Final Report

WEALTH IN SOUTH DAKOTA

Inter-Generational Wealth Transfer Scenario

Abstract

*This report – **Wealth in South Dakota** – provides estimates of the inter-generational wealth transfer occurring in the State of South Dakota and its counties between 2000 and 2050. This is a draft report submitted to the South Dakota Community Foundation for its review and use.*

Executive Summary

This report – **Wealth in South Dakota** – provides estimates of the inter-generational wealth transfer occurring in the State of South Dakota and its counties between 2000 and 2050. This is a final report submitted to the South Dakota Community Foundation for its review and use.

Based on our analysis of South Dakota and its counties, we have reached the following insights regarding the inter-generational wealth transfer scenario for the service area of the South Dakota Community Foundation:

- According to Boston College in their landmark study – ***Millionaires and the Millennium*** - the United States is in the midst of the largest inter-generational wealth transfer in American history. The Boston College researchers conservatively estimate that during the first half of the 21st Century $41 trillion of wealth will pass from the current generation to the next.

- On average, per household wealth to be transferred in the United States is $389,000 (in current dollars). Because the United States is growing demographically and is likely to continue creating new wealth faster than old wealth is transferred, the trend line for U.S. wealth transfer is projected to expand over time.

Inter-Generational Wealth?

Inter-generational wealth transfer is not a common concept discussed nightly at our dinner tables. So what do we mean by this term? Simply put, we are referring to primarily household estate wealth that is transferring from the current generation to the next. Typically, a death is the trigger that puts into motion this transfer.

- South Dakota is part of this trend. We estimate that during the next 50 years South Dakota will experience between $34 and $42 billion in inter-generational wealth transfer. This is a remarkable legacy and reflects on the hard work, prudence and enterprise of the current generation over their lifetimes. *We will use the mid-point estimate of $38 billion throughout the balance of this report.*

- On average, each year during this five decade long period, South Dakota will see $760 million transferring from the current generation to the next. The actual inter-generational transfer levels will vary by year driven by the timing of current wealth holders transferring their estates.

Where?

Generations come and go – it is a fact of nature. Wealth created in South Dakota over the current generation and stored in the estates of families will transition over the next 50 years. The question is where will this wealth transfer? Typically the wealth is gifted to heirs, churches and other causes close to the hearts of the people who earned this wealth. Because of low financial planning rates – too much of this wealth may be unnecessarily lost to taxes. Communities in South Dakota have the opportunity to ask donors to give back to the communities that have supported them.

- It is difficult for the average person to grasp the implications of such large numbers. What does $38 billion over 50 years or $760 million per year mean for South Dakota and its residents? It is also hard to anticipate what South Dakota will look like in 2050.

  So if we focus on the next ten years what does this trend mean for South Dakota? We estimate that in the coming decade 15% or $5.6 billion will be transferred. This scenario represents a significant opportunity for South Dakota and its ability to build a brighter future for itself.

- If just five percent of the wealth being transferred over the next 10 years were pledged to community-based endowments, a cumulative endowment of $280 million could be created. These endowments could mean new resources essential to building stronger communities throughout South Dakota.

- Typically a conservative payout rate is five percent of the endowment value. At this rate, the endowment will continue to grow and remain inflation proof. Under such a scenario the endowments built in South Dakota would be able to support community betterment throughout time. At this rate, South Dakota's communities would have approximately $14 million annually for betterment projects. This is a remarkable opportunity for strengthening communities, economies and families in South Dakota year in and year out.

$14 Million Per Year Forever!

Think of what $14 million per year of new resources could mean for South Dakota's communities. Within a decade it could mean new libraries, athletic fields, programs to help entrepreneurs, upgraded swimming pools, needed health care facilities and so much more.

- The level of inter-generational wealth transfer in South Dakota is projected to be lower when compared to the United States' average. This is due to many factors and we cite the following considerations for this finding:

  - The Boston College estimate of inter-generational wealth transfer may now be optimistic given the weak growth in the United States and decline rates of wealth formation particularly among middle income households.

