The Reagan administration's budget cuts: Their impact on the poor

by Sheldon Danziger and Robert Haveman

The decision on the part of the Department of Health and Human Services not to fund a center for poverty research is a small indication of an enormous change in the making: the Reagan administration's shift in national priorities.[1] Indeed the President's 1982 and 1983 budget reform plans[2] and the allocation of funds among programs (current and proposed) have represented a sharp break with the recent past. It is evident that the administration is attempting to reverse the trend of the 1960s and 1970s, which had been to move away from military expenditures and toward outlays for social programs. The proposals already implemented as well as those announced as part of the fiscal 1983 budget are designed to reduce government spending as a percentage of the gross national product and to increase the proportion of the budget spent on national defense.

Budget policy since 1965

Between 1965 and 1981, the federal budget grew from 18% of GNP to 23%, doubling in real terms from $330 to $660 billion in 1981 prices. During this period, expenditures for income security (social security, Unemployment Insurance, Aid to Families with Dependent Children, and other programs that provide cash transfers or access to essentials) increased from 22% to 34% of the budget. In percentage terms, the growth in health expenditures—now largely Medicare and Medicaid—was even more rapid, from 1.4% to 10% of the budget. Similarly, the share of the budget devoted to education, training, employment, and social services increased from 1.9% to nearly 5%. Taken together, the budget share of these three categories of social programs doubled from 25% to 50%.

Whereas the budget in 1965 could have been characterized as defense-oriented, by 1981 it was clearly oriented toward social welfare (Table 1). The budget share devoted to national defense, international affairs, and veterans' benefits and services declined from 50% to 29%. In spite of the Vietnam war, solutions to the problems of

Table 1

The Composition of the Federal Budget, Fiscal Years 1965, 1981, and 1986 (in percentage terms)

Category	(1) 1965	(2) 1981	(3) 1986[a]
National defense, international affairs, and veterans' benefits and services	50.4%	29.5%	40.1%
Transportation, community and regional development, and revenue sharing	6.5	6.0	3.6
Natural resources and environment, energy, and agriculture	5.8	4.5	1.5
Income security	21.7	34.3	33.0
Health	1.4	10.0	11.0
Education, training, employment, and social services	1.9	4.8	1.9
General government, interest on the debt, general science, space and technology, other	14.8	15.5	14.7
Offsetting receipts	-2.6	-4.6	-5.8
Total	100.0	100.0	100.0
Total outlays as a percentage of GNP	18.0	23.0	19.9
Total outlays (billions of current dollars)	$118.4	$657.2	$927.0
Total outlays (billions of real 1981 dollars)	$333.3	$657.2	$711.4

Sources: Office of Management and Budget, *The United States Budget in Brief, Fiscal Year 1975* (Washington, D.C.: GPO, 1975), p. 48; Office of Management and Budget, *Budget of the United States Government, Fiscal Year 1983* (Washington, D.C.: GPO, 1982), pp. 3-34, 9.50-9.56

[a]Estimate.

poverty, inequality, urban decay, and limited access to health care and education were the focal points of a concerted federal effort.

The Reagan budget cuts

The pendulum has now swung in the other direction. Many of the programs which grew most rapidly from 1965 to 1981 (Food Stamps, Comprehensive Employment and Training Act, federal guaranteed loan programs for higher education, and Legal Assistance, for example) have sustained the largest cuts. Compared to Carter's proposed 1982 budget, the fiscal 1982 budget that was proposed by Reagan represented a reduction of $44 billion, or 5.7%, and all categories except national defense were reduced.[3] Over half of the $44 billion budget reduction came from two areas: income security; and education, training, employment, and social services.

The full extent of the shift in priorities being carried out by President Reagan can be seen in the estimates for the 1986 budget, in which 19.9% of GNP, rather than the current 23%, is scheduled to be spent. The composition by category of the 1986 budget is shown in the third column of Table 1. By that time, national defense, international affairs, and veterans' benefits and services will account for 40% of the total budget. All of the other categories except health will be reduced in relative importance.

The effects of fiscal retrenchment

The budgetary retrenchment and reallocations are likely to affect income distribution and to alter economic behavior. The 1982 budget cuts exceed 20% in many of the programs introduced or expanded since the 1960s and are likely to increase poverty, despite assurances that the "safety net" will be maintained.

Table 2 shows the size of the 1983 budget for social programs, both with and without the new cuts proposed by the Reagan administration. It gives the anticipated budgetary costs for each program through 1987. Table 3 shows the percentage by which each program will be reduced in fiscal year 1983 by the Reagan cuts. It can be readily seen that while deep cuts are planned for programs designed for the poor and near poor—such as AFDC, Food Stamps, Medicaid, education aid, Low-Income Energy Assistance, and training and employment programs, there will be almost no change in the level of spending in most of the programs that benefit the middle class as well as the poor.

