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RECENT INCREASES IN POVERTY: TESTIMONY BEFORE THE HOUSE WAYS AND MEANS COMMITTEE

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Recent Increases in Poverty: Testimony before the House Ways and Means Committee

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Abstract

This paper contains the testimony presented by IRP research affiliates and the Assistant Secretary for Planning and Evaluation at DHHS to the U.S. House of Representatives, Ways and Means Committee, Hearings before the Subcommittee on Oversight and the Subcommittee on Public Assistance and Unemployment Compensation, on October 18 and November 3, 1983.

The presentation by Danziger discusses alternative measures and definitions of poverty, then tabulates the trend in poverty rates under different income concepts. The absolute measures show a general decline in poverty from 1965 to 1978 and steady increases thereafter; relative measures show no declines for the earlier period and small increases in poverty for the later period. In terms of antipoverty effectiveness, public transfers exerted increasing effect until 1978, then diminished in strength. In-kind transfers have had a smaller antipoverty effect than cash social insurance, and a much larger effect than cash public assistance transfers. The poverty deficit, a measure of the extent of poverty for those below the threshold, follows the same pattern of decline to 1979 and increases through 1982. The elderly have experienced the greatest rise out of poverty since 1967; blacks, persons of Spanish origin, and women heading households have experienced the least decline in poverty.

The testimony by Gottschalk assesses the relative effect of economic growth versus public transfer payments on the incidence of poverty. Evidence for the period 1967-79 shows that increases in average transfers were somewhat more important than increases in average market incomes in

reducing poverty, and that both were partly offset by increases in inequality. From 1979 to 1982 poverty rose, despite increased transfers, because of the recession and even more so because of an increase in inequality. Transfer increases have had varying effectiveness across groups. Among men of working age, growth in market incomes was more important than transfer benefits in lowering poverty, but changes in the income distribution diminished the gains. For the elderly, almost all of the decline in poverty was due to increased transfers. Past patterns lead to the conclusion that poverty rates will remain high in the mid-1980s even if economic conditions improve.

Rubin discusses the benefits that an improved economy can be expected to bring through increased employment and reduced inflation, and describes federal programs to encourage the work effort of the poor. Another federal proposal would counter the problem of the growing number of single mothers with children by strengthening collection of child support payments. Studies assessing the effects of recent changes in the AFDC program indicate that those changes have not been an important factor in increasing the poverty rate.

Smeeding describes the valuation of in-kind transfers and the extent to which they have reduced poverty. He also discusses the effect of taxes on income and the problem of adjustments for underreporting of money income. The official definition of poverty fails to take all three issues into account. Adjusted to take account of these factors, poverty rates are lower than the official ones by several percentage points, but show the same marked rise each year since 1979. In those years poverty increased especially among traditional husband-wife families. Despite recent reductions in income taxes, the tax burden on poor families has increased: payroll and income taxes took 9.6 percent of the income of a family of four at the poverty level in 1982, as compared to 6.2 percent in 1979.

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Alternative Measures of the Recent Rise in Poverty

Sheldon Danziger

Poverty as officially measured by the Census Bureau declined from 22.4 percent of all persons in 1959 to 11.1 percent in 1973, remained in the 11 to 12 percent range for the rest of the 1970s and then increased to 13.0 percent in 1980, 14.0 percent in 1981 and 15.0 percent in 1982. This recent rise in poverty is the focus of today's hearings. While there are many valid criticisms of the official poverty series, I show that the recent rise in poverty is not an artifact of the official measure. Poverty increased rapidly between 1978 and 1982 for each of the alternative poverty measures discussed here. And, while poverty has been increasing, the antipoverty impact of income transfers has been declining. This is because a smaller percentage of poor households are receiving transfers that have been declining in real terms.

ALTERNATIVE MEASURES OF POVERTY

The official measure of poverty provides a set of income cutoffs adjusted for household size, the age of the head of the household, and the number of children under age 18 (until 1981, sex of the head and farm-nonfarm residence were other distinctions). The cutoffs provide an absolute measure of poverty which specifies in dollar terms minimally decent levels of consumption. The official income concept, current money income received during the calendar year, is defined as the sum of money wages and salaries, net income from self-employment, Social Security income and cash transfers from other government programs, property income (e.g., interest, dividends, net rental income), and other forms of cash income (e.g., private pensions, alimony). Current money income does not include capital gains, imputed rents, government or private benefits in-kind (e.g., food stamps, Medicare benefits, employer-provided health insurance), nor does it subtract taxes, although all of these affect a household's level of consumption.

The official poverty cutoffs are updated yearly by an amount corresponding to the change in the Consumer Price Index so that they represent the same purchasing power each year. According to this absolute standard, poverty will be eliminated when the incomes of all households exceed the poverty lines, regardless of what is happening to average household income.

There have been numerous discussions over the past fifteen years as to whether the official poverty thresholds and income concept are relevant to policy choices (U.S. Department of Health, Education, and Welfare, 1976). Despite these controversies, the adoption of an official measure of poverty in the mid-1960s and its use as a social indicator became a symbol of this country's commitment to raising the standard of living of the poorest citizens.

Income poverty is a complex concept, and different types of poverty thresholds and income concepts are appropriate for different purposes. An absolute perspective, such as the official measure, focuses on those with incomes that fall short of a minimum (fixed) level of economic resources. On the other hand, relative poverty indicators emphasize not only the household's own level of resources, but how its position compares to that of others. A relative definition draws attention to the degree of inequality at the lower end of the income distribution. Those whose incomes fall well below the prevailing average in their society are regarded as poor, no matter what their absolute incomes may be. A relative poverty threshold, therefore, changes at about the same rate as average income.

The recent Census Bureau technical paper (1982) on the valuation of in-kind transfers addresses only the issue of augmenting the official income concept, not the issue of changing the current poverty thresholds. However, just as the valuation of in-kind transfers reduces measured poverty, the use of a relative poverty threshold during a period of rising real incomes or an updating of the official thresholds would increase measured poverty (e.g., see Fendler and Orshansky, 1979).

Figure 1

A Matrix of Poverty Measures

	Income Concept	
	Pretransfer Income	Posttransfer-Posttax Income
Absolute	I	II
Relative	III	IV

A matrix of poverty measures showing two income concepts and two types of poverty thresholds is presented in Figure 1. The official income concept lies somewhere between pretransfer income and posttransfer-posttax income on the first row. Census money income does not distinguish between income derived from market and private transfer sources (e.g., wages, dividends, alimony) and income derived from government sources (e.g., Social Security, Public Assistance income). As such, it fails to separate the private economy's antipoverty performance from the performance of government cash transfer programs. Households that do not receive enough money income from private sources to raise them over the poverty lines constitute the pretransfer poor (a more exact title would be pre-government-transfer poor). Pretransfer poverty has received little attention, yet it reveals the magnitude of the problem faced by the public sector after the market economy and private transfer system (e.g., private pensions, interfamily transfers) have distributed their rewards. This information is essential for analyzing the "trickle-down" effects of economic growth and for assessing the extent to which public transfer programs reduce poverty.

A related concept is prewelfare income. While pretransfer income does not count any money income from government programs, prewelfare income excludes only income from cash public assistance (i.e., welfare) programs. Social insurance benefits (e.g., Social Security, Unemployment Insurance), which are based on past earnings and tax contributions, are included in prewelfare income along with private market income because they are generally perceived by the public as earned. For many, the "real" poverty population, the one to whom antipoverty policy should be addressed, is the prewelfare poor.

The valuation of in-kind transfers does move the Census closer to the concept of posttransfer-posttax income. This preferred measure could have been obtained if, in addition to adding in-kind government transfers received by the poor, the report had also added in-kind private transfers (e.g., fringe benefits) and subtracted direct taxes paid. Nonetheless, recent studies suggest that the report's results would not be significantly affected by these adjustments.

Table 1 presents seven different time series of the incidence of poverty for all persons for selected years between 1965 and 1982. Four series using the official poverty thresholds appear in the top panel; three series using a relative measure, in the bottom.

The relative measure is one developed by Robert Plotnick (Plotnick and Skidmore, 1975). In 1965, the first year for which detailed data is available, the relative poverty lines are set equal to the official (absolute) ones. (In 1965, the official lines were equal to about 44 percent of the median income.) In succeeding years the relative lines are changed at the same rate as the median income.[1] With this approach, trends in absolute and relative poverty are easily compared because they begin with the same base year value.

Consider first the four series in the top panel. Each shows that poverty declined over the 1976 to 1978 period and then increased rapidly in the 1978 to 1982 period. That the official data overstate poverty because of the failure to adjust for in-kind transfers can be seen by comparing columns three and four. Nonetheless, poverty adjusted for in-kind transfers is higher than at any point since the late 1960s. Also, column 1 shows that about a quarter of all persons in 1982 live in households that do not receive market incomes high enough to take them out of poverty.

While the three series based on the official measure show a decline in the 1965-1978 period and then an increase, the three series based on the relative measure are more stable.[2] They show no significant declines for the early period, and smaller increases for the later period. Because the relative poverty line has been about 10 to 15 percent above the official line, it shows more poverty in every year.

