuals might well prefer to live in a meritocracy with more income inequality than in a class-stratified or "fortune cookie" society with a more equal income distribution. However, even in a meritocracy people are born with different genetic endowments and are raised in different family environments over which they have no control, raising fundamental questions about the fairness of even a perfectly functioning meritocracy. These circumstances of birth may be the ultimate inequalities in any society. That said, a meritocracy with a high degree of relative mobility is clearly better than the alternatives.

Relative mobility has received far less attention than absolute mobility since it requires following what happens to specific individuals' incomes over their life course or even over several generations. But it is only through an analysis of relative mobility that we can understand the status of the American meritocracy — and determine how closely a child's chances of achieving financial success is tied to the income of his or her parents.

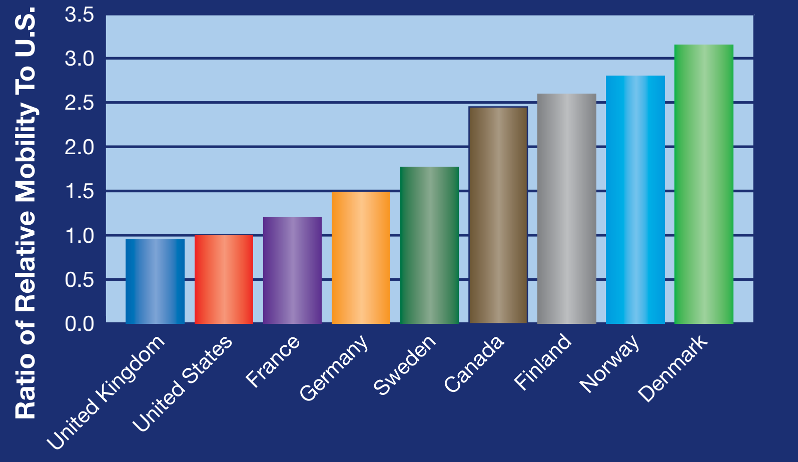
Relative Mobility: The United States Has Less Relative Mobility Than Many Other Developed Countries

Data on relative mobility suggest that people in the United States have experienced less relative mobility than is commonly believed. Most studies find that, in America, about half of the advantages of having a parent with a high income are passed on to the next generation.[11] This means that one of the biggest predictors of an American child's future economic success — the identity and characteristics of his or her parents — is predetermined and outside that child's control. To be sure, the apple can fall far from the tree and often does in individual cases, but relative to other factors, the tree dominates the picture.

These findings are more striking when put in comparative context. There is little available evidence that the United States has more relative mobility than other advanced nations. If anything, the data seem to suggest the opposite. Using the relationship between parents' and children's incomes as an indicator of relative mobility, data show that a number of countries, including Denmark, Norway, Finland, Canada, Sweden, Germany, and France have more relative mobility than does the United States (see Figure 3).[12]

Compared to the same peer group, Germany is 1.5 times more mobile than the United States, Canada nearly 2.5 times more mobile, and Denmark 3 times more mobile. Only the United Kingdom has relative mobility levels on par with those of the United States. To be sure, analyzing the relationship between parents' and children's incomes is but one way of defining relative mobility from one generation to the next. The full story may be more complicated, and the Economic Mobility Project intends to further investigate relative mobility using additional measurement and analysis.

Figure 3. The U.S. Has Less Relative Mobility than Many Industrialized Nations



Source: Authors' calculations of intergenerational income elasticities in Corak, 2006.[13]

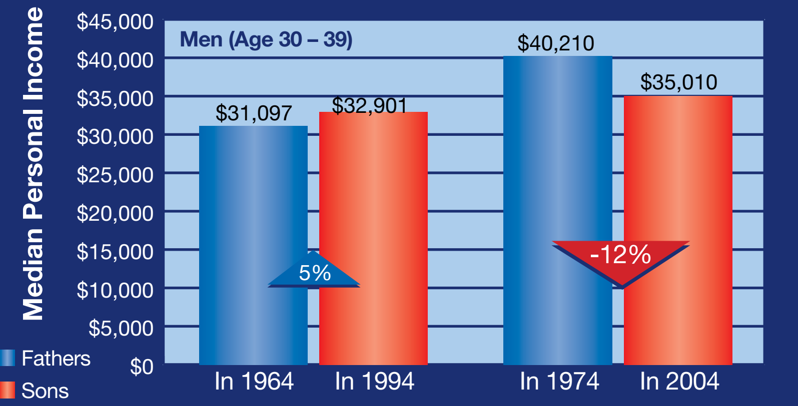
ABSOLUTE MOBILITY: Men in Their 30s Today Earn Less Than Men in Their Fathers' Generation and Family Income Growth Has Slowed

