Session 4: The labor market and poverty

The poor have good reason to fear the recessions that lie ahead.

Rebecca Blank and Alan Blinder

These findings suggest that employment and training programs have been neither an overwhelming success nor a complete failure.

Laurie Bassi and Orley Ashenfelter

Reductions in work effort in response to increased income transfers and the failure of those transfers to promote self-sufficiency have prompted renewed interest in employment as an antipoverty strategy. The two papers presented at this session together summarized much of what is now known concerning the effects that economic fluctuations exert on the poor, and why two decades of government employment and training programs seem to have had little effect in reducing pretransfer poverty.

Which is the cruelest tax?

Blank and Blinder investigated the relative effects of inflation, unemployment, and taxation on the status of the poor. Some have claimed that inflation is the "cruelest tax" because it more severely victimizes the poor, whereas others assert that high unemployment rates serve to bring down inflation but force the poor to bear a disproportionate share of joblessness. And while inflation and unemployment continue to fluctuate, our national tax structure has moved toward greater regressivity.

Examination of the relationship between the poverty rate and economic performance clearly shows that when the economy is recovering from a recession, and mean incomes consequently rise, poverty declines; and vice versa. During cyclical upturns, income inequality generally diminishes; the reverse is true during downturns. The poor lose more than the rich in a recession and gain more during upturns.

The business cycle and the poor

The authors' regression analyses identified the effect of unemployment as a much more serious problem than the effect of inflation on low-income households: when unemployment rises by 1 percentage point, the poverty count goes up 1.1 points; yet when inflation rises by 1 percentage point, poverty increases only 0.15 points. Inflation does, however, hurt the wealthy, because it reduces the value of property income as well as of stocks and bonds—forms of wealth more prevalent in the upper reaches of the income distribution than in the lower ones. The rich more than the poor have reason for branding inflation a cruel tax.

More detailed analysis of the relationship between inflation and the incomes of the poor reinforced the conclusion that inflation does not inflict special hardship on that group. The relative earnings of low-wage workers have not fallen with inflation, and most of the larger transfer programs, with the major exception of Aid to Families with Dependent Children, have been indexed to keep pace with the cost of living.

The business cycle is not neutral in spreading the burden of unemployment. The authors demonstrated that minority men suffer larger increases in unemployment than any other group when unemployment rises. Younger workers are also severely affected, but women and older workers are not as sensitive to changes in unemployment levels, probably because they have available other forms of income, such as transfers and the earnings of other family members.

We expect unemployment insurance (UI) to protect workers from the vicissitudes of the economy, yet its benefits are less likely to accrue to low-wage jobholders, who often have an unstable work history. New entrants and reentrants into the job market are not eligible for UI; others do not draw benefits because they quit in anticipation of being fired or remain unemployed after benefits expire. And in any case, recent program changes have reduced the coverage of UI. The proportion of unemployed workers receiving its benefits reached a high of 78 percent in the 1975 recession, but registered only 43 percent in the recession of 1982.

Taxes and the poor

Blank and Blinder explored the changing structure of taxation at the federal, state, and local levels since 1950, and concluded that "where the poor are concerned, the main 'event' in postwar tax history seems to have been the rapid and continuing growth of the payroll tax" (pp. 39–40). As Table 4 shows, in 1955 a family of four with income at the poverty line, filing jointly and claiming the standard deduction, paid 4.9 percent of earned income in federal payroll plus income tax; by 1983 that rate had risen to 16.5 percent, despite enactment of personal income tax cuts under the first Reagan administration. The rise in state and local sales and property taxes has also taken a large bite out of the incomes of the poor.

