Is a golden age in poverty policy right around the corner?

by Eugene Smolensky

Eugene Smolensky, professor of economics at the University of Wisconsin and Institute affiliate, served as director of the Institute from July 1980 to July 1983. He delivered this address at the Fourth National Conference on Research, Demonstration and Evaluation in Public Social Services, sponsored by the National Council of State Public Welfare Administrators of the American Public Welfare Association, November 9, 1984, in Washington, D.C.

A lot of people interested in the well-being of the poor are discouraged just now. In the presence of the massive budget deficit we expect to see further cuts in antipoverty programs.

I have my own private reason for being especially discouraged. This is the twentieth anniversary of my first paper on poverty in the United States. The argument of that paper was that poverty is a relative concept, which implies that reducing poverty over the long term requires changing the distribution of income, but that we simply don't know how to do that. There was one sustained reduction in income inequality in the United States in the period for which we have reliable data. That came abruptly, when the economy was in the heated, over-full employment of the Second World War, and we certainly did not expect to see levels of employment like that in peacetime. The record since, of course, bears my expectations out. Measures of poverty which define poverty as a proportion of average income show no significant sustained decline in the incidence of poverty at any time during the past four decades. But it's worse than that. At the time that speech was published, by the fixed absolute measure of poverty that is the official standard, poverty stood at 15.7 percent. The most recent official number is 15.2 for 1983, although the 1984 rate will probably be a little below that. Twenty years ago, I thought that a fixed measure of poverty was a copout. Any economy would look good against such a measure, I thought. How wrong I was.

A person could be discouraged. I am not discouraged. Indeed, I am quite optimistic. Two kinds of data make me optimistic. First, we have been successful before. There was a golden age of poverty reduction in this country. It occurred during the Johnson-Nixon years—from 1965 to 1974—when poverty as officially measured fell from 17.3 to 11.6 percent. Taking account of in-kind transfers would have taken the poverty rate down to close to 7 percent in 1974. What Nixon hath wrought so can Reagan, and without a war. Reagan has something Johnson and Nixon did not have—extraordinarily good luck.

The second body of data that makes me optimistic is the research now under way at the Institute for Research on Poverty. Let me now turn to each of these—the lessons from the golden age and of current research—starting with the work of the Institute.

One of our major research efforts during the past year has been to quantify the impact of Reagan administration policies on the poor. That analysis has had to separate the effects of mandated changes in tax and transfer programs from changes in unemployment—all of this with at most three years' data. We simulated the effects of changes in unemployment on the joint distribution of market and transfer income to obtain the effects of changes in the macroeconomy on the incidence of poverty. The programmatic changes made by Reagan were treated as a one-time change in each of the moments of the distribution, by relying on dummy variables.[1]

The incidence of poverty began to rise during the 1979 recession, more than a year before Reagan took office. When the first tax and budget cuts went into effect in 1981, the economy was two years into a severe recession during which the average income-to-needs ratio fell 8 percent. In addition, transfer growth has been slow for almost a decade. We nevertheless think that we have been able to decompose the 2.2 percentage point official increase in poverty between 1980 and 1983 into components due to changing unemployment rates, to a secular trend, and to the noncyclical nonsecular changes attributable to the Reagan program. Our model attributes about 40 percent of the recent increase in poverty to the Reagan tax and budget programs. (We also find that, *ceteris paribus,* Reagan's program raised mean market incomes by about 2.3 percent. Just as the president's supporters predicted, both average income and inequality increased.)

The key point for us today is that sustained prosperity will take us to a poverty rate only one percentage point higher than would have been the case in the absence of the Reagan cuts. While one percentage point is hardly a negligible amount—about 2.5 million people—it is not so large that it cannot be overcome.

One way it's going to be overcome is the focus of a second major research effort at the Institute. We are engaged in a practical effort to restructure the nation's approach to child support.

