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Inequality and Poverty in the United States

FOCUS: Leadership St. Louis
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**These are my own views, and not necessarily the views of the Federal Reserve Bank of St. Louis, Federal Reserve System, or the Board of Governors*



Overview

- Measuring Income Poverty
- Income vs. Asset Poverty
- Income vs. Wealth (Net Worth) Inequality
- The Demographics of Wealth
- Why Are Demographics So Powerful?
- Ideas for Moving Forward

MEASURING INCOME POVERTY

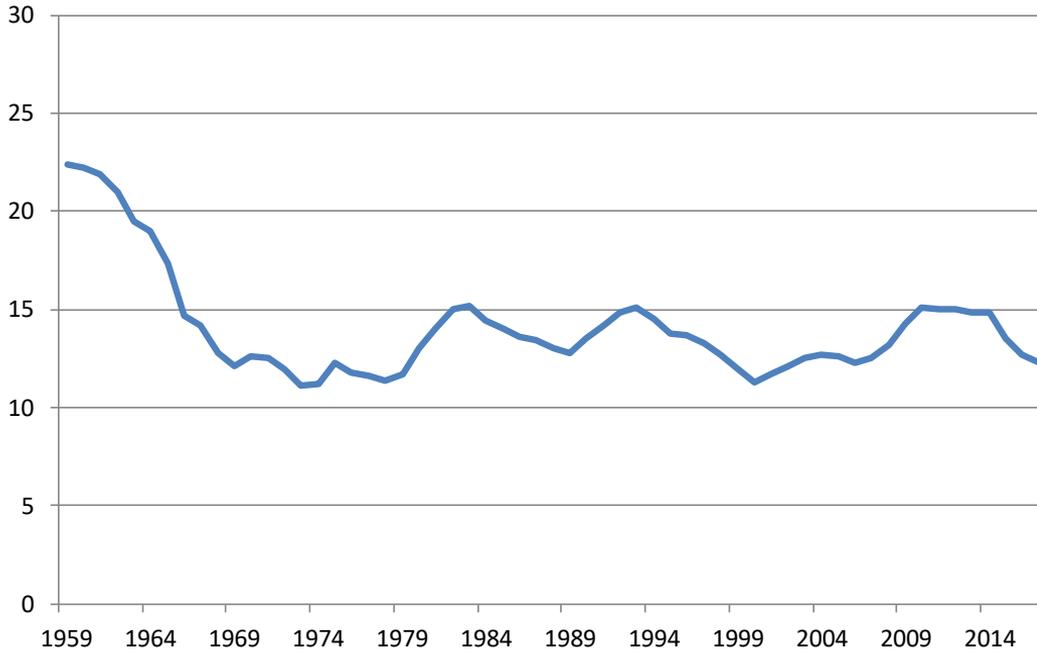
Traditional Measure of Income Poverty

- Official definition uses money income before taxes.
- If total income is less than the family's threshold, every individual is considered in poverty.
- Caveats:
 - Thresholds don't vary geographically (San Francisco = STL)
 - Ignores noncash benefits (public housing, Medicaid, food stamps)
 - Ignores tax credits (Earned Income Tax Credit)

Poverty Declined Until 1970; Stagnant Since

Official Poverty Measure: Share of Total Population Living Below Poverty Line

Percent



Source: Census Bureau/ Haver Analytics.

- One (incorrect) interpretation of the post-1960s trend is that the many programs aimed at eliminating poverty have had no effect.
- In addition to the measurement issues raised earlier, the official measure lacks a lot of additional information.