  - The rapidly concentrating wealth in upper income households (i.e., top 1, 5 & 10% high net work households) and the relatively smaller percentage of South Dakota households that fall into these categories.

  - The anticipated slower population and income growth rates in South Dakota relative to the United States.

Putting the Estimates into Perspective

There is no broadly held methodology for estimating the actual inter-generational wealth transfer opportunity over time. The farther we push out into the future – the harder it is to ensure reasonableness of our estimates.

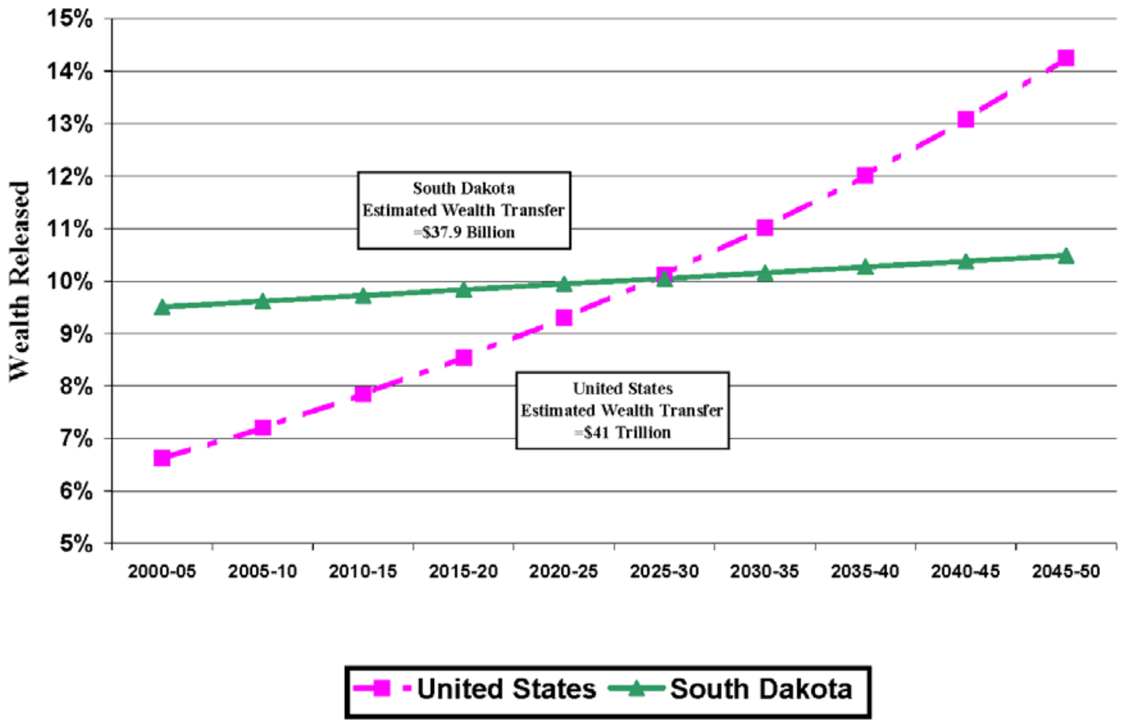
"Transfer of wealth" or TOW analysis has now been completed for a number of places and states (i.e., Nebraska, Wyoming, Iowa, and selected counties in North Dakota, Kansas and Louisiana. A quick comparison of these studies provides a range of results. Some of these differences can be explained by the unique circumstances of these varied places. However, this explanation does not rationalize all the differences.

Our methodology for estimating TOW is a work in progress. With each opportunity and study we evolve our thinking in the hope of generating better estimates. We have learned that when dealing with the future – being more conservative is best. With each new study we refine our assumptions that have tended to generate somewhat more conservative estimates beginning with Nebraska five years ago and now with South Dakota in 2005.

Additionally, we have begun to question the findings from the Boston College study that anchors all this work. We are not challenging the researchers at Boston College as they have a strong methodology well executed. But the American economy and society is undergoing profound change that may not be adequately reflected in the original Boston College work. Wealth formation among America's riches households is growing and growing rapidly – but wealth formation rates among the remaining 80% of American households are falling and for a majority of Americans falling rapidly. These trends hold tremendous implications for our TOW estimates.

