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POVERTY: TRENDS, CAUSES AND CURES

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## ABSTRACT

The number of people in poverty in the United States rose to 15 percent of the population in 1982, following 10 years of decline and 10 years of relative stability.

This report summarizes the trends in poverty during the last 24 years; examines reasons for the changes in rates of poverty; analyzes measures used to calculate the number of poor Americans; and presents several proposals to reduce the rate of poverty in the United States.



CONTENTS

ABSTRACT .....	iii
I. INTRODUCTION .....	1
II. HOW POVERTY IS MEASURED .....	3
III. CAUSES FOR LEVELS AND TRENDS IN POVERTY .....	11
IV. PROPOSALS TO REDUCE POVERTY .....	17



## POVERTY: TRENDS, CAUSES AND CURES\*

### I. INTRODUCTION

After a decade of steady decline followed by another decade of relative stability, the share of people in poverty in the United States began a sharp rise in 1978, which continued through 1982 and now equals 15 percent of the population--the highest level since 1965. In 1982 the poverty rate stood about one-third higher than when it began to rise. The number of individuals in poverty increased by 9.9 million during those 4 years.

The poverty rate at a given time reflects economic opportunities, Federal and State government income transfer programs, and demographic conditions. Complex interactions among these factors account for the progress against poverty in the 1959-1969 period, the plateau from 1970 to 1978, and the ground lost from 1979 to 1982.

This report summarizes trends in poverty during the past 24 years. It examines reasons for changes in the rate of poverty and discusses demographic characteristics of the poverty population. Further, the report analyzes the methods used to calculate the number of poor Americans. The measure itself is controversial. One critic contends that, no matter how measured, poverty

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\*A slightly different version of this report appeared as the Executive Summary of a Committee Print, issued by the House Ways and Means Committee, entitled, "Background Material on Poverty" (WMCP: 98-15, Oct. 17, 1983).

has been rising over the past three years. Some critics claim that the measuring technique overstates, and some that it understates, the nature and extent of the poverty problem.



## II. HOW POVERTY IS MEASURED

When the Federal Government began measuring poverty in the early 1960s, the continued existence of poor people in a time of the "Affluent Society" seemed anomalous. The search for programmatic ways to alleviate poverty soon generated efforts to measure the size of the poverty population. The first rough estimates of the incidence of poverty were built on survey data indicating that families generally spent about one-third of their incomes for food. A poverty level income was then calculated by using as a yardstick the amount of money necessary to purchase the lowest-cost "nutritionally adequate" diet calculated by the Department of Agriculture (roughly equivalent to the current Thrifty Food Plan). This price tag was then multiplied by three to produce a poverty income threshold.

Thus, this procedure assumed that if a family did not have enough income to buy the lowest-cost nutritionally adequate diet, and twice that amount for other goods and services, it was "poor." Crude as this assumption is, adjustments were made for the size of the family, sex of family head, and for whether the family lived on a farm or not. Farm families were assumed not to need as much cash income because more of their needs could be met through homegrown farm products--particularly food. (Differentials for sex of family head and for farm-nonfarm residence were abolished in 1981.) These first estimates found that 39.5 million--22 percent of the population--persons were poor in 1959.

Since the earliest estimates were made, individuals, agencies, foundations and commissions have studied poverty, and some have focused on how it

is defined and measured. The research supporting these activities has illuminated the issues surrounding poverty and its measurement. The basic concepts, problems associated with them, and measurements have changed little since 1959, although in 1969 policy officials made one basic change in the method for calculating the poverty level of income. The poverty threshold is now established each year by increasing the previous year's level by the change in the Consumer Price Index (CPI) rather than multiplying the cost of the Thrifty Food Plan by three.

A. Issues in the Concept of Poverty and Its Measurement

Even though the concepts underlying the official measurement of poverty have not changed since their development almost two decades ago, they continue to be debated. Controversy has centered around two questions: (1) whether to define poverty in relative or absolute terms, and (2) what definition of income to use. Other issues in the measurement of poverty are simply extensions or derivatives of these basic two.