Table 1

The Trend in the Incidence of Poverty Among Persons, Selected Years 1965-1982

Type of Measure, Year	Pretransfer Income (1)	Prewelfare Income (2)	Posttransfer Income (Census Money Income) (3)	Adjusted Income[a] (4)
Official Measure				
1965	21.3%	16.3%	15.6%	12.1%
1968	18.2	13.6	12.8	9.9
1972	19.2	13.1	11.9	6.2
1974	20.3	13.1	11.6	7.2
1976	21.0	13.1	11.8	6.7
1978	20.2	12.6	11.4	n.a.
1979	20.5	12.9	11.7	6.1
1980	21.9	14.2	13.0	n.a.
1981	23.1	15.1	14.0	n.a.
1982	24.0	15.9	15.0	8.8[b]
% Change				
1965-1978[c]	-5.2	-22.7	-26.9	-49.6
1978-1982[c]	+18.8	+26.2	+31.6	+44.3
Relative Measure				
1965	21.3%	16.3%	15.6%	n.a.
1968	19.7	15.3	14.6	n.a.
1972	22.2	n.a.	15.7	n.a.
1974	22.9	16.1	14.9	n.a.
1976	24.1	16.3	15.4	n.a.
1978	23.9	16.5	15.5	n.a.
1979	23.8	16.6	15.7	n.a.
1980	24.5	16.9	16.0	n.a.
1981	25.5	17.8	16.9	n.a.
1982	26.5	18.5	17.8	n.a.
% Change				
1965-1978	+12.2	+1.2	-0.6	n.a.
1978-1982	+10.9	+12.1	+14.8	n.a.

Source: Unless noted otherwise, the data are computations by the author from the Survey of Economic Opportunity (for 1965) and various March Current Population Surveys (for other years).

[a]Adjusted income data are from Timothy Smeeding (1982).

[b]This is an estimate from Gottschalk and Danziger (1983).

[c]Percentage changes for adjusted income data are from 1965-1979 and 1979-1982.

n.a. = not available

THE ANTIPOVERTY EFFECTIVENESS OF TRANSFERS

Between 1965 and the mid-1970s, the growth in real expenditures for cash and in-kind transfers per recipient household far exceeded the real increase in per household income. This growth, a major development in American social welfare policy, accounts for much of the observed declines in poverty over this period. Growth rates for transfers have slowed in recent years.

Table 2 measures the antipoverty effectiveness of major income transfer programs by the percentage of the pretransfer poor persons removed from absolute or relative poverty by transfers.[3] The table divides all government transfers into cash social insurance transfers, cash public assistance transfers, and in-kind transfers (whether social insurance or public assistance).

For each type of transfer and for each measure of poverty, public transfers became increasingly effective until 1978.[4] The fraction of absolute pretransfer poor households receiving a cash transfer payment rose from less than 70 percent in 1965 to over 80 percent in 1978 and declined slightly since then. The real value of recipients' transfers increased from 1965 to 1978, but declined thereafter. For example, the average cash transfer received by a pretransfer poor household declined by about 5 percent between 1978 and 1982, to about $6000. The decline was over 10 percent for the same period for nonaged women heading households, to about $4400. As a result, transfers removed about 43 percent of the pretransfer poor from absolute poverty in 1965, over 70 percent in 1976, but less than 65 percent in 1982.

Table 2

The Antipoverty Effectiveness of Major Income Transfers, Selected Years, 1965-1982

Poverty Measure	Percentage of the Pretransfer Poor Persons Removed from Poverty by:			
	Cash Social Insurance Transfers[a]	Cash Public Assistance Transfers[b]	In-Kind Transfers[c]	All Transfers
Absolute Measure				
1965	23.5	3.3	16.4	43.2
1976	37.6	6.2	28.1	71.9
1978	37.6	5.9	n.a.	n.a.
1980	35.2	8.5	n.a.	n.a.
1982	33.8	3.8	25.8[d]	63.3[d]
Relative Measure				
1965	23.5	3.3	n.a.	n.a.
1976	32.4	3.7	n.a.	n.a.
1978	31.0	4.2	n.a.	n.a.
1980	31.0	3.7	n.a.	n.a.
1982	30.2	2.6	n.a.	n.a.

[a]Cash social insurance transfers include social security, railroad retirement, unemployment compensation, workers' compensation, government employee pensions, and veterans' pensions and compensation.

[b]Cash public assistance transfers include AFDC, SSI (OAA, APTD and AB in 1965), and general assistance.

[c]In-kind transfers include Medicare, Medicaid, Food Stamps, and, for 1976, school lunch and public housing; this figure also adjusts for direct taxes and the underreporting of cash transfers.

[d]Based on estimate for adjusted income poverty 1982.

n.a. = not available

Cash social insurance transfers remove more persons from poverty in all years and for all measures than do cash public assistance transfers, because a greater portion of the pretransfer poor receive them, and because the average social insurance benefit is higher. In-kind transfers--which include benefits from both social insurance and public assistance programs--have a smaller antipoverty impact than cash social insurance and a much larger impact than cash public assistance transfers.

POVERTY DEFICIT

The incidence of poverty reveals the percentage of persons whose incomes fall below the poverty threshold, but does not distinguish the degree of poverty. The "poverty deficit," which measures the total amount of income required to bring every poor person up to the poverty threshold, does distinguish between poor persons who are very close to being nonpoor and those who are farther away from the thresholds. Table 3 shows the pretransfer (column 1) and posttransfer (column 3) poverty deficits in billions of current dollars for selected years between 1967 and 1982. Cash transfers received by the pretransfer poor are shown in column 2. The fourth column shows the percentage reduction in the poverty deficit due to these cash transfers. The fifth column shows the posttransfer poverty deficit as a percentage of GNP. The bottom panel shows the percentage growth in current dollars for these concepts.

Between 1967 and 1979, total cash transfers to the pretransfer poor grew faster than the pretransfer poverty deficit, so the posttransfer deficit grew more slowly. Between 1979 and 1982, the pretransfer deficit grew faster than did transfers. As a result, the posttransfer deficit

Table 3

Poverty Deficit Before and After Cash Transfers, Selected Years, 1967-1982

Year	Pretransfer Poverty Deficit[a] (1)	Cash Transfers Received by Pretransfer Poor Households[a] (2)	Posttransfer Poverty Deficit[a] (3)	Percentage Reduction in Poverty Deficit Due to Cash Transfers (4)	Posttransfer Poverty Deficit as a Percentage of GNP (5)
1967	$22.6	$17.5	$10.0	55.5%	1.29
1974	45.0	57.3	15.1	66.4	1.04
1979	70.5	80.0	23.9	66.0	1.02
1980	88.9	95.9	31.4	64.6	1.22
1981	104.1	109.0	39.3	62.2	1.37
1982	114.9	118.1	45.3	60.5	1.47
% Increase					
1979/1967[b]	211.9	357.1	139.0	--	--
1982/1979[c]	63.0	47.6	89.5	--	--

Source: Computations by author from various March Current Population Survey data tapes.

[a]Billions of current dollars.

[b]Between 1967 and 1979, the Consumer Price Index increased by 117 percent.

[c]Between 1979 and 1982, the Consumer Price Index increased by 33 percent.

grew more rapidly than the pretransfer deficit. This deficit declined from 1.29 percent of GNP in 1967 to 1.02 percent in 1979, and then increased rapidly until it was about 1.47 percent of GNP in 1982. The 1982 pretransfer poverty deficit of $114.9 billion means that the pretransfer income of the typical poor household is about $4540 below the poverty line; the posttransfer deficit of $45.3 billion, that the posttransfer poor are about $3200 below the line. These data reinforce the points made above--poverty has been increasing and the antipoverty impact of transfers has been decreasing in recent years.

DEMOGRAPHIC DIFFERENCES

Table 4 highlights the differences in poverty levels and trends for several major demographic groups for the 1967-79 period. It also shows the effect of in-kind transfers on each group in 1979, the last year for which detailed data on the receipt of in-kind transfers is available. The largest reduction in poverty for the 12 year period and the largest impact of in-kind transfers in 1979 are for elderly persons. For example, between 1967 and 1979 poverty declined by about 20 percent for all persons, but by about 50 percent for the elderly. And, in 1979, in-kind transfers reduced poverty for all persons by about 42 percent but by almost 70 percent for the elderly. Adjusted poverty rates in 1979 for blacks, persons of Spanish origin, and female household heads remain above the official rates that existed for whites in 1967, when in-kind transfers had little impact.

Table 5 shows the composition of pretransfer poor households in column (1) and posttransfer poor households in column (2). Each poor household has been placed into one of the eight categories shown. That

Table 4

Alternative Measures of the Incidence of Poverty: Official Measure for 1967 and 1979 and Money Income Plus the Market Value of In-Kind Transfers for 1979

Persons Living in Poverty, by Type of Household Head	Official Measure 1967 (1)	Official Measure 1979 (2)	Percentage Decline in Poverty between 1967 and 1979 (3)	Money Income Plus In-Kind Transfers at Market Value 1979[a] (4)	Percentage Decline in Poverty Due to In-Kind Transfers, 1979 (5)
All Persons	14.2%	11.1%	21.8%	6.4%	42.3%
White	11.0	8.5	22.7	5.2	38.8
Black	39.3	30.4	22.6	15.1	50.3
Hispanic	n.a.	21.4	n.a.	12.0	43.9
Female householder, no husband present	40.6	34.8	14.3	17.6	49.4
Elderly (65 and over)	29.5	14.7	50.1	4.5	69.4

Sources: For 1979, U.S. Bureau of the Census, Alternative Methods for Valuing Selected In-Kind Transfer Benefits and Measuring Their Effects on Poverty, Technical Paper #50 (Washington, D.C.: U.S. Government Printing Office, 1982). For 1967, U.S. Bureau of the Census, Money Income and Poverty Status of Families and Persons in the United States: 1982, Series P-60, No. 140 (Washington, D.C.: U.S. Government Printing Office, 1983).