Everyone knows the facts. Twenty percent of children live apart from one parent. Half of all children in single-parent families are impoverished. If current trends continue, a quarter of American children will experience poverty before age 18. But only 59 percent of eligible women now receive child-support awards from the courts. Nearly 90 percent of unmarried women, and half of those who are separated, receive no award. Even of divorced women, 20 percent fail to get a support award. Furthermore, an award is hardly good enough. Of all children awarded support in 1978, only 49 percent received the full amount due them, and 28 percent received nothing. Consequently, half of all welfare expenditures are devoted to families potentially eligible for child support from an absent parent.

These grim statistics have led Irwin Garfinkel to champion what he calls a "Child Support Assurance Program."[2] If he has his way, all parents who live apart from their children will be liable for a child support tax, expressed as a percentage of gross income per child. Children with a living absent parent would get an amount equal to that paid by the absent parent. If the payment fell below some minimum amount, it would be supplemented out of general revenues. Under this plan, AFDC would be returned to the role envisaged for it in the 1935 Social Security Act—a support system for a few destitute widows, abandoned women, and women who cannot or will not identify the fathers of their children. Under any of several specific plans, budgetary costs for AFDC would decline sharply, and total budgetary costs would decline modestly. Many children would be taken out of poverty; their mothers would not be on welfare and would have increased incentives to work.

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The Child Support Assurance Program is not merely a paper program. A demonstration is in the field in Wisconsin in ten counties, testing the workability of two of the three main planks of the program. Wages are being garnisheed and sent to the clerk of courts according to a standard schedule (17 percent of gross income for the first child and up to 33 percent for three or more children). The minimum benefit provision may be tested at a later date. While these demonstrations have no effect on women now on AFDC, a waiver to permit us to extend the demonstration to AFDC recipients was passed by the last session of Congress.

Getting fathers to support their children and thereby reducing the AFDC rolls would permit us to turn away from relying on transfers and toward the private market. Here too research from the Institute is relevant and encouraging.

The Supported Work Demonstration, in which the Institute played a key part, subjected a study sample of 6616 individuals, half participants and half controls, to intense evaluation. Of the four target groups (long-term AFDC recipients, former drug addicts, former criminal offenders, and delinquent youth) the excess of benefits over costs was by far the highest for AFDC women ($8000). In the 25th to 27th month of observation, long after the period during which the experimental groups held guaranteed jobs, the employment of experimentals was 20 percent above that of controls, hours worked were 35 percent higher, and earnings were almost 50 percent higher.[3] The gains were particularly large for middle-aged women (aged 36 to 44 at the outset of the demonstration). Only one-third of these women were high school graduates. Fourteen percent had never worked, and 61 percent had not held a full-time job during the preceding two years. Many of these women lost their food stamp and Medicaid benefits along with AFDC, so that only 50 percent of their earnings represented an increase in real income. Clearly, despite substantial disincentives, female heads of households will work if given the opportunity.

Our studies of the effects of the Reagan program on the poor provide further evidence in support of the eagerness of AFDC women to work, if such evidence is required. We followed about 1000 Wisconsin women whose benefits were reduced or terminated under the Omnibus Budget Reconciliation Act (OBRA) of 1981.[4] We found that on average women worked about as much as before, despite the fact that those still on AFDC now faced a 100 percent tax rate. Some women worked less, but others worked more. There was some small reduction in hours worked, but that may have been due to the recession. We observed a large increase in wage rates, which we are at a loss to explain. The net result of the OBRA cuts was that work effort was maintained, welfare dependency declined, but on average total real money income of the household fell by 7 percent. That this average masks considerable diversity can be seen by the fact that the poverty rate among AFDC women working before OBRA more than doubled.[5]

Since the administration of welfare in Wisconsin is highly automated, we were able to study women who were not working as well as those who were. We found that the probability of going from no work to some work was also unaffected by OBRA. Two-thirds of the women not working at a point in time were still not working in the subsequent year both before and after the restructuring of AFDC benefit levels.[6]

It seems clear to me, then, that a labor-short economy and a restructured child support system, when combined with the determination of older AFDC women to work if carefully guided into the labor force, promises a dramatic decline in poverty and in welfare. Which takes us to the fabled luck of Ronald Reagan. It seems extremely plausible to me that apart from the cyclical downturn looming in a year or so, the prospects for a very tight labor market are quite bright. As we roar past the mid-term election toward the presidential elections of 1988, unemployment may be as low as it has been in the postwar period. If that is the case, we will have an unusual opportunity to move many of the poor into the labor market while raising benefit levels for those unable to take advantage of even these especially propitious circumstances.