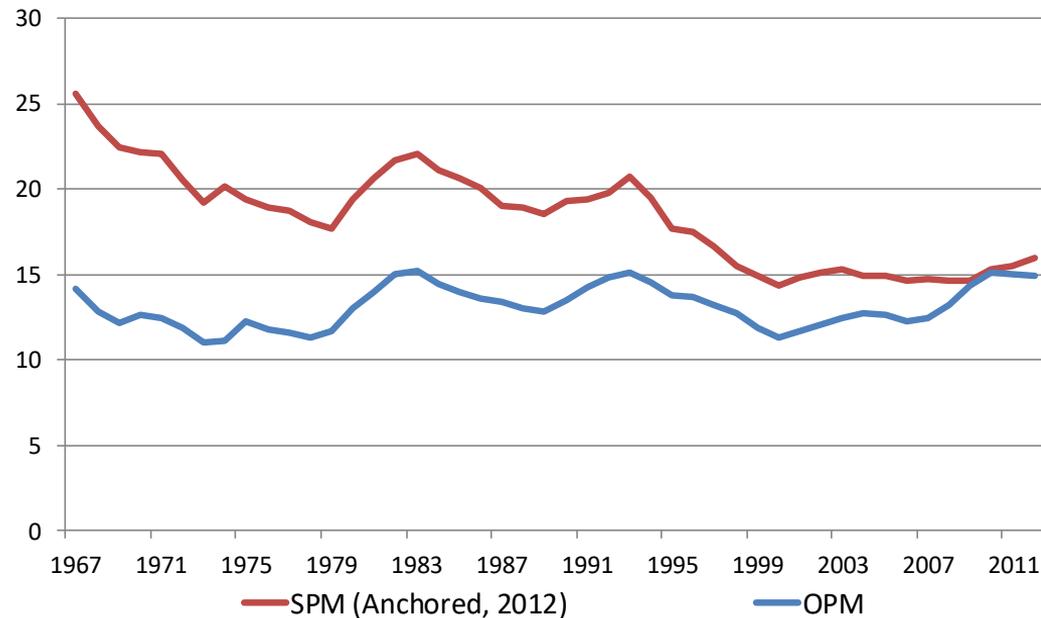
Supplemental Poverty Measure

- Adds in-kind benefits and subtracts necessary expenses.
- In-kind benefits include:
 - Nutritional assistance, subsidized housing, Earned Income Tax Credit (EITC)
- Necessary expenses include:
 - Food and shelter (geographic differences are accounted for), child care and other work-related expenses, costs of medical care and insurance premiums

SPM Shows Greater Poverty, Policy Impact

Official vs. Supplemental Poverty Measure: Share of Total Population Living Below Poverty Line

Percent



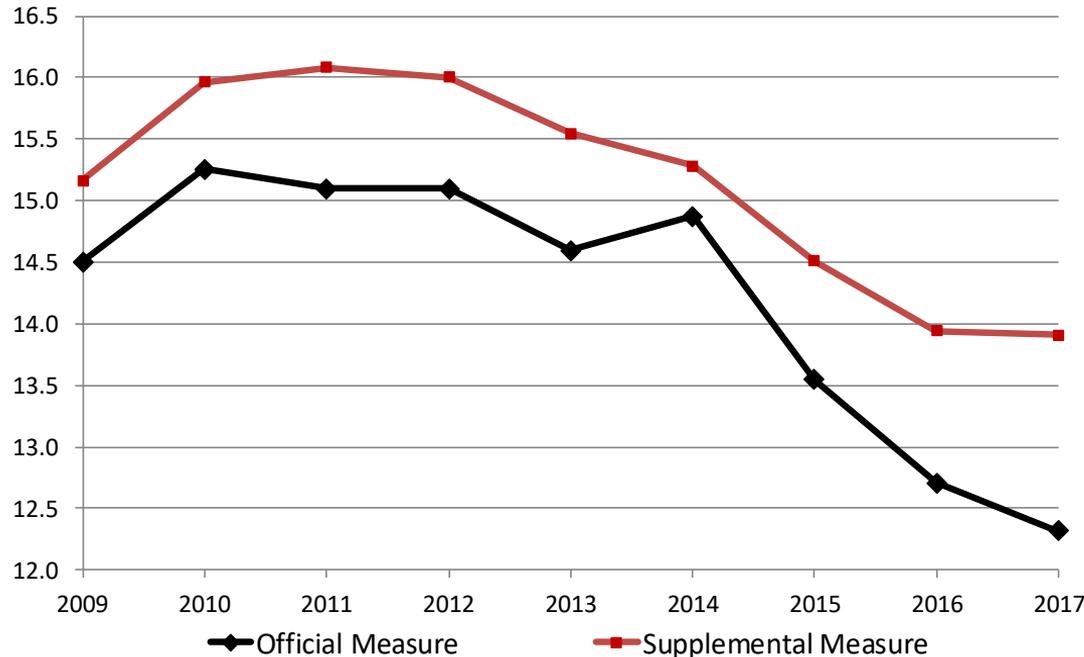
Source: Census Bureau/Haver Analytics and (2013: Wimer, Fox, Garfinkel, Kaushal, and Waldfogel).