We therefore urge great caution when making comparisons. We recommend that this information be used to raise community awareness of the inter-generational wealth transfer opportunity whether it is $10 billion or just $5 billion.

Figure 1 – South Dakota's Wealth Transfer
A Likely Scenario



- Given the demographics of South Dakota (e.g., migration, age, growth & death rates) compared to the U.S., we expect that the transfer of wealth will occur sooner in South Dakota with peak wealth transfer occurring in this decade.

- South Dakota is a large state physically with considerable diversity from the more urbanized areas around Sioux Falls to the very rural ranching country west river. The following summarizes some of these varied findings. Figure 2 below benchmarks each region to the state averages for comparison purposes.

  - The more rural regions (east river farming, transition farming to ranching & west river ranching) all have higher per household current net worth when compared to the state averages. This makes sense since these areas have considerable real property relative to small population bases.

    Anticipated transfer of wealth over the next 50 years levels are below the state averages reflecting declining populations and weak new wealth formation rates.

The anticipated transfer of wealth levels over the next decade are significantly above the state averages reflecting the older and aging populations of these counties. Bottomline, the opportunity associated with the inter-generational transfer of wealth is coming sooner to these counties and will decline over time.

Figure 2 – Regional TOW Estimates

Geography	CNW	50 Yr. TOW	10 Yr. TOW	Households
South Dakota	$28,800	$37,988	$5,613	290,245
East River	$5,313	$5,142	$1,199	50,337
West River	$1,528	$1,542	$340	14,672
Transition	$1,644	$1,527	$387	14,591
I-29	$9,908	$13,919	$1,698	98,441
Centers	$4,265	$5,070	$830	44,132
Reservations	$429	$417	$83	9,648
Black Hills	$5,713	$10,370	$1,054	58,424
		(Millions of Dollars – 2000 Dollars)		
East River	106%	78%	123%	17%
West River	105%	80%	120%	5%
Transition	114%	80%	137%	5%
I-29	101%	108%	89%	34%
Centers	97%	88%	100%	15%
Reservations	45%	33%	44%	3%
Black Hills	99%	136%	93%	20%
Average	95%	86%	101%	---------

(Benchmarked to State Values)

- The more urban regions (Interstate 29, Black Hills & Trade Centers) have current net worth values near the state average. About 70% of the state's households live in one of these three regions. The strength of this population base alone ensures current net worth values near the state average.

  Over the next 50 years two of these areas will likely experience transfer of wealth levels significantly above the state average. Because the Black Hills and the Interstate 29 counties are growing both demographically and economically – new wealth is being created shaping this pattern. The trade center communities are seeing weak to flat growth accounting for their below average 50 year TOW values.

  In the coming decade the transfer rates are somewhat lower for the Interstate 29 and Blackhills counties (due to younger populations) and around the average for the Trade Center communities.

- We struggled with adequately estimating the current net worth and TOW values for those counties with Indian Reservations. Given the high rates of poverty, we estimated significantly lower current net worth and TOW values.

Note – *All value are in real dollars bench marked to 2000 currency rates. In other words – our estimates remove the influence of inflation from the estimates. Additionally, we have become more conservative in our estimates regarding real economic growth and wealth formation rates given the trend lines of the past decade.*

The Numbers Could be Greater!

We have developed a very conservative estimate of the inter-generational transfer of wealth for South Dakota. These estimates could be significantly higher. There are two rationales for this bold statement.

- *First, we state with estimates of current net worth that exclude all ex patriot and external ownership of real property from our estimates.*

- *Second, we have assumes very low real growth rates in both population and wealth formation.*

Let us go ahead and illustrate the power of both points through two illustrations.

Based on information from the State of South Dakota's tax authorities – the current market value of real property in South Dakota is $40 billion alone. Our total current net worth estimate for South Dakota based on Census research is only $28 billion. One could clearly argue that the current net worth (even adjusting for debt) value should be higher than the real property values.