My rosy projection rests not so much on Reagan's supply-side miracle as the long demographic cycle, more specifically Richard Easterlin's "relative-cohort size" thesis.[7]

The ratio of young adults (under 29) to older adults (30–64) is falling now and will continue to fall until at least the mid-1990s. This means that the number of jobs that must be added each year to achieve full employment will be falling since, of course, young workers are new workers. Similarly the capital stock can grow more slowly while still raising the capital-to-labor ratio and productivity per worker. Thus the wages of the young will grow relatively rapidly, and if past history is a guide, the gap between young and old workers, which has been widening since the mid-1950s, will close.

Most important, the smaller cohorts will feel reduced competitive pressures; they will have a better psychological outlook; there will be fewer incentives for women to work outside the home and fewer marital strains. Now the birthrate will rise too, but, all in all, the rate of change in demographic events affecting families is going to be considerably slower in the next decade than it was during the past two decades. The more rapid rise in income and the less rapid rate of demographic change due to these "relative cohort size effects" should lessen the welfare caseload. A smaller caseload and a tight labor market open up exciting opportunities for progress against poverty. The stage is set for Reagan and his immediate successor to provide us with a second golden age of poverty reduction. And we don't need a war to do it.

It is often said that people make their own luck, and somehow it does seem appropriate to each of their public personalities that Jimmy Carter should have presided at a time when the labor force was growing at a record rate while Reagan reigns during a steep decline in labor force growth. But neither Carter nor Reagan determined that the baby boom should peak in 1957 and that hence the rate of growth of the labor force should peak in 1977 and 1978. Carter put more people to work in the years 1977 and 1978 than Reagan did during the whole of his first term.

During that peak year of 1977, President Carter proposed his Program for Better Jobs and Income (PBJI). That proposal embodied most of the items on the welfare reform agenda: welfare reform was combined with job creation, an earnings supplement was integrated with income-conditioned cash assistance and extended to individuals and intact families, a uniform national benefit structure was established which raised benefits in the lowest-paying states, a work requirement as a condition of receiving benefits was imposed, and the administration of several existing income-conditioned programs was consolidated. Like many of Carter's proposals, it was technically complex, bold, embodied the best parts off the research shelf, and was doomed to legislative failure.

The program undoubtedly died in the Congress for a variety of reasons—not the least of which was the $8.8 billion job-creation component. The nation would have had to embark on the mass creation of public service jobs for low-wage, low-skill workers, a task for which the country had no previous experience. At that time, the number of jobs that would have to have been created was massive, even though those jobs were meant only for those unable to find a job on their own. Finding a job in 1977 and 1978 meant competing with nearly 8 million new job seekers. In 1987-88 there will be half as many new entrants into the job market. A very modest job-creation program will do, and we have the Supported Work model to guide us. It may be time to return to the principles that underlay PBJI—a work bonus system that ensures that anyone at work is substantially better off than anyone who does not work: high benefit levels and high benefit reduction rates for those not expected to work, and low basic benefit levels and low benefit reduction rates for those expected to work, and a raised income threshold before becoming liable under the regular income tax.

As for the future, I envisage a tight labor market and some budget slack two years down the road. Poverty will stand at 7 or 8 percent when in-kind benefits are included, as compared to 10 percent now. In that environment I would hope that many local programs will be in place to shift the burden of children onto their fathers. For women remaining on AFDC, especially older women, there will be job placement under "graduated stress" (work discipline), as pioneered in the Supported Work demonstrations. The success of these women, and the decline in their numbers along with the budgetary slack, feeds a rise in benefit levels for those unable to work. Between 1965 and 1972, that golden age, Old Age Insurance benefits were increased five times, by 7, 13, 15, 10, and 20 percent. In the process, poverty for the aged

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was virtually eliminated. We did that, at least in part, out of love for the elderly. Can we love women heading households? Probably not—but we will like them better when there are fewer of them, and when more of them work.