Using new analysis of U.S. Census Bureau data, the Economic Mobility Project has found that absolute mobility is declining for a significant group of Americans. We look at four generations of men born during different periods between 1925 and 1974, and focus on their individual incomes when they were in their thirties — thereby holding constant the point in their careers when measuring their economic status. Research also suggests that income in one's thirties is a reasonably good indicator of what one's lifetime income will be.

Male Income Trends: Beginning with a comparison of men ages 30-39 in 1994 with their fathers' generation, men ages 30-39 in 1964, we see a small, but fairly insignificant, amount of intergenerational progress (see first two bars of Figure 4). Adjusting for inflation, median income increased by less than $2,000 between 1964 and 1994, from about $31,000 to under $33,000 — a 5 percent increase (0.2 percent per year) during this thirty-year period.

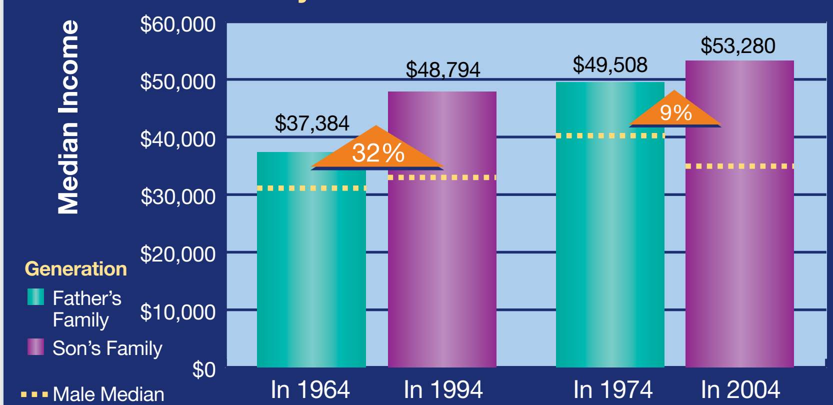
The story changes for a younger cohort. Those in their thirties in 2004 had a median income of about $35,000 a year. Men in their fathers' cohort, those who are now in their sixties, had a median income of about $40,000 when they were the same age in 1974 (see last two bars of Figure 4). **Indeed, there has been no progress at all for the youngest generation. As a group, they have on average 12 percent less income than their fathers' generation at the same age.**[14] **This suggests the up-escalator that has historically ensured that each generation would do better than the last may not be working very well.**

Figure 4. Today, Men in their Thirties Have Less Income Than Men in their Fathers' Generation



Source: Brookings Institution analysis Current Population Survey of the U.S. Census Bureau.[15]

Figure 5. Families with Men in Their Thirties Have More Income Today Than Their Parents' Generation



Source: Brookings Institution analysis Current Population Survey of the U.S. Census Bureau.

Family Income Trends: Does this mean that *family* incomes have been stagnant over this entire period? Hardly. But the main reason that family incomes have risen is that more women have gone to work, buttressing the incomes of men by adding a second earner to the family.[16] And, as with male income, the trend is downward, with income growth for families with men in their thirties slowing from 32 percent (0.9 percent per year) for the older cohort, to only 9 percent (0.3 percent per year) for the youngest cohort (see Figure 5).