Effects on inequality

The authors concluded by estimating the influence of the business cycle on poverty rates and income inequality over the decade 1973–83, comparing what would have happened if inflation and unemployment had remained at their 1973 levels with what actually occurred. The results showed that substandard economic performance over those years—particularly unemployment—raised the poverty rate by 4.5 points and reduced the income share of those in the lowest

Table 4

Average Federal Tax Rates on Earned Income

Income Level	1955	1965	1975	1980	1983
At 5,000 1983 dollars					
Personal income[a]	0.0	0.0	−10.0%	−10.0%	−10.0%
Personal income plus payroll	4.5%	7.3%	1.7	2.3	3.4
At poverty line					
Personal income[a]	0.4[b]	2.2	−0.9	−0.7	3.1
Personal income plus payroll	4.9[b]	9.4	10.8	11.6	16.5
At one-half median income					
Personal income[a]	0.0	2.9	3.9	4.3	4.9
Personal income plus payroll	4.5	10.2	15.6	16.6	18.3

Source: Rebecca M. Blank and Alan S. Blinder, "Macroeconomics, Income Distribution, and Poverty," Institute for Research on Poverty, Conference Paper, revised February 1985, Table 12.

[a]For a family of four filing jointly and claiming the standard deduction.
[b]A 1955 "poverty line" was constructed by adjusting the 1959 poverty line for the change in the consumer price index.

fifth of the income distribution by almost 1 percentage point. Both are major effects, as illustrated by the fact that in the entire postwar period the share of the lowest fifth fluctuated only from a high of 5.6 percent (1968) to a low of 4.7 percent (1983), a total change of 0.9, compared to the 0.8 percent drop since 1973.

This paper gave discouraging evidence on the role of government in cushioning the effect of recent economic downturns on those at the low end of the income distribution. Over the last twenty years the government has run employment and training programs that were designed, at least in part, to offset the effects of cyclical unemployment. These programs have waxed and waned, reaching a peak in terms of funding in the late 1970s and then ebbing to the relatively modest effort of the Job Training Partnership Act in the early 1980s. The next paper dealt with the effectiveness of those programs.

Does providing employment and training make a difference?

Laurie Bassi and Orley Ashenfelter reviewed several studies that have attempted to evaluate the effect of employment and training programs on subsequent employment rates and earnings levels of participants. Such studies have been severely hampered by the difficulty of constructing appropriate comparison groups and by the varying estimation strategies utilized in the absence of controlled experimental data. These problems have been reduced to some extent by data bases that have recently become available. Analysts are now enjoying expanded ability to construct comparison groups of various types and to apply new estimation techniques.[1]

Positives and negatives

Some consistent findings have emerged across different studies. First and perhaps foremost, women have benefited more than men in terms of increased earnings gained from program participation. In fact, the programs grouped under the Comprehensive Employment and Training Act (CETA) of the 1970s, which provided both jobs and training, seem to have produced no significant earnings gain for men at all. The main reason for the more favorable results for women seems to be that employment and training programs raise earnings chiefly by means of more hours of work rather than higher wages per hour. Since women in the past generally have worked fewer hours than men, when they extend their work time they show a marked increase in earnings relative to their male counterparts.

Individuals who benefited most from CETA often were those who had the least prior work experience. This finding suggests that the program was good at preparing candidates for entry-level positions, benefiting women and young men but not necessarily older men, who needed to improve their occupational position, not enter it. For example, one study showed that the only male group to experience substantial postprogram employment and earnings gains consisted of young men.[2]

Another consistent finding from CETA studies is that work experience programs, reserved for the most disadvantaged and consisting mainly of acclimation to the "world of work"—showing up on time, dressing appropriately, etc.—instead of specific training or specialized job experience, was the least effective method of improving employment prospects and earnings.

The severity of employment problems among youth—especially among blacks—has directed attention to the programs designed specifically for them, notably the Job Corps, which has been continuously in operation since 1965. Studies of it have found strong effects in increased employment and earnings, reduced welfare dependence, lower unemployment and criminal activity, and fewer out-of-wedlock births. Emerging results from the Youth Employment and Demonstration Act of 1977 also indicate the benefits of some interventions for youth.

A strategy that involves the private sector is the Targeted Jobs Tax Credit, which offers companies a tax break for employing certain disadvantaged workers. But the program has been little used. A recent experiment in Dayton, Ohio, provided some welfare recipients with vouchers that explained their potential employers' eligibility for a tax credit—or, in a variant to test whether fear of a tax audit was the deterrent, a cash payment. The results showed that vouchered workers, offering either a tax credit or a cash payment, evidently were not considered good prospects for employment, and their welfare identification constituted a form of stigma.