Our conservative real growth assumptions also lead to modest estimates. In Minnehaha County where Sioux Falls is located we assumed an average 2.2% real growth rate (both population & economic growth) over the 50 estimation period. Given historical trends for this county our assumption is low. By simply assuming a somewhat higher real growth rate that is one percentage point higher per year results in a one-third increase in estimated TOW for the period from $8.3 billion to $10.9 billion!

Bottomline – we could argue with more optimistic assumptions about current net worth and future growth that a reasonable scenario for TOW could be from one-third to 50 percent higher! That would mean for South Dakota that the TOW estimate over the coming five decades could be as high as $50 to $60 billion versus our conservative estimate of $38 billion. Consideration of ex patriot giving potential would further increase this number dramatically.

Analysis

With high degrees of certainty we can learn what the population, age demographics, income, poverty, housing and economy of a community look like. Unfortunately, there is not a published research report or data set we can review that gives us an idea of what the intergenerational wealth transfer amounts will be over the coming decades. Fortunately, researchers at Boston College in their study ***Millionaires and the Millennium*** give us reasonable estimates at a national level. We have taken the work of Boston College and developed a methodology for estimating inter-generational wealth transfer at the state, county and even community level. This section of the report provides insight into the analytic process we have employed to generate wealth estimates for South Dakota from 2000 through 2050.

This Analysis Section is organized into the following parts:

- Client.
- Geography of Analysis.
- Timeframe of Analysis.
- Forms of Wealth.
- Indicators of Inter-Generational Wealth.
- Considerations.
- Methodology.

Client

This analysis and report have been prepared under contract for the South Dakota Community Foundation based in Pierre South Dakota. The Foundation has a statewide mission and service communities and donors through affiliated funds throughout this state.

Geography of Analysis

This analysis has been prepared for the state of South Dakota and all its current counties. The state's counties have been organized into one of seven county types to facilitate analysis, these are:

- ❖ East River Farming Counties
- ❖ West River Ranching Counties
- ❖ Transition Farming to Ranching Counties
- ❖ Interstate 29 Counties
- ❖ Trade Center Counties
- ❖ Indian Reservation Counties
- ❖ Black Hills Counties

Timeframe of Analysis

The original Boston College study selected the timeframe of 2000 through 2050. We have elected this same timeframe for our analysis. We realize that we are already four years into the first of these five decades. But our ability to employ 2000 Census data is critically important to our analysis and drove our decision to stay with this timeframe.

Forms of Wealth

We have not attempted to precisely define all the forms of inter-generational wealth. Our analysis has focused on the three primary forms of wealth holding:

- Property.
- Investments.
- Insurance.

Property. For most Americans, the primary form of wealth holding is in the form of property. Property can includes one's residence, farm, timber stands, minerals holdings, businesses and some forms of personal property.

Property Wealth

Real property wealth in South Dakota is estimated at over $40 billion. The Department of Revenue assisted us in adjusting assessed values to generate an estimated market value for real property. This value is larger than the estimated current net worth for all households in the state (estimated at $29 billion). Part of this wealth is captured in debt, owned externally or controlled by corporations.

Investments. Americans in general, secure investments throughout life. These investments can include checking accounts, savings accounts, money market funds, stocks, bonds, retirement accounts and other investment vehicles that can be liquidated into cash.

Insurance. Finally, insurance has become widely accepted and life insurance is often a primary asset at the end of one's life.

Other forms of wealth such as rare coins, art or jewels are clearly part of wealth holdings. However, we do not attempt to make any adjustments or estimates of these types of wealth. Determinations of market value for purposes of gifting are challenging at best and generally circumstantial.

Figure 3 – U.S. Asset Ownership Rates for Households, 2000.