The story for men and families over the last thirty years is provocative and illustrative. To be sure, the American economy grew over this period but at a much slower pace than in previous generations. Going back to 1820, per capita gross domestic product in the United States has grown an average of 52 percent for each generation. But since 1973, overall median family income has grown only 0.6 percent per year, a rate that produces a 17 percent increase in the average family's income for each generation. Thus, unless the rate of economic growth increases, the next generation will experience an improvement in its standard of living that is only one-third as large as the historical average for earlier generations.[17]

Finally, even if growth were to resume at its former pace, a growing gap between U.S. productivity and median family income challenges the notion that a rising tide will lift all boats. For nearly thirty years after the end of World War II, productivity growth and median household income rose together in lockstep. Then, beginning in the mid-1970s, we see a growing gulf between the two, which widens dramatically at the turn of the century. As the data in Figures 6-9 indicate, the benefits of productivity growth have not been broadly shared in recent years.

Figure 6. Productivity and Median Family Income Growth 1947-2005

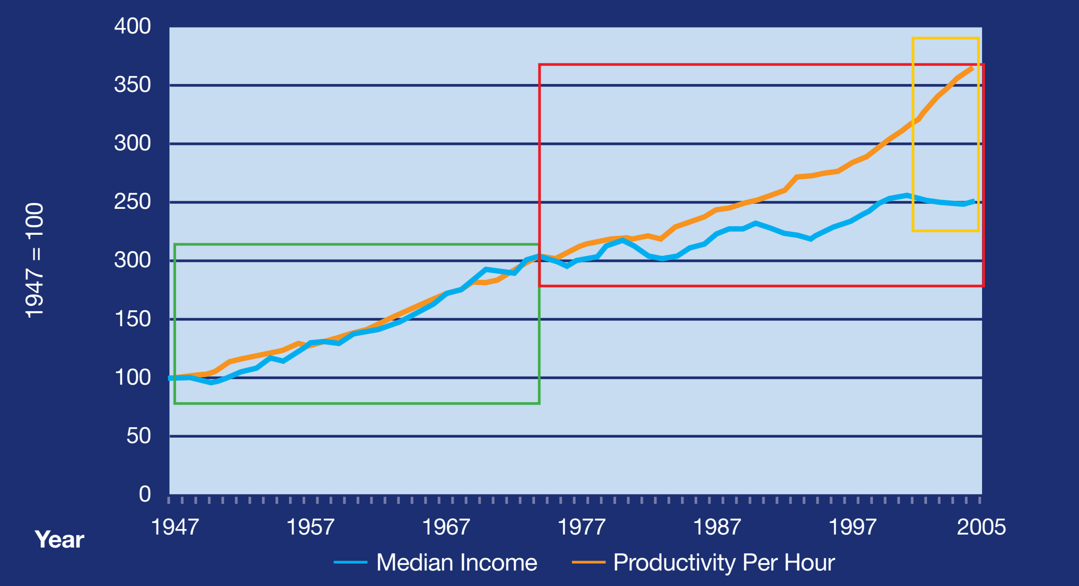


Figure 7. Productivity and Income Grow Together 1947-1974

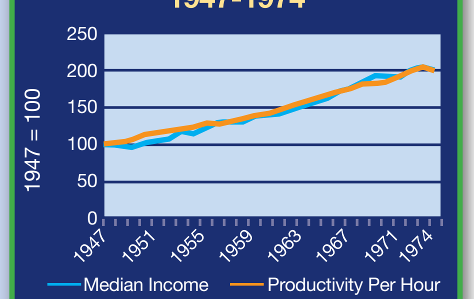


Figure 8. Productivity and Income Grow Apart 1974-2005

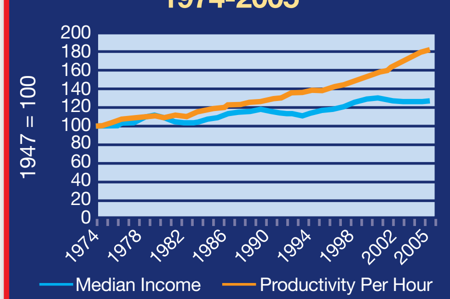
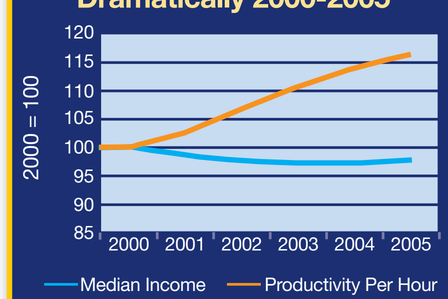