Experts in the study of poverty identify two ways to think about the problem: Poverty can be viewed as relative or absolute. In general, an absolute standard measures basic subsistence needs, but a relative one measures income distribution.

Relative standards of poverty are directly linked to the distribution of income in the society. Under this concept, poverty is not a condition of absolute want. Rather, it is defined as "having a lot less than most people" even if that means having more than what is considered to be "enough to get by." Using a relative poverty standard, economic growth alone would not eliminate nor necessarily reduce poverty. Under a relative standard, poverty would be reduced only if income became distributed more equally.

The Federal Government measures poverty as an "absolute" concept, which changes only with inflation. Under this approach, the number of poor households would be expected to decline during times of rapid growth, and to increase during times of rising unemployment, rapid inflation or outright economic recession, such as characterized much of the decade of the 1970s. The absolute concept of poverty makes possible the elimination, or at least the reduction, of poverty without a change in the distribution of income.

Determining the appropriate concept of income causes controversy in a number of public policy settings. Whether it is for purposes of taxation, eligibility for welfare benefits, or establishing a poverty yardstick, arriving at agreed upon definitions of countable income requires extensive analysis coupled with compromise, and in the end remain controversial.

The current policy definition counts cash income from earnings, returns on property, and government transfer payments (Social Security, welfare, etc.). It does not include noncash employment compensation such as employer-paid health insurance, employer contributions to Social Security or other pension coverage; nor government in-kind benefits such as food stamps, Medicare and Medicaid, and housing assistance; or tax "expenditures" such as child-care tax credits, earned income tax credits, etc. Substantial government in-kind benefits go mainly to low-income persons. Excluding them from income hampers efforts to assess the effect of government policies on the poor, particularly since in-kind benefits have been the fastest growing programs targeted on the poor during the past decade. In addition to conceptual questions regarding the proper definition of income, practical issues of how to value in-kind benefits have plagued efforts to count them.

The exclusion of in-kind benefits has been the most frequently criticized feature of income measurement for poverty purposes. However, other

features, while not so well known, may affect the accuracy of the measures as well. For example, the income measure used to determine the population in poverty is before-tax income, although the original definition of the poverty threshold was based on a concept of after-tax income. If the official measure were based on after-tax income, countable income would be less and a larger number of earners and their families would fall below the poverty threshold. Although low-income families pay little income tax, those who work pay 6.5 percent of their earned incomes in Social Security contributions. Furthermore, income is counted as an annual total without cognizance of periods of time during a year when a family had little or no income. If a shorter time were used for measuring poverty, the number of people deemed to be poor would rise because the number of poor for some period of time during a year is greater than the number of poor for the year as a whole. On the other hand, the official poverty counts may be too high because cash income is unreported in census surveys and because the value of assets, even liquid financial resources, is not considered.

All in all, many such anomalies subject the current poverty measure to criticism. However, the present methodology has the advantage of being consistent over the entire 24-year period, permitting assessment of trends and changes in trends in the number and percent of people who are poor. It would also appear that a perfect measure probably could not be designed.

#### B. Poverty Rates

The proportion of people in poverty declined steadily during the 1960s. From a high of 22 percent of the population in 1959, the first year of measurement, the rate dropped each year until 1970. With a few bumps up and down,

including the lowest recorded level of 11.1 percent in 1973, the rate essentially stabilized during most of the 1970s--never dropping below 11 percent and never rising above 12.5 percent. Then, starting in 1979, the poverty rate turned up, increasing each year, until it reached 15 percent in 1982 (the latest year for which data are available), an increase of nearly one-third in just 4 years. These trends paint a valuable picture of the progress and setbacks in the Nation's efforts to reduce poverty. But the overall rates tell only part of the story. They disguise some important issues. Within these overall averages, the rates for particular groups of people have varied substantially.