Particularly hard hit will be the demographic group with the lowest mean census income—households headed by women with children. This is a rapidly growing group. The percentage of children now living in one-parent households is 17.6, a figure which has doubled since 1965. Available data indicate that 55.6% of these households receive transfers, which account for 21.5% of their cash income. Although 65% of these women work, 40% of them fall below the poverty line after transfers. Among mothers who never married and mothers in minority ethnic groups, the incidence is much higher. It was estimated by the University of Chicago's Center for the Study of Welfare Policy that the typical AFDC mother who worked would experience a 20% to 30% decline in her monthly income.[4] For example, in New York the typical working welfare mother with two children was expected to experience a decline in monthly income from 119% to 90% of the poverty line; in Texas the decline for the same woman would be from 63% to 48% of the poverty line; in Michigan from 108% to 87%.

Blacks will suffer disproportionately from the Reagan programs. Because a higher proportion of blacks are poor than whites, a greater proportion will be affected by the reductions in transfers. Furthermore, since 55% of the net employment increase for blacks has occurred in the public sector, and much of that in social welfare programs, reductions in these programs will cause a higher percentage of blacks than whites to lose their jobs.

Also greatly affected will be the near poor. This group has been losing ground over the last decade relative to the top income groups. Although their incomes tend to be too high for them to qualify for most transfer programs, their wages are neither high enough nor stable enough to carry them through economic or personal hard times. This group has stayed above the poverty line with the help of food stamps and extended unemployment insurance coverage in economic downturns; it has depended upon job training and education subsidies to provide opportunities for a better life. Yet because the near poor are not being classified as truly needy, their eligibility for food, housing, medical care, and cash benefits is being most restricted.

Ironically, the cuts in social programs may well reduce the work effort of many lower-income families, and in doing so increase the budget costs. One of the immutable laws of public finance is that the adequacy and moderate work disincentives of income transfer programs cannot both be held constant while the population covered is simultaneously reduced. The Reagan program has aimed at maintaining adequacy (the safety net), while removing a large number of families just above the poverty line from the benefit rolls. As a result, work disincentives have increased for those still receiving benefits. For example, before the fiscal year 1982 changes, the typical working welfare mother with one child in Wisconsin earned $432 per month, reported average work expenses of $108, and

Table 2

The Budget and Social Programs: Costs
($ Billions per fiscal year)

Cost	1981	1982	1983	1984	1985	1986	1987
Food stamps[a]							
Without Reagan cuts	$10.3	$10.6	$11.8	$12.1	$12.5	$12.8	$13.1
With Reagan cuts	10.3	10.3	9.6	9.7	10.0	10.2	10.4
AFDC							
Without Reagan cuts	8.1	7.8	6.6	6.6	6.7	6.8	6.9
With Reagan cuts	8.1	7.6	5.5	5.5	5.6	5.6	5.7
Medicaid							
Without Reagan cuts	16.8	18.1	19.0	21.0	24.2	26.5	29.2
With Reagan cuts	16.4	17.8	17.0	18.6	20.4	22.1	24.3
Medicare							
Without Reagan cuts	42.5	49.9	57.8	66.3	76.2	87.0	99.1
With Reagan cuts	42.5	49.6	55.4	61.2	68.4	75.6	83.1

Source: R. Pear, "Benefits for Poor Face Deepest Cuts," *New York Times*, Feb. 14, 1982. © 1982 by the New York Times Company. Reprinted by permission.
Note: The 1981 figures are actual outlays; the other figures are projected spending.
[a] Figures do not include Puerto Rico.

received $217 from AFDC. Her monthly disposable income was $140 higher than that of a nonworking AFDC mother with one child, who received $401 per month. Now after four months of welfare recipiency, her earnings reduce her welfare benefits even further, and she receives only $44 from AFDC. Her income after work expenses is now actually $33 per month lower than that of the nonworking woman, and 32% lower than it was in fiscal year 1981. Such an arrangement is hardly likely to encourage work effort.

These work disincentives may be offset to some extent if the lower benefit reduction rates for those no longer eligible for welfare induce individuals who are affected to increase their work effort. The Reagan administration also seeks to offset the increased work disincentives for welfare recipients by enforcing work requirements.

Thus at the same time that income tax reductions are cutting tax rates for the rest of the population and thereby increasing their prosperity, many lower-income families who receive welfare benefits and already face high benefit reduction rates are confronted by even higher rates, the elimination of programs that made economic advancement possible, and work disincentives.