[a]In-kind transfers for food, housing, and medical benefits.

n.a. = not available.

Table 5

Composition of Households with Incomes Below the Poverty Line, Official Measure, 1982

Percentage of Poor Households Where Head Is:	Pretransfer Poor (1)	Posttransfer Poor (2)
Over 65 years of age	43.31%	22.01%
Female, with children under six	7.74	12.61
Student	4.08	6.56
Disabled	10.01	11.09
Persons working full-time, full-year	8.51	13.07
Single persons working less than full-time, full-year	10.52	14.78
Male family head, working less than full-time, full-year	10.31	11.95
Female family head, no children under six, working less than full-time, full-year	5.54	7.92
Total	100.00	100.00
Number of households (millions)	25.3	14.2

Source: Computations by author from March 1983 Current Population Survey data tape.

Note: Classification is mutually exclusive and is hierarchical: Any household head who fits in more than one category has been classified only in the one closest to the top of the table.

the direct effects of economic growth on poverty for all persons are not large should not be surprising, as only about one-third of those who are poor before the receipt of transfers can be expected to work. The remaining two-thirds--the aged, female-headed households with children under six, students and the disabled--are likely to remain dependent upon public programs.

A comparison between the pretransfer and posttransfer poor shows the relative success of cash transfers in relieving poverty among the aged, who are about 43 percent of the pretransfer poor and only about 22 percent of the posttransfer poor. There are also significant differences in the composition of the poor by race. The major difference is that while 12.61 percent of all posttransfer poor households are headed by women with children under six, the corresponding percentage for blacks is 22.46 (data not shown).

CONCLUSION

Poverty, no matter how measured, has increased in recent years. And, while the antipoverty impacts of income transfers have declined, they still significantly reduce poverty. Transfers also protect against income losses due to unemployment, retirement, disability and death and guarantee access to minimum levels of food, shelter, and medical care. The growth in transfers has been accompanied by some declines in work effort and savings that may have contributed to sluggish economic performance. But the magnitude of these declines is estimated to be small (see Danziger, Haveman and Plotnick, 1981). While reductions in poverty through increased market incomes has always been the primary stated goal of antipoverty policy, increased cash and in-kind transfers have been major factors in the reductions in poverty that have occurred in the past 15 years. If our projections of the effects of economic growth on poverty (Gottschalk and Danziger, 1983) are accurate, then further reductions in transfer benefits will lead to higher levels of poverty, however measured.

NOTES

[1]The specifics of this measure are as follows. Each family's current money income is divided by its official poverty line. This yields a "welfare ratio" that indicates the fraction by which the family's income exceeds or falls below the official poverty line. Families with the same welfare ratio are assumed to by equally well-off. The relative poor are defined as those families with welfare ratios below .44 of the median ratio.

The fraction .44 was not an arbitrary choice. In 1965, the base year for this analysis of changes in poverty, the median welfare ratio was 2.25. All living units with incomes below the official poverty lines had, of course, welfare ratios less than one. Thus, any household that in 1965 was poor under the official definition necessarily had a welare ratio less than 1.00/2.25 of the median. Defining the relative poor as those with welfare ratios below 1.00/2.25 = .44 of the median yielded, in 1965, the same group of households as were poor from the absolute perspective.

[2]The adjusted income data are not compared to the relative poverty line. Estimating in-kind income from private sources (e.g., fringe benefits) and taxes paid by the nonpoor poses measurement problems that have not yet been solved. Thus, we could not compute a relative measure based upon the median adjusted income.

[3]The antipoverty impacts of seven cash and three in-kind transfer programs are assessed here. They are 1) Social Security and Railroad Retirement, 2) Medicare, 3) federal, state and local government employee pensions, 4) unemployment insurance, 5) workers' compensation, 6)

veterans' compensation and pensions, 7) Supplemental Security Income, 8) public assistance (AFDC, AFDC-U, General Assistance and, prior to 1974, OAA, APTD, and AB), 9) Food Stamps, and Medicaid. While several in-kind transfer programs and all expenditures on public education have been omitted, Food Stamps, Medicare, and Medicaid alone account for over 80 percent of all federal in-kind transfers. For 1976, and the estimate for 1982, school lunch and public housing benefits are also included.

[4]Pretransfer income is calculated by subtracting government transfers from posttransfer income. While this definition assumes that transfers elicit no behavioral responses, transfers do induce labor supply reductions. As a result, recipients' net incomes are not increased by the full amount of the transfer and the pre/post comparisons made here will provide upper-bound estimates of the antipoverty effects of transfers.

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Will a Resumption of Economic Growth Reverse the Recent Increase in Poverty?

Peter Gottschalk

Thank you for giving me the opportunity to report on the results of a study, "Macroeconomic Conditions, Income Transfers, and the Trend in Poverty," which Sheldon Danziger and I recently completed. I am submitting this study for the record. This research attempts to determine the factors that have affected poverty over the 1967-1982 period and the degree to which poverty will be reduced by economic growth in the next several years. This question is particularly important since poverty, as officially measured, has risen from 11.7 to 15.0 percent of all persons between 1979 and 1982. I will first present the general conclusions of that study and then the key supporting materials.

MAJOR FINDINGS

An understanding of what will happen to poverty rates in the future must be grounded in an analysis of the factors which caused poverty to change in the past. Our review of recent history leads us to the following conclusions:

- There have been two offsetting factors influencing long-term changes in poverty. Increases in overall economic performance have helped low-income people. This has been partially offset, however, by an increase in inequality of earnings which has tended to increase poverty.
- Long-term growth in public transfer payments has been at least as important as economic growth in explaining past reductions in poverty.

• Experiences have differed across demographic groups. For persons living in households headed by nonaged males, increases in earnings were roughly four times as important as changes in transfers in reducing poverty. For the elderly, transfers accounted for almost all of the decline in poverty. Increased inequality of income was a poverty-increasing factor for all demographic groups.

Our review of past patterns leads us to be pessimistic about the possiblities for reducing poverty in the near future:

• Poverty is likely to remain above the mid-1970s rates through the mid-1980s, even if the economy grows according to official predictions. The overall poverty rates will remain above 14 percent in 1983 and 1984.

SUPPORTING EVIDENCE

Table 1 provides the basic data on the level of economic activity (real GNP per household in column 1 and the unemployment rate in column 2), the growth in real cash (column 3) and real in-kind (column 4) transfers per household, and the poverty rate for all persons for selected years between 1950 and 1982. Data is presented on the official poverty rate (column 5) and, when available, a poverty rate based on a broader definition of income which includes the receipt of in-kind transfers and the payment of taxes (column 6). Column 5 shows that official poverty rates declined sharply in the 1960s and early 1970s, from about 20 to 12 percent, remained in the 11 to 12 percent range through 1979, and then increased sharply in 1980, 1981, and 1982 to 15 percent. I will present evidence that the recent rise in poverty has been caused both by recession and by longer-term trends in some underlying factors.

Table 1

Time Series on Macroeconomic Conditions, Income Transfers and Poverty, Selected Years 1950-1981

Year	Real GNP per Household (1972 dollars) (1)	Unemployment Rate (2)	Real Cash Transfers per Household[a] (1972 dollars) (3)	Real In-Kind Transfers per Household[a] (1972 dollars) (4)	Official Incidence of Poverty (5)	Incidence of Poverty Adjusted for In-Kind Transfers[b] (6)
1950	$10,880	5.3%	$ 365	$ 29	n.a.	n.a.
1955	12,490	4.4	460	31	n.a.	n.a.
1960	13,060	5.5	664	40	20.2%	n.a.
1961	13,170	6.7	730	43	21.9	n.a.
1962	13,810	5.5	770	49	21.0	n.a.
1963	14,200	5.7	791	54	19.5	n.a.
1964	14,630	5.2	801	58	19.0	n.a.
1965	15,350	4.5	816	63	17.3	12.1%
1966	16,010	3.8	878	71	15.7	n.a.
1967	16,020	3.8	891	150	14.3	n.a.
1968	16,390	3.6	911	204	12.8	9.9
1969	16,470	3.5	958	231	12.1	n.a.
1970	16,080	4.9	1010	242	12.6	9.3
1971	16,170	5.9	1150	273	12.5	n.a.
1972	16,710	5.6	1225	304	11.9	6.2
1973	17,170	4.9	1272	320	11.1	n.a.
1974	16,720	5.6	1263	327	11.2	7.2
1975	16,130	8.5	1395	386	12.3	n.a.

(table continues)

Table 1 (cont.)

Time Series on Macroeconomic Conditions, Income Transfers and Poverty, Selected Years 1950-1981

Year	Real GNP per Household (1972 dollars) (1)	Unemployment Rate (2)	Real Cash Transfers per Household[a] (1972 dollars) (3)	Real In-Kind Transfers per Household[a] (1972 dollars) (4)	Official Incidence of Poverty (5)	Incidence of Poverty Adjusted for In-Kind Transfers[b] (6)
1976	16,630	7.7	1,513	427	11.8	6.7
1977	17,070	7.1	1,508	452	11.6	n.a.
1978	17,440	6.1	1,488	464	11.4	n.a.
1979	17,580	5.8	1,419	472	11.7	6.1
1980	16,850	7.1	1,414	482	13.0	n.a.
1981	17,020	7.6	1,458	505	14.0	n.a.
1982	16,160	9.7	1,475	508	15.0	n.a.