1. Poverty Higher for Blacks

The poverty rate for blacks has stubbornly stayed two to three times higher than the rate for whites. During the 24-year period for which we have data, the poverty rate for blacks declined by 55.1 percent to 30.3 percent in 1982, still very high. In 1982 nearly one-third of all black households in the Nation had incomes below the poverty level. This figure is influenced, however, by another characteristic of the poverty population: The group with the highest poverty rate of all continues to be female-headed households. This is largely because women's earnings average approximately 40 percent less than men's and because their average rates of participation in the labor force are lower. Since a disproportionate share of female-headed families are black, this factor increases the incidence of poverty among blacks. Even excluding the relatively high proportion of black female-headed households, the poverty rate for blacks is almost double that of whites: 18.0 percent, compared to 9.3 percent.

## 2. The Number of Poor Elderly Continued to Decline

The greatest success in reducing the rate of poverty occurred among the elderly. Starting at a rate of 35.2 percent in 1959, over two times the rate for other adults, the rate had dropped by 1982 to 14.6 percent, just slightly lower than the overall rate--which by this time was on the rise. Although the overall poverty rate began rising in 1979 and by 1982 had risen by 32 percent, the poverty rate for the elderly held steady at a rate near its low point. Three main factors reduced poverty among the aged: The Social Security program grew rapidly during the entire 1970s and into the 1980s; Congress established the Supplemental Security Income (SSI) program, which provides, by itself, a level of income almost at the poverty level for elderly couples; and private pensions expanded rapidly. Although the overall poverty rate for the elderly continued to decline in the face of rising poverty for some other groups, the rate of poverty has remained high for some aged persons--the very old, the elderly living alone, and elderly blacks.

## 3. Poverty Among Children

The poverty rate for children has consistently been higher than that of of the population in general. In 1982, over one in five children under 18 years of age (21.3 percent) was poor. The poverty rate among children was 54 percent higher than its 13.8 percent low point in 1969.

The poverty rate for children in female-headed households was much higher (56 percent) than that of children in male-headed families (13 percent). The growth in the number of female-headed families combined with the high incidence of poverty among such families has helped to keep the poverty rate for children high. Since 1959, the proportion of children living in female-headed families

has more than doubled--from 8.9 percent in 1959 to 19.4 percent in 1982. In 1982, every other poor child lived in a female-headed family, compared to about one in every four poor children in 1959.

The more recent increase in the incidence of poverty among children has been the result of more two-parent families joining the poverty ranks--presumably as a result of the recession. Children in two-parent families accounted for about 70 percent of the increase in poverty among children since 1978.





### III. CAUSES FOR LEVELS AND TRENDS IN POVERTY

As is true for all complicated social phenomena, the causes of poverty and trends in its development are hard to explain. One obvious way to begin such an analysis is to examine the main sources of income to the poor.

Poverty discussions often give the impression that the poverty population consists of the same people from year to year. Moreover, reported year-to-year variations hide substantial numbers of the overall population, who move into and out of poverty over a period of years. Recently released reports of longitudinal studies conducted by the University of Michigan (Panel Study of Income Dynamics) have indicated that over a 10-year period between 1969 and 1978, 25 percent of the population was poor at least one of those years. About one percent of the population was poor during the entire period, and about five percent were reported poor in five out of seven years. These studies identified the principal causes of movements into and out of poverty as changes in family composition (divorce, marriage, birth of a child, departure of a child, or the entrance of additional family members into the work force).

In addition, during the period under study, performance of the economy and the size of government transfer programs have affected wages, work-related benefits, and need-tested benefits, all of which help determine the number of the poor. Changes in demographics and living arrangements also figure heavily in explaining past poverty trends.