Asset type	2000		
	Percent of households that own asset type	Median value of asset for asset owners (dollars)	Percent distribution of net worth[1]
All assets	**(X)**	**55,000**	**100.0**
Interest-earning assets at financial institutions	65.0	4,000	8.9
Other interest-earning assets	3.3	29,013	1.7
Regular checking accounts	37.5	600	0.3
Stocks and mutual fund shares	27.1	19,268	15.6
Own home	67.2	59,000	32.3
Rental property	4.9	70,000	3.7
Other real estate	6.6	40,000	3.6
Vehicles	85.8	5,875	3.7
Business or profession	10.8	10,000	7.7
U.S. savings bonds	14.7	1,000	0.5
IRA or Keogh accounts	23.1	24,000	8.6
401K and thrift savings plans	29.9	20,000	9.7
Other financial investments[2]	3.9	22,000	1.6
Unsecured liabilities[3]	52.7	4,000	–3.0

X Not applicable.

Source: *U.S. Census Bureau, "Household Economic Studies," May 2003.*
Reprinted from page 5 of "Net Worth and Asset Ownership of Households: 1998 and 2000" as published by the U.S. Census Bureau (P70-88).

Indicators of Inter-Generational Wealth

We did not replicate the Boston College study for South Wood County. We accepted the College's low range estimate of $41 trillion for the Nation as a starting point. We then considered the following indicators to estimate the likely level of inter-generational wealth to be transferred in South Wood County between 2000 and 2050:

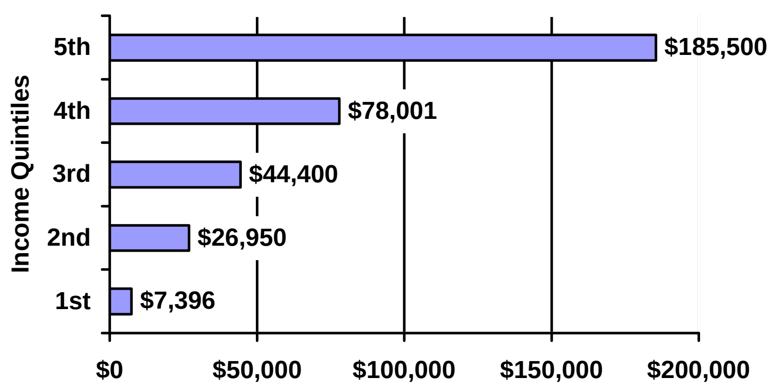
- Population.
- Income.
- Age Demographics.
- Growth.

Population. As simple as it might seem, the United States is more uniform from one corner to the next than not. Our first indicator is population. Simply put, we assume that South Dakota has a proportional share of inter-generational wealth based on its population. Adjustments regarding demographics, passive income, real property holdings and growth rates are then factored into our analysis.

Income. There is a strong correlation between income and wealth formation. While there are many stories where households with high incomes have few assets (but high spending & debt) and families with lower incomes with significant assets (modest spending & prudent investing) – the fact remains that with more income, assets and net worth rise. Figure 4 provides information nationally on the relationship between household income and net worth.

The pattern from the data in Figure 4 is clear. As income rises, so does net worth or wealth assets. The fifth quintile or the 20% highest income households in the United States have net worth values 25 times higher than the first quintile or the 20% of American households with the least income. These are national numbers, but we believe it is fair to assume that this same relationship is generally true for the families and residents of South Dakota.

Figure 4 – U.S. Net Worth & Income Link, 2000.



Source: *U.S. Census Bureau, "Household Economic Studies." May 2003.*

Overall, South Dakota has a lower percentage of its households in the top two income groups when compared to both the United States. Conversely, South Dakota has more households in the lower income groups. From one county to next and region to the next, this mix changes slightly.