Sources: For GNP, consumer price index, and unemployment rate, 1982 Economic Report of the President; for cash and in-kind transfers, "Social Welfare Expenditures Under Public Programs in the U.S.," Social Security Bulletin, December 1968, December 1972, January 1971, January 1977, November 1981; for official poverty incidence and number of households, Current Population Reports, Series P-60, "Consumer Income"; for adjusted poverty Smeeding, Policy Studies Journal 10, 1982.

[a]Transfers are divided by all households, not by recipient households.

[b]This series also adjusts census incomes for simulated values of taxes and income underreporting.

n.a. = not available.

Changes in the aggregate poverty rates can be viewed as the result of changes in the shape and position of the income distribution. If the incomes of all households increased proportionately, then average incomes would increase and relative inequality would remain unchanged. This would leave a smaller proportion of people in households below the fixed poverty line. Changes in average incomes are, however, not the only factor affecting poverty rates. If the shape of the income distribution changes, then poverty may increase in spite of increases in average incomes. This can happen if economic growth does not increase the incomes of all households equally.

Table 2 shows the impact of changes in average incomes (columns 2 and 3) and changes in inequality (column 4) on the official poverty rate. Changes in average incomes are decomposed into two parts: changes in average <u>market incomes</u> (wages, salaries, private pensions, dividends, etc.) and changes in average cash <u>income transfers</u> (social security, unemployment compensation, welfare, etc.). In order to focus on the recent rise in poverty we look at the periods 1967 to 1979 and 1979 to 1982 separately.

Column 1 shows that while the actual poverty rate for all persons declined by 2.6 percentage points between 1967 and 1979, increases in average market incomes would have reduced poverty by 2.4 points if transfers had remained constant in real terms and the shape of the distribution had not changed. However, real transfers did increase, reducing poverty by an additional 3.1 points. Thus, between 1967 and 1979, <u>increases in average transfers were slightly more important than increases in average market incomes in reducing poverty</u>. Column 4 shows that changes in the shape of the distribution increased poverty by 2.9

Table 2

Decomposition of Changes in Poverty Rates

Household Head:	Actual Percentage Point Change in Poverty (1)	Percentage Point Change in Poverty Associated with Change in: Mean Market Income (2)	Mean Transfer Income (3)	All Other Factors (4)
All Persons				
1967-79	-2.6	-2.4	-3.1	2.9
1979-82	3.3	0.8	-0.4	2.9
Young Men				
1967-79	-1.9	-2.5	-0.6	1.2
1979-82	5.8	3.0	-0.6	3.4
Prime-Aged Men				
1967-79	-1.7	-3.1	-0.8	2.2
1979-82	3.0	0.8	-0.2	2.4
Elderly Persons				
1967-79	-12.9	0.5	-19.6	6.2
1979-82	-0.6	-0.1	-1.8	1.3

Source: Computations from data derived in Gottschalk and Danziger (1983) [cited in Danziger testimony].

Note: The sum of the changes in columns 2, 3 and 4 is equal to the change shown in column 1.

points. <u>Increases in inequality were sufficiently large to offset about half of the poverty-reducing effects of increases in market and transfer incomes.</u>

Row 2 shows the importance of each of these factors in explaining the 3.3 percentage point increases in poverty between 1979 and 1982. The recession led to a decline in average market incomes which increased poverty by 0.8 percentage points. This drop in market incomes was partially offset by countercyclical increases in transfers which reduced poverty by 0.4 points. However, by far the most important factor was the change in the shape of the distribution, which accounted for a 2.9 point increase in poverty. In other words, if all households had experienced equal decreases in market incomes and equal increases in transfer incomes, poverty would have risen by only 0.4 points instead of 3.3 points between 1979 and 1982.

Because there have been large demographic shifts in the composition of households and because different demographic groups have had different experiences, the remaining rows in the table show the poverty rate decomposition for persons in households headed by young men, prime-aged men, and elderly persons. (We were not able to perform the same decomposition for households headed by nonaged women.) For young and prime-aged men, growth in mean market incomes were more important than transfer growth, but changes in the shape of the distribution were again offsetting in both periods for both groups. The largest drop in poverty between 1965 and 1982 occurred for households headed by elderly persons (males and females). This decline was almost solely a result of growth in real transfers.

In summary, economic growth does have an important impact on poverty by increasing the market incomes of the poor directly. However, there are other factors tending to counter the poverty-reducing impact of economic growth. The two most important factors are cyclical decreases in economic activity and long-term increases in inequality of market incomes.

We turn to some projections in order to see whether economic growth will be sufficiently strong to reduce poverty without substantial increases in transfers between now and 1984. Table 3 presents the actual poverty rates for selected years between 1967 and 1982 and our projections for 1983 and 1984 for all persons and for selected demographic groups. The projections are based on the Office of Management and Budget's July 1983 economic assumptions and proposed expenditures under the major transfer programs shown in the FY 1984 budget.

Our projections indicate that the poverty rate for all persons will drop from 15 percent in 1982 to 14.6 percent in 1983 and will stay at that level through 1984. It would take either a stronger than expected recovery or an unexpected increase in income transfers to bring poverty as officially measured back to the 11-12 percent range of the late 1970s.

Table 3 also indicates how experiences differ among demographic groups. Let me mention two of the more striking conclusions. First, elderly persons were the only group to experience continuous declines in poverty between 1980 and 1982 and they are the only group projected to experience continuing declines in poverty in 1983 and 1984. Second, while households headed by white males have below-average poverty rates, they experienced some of the sharpest increases in poverty between 1979

Table 3

Actual Poverty Rates and Projected Poverty Rates (Official Measure)
Based on OMB Economic Assumptions and Proposed Legislation

			Percent Persons with Income Below the Poverty Line who Live in Households where Head Is:					
			White		Black		Hispanic	
	All Persons (1)	Elderly Persons (2)	Male (3)	Female (4)	Male (5)	Female (6)	Male (7)	Female (8)
Actual								
1967	14.2	29.5	8.1	33.9	30.0	61.6	n.a.	n.a.
1970	12.6	24.5	6.8	31.4	21.7	58.8	n.a.	n.a.
1975	12.3	15.3	6.6	28.1	18.2	53.6	20.1	55.6
1979	11.7	15.2	5.9	24.9	16.2	52.2	15.5	48.9
1980	13.0	15.7	6.9	27.1	17.9	53.1	18.5	52.5
1981	14.0	15.3	7.6	28.4	19.4	55.8	18.6	54.0
1982	15.0	14.6	8.7	28.7	20.0	57.4	22.0	57.4
Projections								
1983	14.6	14.2	8.4	27.8	18.5	55.2	19.9	56.2
1984	14.6	13.9	8.3	28.5	19.8	55.4	21.7	54.7

Note: The projections of poverty are based on the July 1983 OMB economic assumptions for 1982 and 1983 (growth in real GNP of -1.7 and 3.1 percent; unemployment rate of 9.5 and 9.9 percent); the budget projections for transfer programs found in the FY84 Budget (growth in real cash transfers of 9.4 and -4.0 percent); and the U.S. Bureau of the Census demographic projections. Actual data from Current Population Reports, P-60 Series, #140.

and 1982. Their poverty rates are also expected to show some of the smallest declines by 1984, at which time their rates will still be above their 1967 levels. All other groups are projected to have poverty rates below their 1967 levels, but above the levels experienced during the 1974 recession.

Projections of poverty using an income definition which includes in-kind transfers are less reliable, since the Bureau of the Census has not published a consistent time series on poverty that counts the value of in-kind transfers. Our rough estimate is that these poverty rates increased from 6.1 percent in 1979 to 8.8 percent in 1982. By 1984 adjusted poverty is projected to be 8.2 percent, which is comparable to levels of the early 1970s.

CONCLUSION

Our overall conclusion is that the changing rate of economic growth is but one factor which has contributed to the past decline and recent increase in poverty. Clearly, increased income transfers have had a substantial impact, especially for the elderly. More disturbing is our conclusion that changes in inequality of earnings have had a large impact on poverty. At this time we cannot explain the causes of this increased inequality. However, if inequality does continue to grow, it will become increasingly difficult to get poverty rates back to their mid-1970s levels.

Statement before the Subcommittee on Oversight and Subcommittee on Public Assistance and Unemployment Compensation, November 3, 1983

Robert J. Rubin
Assistant Secretary for Planning and Evaluation, DHHS

The existence of poverty in American society today is troublesome to us all. Because some of the programs administered by HHS are in large part designed to alleviate the plight of our nation's poor, we welcome the opportunity to discuss the serious issue of poverty in our country today.