A. Effects of Changes in the Economy on Earnings of the Poor

On the surface, the trend in poverty over the past 24 years mirrors closely conditions in the economy during that period. The rapid economic growth of the 1950s and 1960s boosted the standard of living for all Americans--low income as well as high income. Since the official measure of poverty is "absolute," rising productivity pushed up standards of living across the board, and the share of the population left below the poverty line declined. However, economic stagnation of the 1970s halted the decline in the incidence of poverty. Real wage growth was negative on average during the decade overall, and real family median incomes also declined. The proportion of families in poverty totaled about the same near the end of the decade as it was at the beginning. Then in January 1980, the economy began a decline, which after a brief reversal dropped into the worst downturn since the Great Depression. During this time, the rate of poverty rose markedly.

B. Government Transfers and Elderly Poverty

The rate of poverty for the elderly showed a dramatic decline over the 24-year period for which such data have been tabulated. From 35.2 percent in 1959, substantially above the rate of other persons, the rate of poverty for the elderly has dropped steadily until in 1982 it reached 14.6 percent, about the same as the overall rate. The growth in Federal Government transfer payments to the elderly is the primary reason for the general decline in the rate of poverty for the elderly. Other sources of income for the elderly grew as well, particularly private pension benefits, which have increased rapidly since the end of World War II. The Social Security program itself had the

most effect. Without income from Social Security, over one-half of the elderly would be poor.

Social Security payments increased over the entire period for a number of reasons. These monthly checks to some 35 million persons (two-thirds of whom were aged) now provide inflation-proof income. The major increases in Social Security came as a result of the following:

1. Periodic ad hoc benefit increases during the 1960s which culminated with the largest increases ever in the early 1970s. Congress increased Social Security benefit levels five times in the late 1960s and early 1970s. These five increases, ranging from seven percent in 1965 to 20 percent in 1972, raised the benefit base by a cumulative 84 percent. The result was that when the first automatic cost-of-living adjustment (COLA) occurred in 1975, it was calculated at a higher base.
2. The enactment of an automatic COLA in 1972. Originally touted as a conservative change that would make it less likely that the Congress would seek periodic increases during election years, this change resulted in large-scale increases in benefit levels during the mid-to-late 1970s and early 1980s. These increases, which permanently increased the base for all subsequent changes, were tied to increases in the consumer price index (CPI). Thus, during the latter half of the 1970s, when inflation rates were highest, the purchasing power of recipients of Social Security was fully protected and keeping the elderly from falling into poverty. At the same time, however, the standard of living of many working people deteriorated as increases in wages failed to match increases in prices. The poverty threshold, tied to the CPI, thus outstripped increases in earnings, and more non-elderly earners fell into poverty. The weak economy from 1980 to 1982 led to increasing poverty rates among families with working members, while the number of elderly in poverty stabilized.

#### C. The Effect of Changes in Earnings and Transfers on Children

The 1979-1982 increase in the rate of poverty was sharpest among children in male-headed families. The poverty rate for children in such families, although below the overall rate, climbed 53 percent from 1979 to 1982, reaching 13 percent. The poverty rates for children in female-headed families, always high, rose 15 percent in the same period, reaching 56 percent.

The 1982 rate of poverty for female-headed families was more than two and one-half times that of all families. Of all children living in poor families, 52 percent were in female-headed families.

Although female-headed families no longer are the fastest-growing poverty group, their problems seem to be the most intractable. For many of these, particularly those who rely on governmental transfer programs for their basic sustenance, even a strongly rebounding economy could not be expected to provide much help. Of the 3.2 million female-headed families with children in poverty, about half get most of their income from income transfer programs. Except for Alaska, no State provides a level of assistance through its Aid to Families with Dependent Children (AFDC) program which takes families up to the U.S. official poverty threshold. In fact, over the past 10 years, the real level of AFDC assistance has declined as inflation has eroded purchasing power of AFDC levels, which are decided by States and lack automatic adjustments for rising prices. In some areas the decline in purchasing power has cut the real value of the benefit by as much as one-third. For example, in New York City, the maximum benefit level for a three-person AFDC family in September, 1983 is \$515, compared to \$766 (in July 1983 dollars) 12 years earlier. Since food stamps do not count as income for poverty purposes, adding the value of this indexed transfer program has no effect on reducing the number counted as poor, even though it reduces need among the poor.