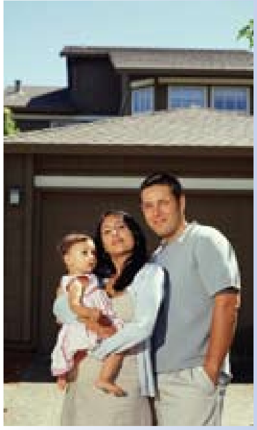
Figure 9. Productivity and Income Gap Widens Dramatically 2000-2005



Source: Author's calculations of U.S. Census Bureau and Bureau of Labor Statitics data.[18]

Is the American Dream Alive and Well?

One thing is clear. A society with little or no absolute mobility is one in which for every winner there is a loser. It's a zero sum game. And a society with little or no relative mobility is one in which class, family background or inherited wealth loom large. Equal opportunity is a mirage. Recalling the three hypothetical societies, it is easy to envision why, for these reasons, high levels of both absolute and relative mobility are desirable. Society should strive for both. But rates of growth in mature economies are often slower than they are in societies that are still developing, and this fact makes a focus on relative mobility of increasing importance.



In subsequent reports, the Economic Mobility Project will further explore the extent of relative mobility in the United States and whether it has increased or decreased over time. The project will also introduce a new hybrid measure of mobility — one that combines the effects of absolute and relative mobility to see how they are affecting the fortunes of individual Americans.

The desire to achieve beyond one's parents' economic status or ensure a child's greater success in life has inspired generations of Americans to study hard, work industriously, save carefully, and connect to a set of larger social ideals. Indeed, the promise of economic opportunity was part of what forged the idea of the United States of America more than two centuries ago. It has since served as a powerful engine of growth and social cohesion.

While belief in this American Dream remains a unifying tie for an increasingly diverse populace, it is showing signs of wear, with both public perceptions and concrete data suggesting that the nation is a less mobile society than once believed. This is not good: the inherent promise of America is undermined if economic status is, or is seen as, merely a game of chance, with some having the good fortune to live in the best of times and some the bad luck to live in the worst of times. That is not the America heralded in lore and experienced in reality by millions of our predecessors.

To help strengthen our nation's promise, the Economic Mobility Project and its partners will prompt a continuing national conversation about this trend, informing the discussion with facts about its scope and the forces propelling it. Over the next year and a half, the Economic Mobility Project will research, analyze, and present data, addressing fundamental questions such as these:

- ★ *How has mobility, both relative and absolute, changed over time?*
- ★ *How does mobility differ by race?*
- ★ *How does mobility differ for men and women?*
- ★ *How does mobility differ based on parents' income?*
- ★ *How does mobility differ based on one's family structure?*
- ★ *How does mobility differ based on one's education?*
- ★ *How does mobility in the United States compare to mobility elsewhere in the world?*
- ★ *How does mobility for recent immigrants compare to mobility for existing U.S. citizens, and are immigrants today more or less mobile than they used to be?*

The project will also try to answer the very difficult question of what factors influence or determine one's ability to move up the economic ladder. What are the channels by which economic advantage or disadvantage is transmitted from parent to child? Through analysis of a broad range of factors, we will produce a report on mobility indicators. In it, we will address questions such as:

- ★ *What role do economic factors, like savings and asset accumulation, play in one's economic position?*
- ★ *What role do social networks and other cultural factors play?*
- ★ *What role do human capital factors, like childhood health or education, play in determining one's economic position and trajectory?*

Is the American Dream alive and well today? It is this simple question that lies at the heart of the Economic Mobility Project. By forging a broad and nonpartisan agreement on the facts, figures and trends related to mobility, the Economic Mobility Project hopes to focus public attention on this critically important question and generate an active policy debate about how best to ensure that the dream is kept alive for generations that follow.

Notes

1 Remarks before the Greater Omaha Chamber of Commerce, Omaha, NE, February 6, 2007, http://www.federalreserve.gov/BoardDocs/Speeches/2007/20070206/default.htm.