Costs and benefits

Even at their height, employment and training programs did not cover a very large number of disadvantaged workers. Those who did participate received fairly intensive treatment, yet even so, the programs seem to have made little dent in the problems of unemployment and poverty among those able to work. That being the case, do they represent a worthwhile investment?

Though it is difficult to generate reliable cost-benefit ratios, that performed for the Job Corps is among the most thorough. Expensive as it is, the Corps seems almost to pay for itself, returning 96 cents on every taxpayer's dollar invested, if returns are defined as output during program participation, increased tax payments on postprogram income, reduced transfer payments, less criminal activity, and reduced use of other federally provided services. For the more traditional and less comprehensive types of programs, such as those under CETA, the evidence suggests that training programs are a more cost-effective method of raising participants' earning power than are employment programs.

In sum, there is no simple solution to the problems of the hard-to-employ, and with some exceptions the level of attention and resources devoted to a program has never been more than modest in relation to the size of the target population.

Discussion of labor market factors

In his comments, Peter Gottschalk focused on the role of macroeconomic events in reducing poverty. He argued that care should be exercised in interpreting the results presented by Blank and Blinder. The authors emphasized that their study showed only that improved cyclical conditions reduced poverty; those results should not be extrapolated to the effect of general economic growth on poverty, since secular growth can be accompanied by increasing income inequality—as happened in America during the nineteenth century, whereas the reverse was true in the first half of the twentieth century. Gottschalk pointed out that it is the particular source of long-term economic growth that is crucial. For example, a rise in the demand for capital that raises the demand for high-skilled labor more than for low-skilled workers may not benefit the poor unless other factors are strong enough to offset those shifts in demand.

Responding to the paper by Blank and Blinder, Joseph Antos made the point that their use of aggregate data masked the differential effects of unemployment and inflation among various groups of the poor. Female-headed families and the elderly are less affected by the business cycle than are other members of the poverty population, since they have weaker attachments to the labor market. On the other hand, the elderly are relatively insulated from inflationary effects because social security benefits are indexed, whereas inflation has substantially reduced the living standard of single mothers on welfare by diminishing the real value of their unindexed benefits. Since inflation and unemployment affect different groups of the poor in different ways, Antos argued that it is misleading to identify unemployment as the "cruelest tax."

Antos stressed the need to evaluate employment and training programs not simply in terms of participants' later earnings, but by asking what that outcome costs the taxpayer. Does the benefit outweigh the cost? And is there a more cost-effective way of achieving the same ends? Moreover, some evaluations are still seriously flawed by selection bias and inadequate control groups. It is imperative, he felt, to include in any future programs an integral evaluative mechanism.■

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[1]Among the studies summarized were Westat, Inc., "The Net Earnings Impact of the Public Employment Program (PEP)," report prepared for the Office of Program Evaluation, Rockville, Md., 1979; Laurie Bassi, "The Effect of CETA on the Postprogram Earnings of Participants," *Journal of Human Resources*, *18* (1983), 539–56; Bassi, L. Burbridge, M. Simms, and C. Betsey, "Measuring the Effect of CETA on Youth and the Disadvantaged," Final Report, The Urban Institute, Washington, D.C., 1984; Charles Mallar, S. Kerachsky, Craig Thornton, M. Donihue, T. Jones, D. Long, E. Noggoh, and J. Shore, "The Lasting Impact of Job Corps Participation," Final Report, Mathematica Policy Research, Inc., Princeton, N.J., 1980; and Robert Taggart, *A Fisherman's Guide: An Assessment of Training and Remediation Strategies* (Kalamazoo, Mich.: Upjohn Institute for Employment Research, 1981).

[2]T. Fraker, R. Maynard, and Z. Nelson, "An Assessment of Alternative Comparison Group Methodologies for Evaluating Employment and Training Programs," Final Report, Mathematica Policy Research Inc., Princeton, N.J.