The recent cuts in the budget AFDC are likely to have depressed the incomes of female-headed families in poverty. The new AFDC rules prevent sustained welfare assistance to families (female-headed or not) who have earnings. These changes also reversed two decades of policy concerning assistance to the poor. Since large numbers of family heads work nearly full time and yet are unable to earn an income equal to the poverty level, AFDC assistance had been

considered appropriate for such a family. The recent changes countered that policy. Furthermore, these amendments reversed a policy tenet held for a number of years that those who work should always receive more income than those who do not.

Defenders of these changes have argued that participation in the welfare programs constitutes a "welfare trap" from which one should be encouraged to extricate oneself and that continued dependence on welfare saps the initiative a person might have to work himself or herself out of poverty. The proponents of welfare cuts argue that high levels of welfare payments actually increase the incidence of poverty among working-age adults because they constitute a disincentive. Furthermore, the basic welfare program for working-age adults with children is AFDC. This program for the most part is limited to one-parent families--usually with female heads. Thus the AFDC program has been said to induce some poor families to split up in order to qualify for cash help.



#### IV. PROPOSALS TO REDUCE POVERTY

One overriding conclusion of any analysis of poverty is that fluctuations in economic growth bear most directly on the extent of such hardship. This conclusion is supported by analyses of the changes in poverty during the past 20 years as well as by preliminary analyses of the effect of the 1981-1982 recession. Through overall fiscal policies designed to promote economic growth, the Congress has taken actions, which, if successful, will improve the status of people in poverty and will facilitate movement out of poverty through expanded work and earning opportunities. In addition, the Congress has recently enacted a new program of job training to assist poor working-age adults improve their work skills and enhance their earnings capabilities.

Changes in the income tax laws could increase after-tax incomes of those in poverty who pay income taxes although it would not reduce the officially measured number in poverty, because measurement is based on before-tax income. Federal income and payroll taxes have increased from \$35 in 1978 to \$440 in 1983 for a family of three with earnings equal to the poverty threshold. This represents an increase in taxes from 0.7 percent to 5.5 percent of income, and results partly from the effect of inflation adjustments on the threshold itself. In terms of aggregate revenue loss per dollar of benefit to poor taxpayers, the two most effective tools to reduce the tax burden of the poor are the earned income credit (EITC) and the zero bracket amount (ZBA). The EITC is phased out for incomes above \$10,000 and, therefore, all of the benefits from increasing the credit go to people with incomes below the phaseout. The credit is available

only to persons who support a child, but it is not increased for family size; therefore, it does not raise the tax entry point for childless persons, nor does it raise the taxable threshold for large families above that for small ones. If it were extended to poor workers without children, or adjusted for family size, it would provide extra cash aid to more of the poor.

Increasing the ZBA is also a relatively cost-effective way of providing tax relief concentrated on lower-income people because the tax reduction does not go to the taxpayers who itemize their deductions. However, married couples receive the same ZBA regardless of their family size; therefore, it, too, is not a very good way of providing extra relief to larger families. Sizable increases in the ZBA would be needed to raise the tax-free incomes of single people and married couples to the poverty level (a \$2,000 increase for single people to \$4,300 and a \$1,400 increase for married couples to \$4,800).

Substantial increases in the personal exemption would be necessary to raise the tax-free income level for large families up to the poverty level for them. The differences between the poverty lines for four- and five-person families is almost \$2,000, and it is over \$1,600 between five- and six-person families. Therefore, a personal exemption of around \$1,800 would be needed to provide the difference in tax-free income levels between four-, five- and six-person families that would correspond to their respective poverty lines. All of these options would be expensive in terms of tax revenue foregone--for both the poor and the many nonpoor tax filers who would benefit.