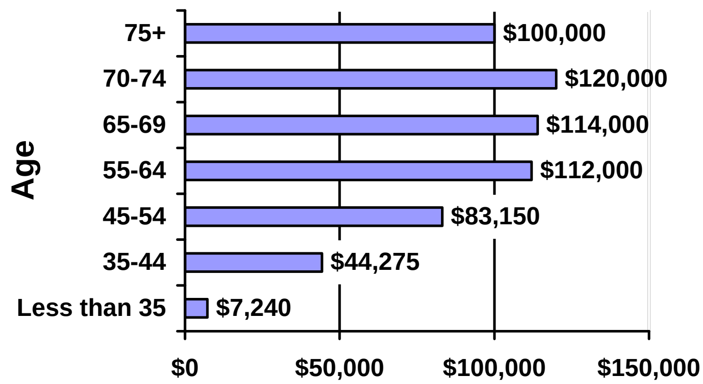
Age. National research also clearly shows a powerful relationship between wealth holdings and the age of the household. Figure 5 below summarizes this relationship. Simply stated, as the age of households increases, so does their net worth or wealth standings. There is a decline in wealth holdings in the 75 years of age and older group.

So what does this potentially mean for South Wood County? First, like with income, we assume that South Wood County is more like the U.S. than not. Second, when we apply this research to the demographics or age structure of South Wood County, our inter-generational wealth estimate increases by about

13%. Overall, the residents of South Wood County are older than when compared to both the U.S. and Wisconsin numbers. To illustrate this point, South Wood County has 25% more households in the age groups of 65 years of age and older when compared to the U.S. (i.e., 15.5% vs. 12.4%).

Given the relatively flat growth history in South Wood County, coupled with emergent second and retirement home development, it is reasonable to assume that (relative to both the U.S. & Wisconsin) South Wood County will continue to age demographically triggering inter-generational wealth transfer sooner than would be the case in either Wisconsin or the U.S..

Figure 6 – U.S. Net Worth & Age Link, 2000.



Source: *U.S. Census Bureau, "Household Economic Studies," May 2003.*

For South Wood County, the net effect is largely neutralizing. This area is somewhat poorer than the nation, but older. But there is a local factor that must be accounted for in our analysis – Consolidated Paper Company sale.

The Income & Age Link

When income and age are combined, the national research shows a powerful connection as both income and age re-enforce the wealth holding link. For example, a household in the lowest income group that is 35 years of age or younger has (on average) only $104 of net worth compared to a household in the highest income group and that is 75 years of age or older with $548,000 of net worth. There is a 5,269 times difference over this range!

Growth. Fifty years is a long time. It is very difficult for any of us to anticipate what our world will look like in 2050. Estimating inter-generational wealth over such a long time frame in a dynamic world is challenging. What we do know is that wealth is being created every second of every day. Wealth is being consumed and saved as well. There is a strong potential connection between a growing community and its potential to create new wealth. An example might be helpful to illustrate this point.

As a family gets established, typically its earning power grows. As earning power grows it is creating more wealth for the family. Depending upon the management preferences of that family, wealth can be accumulated in assets that are longer-term and can be passed on to the next generation or community. Investments into stocks, bonds, insurance, property and other fixed assets create net worth and wealth holdings. At a much larger scale, the same is true for communities.

Retirement & Second Home Development

The vast majority of Americans now live and work in large metropolitan areas. But increasingly, Americans are establishing second and retirement homes in more rural areas of America. After urbanization, this is the most powerful trend transforming rural America today. South Wood County is experiencing both second and retirement home development. This development can impact our estimates and the potential for legacy giving. As outsiders develop second/retirement homes in the area, they link their wealth to the area as well. New wealth is created through these properties.

Between 1950 and 2000, the population in the United States grew from 150 million to 281 million persons or by 87 percent. In Wisconsin over this same period, its population grew from 3.43 million to 5.36 million or by 56 percent. However, population growth for South Wood County was more modest changing from 50,500 residents in 1950 to 52,750 in 2000 or increasing by only 4.5 percent!

All indications would suggest that South Wood County will see little or no growth into the future. However, times change and this assumption could change with changing times.

The implications for South Wood County and our assumption that over the coming five decades there will be little or no growth, significantly reduces our estimate of inter-generational wealth transfer by nearly 30 percent.