The Census Bureau reports that in 1982, 15 percent of Americans lived in poverty. The increase in 1982 continues the trend begun in 1979 under the prior administration. Although poverty continued to increase in 1982, the rate of increase declined--despite the recession--over that of the previous two years. This administration, this President, and this Secretary of Health and Human Services want to stop this trend during our tenure. Our policy for reducing poverty is twofold. First, we believe that a sound growing economy is the essential element to reducing poverty and improving the economic well-being of all Americans. A strong economy will produce jobs that provide income to those capable of working. Employment not only provides immediate income but ensures the long-run potential for improving a family's standard of living. Second, for those who are unable to provide for themselves, the federal and state governments must maintain public assistance programs that assure that every American can maintain a decent standard of living. Let me emphasize that we believe that public assistance should not be used as an alternative to work. For those unable to obtain jobs, public assistance should provide temporary support as well as work experience and training to enable employable recipients to become self-supporting. In my testimony I will discuss (1) how the poor can benefit from an improved economy, (2) what can be done to reverse the trend of a growing number of poor female-headed families, and (3) why the changes made in the Aid to Families with Dependent Children (AFDC) program are not an important factor in the increase in the poverty rate for 1982.

ECONOMIC GROWTH AND POVERTY

The economy is the backdrop against which all public policy must be made. In the late 1970s, the scene was bleak. Investment and productivity were down while inflation ran rampant. Job oportunities dwindled. The value of welfare benefits declined rapidly as the cost of living skyrocketed. For example, from 1975 to 1980, the real value of AFDC benefits declined 16 percent, although the nominal value rose 29 percent.

By 1981, when Ronald Reagan took office, the country was entering a severe recession. President Reagan made economic recovery his first priority and, with the help of Congress, set out to reverse the failed policies of the past. However, profound changes in economic policy take time, more than any of us would like. Before the impact of those policies could be felt, many Americans had lost their jobs or suffered a reduction in income. The poverty statistics for 1982 reflect this overall recessionary hardship.

We expect the poverty rate in 1983 to be lower than the 15 percent rate in 1982, largely becuase the President's program for economic recovery is working. The turnaround began in the second half of 1982 and continues at this time. Inflation has been brought under control. The annualized inflation rate for 1983 is 3.7 percent--an eleven-year low. During 1982, two million Americans were newly employed. Unemployment has been declining since December 1982. Without the leadership of the President, economic recovery would not have begun as quickly and the suffering caused by the recession would have been substantially greater.

The importance of economic growth and low inflation in reducing poverty cannot be overstated. The increase in poverty since 1978 is due almost totally to the poor performance of the economy in that period. Research by Sheldon Danziger and Peter Gottschalk, who testified before your Committees two weeks ago, demonstrates this relationship. They found that the large reductions in poverty from 1967-74 were due in equal part to increases in earnings and other private income and to transfer payments. The small reduction in poverty between 1974 and 1978 was due mostly to improvements in earnings and private income. Similarly, the increase in poverty since 1978 is due to the decrease in real value of earnings and private income. Danziger and Gottschalk note that the poverty-reducing impact of eleven years of growth (1967-78) in earnings and private income was canceled by three years of rapid economic declines (1978-81).

Clearly, the most direct way to reduce poverty is through employment. The Reagan administration is committed to helping welfare recipients obtain the necessary job training and experience to obtain jobs and reap the benefits of economic recovery. To this end, the administration has established several new programs. First, we have promoted state use of job search programs for AFDC and Food Stamp applicants and recipients.

As part of the Reagan program, Congress enacted legislation that permits states to require AFDC applicants to participate in job search. Many states now require employable adults to participate in these programs which motivate and train participants to secure jobs. Ten states already have established job search programs and an equal number are considering doing so.

Second, this administration established the Community Work Experience Program (CWEP) in which states have the option of requiring AFDC recipients to participate in a work experience program in return for receiving their grants. Twenty-two states now have these programs. Others have participated in similar demonstration programs for Food Stamp recipients. We believe CWEP provides an opportunity for welfare recipients who have never worked or who have been out of the labor market for a time to establish good work habits and gain work experience that will help them to find and keep a job.

Finally, the administration is encouraging states to experiment with programs to divert welfare grants to wages--called "grant diversion." These programs permit a state to take the AFDC grant that would be paid to a family and use it to subsidize the wages of the family head for a limited period of time. Employers agree to hire the participant at full wages at the end of the subsidy period. This program provides training, work experience, and a guaranteed transition into a job.

While the programs I have discussed are currently optional for the states, the administration has proposed to make participation in job search programs mandatory for all AFDC applicants and recipients. The package now before the Congress also would require all states to establish work experience programs (CWEP) for AFDC and Food Stamp recipients.

We have also requested permanent authority to permit states to use grant diversion in place of the current authority that permits these programs only in conjunction with a WIN demonstration.

The administration's alternatives are not geared to welfare recipients alone: the Job Training Partnership Act (JTPA), enacted last year, creates a new program for training the disadvantaged for jobs. Unlike its predecessor, CETA, which created many public service jobs, JTPA emphasizes short-term training to enable participants to obtain jobs. Welfare recipients must be served in proportion to their numbers among the disadvantaged population. This program, now underway in all states, is designed to help all disadvantaged workers--including those displaced by the new technology.

Although the programs I have just discussed will help welfare recipients prepare themselves for jobs that can make them self-supporting, a strong economy is necessary to assure that stable jobs with opportunities for advancement are available once the training is complete. Moreover, for those who have succeeded in making the transition from welfare to work, a healthy economy is necessary for them to maintain their standard of living. Under the policies of this administration, the real wages of American workers increased in 1982 for the first time in four years.

In addition, for low-income persons--whether workers or those who are unable to work--a low inflation rate is essential to retaining their purchasing power. Especially for these persons, the reduced inflation rate achieved by the Reagan administration has been extremely important. In the absence of benefit increases, reduced inflation limits the erosion of benefits. If the inflation rate of 12.4 percent in effect in the last year of the Carter administration had not been abated, the poverty threshold would be higher and it is likely that the number of persons below the poverty level would be greater.

As an example of the beneficial effects of this reduction in inflation, consider the level of benefits to families entirely dependent on AFDC and other public assistance. From 1970-83, the purchasing power of AFDC benefits declined more than 30 percent because inflation increased the cost of living substantially beyond the means of state and local governments to keep pace. The largest decline occurred between 1977 and 1981, when the real value of benefits fell 21 percent. Since 1981, the value of benefits has continued to decline, but the 6 percent reduction was considerably smaller than for any other recent two-year period. In fact, if the 12.4 percent inflation rate of the Carter administration had continued, the value of benefits would have declined 21 percent rather than 6 percent between 1981 and 1983.

Before proceeding to discuss other possible reasons for the increases in the poverty rate, I would like to make one observation concerning the rate itself: only cash income is considered when measuring poverty; the value of noncash benefits is ignored. In 1982, benefits under the major means-tested in-kind programs of Food Stamps, child nutrition, Medicaid, housing assistance, and energy assistance totaled $56 billion. This is more than double the $24 billion spent for the cash welfare programs of AFDC and SSI. Furthermore, since 1970 spending in real terms for in-kind programs increased 325 percent while spending on cash benefits declined slightly. This tremendous growth in in-kind programs has had a positive effect on the living standards of many low-income Americans. Excluding these benefits underestimates the overall effect on the poverty rate of government programs directed toward low-income persons. In releasing the 1982 figures, the Census Bureau noted that if in-kind benefits were included, there would be 12-42 percent fewer poor people, depending on the way the benefits are valued.

RISE IN FEMALE-HEADED SINGLE-PARENT FAMILIES

Given this important caveat, I will turn now to another major reason for the increase in the poverty rate: the striking increase in the number of single-parent families headed by women. In 1970, there were 6 million female-headed families. By 1980, this number increased nearly 50 percent to 9 million and reached nearly 9.5 million in 1982. In relative terms, the proportion of all families headed by women was 11.4 percent in 1970 and rose to 15.4 percent in 1982. Also over this period, the divorce rate rose from 47 to 100 per 1000 married couples, and the percentage of births to unwed mothers increased from 11 percent in 1970 to 17 percent in 1979. While the aggregate number and proportion of single-parent families headed by women grew dramatically, their likelihood of being in poverty increased only slightly. From 1970 to 1980, slightly under one-third of this type of family was poor. In 1981 this rose to 34.6 percent, and it rose again in 1982 to 36.3 percent. This indicates that although most individual female-headed families are not losing ground in their struggle to stay out of poverty, the number of such families living in poverty will continue to increase as a direct function of their increasing proportion of the general population.

A key factor contributing to the poverty of female-headed families is the lack of child support from absent fathers. A recent Census Bureau study showed that in 1981 child support orders existed for fewer than half of the families with absent parents (4 million out of 8.4 million). Of those 4 million families with support orders, the full amount of support due was paid in only 47 percent of the cases. Nearly $4 billion of support due to children went unpaid. If support orders were obtained for the 4.8 million families that do not have them, the amount of support paid would increase substantially.

To address this problem, the adminstration has proposed legislation that will encourage states to pursue and collect support payments more aggressively. Our proposal would require states to use collection practices that have proven effective in order to ensure that money due as ordered is paid.

In addition, our child support proposal changes the federal financing of the program to reward states with good programs and high levels of collection. The amount of the incentive payments available to states would increase and would be based both on how much support states collect and the efficiency of the state's operation. Also, for the first time, states would receive incentive payments based on their efforts on behalf of nonwelfare children.

With enactment of these proposals, we expect that child support payments for both welfare and nonwelfare children will increase. For welfare children, we expect a 60 percent increase in collections from 1982 to 1986, and for nonwelfare children the amount of support collected should double, from $1 billion in 1982 to $2 billion in 1986.