Other options for reducing poverty concern actions the Congress might take through expanded or better-targeted income transfer programs. Before discussing these possibilities two points should be made: (1) These proposals would increase Federal budget outlays; and (2) Increased income transfers of certain types, by their very nature, create disincentives to work. They are also alleged to affect



family stability, although the extent to which this happens is unclear. In any event, tradeoffs must be made. Value judgments ultimately determine the desirability of income redistribution as a national goal. It is beyond the scope of this analysis to estimate the budget costs of these proposals, and there has been no attempt to assign priorities to them.

Changes in the demographic composition of the population also will continue to affect what happens to the poverty population. If the growth rate of female-headed families does not decrease, their numbers may swamp other efforts to alleviate poverty. Furthermore, as the population ages and lives longer, the number of single women over age 75--a group with a very high poverty rate--will increase.

Some possible changes in Federal transfer programs would provide additional income to the poor but would have no effect on the poverty rate as measured. Cash transfer programs might be increased to provide additional income to certain groups, but if cash benefits were not increased enough to bring the poor up to the official poverty threshold, the poverty rate would not be reduced, although the "poverty gap" would be narrowed. Furthermore, if food stamp benefits were increased, neither the official poverty gap nor the poverty rate would be affected, since food stamps are not counted as income--although the poor clearly would have more disposable income. This is not to suggest that the Congress may not want to consider such changes as being most helpful in reducing the need. But the current official poverty measures would not reflect such changes.

Additional spending for transfer programs would have the greatest effect on reducing poverty if directed at specific groups of the population. For example, increases in social benefits for unremarried widows and widowers would target additional income to a group of the elderly with a high rate of poverty. In addition, the Federal SSI program, which already provides income almost up to the poverty line for poor elderly couples, could be liberalized to guarantee

a poverty line income for all the aged. However, a general boost in Social Security would not lower poverty substantially, because only one-tenth of recipients are poor after receiving current benefits.

Similarly, a general increase in unemployment compensation (UC) outlays would not reduce the official poverty rate substantially because fewer than one out of ten UC claimants is poor. Additional UC outlays for the longterm unemployed who did not receive UC in the last year would, however, have a more target-efficient effect. About two out of five of these individuals were classified as poor in 1982. A special unemployment assistance program for individuals in this category who had substantial work experience in the last three years, for example, could have a greater effect on the official poverty rate. One could also enhance this effect by applying a family income test, but this might stigmatize the program in the eyes of some, by making it similar to welfare.

These changes, while adding to budget expenditures, would be notably less controversial than proposals for increasing transfer payments to younger persons who are poor. Proposals to reform the welfare assistance programs by expanding eligibility for non-elderly adults and children have surfaced over the past 15 years, have been vigorously championed by Republican and Democratic administrations alike, and have failed of enactment. In 1981, however, Congress enacted significant AFDC changes to narrow eligibility and to restrict benefits to those who do not work at all. One possible change to direct additional benefits to the poor would be to restore the so-called "work incentive bonus," which permitted AFDC-eligible persons to receive declining benefits as a supplement to earnings.

Even more controversial would be proposals to enact various basic changes in these programs or replacements for them. Ideas of this sort which have been

proposed in the past include: a program of children's allowances, a negative income tax which would provide benefits through the tax system to all the poor regardless of household composition or source of income, and a requirement that States establish an AFDC income floor that would guarantee all poor one-parent families a minimum income equal to a particular proportion of the poverty threshold (most likely lower than 100 percent).

In summary, the recent economic recession and cuts in social welfare programs have induced a rise in the rate of poverty in the United States. Continued economic recovery could be expected to relieve these conditions for some of the poor--those able and willing to work. Changes in the income tax laws could be designed to increase after-tax income of the poor who have earnings. For those with no close attachment to the work force, income transfer program increases could be directed to those most in need. All such policy changes, whether income tax relief or social welfare spending increases, would put additional pressure on the Federal budget deficit and would be decided on a range of grounds, some beyond those discussed here.