Table 3

The Budget and Social Programs:
Reagan's Proposed Cuts, 1983
(Percentage change)

Programs designed primarily for the poor	
Child nutrition	9.4%
Medicaid	10.4
Welfare	17.5
Social services block grant	17.8
Education aid	17.9
Food stamps	19.1
Low-income energy assistance	25.8
Training, employment	46.2
Programs serving poor and nonpoor	
Social Security	0
Veterans' disability compensation	1.4
Medicare	4.3
Civil Service retirement	2.2
Guaranteed student loans	23.0

Source: R. Pear, "Benefits for Poor Face Deepest Cuts," *New York Times*, Feb. 14, 1982. © 1982 by the New York Times Company. Reprinted by permission.

The outlook for the future

But what of the supply-side miracle? Suppose that the administration's program does succeed in stimulating economic growth. Peter Gottschalk has examined the evidence concerning the trickle-down hypothesis.[5] He concludes that there is little reason to think that the earnings gains from economic growth that accrue to those with labor market disadvantages are likely to be large enough to significantly reduce poverty. He analyzed the economic situation of a sample of middle-aged married men over the 1966-1975 period and found that even though real earnings increased on average, inequality and the proportion of husbands with low earnings also increased. In fact, 43% of those with low earnings in a given year had low earnings in all the years surveyed, and 78% had low earnings in more than half of them. This indicates a good deal of permanence within the low-earnings population, even during prosperous years.

Gottschalk also shows that, unless policies are implemented to alter the structure of the labor market facing the poor, poverty will decline little in the 1980s even if the unemployment rate is 6% and cash transfers were to grow as fast as national income.[6] Table 4 provides data on the incidence of poverty from 1968 to 1980, and some projections to 1986. The projections are based on the administration's own estimates of unemployment rates, price levels, and social spending. Even if the Reagan administration succeeds in achieving its projected levels of economic growth, poverty in 1986 will be higher than it was at the end of 1980. As for the immediate future, poverty as officially measured is estimated to rise above 15% by the end of 1982, a level not seen since the late 1960s, shortly after the declaration of the war on poverty. ■

Table 4

Percentage of Persons with Incomes below Poverty Line, Selected Years 1968-1980 with Projections to 1986

Year	Official Measure[a]	Adjusted to Account for In-Kind Transfers and Taxes[b]
1968	12.8%	9.9%
1972	11.9	6.2
1974	11.2	7.2
1979	11.6	6.1
1980	13.0	7.5[c]
1981[c]	13.7	8.2
1982[c]	15.2	10.2
1984[c]	14.3	9.3
1986[c]	13.7	8.7

[a] U.S. Bureau of the Census, *Current Population Reports*, "Money Income and Poverty Status of Families and Persons in the United States: 1980," P-60, No. 127, August 1981, for 1968 to 1980.

[b] T. Smeeding, "The Anti-poverty Effect of In-Kind Transfers: A 'Good Idea' Gone Too Far?" *Policy Studies Journal*, forthcoming, for 1968 to 1979.

[c] Estimated by S. Danziger and P. Gottschalk, Institute for Research on Poverty, University of Wisconsin, using data on projected unemployment rates, price levels, and social spending as reported in *Budget of the United States, Fiscal Year 1983* (Washington, D.C.: GPO, 1982).

[1] This article is taken in part from Danziger and Haveman, "The Reagan Budget: A Sharp Break with the Past," *Challenge, 24* (May-June 1981), 5-13 (IRP Reprint 434); Danziger, "Children in Poverty: The Truly Needy Who Fall Through the Safety Net," *Children and Youth Services Review, 4* (1982), 35-51; and Danziger, "The Distribution of Income: An Account of Past Trends and a Projection of the Impacts of the Administration's Economic Program," testimony presented to the Joint Economic Committee, U.S. Congress, February 10, 1982.

[2] President of the United States, *America's New Beginning: A Program for Economic Recovery* (Washington, D.C.: The White House Office of the Press Secretary, February 18, 1981); and Office of Management and Budget, *Budget of the United States Government, Fiscal Year 1983* (Washington, D.C.: GPO, 1982), pp. 3-34, 9.50-9.56.

[3] Because of poor economic performance and continuing high interest rates, it is now estimated that the fiscal year 1982 budget will be $725.3 billion, substantially higher than the $695.3 billion expected when the budget was proposed in February 1981.

[4] University of Chicago, Center for the Study of Welfare Policy, "The Poor: Profiles of Families in Poverty," March 20, 1981, mimeo.

[5] P. Gottschalk, "Earnings Mobility: Permanent Change or Transitory Fluctuations?" *Review of Economics and Statistics*, 1982, in press.

[6] Gottschalk, "Transfer Scenarios and Projections of Poverty into the 1980s," *Journal of Human Resources, 16* (1981), 41-60.

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