

METHODOLOGY

Transfer of Wealth Opportunity Analysis

This paper outlines the methodology used to create Transfer of Wealth (TOW) scenarios for specific regions and states. This work was motivated by the early landmark transfer of wealth study, *Millionaires and the Millennium*. Since our first TOW study in Nebraska in 2001, we have developed and refined the methodology to provide scenarios that can be the starting point for fruitful discussions about wealth transfer and its potential as a source of funding for community development.

Before we outline the methodology, it is important to highlight several points about our TOW model:

- The TOW model produces **scenarios** based on projections of likely futures, not predictions or forecasts of actual future outcomes. Scenarios are driven by key assumptions about the future, based on historical trends. In all cases, we work to create conservative scenarios that represent realistic estimates of TOW opportunities. The scenario numbers generated are not predictive – indicating what will result 10 and 20 years from now – but rather demonstrate potential or a “likely future” given past and current trends. They are not designed to dictate policy but rather to provoke strategic discussions driven by a simple question – what if the community were able to capture **just 5%** of the wealth that will transfer between generations over the next 10, 20, or 50 years to support investments in community betterment?
- The first consideration in any TOW study is the establishment of a base year for analysis. For this study, 2010 was chosen as the base year. We consider 50 years of historical indicators starting with the post-World War II period and extending through 2010, the most recent year for which an adequate number of adjusted indicators necessary to establish current net worth are available, and project estimates 50 years (to 2060) into the future, annually.
- The analysis is conducted in “inflation-adjusted dollars.” In other words, these are real dollars – a dollar in 2030 is worth the same as a dollar in 2010.

Steps in Creating TOW Scenarios

1. Estimate Current Net Worth. The TOW analysis uses a data series produced by the U.S. Federal Reserve Board, the [Survey of Consumer Finance Report](#), to match demographic characteristics for the study region with key national indicators. This report provides detailed U.S. asset and liability holdings by key demographic characteristics (e.g., age of household, income of household, race, employment type, region, and housing status). Table 1 shows the relationship between key demographic variables considered in the TOW model and mean household net worth. These data relationships are used to estimate net worth at the state and county levels.

TOW Scenarios

We provide transfer of wealth projections over an extended period of time (up to 50 years in the future). This allows us to illustrate how the TOW opportunity changes as communities mature. It is not possible to forecast in a predictive way with a certain degree of reliability. Rather, we employ scenarios that illustrate a likely future based on reasonable assumptions of both the past and the future. Our scenario models are flexible and are capable of generating a range of scenarios based on different assumptions of the future.

Table 1 - Relationships between Key Demographic Indicators and U.S. Mean Net Worth (NW) 2010 values

Demographic Indicator	Relationship with U.S. Mean NW
Household Income	Strong positive relationship with income <ul style="list-style-type: none"> ▪ Top 10% income group – mean NW = \$2.9 million ▪ Bottom 20% income group – mean NW = \$116,800
Household Age Cohort	Positive relationship with age, up to peak <ul style="list-style-type: none"> ▪ Increasing mean NW up to \$880,500 peak for 55-64 cohort ▪ Declining mean NW beyond age 65
Family Structure	Positive relationship with marital status; inverse relationship with children <ul style="list-style-type: none"> ▪ Couple with no children – mean NW = \$864,800 ▪ Single with children – mean NW = \$143,700
Head of Household Education Level	Positive relationship with education level <ul style="list-style-type: none"> ▪ College degree – mean NW = \$977,700 ▪ No high school diploma – mean NW = \$110,700
Race or Ethnicity	Inverse relationship with non-white status <ul style="list-style-type: none"> ▪ White non-Hispanic – mean NW = \$654,500 ▪ Non-white or Hispanic – mean NW = \$175,900
Head of Household Work Status/Entrepreneurship	Positive relationship with self-employment <ul style="list-style-type: none"> ▪ Self-employed – mean NW = \$1.74 million ▪ Employed – mean NW = \$298,800
Head of Household Occupation	Positive relationship with professional occupations <ul style="list-style-type: none"> ▪ Managerial or professional – mean NW = \$1 million ▪ Other – mean NW = \$162,800
Housing Status	Positive relationship with home ownership <ul style="list-style-type: none"> ▪ Owner – mean NW = \$713,400 ▪ Renter – mean NW = \$57,200



Customization. Final current net worth estimates for the base year are customized for each study area based on the relationships between a number of key indicators at the state and county levels as compared to the national level. Primary indicators include: (a) dividend, interest and rent income, (b) income characteristics, (c) age characteristics, (d) concentrations of creative class employment, (e) concentrations of business ownership, and (f) market valuation of real property by class.

Two of these indicators warrant further discussion – creative class workers and business ownership. There is growing research and analysis that supports the view that significant innovation and wealth result from certain types of economic activities often referred to as the “knowledge economy” or the “creative class”. Richard Florida and others argue that knowledge or creative class sectors and businesses generate significantly higher earnings and wealth creation than other economic activities. In this TOW analysis, we consider the current concentration of creative class workers and the likely growth of this economic segment over the study period, employing methodology developed by the Economic Research Service within the U.S. Department of Agriculture.¹

Entrepreneurship or business ownership is part of America’s tradition and another current net worth indicator. From our earliest history, a promising pathway to economic success and security was through entrepreneurship or business ownership. For many immigrants unable to obtain good jobs, business ownership is the primary route to economic success and wealth formation. Business ownership is full of challenges and risks where most new businesses fail. Despite this reality, on average, self-employed heads of households have 5.8 times more current net worth as compared to those who work for someone else.