2 Bernanke, 2007.

3 "State of the Economy Report" Speech. Federal Hall, New York, NY, January 31, 2007, http://www.whitehouse.gov/news/releases/2007/01/print/20070131-1.html.

4 Mishel, Bernstein, and Allegretto, "State of Working America," Economic Policy Institute, 2007. The authors define CEO pay as "realized direct compensation defined as the sum of salary, bonus, value of restricted stock at grant, and other long-term incentive award payments." Worker pay is "hourly wage for production and non-supervisory workers, assuming an economy-wide ratio of compensation to wages and a full-time, year-round job."

5 National Election Pool Exit Poll Results, Edison Media Research, November 7, 2006. http://exit-poll.net/ or http://www.cnn.com/ELECTION?2006/pages/results/states/US/H/00/epolls.0.html.

6 CNN, "Poll: 74 Percent of Americans Say Congress Out of Touch," October 18, 2007. http://www.cnn.com/2006/POLITICS/10/18/congress.poll/index.html.

7 Gallup Poll April 2001 through April 2006, cited in AEI Public Opinion Studies, "Economic Insecurity: Americans' Concerns About their Jobs, Personal Finance, Retirement, Health Care and More." http://www.aei.org/research/politicalCorner/publications/pubID.25668,projectID.14/pub_detail.asp.

8 For more discussion of this point, see Sawhill and McLanahan, 2006, p. 21.

9 The Pew Research Center, "Trends in Political Values and Core Attitudes: 1987-2007," March 2007.

10 For more discussion, see Sawhill, 1999.

11 For more discussion, see Sawhill and McLanahan, 2006.

12 Corak, 2006. For similar results, also see Jantti, et al, 2006.

13 Intergenerational income elasticities for the countries are as follows: United Kingdom – 0.50; United States – 0.47; France – 0.41; Germany – 0.32; Sweden – 0.27; Canada – 0.19; Finland – 0.18; Norway – 0.17; Denmark – 0.15. The inverted elasticity for the United States is then set to 1.0 to allow direct comparisons with other countries.

14 These figures are based on median incomes for each generation. When means are used the results are less dramatic but tell a similar story.

15 Income for Figures 4 and 5 is adjusted using the Consumer Price Index Research Series Using Current Methods (CPI-U-RS). Personal income and family income include before-tax earnings, interest and dividends from capital, cash benefits from government programs (such as Social Security, welfare, or unemployment compensation), pension or retirement income, child support and other cash income. It does not include the value of non-cash compensation such as employer-contributions to health insurance and retirement benefits, nor do they include the effect of taxes or non-cash benefits such as food stamps.

16 The project will continue to explore the role that changes in family structure and second earners have had on economic mobility. In addition, we will look at the effects of non-wage compensation (such as employer-provided health insurance and retirement benefits), non-cash benefits (such as food stamps), and post-tax benefits (such as the Earned Income Tax Credit) may have on economic mobility.

17 Sawhill and McLanahan, 2006, pp. 4-5. The duration of a generation is defined as twenty five years.

18 As with Figure 5, income includes before tax earnings, interest, rent, government cash assistance, pension, child support, and other cash income. It does not include the value of non-cash compensation such as employer-contributions to health insurance and retirement benefits, the effect of taxes or non-cash benefits. (See note 15.)

Resources

AEI Public Opinion Studies, "Economic Insecurity: Americans' Concerns About their Jobs, Personal Finance, Retirement, Health Care and More." http://www.aei.org/research/politicalCorner/publications/pubID.25668,projectID.14/pub_detail.asp.

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Economic Mobility Project Principals And Advisors

The Economic Mobility Project seeks to broaden the current national economic debate over income inequality, as well as economic insecurity and volatility, to achieve greater consensus about the state of economic mobility in America. Through research and dialogue, this nonpartisan project provides objective information about the status of U.S. economic mobility and addresses factors such as income and education that influence one's economic prospects.

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1025 F Street NW, Suite 900 ★ Washington, DC 20004-1409 ★ Tel: 202.552.2000 ★ Fax: 202.552.2299

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