AFDC CHANGES

I have discussed the economy and the rise in single-parent female-headed families in reference to the increase in poverty. Now I would like to turn to the issue of the effect on the poverty rate of the Reagan administration's changes in social programs, in particular the AFDC program.

The changes enacted in OBRA (the Omnibus Budget and Reconciliation Act, 1981) and TEFRA (the Tax Equity and Fiscal Responsibility Act, 1982) were directed at reducing benefits to families with other sources of income that were not being counted, but which could reasonably be expected to be available for the families' use.

Departing from its basic purpose to assist families with no means of suport, AFDC had developed into a program which provided permanent income supplements to families with a low-income worker. The monthly income disregard of $30 plus 1/3 of earnings that was in effect from 1969 to 1981 was intended as an incentive for AFDC recipients to get a job and to help families make a transition from welfare to work. This intent was never fulfilled. With the disregard in place, the number of families with earnings did not increase. The percentage of families leaving welfare due to earnings declined. Furthermore, the permanent nature of the disregard created a serious inequity. Because the disregard was available only to persons who began working while their families were receiving AFDC, similarly situated families who had never relied on welfare were not eligible. The OBRA changes returned the $30 plus 1/3 disregard to its original purpose of providing a transition period for welfare recipients beginning to work. As modified, the disregard applies only during the first four months on the job. The families affected by this change all had other sources of income.

Many critics of OBRA charged that the AFDC earned-income disregard changes would lead welfare recipients to quit their jobs and rely entirely on welfare. Such behavior would increase government costs as well as the problem of long-term welfare dependency. Evidence from a national sample of welfare recipients studied by the Research Triangle Institute and from a sample of Wisconsin recipients studied by researchers at the University of Wisconsin suggests that the critics were totally wrong. For example, in the Wisconsin study, 80 percent of recipients who lost all benefits and 60 percent of recipients whose benefits were reduced were working at the same job 13 to 17 months after the change in benefits.

One should note that this job tenure was occurring when Wisconsin's unemployment rate increased form 8.7 percent to 13.5 percent and then fell to 10.2 percent. In both the Wisconsin and national samples, less than 18 percent of those who lost benefits were receiving AFDC payments a year later; this is no greater than the rate at which welfare recipients who left the rolls returned in the year prior to the OBRA changes. In addition, the Wisconsin recipients who lost all AFDC benefits and were not receiving assistance 13 to 17 months later realized average wage increases of 10 to 17 percent.

Other changes to assure that all income and resources would be counted had a similar effect. Families unfairly advantaged by the old rules lost benefits and program equity was improved. In all, 408,000 families lost eligibility benefits and 299,000 lost benefits as a result of the OBRA changes. The changes saved the federal and state governments about $1.1 billion in 1983.

These changes affected families most in need in the following ways: they freed funds that could be used to increase assistance to those who have no choice but to rely on governement assistance. Since October 1981, when OBRA took effect, 25 states have increased their AFDC need or payment standards.

Before concluding, I also would like to note that the 1982 report on poverty in America contains some very good news. The poverty gap between the elderly and all other Americans has been closed. In 1982, the elderly were no more likely to be in poverty than the nonelderly. One reason for this relative improvement is that the elderly are not affected by a poor economy because they are generally not employed. In most cases, elderly persons rely on government payments such as Social Security and Supplemental Security Income for at least a portion of their incomes. As you know, these are indexed to the cost of living, which protects beneficiaries from any real loss in benefits. Data just available show that in April 1979, 68 percent of elderly families in a given month would have been poor without government aid. Cash payments (primarily Social Security and SSI) reduced the poverty rate to 24 percent and, with the addition of in-kind benefits, to 7 percent.

Government assistance is essential to assure that those who generally cannot work to support themselves, including many elderly, do not live in poverty. But government aid should not substitute for jobs for people capable of working. Rather than expanding government programs to help families in which there is an adult who can work, we need to strengthen the economy so that jobs and advancement opportunities are available to those workers. For welfare recipients, we need strong work programs that prepare recipients both to enter the job market and to become self-supporting. For women raising children on their own, we need to assure that absent fathers fulfill their basic parental responsibility to support their children.

If we can accomplish these goals, government assistance will rightfully be targeted to those who are not capable of working and have no other private means of support. With fewer people relying on governmental assistance, benefits could be increased without placing additional strain on government resources.

I believe we all share the same ultimate goal--that no person in this country live in poverty. However, every benefit has its cost. With a dragging economy, everyone suffers. Conversely, a strong economy benefits everyone. Economic recovery, which this administration is accomplishing, is the foundation on which a reduction in poverty can be built. It is the administration's goal to restore the economy to vibrant health--and to make sure that all our citizens can partake of this national well-being.

What the Official Estimates Fail to Show

Timothy M. Smeeding

INTRODUCTION

I have been asked to address the effect of alternate measures of income on poverty, particularly as they might bear on the recent increases in the official poverty figures in the U.S. In my opinion, there are three major items which affect the level of poverty in the United States that are not taken into account in the official poverty figures. In order of importance, they are:

1. Failure to include the impact of benefits from in-kind or non-money income transfers such as food stamps, public housing, and Medicaid in the incomes of the poor.
2. Failure to subtract federal and state income and payroll taxes before comparing incomes to poverty levels.
3. The problem of underreporting, non-reporting, and misreporting of survey income.

In this testimony I will first treat these shortcomings in this order, explaining my estimates of their individual impacts on poverty. Second, I will relate these shortcomings to the recent changes in the official poverty count. Finally, I will present estimates of the net impact of these adjustments on the extent of and trend in poverty in the U.S.

ACCOUNTING FOR IN-KIND BENEFITS, TAXES, AND UNDERREPORTING

Having authored the recent Census Bureau report to Congress on the effect of in-kind benefits on poverty (Smeeding, 1982a) and having also written extensively on the effect of taxes and underreporting on poverty (Smeeding, 1975, 1977, 1982b), I am particularly pleased that you have asked me to testify before you today.

Measuring and Valuing In-Kind Transfers and Assessing Their Impact on Poverty

My report to Congress described three different strategies for valuing in-kind transfers and developed the estimating procedures to implement them:

1. The market value is equal to the purchase price in the private market of the goods received by the recipient, e.g., the face value of food stamps; or the government cost of particular goods, e.g., the insurance value of Medicare and Medicaid.
2. The recipient or cash-equivalent value is the amount of cash that would make the recipient just as well off as the in-kind transfer; it therefore reflects the recipient's own valuation of the benefit. The recipient or cash-equivalent value is usually less than the market value. Even though cash-equivalent value is the theoretically preferred measure, it is quite difficult to estimate, especially for medical care.
3. The poverty budget share value, which is tied to the poverty concept, limits the value of food, housing, or medical transfers to the proportions of income spent on these items by persons at or near the poverty line in 1960-61, when in-kind transfers were

minimal. It assumes that in-kind transfers in excess of these amounts are not relevant for determining poverty status because an excess of one type of good (e.g., medical care) does not compensate for a deficiency in another good (e.g., housing).

Because of the importance of medical benefits, which constitute over 80 percent of the total market value of in-kind transfers, and because of the problematic nature of valuing these benefits, three alternative definitions of in-kind benefits to be included as income were also presented in this report. These definitions were: food and housing alone; food, housing, and medical care excluding institutional care (nursing home) benefits; and food, housing, and medical care including institutional care. In summary, the report contains nine basic alternative measures of poverty, each alternative incorporating one of the three valuation strategies and one of the three definitions of in-kind benefits to be counted in income. Each of these measures can be compared to the poverty rate based on Census money income--the official measure of poverty.

Table 1 summarizes these results. It should be noted that each of these different income definitions and valuation strategies are separable. Thus it is possible to combine them in any way that policymakers deem relevant. My first preference as an economist is the cash-equivalent-value approach. But cash equivalents are difficult to measure. Taking into account ease of estimation and protecting against medical benefit overvaluation, I would combine a mixture of all three valuation strategies: the market value strategy for food benefits; recipient or cash-equivalent value for housing benefits; and poverty budget share value for medical benefits. With no other changes, e.g., those for taxes or reporting, such a combination would have produced a

Table 1

All Persons: Comparison of the Number of Poor and Poverty Rates Using Alternative Income Concepts and Valuation Techniques; 1979 (Numbers in thousands)

	Valuation Technique		
Income Concept	Market Value Approach	Recipient or Cash-Equivalent Value Approach	Poverty Budget Share Value Approach
Money income alone			
Number of poor	23,623	23,623	23,623
Povery rate	11.1	11.1	11.1
Money income plus food and housing			
Number of poor	19,933	20,218	20,743
Poverty rate	9.4	9.5	9.8
Percentage reduction[a]	-15.6	-14.4	-12.2
Money income plus food, housing, and medical care (excluding institutional care expenditures)			
Number of poor	14,023	18,393	18,866
Poverty rate	6.6	8.7	8.9
Percentage reduction[a]	-40.6	-22.1	-20.1
Money income plus food, housing, and medical care (including institutional care expenditures)			
Number of poor	13,634	17,318	18,866
Poverty rate	6.4	8.2	8.9
Percentage reduction[a]	-42.3	-26.7	-20.1

Source: Smeeding (1982a).

[a]Percentage reduction in the number of poor from the current poverty estimate based on money income alone.

poverty rate of about 8.5 percent in 1979, a reduction of 22.7 percent from the "official" money-income-only poverty rate of 11.1 percent, and very close to the theoretically preferred 8.7 percent obtained by the cash-equivalent approach. The rationale for these choices can be explained in a few paragraphs.