But wait, I hear you cry. What about the deficit? Don't we have to keep our pockets zipped to bring down the deficit? There are two answers to that. First, while it is true that the federal government will need $100 billion in taxes or spending cuts precisely at the time when I envisage budgets being slack, I expect that to be in the bag by that day next summer when the Congress adjourns. We can expect a lot of talk about restructuring taxes during the next few months, but the breakthrough will probably be something simple like a national sales tax dressed up as a value-added tax, plus, perhaps, fewer brackets in the personal income tax.

More important, the states are not in deficit now, and they will have even larger surpluses (following a lean year) a few years down the road. The action in welfare is not going to be in Washington. Quietly, in the beneficent shadow of benign neglect, change will emanate from the statehouses.

In 1988 a new era can open—one in which, having licked poverty through transfers, we can keep it licked through jobs. At long last we can achieve President Johnson's original objective of eliminating poverty through a hand up rather than a handout. The window of opportunity is narrow, the birthrate is already on the rise. We need to get to work now. ◖

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[1]Sheldon Danziger, Peter Gottschalk, and Eugene Smolensky, "The Effects of Unemployment and Policy Changes on America's Poor," *Journal of Social Policy*, in press. Also available as IRP Discussion Paper no. 770-84, 1985.

[2]Irwin Garfinkel and Elizabeth Uhr, "A New Approach to Child Support," IRP Reprint no. 488, 1984.

[3]The results of Supported Work are reported in Robinson G. Hollister, Jr., Peter Kemper, and Rebecca A. Maynard, eds., *The National Supported Work Demonstration* (Madison: University of Wisconsin Press, 1984).

[4]See "Measuring the Effects of the Reagan Welfare Changes on the Work Effort and Well-Being of Single Parents," in this issue of *Focus*.

[5]Steven Cole, Sandra Danziger, Sheldon Danziger, and Irving Piliavin, "Poverty and Welfare Recipiency after OBRA: Some Preliminary Evidence from Wisconsin," IRP mimeo, October 1983, p. 23.

[6]Dan Feaster, Peter Gottschalk and George Jakubson, "Impact of OBRA on AFDC Recipients in Wisconsin," discussed in "Measuring the Effects," this issue.

[7]*Birth and Fortune: The Impact of Numbers on Personal Welfare* (New York: Basic Books, 1980).

Center for research and retrieval of data from the SIPP and ISDP

In September 1984 the Census Bureau released the first report from its new Survey of Income and Program Participation (SIPP).[1] The SIPP is the most important source of data on the poor since data collection from social experiments began almost twenty years ago. According to the Census Bureau it will

> provide a better understanding of the level and changes in the level of well-being of the population and of how economic situations are related to demographic and social characteristics of individuals. The data collected in SIPP will be especially useful in studying federal transfer programs, estimating program cost and effectiveness, and assessing the effect of proposed changes in program regulations and benefit levels. Analysis of other important national issues, such as tax reform, social security program costs, and national health insurance can be expanded and refined, based on the information from this new survey.[2]

The novelty of the new data series lies in its continuous monitoring of events in the lives of individuals, such as marriage, divorce, and job loss, and relating them to detailed sources of income, including government transfers.

For a history of the SIPP and its pilot, the Income Survey Development Program (ISDP),[3] see the accompanying box.

With funding from the National Science Foundation, Martin David and Alice Robbin are establishing a Research Clearinghouse and Data Center at the Institute for Research on Poverty to provide access to the new data series to interested users throughout the country. This center will carry out four major services:

- It will integrate data and documentation through an information management system.
- It will provide access to the data through a nationwide dial-in system.
- It will furnish instruction and workshops for new users of the system.
- It will develop solutions to problems related to the analysis of data.