Cautions

We have done our best to craft a thoughtful and factually based analysis. Our estimates of inter-generational wealth transfer for South Wood County are reasonable. But, it is important to realize that these are only estimates based on acceptable assumptions. We do not conclude that the inter-generational wealth transfer for South Dakota over the next 50 years is or will be precisely $38 billion. Changing circumstance, unique realities or other factors could increase or decrease our estimate. The bottomline is that there is significant inter-generational wealth present and transferring in South Dakota. There is a huge opportunity to create endowments and provide legacy giving long-term. Whether the final value is $35 or $45 billion can not be determined. The opportunity is massive.

Thanks

This analysis and report would not have been possible without the help of many individuals and organizations. Hopefully, we have succeeded in this section of recognizing all those who have helped.

- The leadership of the South Dakota Community Foundation deciding to commission this work.

- A special thanks to Bob Sutton CEO and President of the South Dakota Community Foundation for his vision and leadership in moving this project forward.

- We also would like to thank Jim Beddow with the South Dakota Rural Learning Center, the South Dakota Department of Revenue and the State Demographer's Office for their assistance.

- We continue to appreciate support from Kathy Miller with the Rural Policy Research Institute for her help with digging deeper into data sources. We also appreciate the on going help of Dr. Tom Harris, Director of the Center for Economic Development at the University of Nevada Reno for his research support. Finally, we extend our appreciation to Jerry Deichert with the University of Nebraska at Omaha for his help with demographic projections.

Special Thanks…

This work would not be possible without the groundbreaking research of two efforts. First, there is the work of Boston College and their study *Millionaires and the Millennium*. Second, there is the work of the Nebraska Community Foundation that underwrote the development of the methodology enabling the South Wood County wealth analysis.

Methodology

Our basic methodology employed in this work is outlined in the Analysis Section of the Report. For seeking to review the foundational work of Boston College and their landmark research *Millionaires and the Millennium* we encourage you to visit the web site for the Center on Wealth and Philanthropy within Boston College at www.bc.edu/research/swri/. We would be happy to personally explore our approach with other interested parties on a request basis.

The following components constitute the methodology we employed in conducting this analysis:

- Our work has been greatly informed by the landmark research and study Millionaires and the Millennium (October 1991) prepared by Boston College. For more information about this study and other relevant work contact the Center on Wealth and Philanthropy at Boston College (www.bc.edu/research/swri).

- Our starting point for this analysis is “current net worth” (CNW) estimates for the United States and for each of the 50 states. The U.S. Census Bureau estimates current net worth based on a sampling of U.S. households. Net worth includes typical assets like houses and stock portfolios less debt. To localize CNW we employ four sets of asset indicators:

  - Dividends, Interest & Rent Income.
  - Asset Holdings by Household Age.
  - Asset Holdings by Income Level.
  - Real Property Asset Holdings.

  Dividends, interest and rent income is estimated by the U.S. Bureau of Economic Analysis for each state and county (or Parish). This indicator provides an estimate of certain kinds of asset holding including stocks, bonds, cash accounts and rental property.

CNW typically increases dramatically by age. As households get older they generally have higher CNW levels than younger households. We employ national data for wealth holding by age group coupled with specific age information for the state or county (parish).

CNW typically increases with income levels. As income levels rise so do CNW levels. We employ national data for wealth holding by income level coupled with specific household income levels by state or county (parish).

Finally, we employ state and county (parish) specific information on real property to support our fourth indicator.

These indicators are used to adjust state CNW to a point estimate for the county (parish).

- Once CNW values are estimated we explore historical population, income and economic trends. When possible we consider a 50 years history for each locality with particular reflection on the most recent 20-year period. This information is employed to create assumptions about future growth in population, income and wealth holdings.

- An advisory group of state and regional experts are engaged through the sponsoring organization to help us test and refine our assumptions regarding future growth. Our baseline growth assumptions are stronger for the first 25 years of the period and become more conservative in the out years.

- The final step in our methodology is to estimate the timing of the transfer of inter-generational wealth over the 2000 to 2050 timeframe. These estimates are based on our model estimating the number deaths (therefore estates) triggered during each five-year period throughout the analysis timeframe.

Questions & Additional Information

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