- Supplemental measure offers a very different story.
- Poverty rate has been *higher* over the historical period.
- Poverty rate *declined* by roughly 10 percentage points, versus no change seen in official measure.

Recently, Both Measures Show Decline

Official vs. Supplemental Poverty Measure

Percent

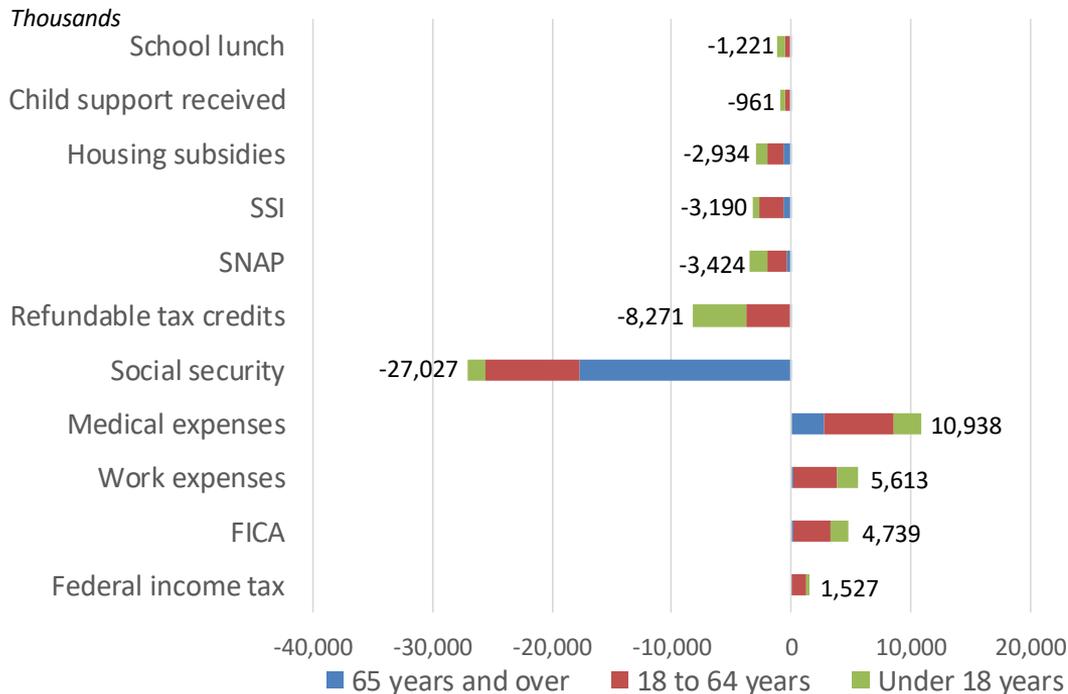


Source: Census Bureau and author's calculations. NOTE: Estimates use sample weights.

- Since 2014, both measures indicate declining rates of poverty.
- Between 2016 and 2017, the OPM fell by 0.4 percentage points while the SPM was effectively unchanged.

SPM Offers Valuable Breakdown of Impact

Change in Number of Individuals in Poverty, by Individual Element, 2017



Source: U.S. Census Bureau, Current Population Survey, 2017-2018 Annual Social and Economic Supplements.

- Income from social security kept 17.7 million seniors out of poverty.
- School lunch support helped keep 772,000 children out of poverty.
- In contrast, medical expenses pushed 10.9 million individuals into poverty.

Official vs. Supplemental Poverty Measure

- Comparison between rates shows that poverty is higher overall, while assistance programs have done more.
- The supplemental rate offers a much more informative look at the dynamics of income poverty.
- For example, refundable tax credits reduce the rate by 2.6 percentage points, or **8.3 million individuals**.
- However, the SPM still takes a narrow view of financial well-being with a focus on income and consumption.

INCOME VS. ASSET POVERTY

Assets: Another Perspective on Poverty

- Household well-being is derived not solely from income and consumption, but also from building savings and assets. (Sherraden 1991)
- However, when poverty is framed in terms of income, the solutions are framed in terms of income.
- Most people don't spend their way out of poverty.

Why Do Assets and Wealth Matter?