A number of additional indicators are used to customize current net worth estimates. Many of these factors are also key considerations in building assumptions for TOW projections:

- Adjacency to high amenity areas, second home development and retirees;
- Pockets of the ultra-rich (locals or newcomers whose wealth puts them in the top 1% in the U.S.);
- Effects of public lands – federal, state and local;
- Pockets of high corporate stock ownership;
- Specific new economic development projects;
- Effects of the gaming industry, if any;
- Behavioral patterns of savings and investing;
- Effects of new immigrants and repatriation of earnings;
- Areas of future population boom, bust, or plateau;

¹ Additional details on the creative class and other indicators, and the ERS Methodology, can be found in our Electronic Library referenced under Additional Resources in this report.

- Public housing impacts;
- Institutionalized populations (e.g., prisons, care homes, military).

2. Build Demographic/Population Models. For each study region, we build a population model for the scenario period and an economic forecasting model. We employ existing and available population forecasts and, if not available, build population forecasts through the scenario period. We rely on a set of historic relationships between drivers of wealth and household current net worth. There are strong and historic relationships between these drivers, defined as changes in population, personal income, and gross domestic product, and change in household current net worth (summarized in Table 2). For example, based on historic data, every 1% increase in population is associated with a 2.6% increase in personal income while a 1% increase in personal income is associated with a 1% increase in current net worth.

Table 2 - Relationships between Drivers of Wealth and Household Current Net Worth (CNW)				
	Population	GDP	Personal Income	CNW
Population	1:1	1:2.45	1:2.60	1:2.62
GDP	2:45.1	1:1	1:1.06	1:1.07
Personal Income	2.60:1	1.06:1	1:1	1:1
CNW	2.62:1	1.07:1	1:1	1:1

We employ these relationships along with demographic and economic forecasts to project household CNW over time. Again, we generate relatively conservative projections benchmarked to the low-range CNW and low TOW projection for the U.S.

3. Discount Assets. Not all assets are equal with respect to TOW opportunity. Many assets will not be available for giveback to heirs, charities or communities. We employ a discounting methodology to reduce the value of our CNW projections and generate a TOW estimate that more closely represents the likely TOW opportunity for each area. This discounting can reduce gross CNW by 50% to 75% depending upon the demographics of households in a particular place. Again, the discounting allows us to estimate TOW that is truly available for potential giveback.

Below are examples of CNW discounting employed in our methodology and analysis.

- Assets that depreciate quickly such as automobiles or household goods;
- Assets where future value is hard to estimate such as collections, art and jewelry;
- Future income associated with defined benefits with no cash value;
- Closely-held assets including farms, ranches and family businesses;
- Assets of lower-income households that are likely to be consumed during retirement, leaving limited estates available for giveback.

4. Estimate Timing of TOW Release. The next step is to estimate the timing of TOW, or when we might expect wealth to transfer from one generation to the next. Projected deaths are the primary indicator of TOW release since most estate transfers occur upon death. Demographic projections estimate the number of deaths throughout the analysis time period and these percentages are used to estimate TOW release.

5. Review and Verification. To ensure that we have captured all material considerations, we undertake a careful review and verification process so that our TOW scenarios reflect each state or region's unique circumstances and realities. We work with a Technical Advisory Committee in each study region throughout the TOW analysis process. The Technical Advisory Committee helps identify unique factors that would impact estimates of either current net worth or TOW.

We continue to update our TOW methodology as new data are released. We also monitor the trends in the data so that we can better understand whether the historical patterns of wealth holding are fundamentally changing, and how those changes might impact TOW scenarios. Most importantly, for each TOW study we conduct, we develop a solid understanding of the unique features of the local, regional and state economies that need to be incorporated into our methodology so that we can provide the most relevant scenarios to jumpstart conversations about the transfer, capture and effective investment of wealth in your community.

Questions & More Information:

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The Center for Rural Entrepreneurship's vision for rural America is one of vibrant communities and regions that embrace entrepreneurship, that find new sources of competitive advantage in their inherent assets, and that invest in a new more sustainable future for both present and future generations. The Center's mission is to help our local, regional and state partners achieve this future by connecting economic development practitioners and policy makers to the resources needed to energize entrepreneurs and implement entrepreneurship as a core economic development strategy.

These development efforts require financial resources. Most traditional sources of funding are challenged as governments, businesses and foundations struggle to meet rising community needs. A core program area for the Center is Community Development Philanthropy, where our team helps your community, region or state build a community wealth road map. Our Transfer of Wealth (TOW) research offers insight into possibly the greatest opportunity to tap new, significant and sustainable funding streams in support of growing better and stronger communities. For many communities and regions, TOW research can help jump start important conversations leading to greater community giveback.

The Center has conducted TOW studies for clients around the nation for more than 10 years, and has published a book titled, *Transfer of Wealth in Rural America: Understanding the Potential, Realizing the Opportunity, Creating Wealth for the Future*. More product offerings are planned under our Community Development Philanthropy area.

To learn more about the Center's history and program areas, go to www.energizingentrepreneurs.org.

The Rural Policy Research Institute (RUPRI) provided founding support to create the Center for Rural Entrepreneurship in 2001. RUPRI's mission is to provide independent analysis and information on the challenges, needs, and opportunities facing rural people and places. The work of the Center for Rural Entrepreneurship, along with other centers and collaborations, helps RUPRI achieve this mission. To learn more about RUPRI, visit www.rupri.org.