The recipient or cash-equivalent value of food stamps (and school lunch) subsidies is virtually identical to their market value. In other words, recipients spend at least as much on food (and school lunch) as these benefits afford. In particular, food stamps are virtually as good as cash. The face value of food stamps is already reported in the March Current Population Survey (CPS) and the market values of school lunch subsidies are easily calculated. There is no need to move on alternative valuation strategies in this case.

The recipient or cash-equivalent value of public housing subsidies averages 80 percent of their market value, and averages 60 percent of market value for the lowest income groups. Thus market value overstates the true welfare gain, as measured by the recipient value of housing subsidies, by a substantial amount. In calculating recipient value, good up-to-date information on housing expenditures among non-public housing low-income families is a necessity. The Census Bureau's Annual Housing Survey provides all of the data that is needed to update annually these estimates of recipient value with a reasonable degree of accuracy. The Census Bureau is developing an easily replicable methodology which will allow them to carry out this task. In the case of housing benefits, then, market value clearly overstates the true welfare gain of the poor, while a reasonably good estimate of recipient value is available and should be used.

Medical care is much more problematic. On average the recipient value of Medicare and Medicaid is only 47.3 percent of the market value. Clearly market value overstates true welfare gain in this case. However, calculating recipient value is problematic. In addition, the problem of whether or not to include institutional care expenditures in medical benefits remains.

Because of their enormous market value, the treatment of medical benefits is the crucial element in assessing the impact of in-kind benefits on poverty. Unless one assumes that medical benefits can be used to heat homes or to feed people, there is a distinct danger of overvaluation by assigning medical benefits at their market value, particularly for the elderly. For instance, at current (1983) market values for Medicare and Medicaid benefits, there would be virtually no poverty among the elderly at all, or in almost all the population of New York State, based on these benefits alone! While the recipient value estimates adjust for this problem and are therefore preferable to the market value approach, they are highly speculative. The poverty budget share approach, which limits the value of medical benefits to the amount needed to fulfill an estimated fraction of the overall poverty budget, seems to be the best choice.

Let me explain why. Viewed from a different perspective, the poverty line estimates the amount of a person's basic human needs. Certain amounts are implicitly budgeted for specific needs, e.g., food and medical care. If a person needs more medical care than is budgeted, there is a problem with the poverty line needs share for medical care. If a person needs more medical care than is budgeted, there is a problem with the poverty line needs share for medical care. Other basic needs are not met by excessive medical benefits. As such, the poverty share approach guards against the overvaluation problem and is free of the recipient value estimation vagaries. Moreover, the antipoverty effect of medical transfers under this approach is exactly the same whether or not institutional care benefits are included. Since the poverty budget shares have already been calculated, it is a simple procedure to implement this approach on an annual basis. In summary, in terms of accuracy in measurement, fairness, and efficiency in being able to rapidly calculate the impact of in-kind benefits on an annually updated basis, this combined strategy seems the most appropriate choice.

The Treatment of Taxes

The current poverty line is based on the ratio of food expenditures to after-tax income, but Census money income does not subtract out the taxes paid by families before determining their poverty status. If we interpret the poverty line as an expenditure needs standard, fairness and common sense demand such an adjustment. You can't buy the poverty budget with tax dollars. According to my estimates, subtracting federal income and payroll taxes would have decreased the income of many borderline poor families and thus would have increased the poverty rate by about 8 percent in 1979. Earlier estimates for 1972 and 1974 indicate increases in poverty of 6 to 7 percent.[1]

Moreover, the Economic Recovery and Tax Act (ERTA) of 1981 did not adjust personal exemptions or the standard deduction (zero bracket amount) to account for their erosion by inflation. Since these were the two major progressivity features which prevented most poor families from paying federal income taxes, their ignoral by ERTA, coupled with scheduled Social Security payroll tax increases, will magnify the poverty-increasing impact of personal taxes in the foreseeable future. This inconsistency will grow in importance over the next few years. Based on recent trends in poverty, I estimate that the impact of subtracting state and federal income and payroll taxes would increase the poverty count by at least 10 percent today.

While there are no recent (post-1979) estimates of the effect of income and payroll taxes on poverty to document my assertion, Tables 2 and 3 suggest the growing burden of federal income and payroll taxes on poverty families near the line.[2] In Table 2 we compare the income tax threshold (the level at which income taxes become positive, after netting out the EITC) to the poverty threshold for a four-person family. Before the EITC came into effect in 1975, the tax level was generally below but close to the poverty line. Low income families with earned income as their primary means of support were thus liable for small amounts of income taxes. All earnings were also subject to payroll tax liability, but payroll taxes were relatively low (about 5 percent in 1970). When the EITC came into effect (1975), the small positive income tax liabilities were more than made up for by EITC benefits. The income level at which taxes were due was 21.7 percent above the poverty level for families with children during 1975. In fact, because of EITC refundability, income taxes were actually negative at poverty-line income levels. However, as the 1970s progressed the difference between the income level at which income taxes were due and the poverty line decreased constantly. The last increase in personal exemptions and the zero bracket amount took place in 1979. Since 1980, the income level at which taxes are due has changed only slightly.[3] However, inflation has driven the poverty line

Table 2

Poverty Lines for Four-Person Families vs. the Income Tax Threshold for a Four-Person Family, 1970-1985

Year	Tax Threshold[a]	Poverty Line	Tax Threshold Minus Poverty Line	Tax Threshold as a Percentage of Poverty Line
1970	$3,750	$3,968	$ -218	94.5%
1975	4,900	5,500	1,192	121.7
1976	5,892	5,815	1,077	118.5
1978	7,533	6,662	871	113.1
1979	8,626	7,412	1,214	116.4
1980	8,626	8,414	212	102.5
1981	8,634	9,287	-653	93.0
1982	8,727	9,860	-1,133	88.5
1983	8,783	10,166[b]	-1,383	86.4
1984	8,783	10,613[c]	-1,830	82.8
1985	8,783	11,101[d]	-2,318	79.1

Sources: Joint Committee on Taxation, U.S. Congress; U.S. Bureau of the Census.

[a]Assumes all income in the form of earnings and accounts for the effect of the Earned Income Tax Credit (EITC) on federal income tax liability.
[b]Assumes an inflation rate of 3.1 percent for 1983.
[c]Assumes an inflation rate of 4.4 percent for 1984.
[d]Assumes an inflaiton rate of 4.6 percent for 1985.

Table 3

Income Tax Liabilities at Poverty-Line
Income Levels, 1979-1985

	Family Size	1979	1980	1981	1982	1983	1984	1985
1. Poverty level	2	$4,727	$5,363	$5,917	$6,280	$6,475	$6,760	$7,071
	4	7,412	8,414	9,787	9,860	10,166	10,613	11,101
	6	9,892	11,269	12,449	13,210	13,620	14,219	14,873
2. Income tax due	2	0	0	74	106	118	150	158
	4	4	144	263	285	318	365	383
	6	74	163	442	491	507	570	599
3. Payroll tax due	2	290	329	393	421	434	453	499
	4	454	516	618	661	681	711	783
	6	606	691	828	885	913	953	1,049
4. Combined taxes due	2	290	329	467	527	552	603	657
	4	458	660	881	946	999	1,076	1,166
	6	680	954	1,276	1,376	1,420	1,523	1,648
5. Combined tax as percentage of poverty level	2	6.1%	6.1%	7.9%	8.4%	8.5%	8.9%	9.3%
	4	6.2	7.8	9.5	9.6	9.8	10.1	10.5
	6	6.9	8.5	10.2	10.4	10.1	10.7	11.1

Sources: Joint Committee on Taxation; Social Security Administration, U.S. Department of Treasury; U.S. Bureau of the Census.

Note: The assumption is that all income from earnings for families of size 4 and 6 are eligible for the EITC. Same inflation estimates as Table 2.

increasingly higher, to the point where a family of four with poverty-line earnings this year, even counting the EITC, will have nearly $1400 of federally taxable income. Next year this amount will increase to $1830, and unless some changes are made, in 1985 the difference will be $2318.

Table 3 indicates the amount of income, payroll, and combined taxes that would be due for families of two, four, and six persons with earnings equal to the poverty line from 1979 through 1985. These figures bring out several important points. First of all, payroll taxes are a much heavier burden on low-income earners than are income taxes. Second, these tax burdens are not insubstantial. Even though state income taxes are ignored, a poverty-line family of four was liable for $946 in income and payroll taxes in 1982. Average food stamp benefits for working families at this income level last year were less than $900. Thus, for this family, the net effect of taxes and food stamps (the in-kind program which they are most likely to benefit from) was to reduce their net income by $46! Finally, we note that combined income and payroll tax rates are higher for larger families, and that they have steadily increased since 1979 for all family size groups. Clearly there are poor and near-poor people in America today who are eligible for significant amounts of tax; they can no longer be ignored.

Underreporting

The final major problem with current poverty estimates is their failure to deal with survey income underreporting. The report which I prepared for the Census Bureau did not adjust for this problem because the Census Bureau does not believe that a reasonable methodology for making such adjustments is currently available. The Bureau takes a very defensible position. Still, recent experience with the Current Population Survey (CPS), upon which poverty estimates are based, indicates that only about 90 percent of the money income amounts which should have been reported are actually reported each March. Similarly, in-kind benefit recipiency, and consequently in-kind income, is underreported as well. For instance, only about 87 percent of all Medicaid beneficiaries and only 77 percent of food stamp recipients reported coverage in 1980. Faced with this anomaly, it is fair to ask, Why won't the Census Bureau make any adjustment?