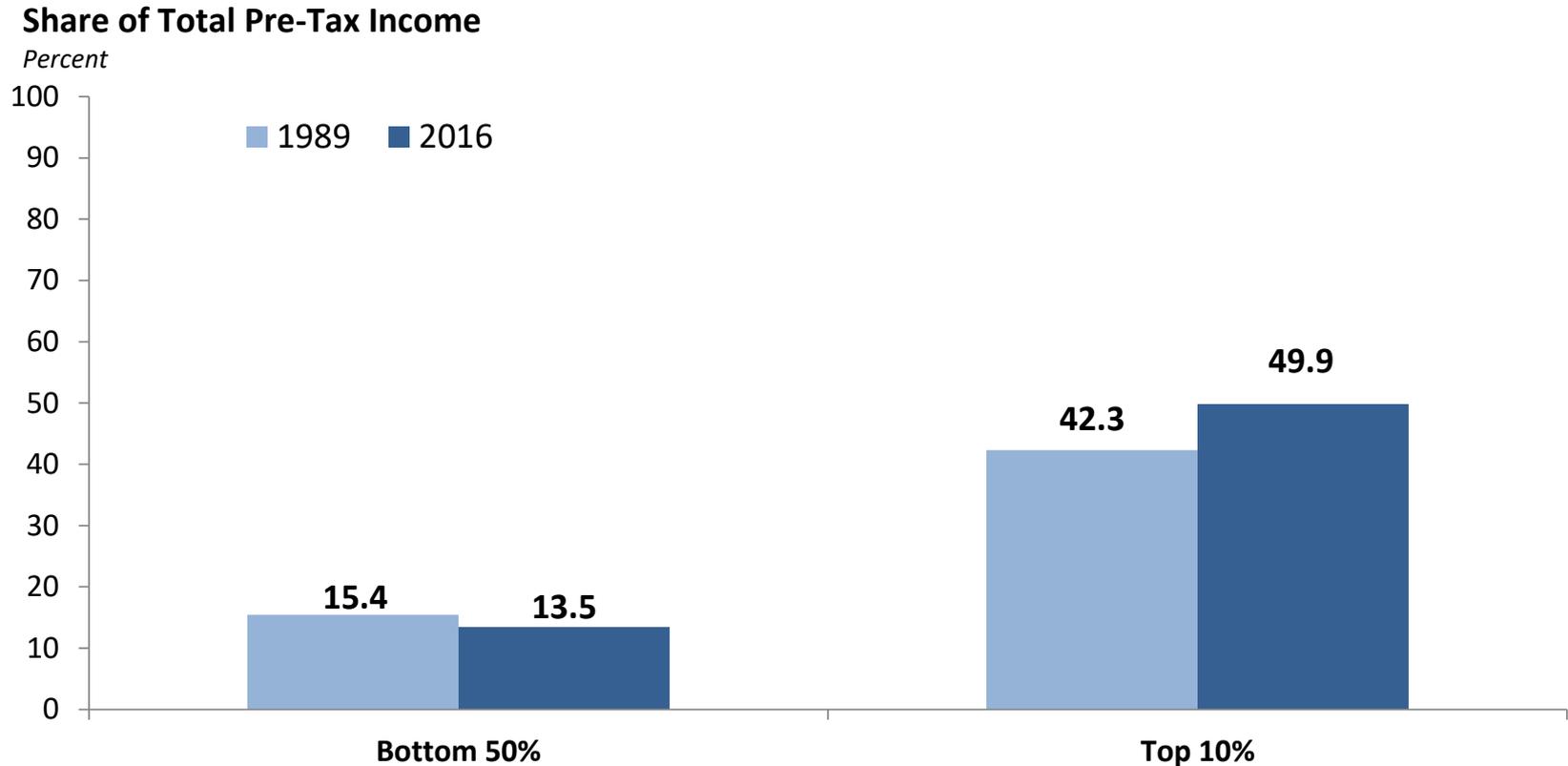
- Wealth buffers against misfortune and helps build your future: retirement, children's education, a bequest.
- When confronted with a negative shock, asset-poor families are 2-3 times more likely to experience material hardship. (McKernan et al. 2009)
- Lack of income means you don't get by; lack of assets means you don't get ahead. (Boshara 2002)

Defining Asset Poverty

- **Asset poor:** lacking sufficient net worth to sustain livelihood above poverty level for at least 3 months. (Haveman and Wolff 2004, CFED)
- **41% of adults** could not cover an emergency expense of **\$400** without selling something or borrowing money. (2017 SHED)
- Almost **55% of households are savings-limited**, meaning they cannot replace even one month of income through liquid savings. (PEW 2015)

