Abstract

Even people with income below average will not support high rates of redistribution, because of the prospect of upward mobility: they take into account the fact that they, or their children, may move up in the income distribution, and therefore be hurt by high tax rates. This "intuitive" hypothesis is commonly advanced as part of the explanation for why democracies, where a relatively poor majority holds the political power, do not engage in large-scale expropriation and redistribution. But does it make sense, or does it require that some of the poor overemphasize the prospects of good outcomes relative to bad ones, due either to irrationally optimistic expectations or to a form of risk-loving?

A key premise is that some individuals or families who are currently poorer than average – for instance, the median voter– expect to become richer than average. This "optimistic" view clearly cannot be true for everyone. But is it possible for, say, a majority of the population to be simultaneously poorer than average in terms of current income, yet richer than average in terms of expected future income –especially when the income distribution is invariant over time?

This paper establishes the formal basis for the "prospect of upward mobility" (POUM) hypothesis concerning the political economy of redistribution. The key to the puzzle is surprisingly simple. We show that there exists a range of incomes below the mean where agents oppose lasting redistributions if (and, in a sense, only if) tomorrow's expected income is an increasing and *concave* function of today's income. Convergence of individual incomes to a common limiting distribution is not sufficient. The coalition in favor of laissez-faire is larger, the more concave the transition function, the longer the duration of the proposed tax scheme, and the more farsighted the voters. We construct an example where, in steady–state, three quarters of families have less than mean income, so that they would support contemporary redistributions. Yet, a two–thirds majority has expected future incomes above the mean, and will therefore vote down (or seek to prevent constitutionally) redistributive policies which impose high tax rates on their descendants. A calibrated version of this simple model matches the main features of the US income distribution and intergenerational persistence quite well.

We also analyze empirical mobility matrices from the PSID to determine whether the POUM effect is present in the actual data. The proportion of agents who have expected future incomes above the mean is found to rise with the length of the forecast horizon, in conformity with the theory. Over a horizon of about twenty years, it reaches a strict majority.

At the same time, the prospect of upward mobility effect is subject to limitations, which we also analyze. In particular, there must be sufficient inertia or commitment power in the choice of fiscal policy or institutions, and voters' risk–aversion must not be too large compared to the curvature of the transition function.

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