First of all, the issue of how to deal with money income underreporting is quite complex. While on average only $9 out of every $10 is reported, this figure differs considerably by income type. Wage and salary income is 98 percent perfect, while some reported tranfer and property income amounts are 75 percent or less of the benchmark amount. Once specific types of income, e.g., interest or AFDC benefits, are singled out, the problem of misreporting (i.e., reporting one type of income as another type) need also be considered. For instance, one recent study (Goudreau, Oberheu, and Vaughn, 1981) indicates that misreporting of AFDC as general assistance or child support is more prevalent than either underreporting dollar amounts of AFDC or failing to report AFDC altogether. Moreover, of those reporting AFDC in that study, only 70 percent reported the correct amount. Twenty-one percent underreported the correct amount by an average of 26 percent. Nine percent overreported the correct amount by an average of 37 percent. Merely "blowing up" reported amounts of AFDC to reach the aggregate benchmarket total totally ignores both of these problems. The state of the art in making such adjustments has not moved much beyond this level. Thus, the Census Bureau position. However, until underreporting adjustment methodologies are improved upon, one can get a rough idea of how much difference such changes might make by looking at the results of the several research efforts which adjust for cash and non-cash underreporting and misreporting using various methodologies (including at least one study which directly matched tax and Social Security administrative records to reported survey income amounts). These studies indicate a net reduction in poverty ranging from 14 to 26 percent from such adjustments.[4] Until better estimates are developed I would guess that a 20 percent reduction in reporting error in the poverty estimates presented in Table 1 not be too far off the mark.

RECENT CHANGES IN POVERTY

When I prepared the Census report to Congress, the official poverty rate for 1979 was 11.7 percent.[5] Since then it has risen steadily to 13.0 percent (1980), 14.0 percent (1981), and finally to 15.0 percent last year. Some of this poverty increase was due to the growing problem of poor persons living in younger, female-headed families, the so-called feminization of poverty, yet as a group they declined from 36.8 percent of the poor in 1979 to 34.0 percent in 1982 (U.S. Bureau of the Census, 1983b). As officially measured, poverty among the elderly is still a problem, though less pressing than earlier believed. In 1979, 14.1 percent of the poor were over 65, while today 10.9 percent of the poor are elderly.

I single these two groups out because they are the groups whose poverty status is most affected by in-kind transfers (especially medical care benefits), least affected by income and payroll taxes (because most of their income is from transfer payments), and most affected by income underreporting (because the types of income they receive are most subject to underreporting). Because of large in-kind and underreporting adjustments (which tend to lower poverty) and a small tax effect (which tends to increase poverty), these are precisely the groups whose poverty status would undergo the greatest downward change were these adjustments made. Yet they have shrunk from 50.9 percent of the poor in 1979 to 44.9 percent in 1982. Who has taken their place?

I would argue that the major increases in poverty experienced during the past four years have been among persons, adults but especially children, living in traditional husband-wife families. In 1979 these persons constituted about 34 percent of the poor, while today they constitute almost 40 percent of the poor. From 1981 to 1982 alone, over half of the increase in poor persons included husbands, wives, or related children under 18 living in traditional husband-wife families. Sixty percent of the increase in poor families last year was made up of husband-wife families.

I single this group out for precisely the <u>opposite</u> reason. These families are least likely to be affected by in-kind benefits (because of ineligibility or low benefit amounts), most likely to pay taxes, and least likely to be affected by underreporting (both being due to the heavy reliance on heavily taxed but also well-reported earned income in these families).

For instance, in 1982 42.7 percent of all poor households had at least one member who received food stamp benefits, 23.0 percent lived in public housing, and 39.2 percent benefited from Medicaid (U.S. Bureau of the Census, 1983c). In contrast, only 36.2 percent of poor husband-wife families got food stamps, only 6.3 percent lived in public housing, and only 27.0 percent were eligible for Medicaid benefits. The point is that the increasing numbers of poor families of this type are least likely to be reduced by adjusting for in-kind income and reporting, but most likely to be increased by adjusting for taxes. Thus I would not expect much of a reduction in poverty for these families once the adjustments are made.

Moreover it is just this group of low earners and their children who have been most adversely affected by the Reagan administration's taxation and social policies. These individuals are increasingly becoming poor because of recession-induced job loss and subsequent declines in earned income; because less than 40 percent of the unemployed are covered by unemployment insurance today (as compared to over 75 percent during the 1975 recession); because the 1981 ERTA did not provide them with much, if any, overall direct tax relief (but as seen above large effective tax increases); and finally, because cutbacks in Food Stamps and other social programs have most affected precisely these low earnings people.

If you are wondering who it is that is falling through the Reagan safety net, these are the truly needy. You ought to spend some time in my old neighborhood in South Buffalo, New York, where major permanent shutdowns in the steel and other heavy industry have utterly decimated the income base of the neighborhood. Once proud union steelworkers are delivering 100 newspapers a day to feed the children and save the house.

A SUMMING UP

It remains to put these pieces of information together to attempt to update the net impact of in-kind benefits, taxes, and income underreporting on the recent increase in poverty from the most recent (1979) estimates. I should emphasize that these 1982 estimates have not been constructed on a microdata basis. All of the figures in Table 4 other than those for 1982 are based on sophisticated income microdata modeling and imputation procedures. As I understand it, the Census Bureau is making an effort to update my report on in-kind benefits to 1982.[6] But even then the net effects of income underreporting and taxes will not be known.

Table 4 indicates that poverty in the U.S. is on the rise even after adjustments for in-kind benefits, underreporting, and taxes are carried out. I expect that the Census update of my report will show an increase from about 8.7 percent to the 10-10.5 percent range, adjusting only for in-kind benefits (measured at their cash equivalent value) and ignoring taxes and reporting problems, as was the case with my earlier report. Recent cutbacks in in-kind transfer income support systems and growing numbers of poor husband-wife families who benefit least from such programs explain this increase.

In 1979, once adjustments for taxes and income underreporting were made as well, poverty fell to about 6.1 percent. However, I estimate that taxes had a larger poverty-increasing effect in 1982 than in 1979. Thus, assuming that underreporting had as substantial an effect in reducing poverty in 1982 as in earlier studies, we still end up with a

Table 4

Percentage of Persons with Incomes below the Poverty Line; 1965-1982

Year	Official Census Money Income[a]	Adjusted Income: In-Kind Only[b]	Adjusted Income: Taxes, Underreporting, and In-Kind[c]
1965	17.3	--	12.1
1968	12.8	--	9.9
1970	12.6	--	9.3
1972	11.9	--	6.2
1974	11.2	--	7.2
1976	11.8	--	6.7
1979	11.6	8.7	6.1
1982	15.0	10.0 - 10.5	8.5 - 9.0

Sources: Unless otherwise noted, tabulated from the Survey of Economic Opportunity (for 1965) and various March Current Population Survey Data Tapes.

[a]From various issues of the Current Population Reports, P-60 series.

[b]Census money income adjusted by adding food, medical, and housing in-kind transfers at their cash-equivalent value. See Smeeding (1982a) and Table 1 above.

[c]Census money income adjusted for underreporting, in-kind public transfers added at their cash-equivalent value and federal payroll and income taxes subtracted. The data for 1965-1979 are as in Smeeding (1982b).

poverty rate of somewhere around 8.5-9.0 percent after all adjustments have been made.

Such a figure has far-reaching policy implications. It says that the administration statements are correct in that in-kind benefits reduce poverty below the official figures. This was obvious all along. But what the administration didn't tell us was that (a) an 8.5 to 9.0 percent poverty rate means over 20 million poor and needy Americans, even after counting these benefits; (b) that the income and payroll tax burden on the working poor is both substantial and growing at a rapid rate; and (c) that the poverty rate including in-kind benefits, taxes, and reporting adjustments is now higher than any year since 1970 and is increasing at an even faster rate than is the official poverty population. In case you ever had a doubt, America still has a serious poverty problem and, all the in-kind benefit rhetoric aside, that problem is growing very rapidly.

Notes

[1]See Smeeding (1975) and Plotnick and Smeeding (1979). A recent Census report (U.S. Bureau of the Census, 1983a) indicates an increase in poverty of 1.2 percent among households in 1980 accounting for income taxes and the Earned Income Tax Credit only. Payroll taxes, which are quite a bit larger at poverty-line income levels than are income taxes, were not counted. No later or more complete estimates of the effect of taxation on poverty currently exist.

[2]State income taxes are not included in these calculations.

[3]These changes are due to the effect of slightly lower income tax rates and their interaction with the EITC.

[4]See Hoagland (1980), Smeeding (1975), Plotnick and Smeeding (1979), Budd and Radner (1975), and Paglin (1979).

[5]This rate differs from the 11.1 percent reported in Table 1 owing to changes in population weights from the 1980 Census which were not available when writing the report to Congress, and other minor technical differences.

[6]This may take an act of Congress, but instead of speculating about the impact of in-kind benefits on poverty, it would be nice if the federal government could move towards providing estimates of the effect of in-kind transfers on poverty on an annual basis.

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