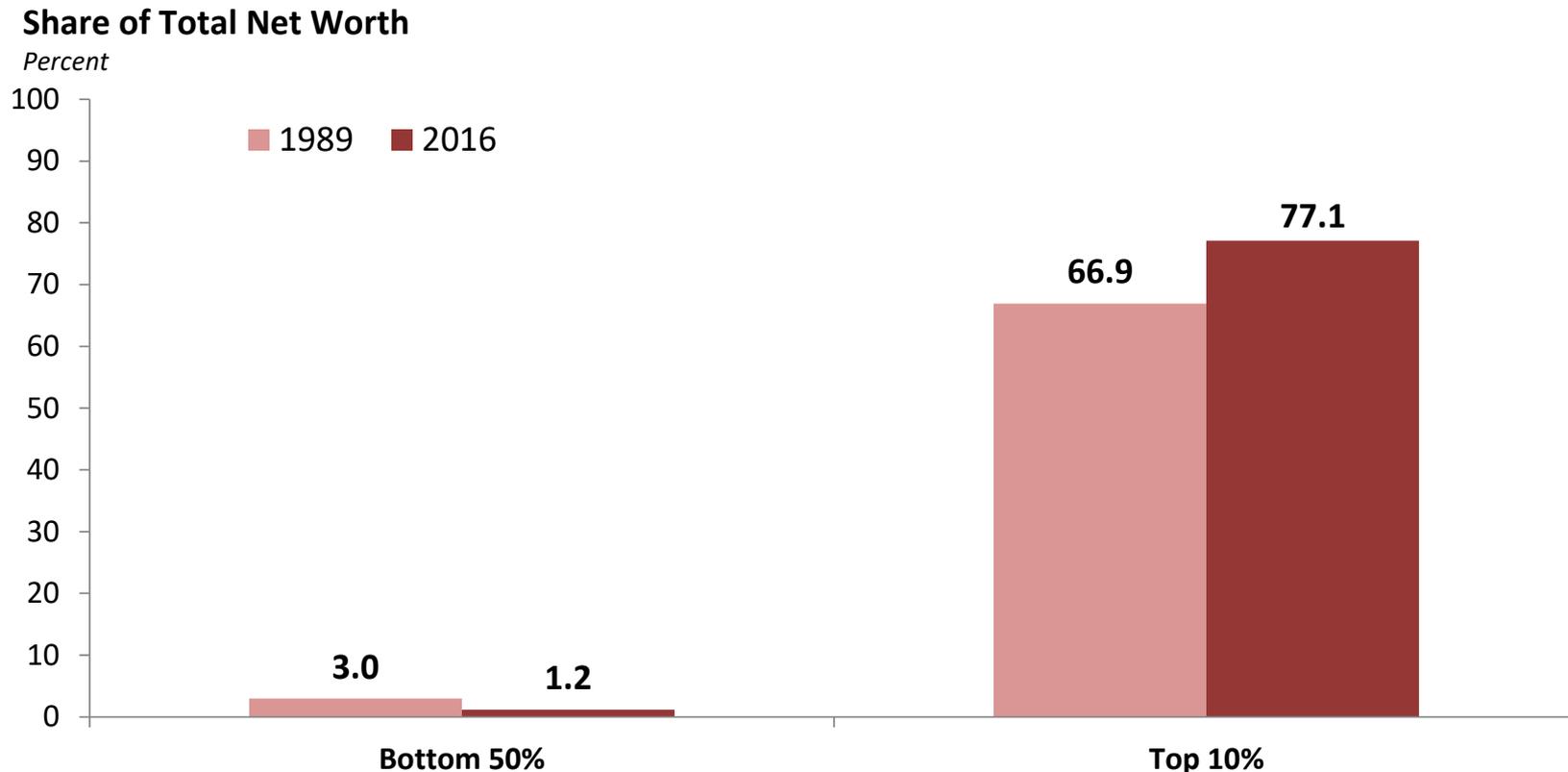
INCOME VS. WEALTH INEQUALITY

Income Inequality is Significant and Growing



Source: Federal Reserve Survey of Consumer Finances and authors' calculations.

But Pales in Comparison to Wealth Inequality

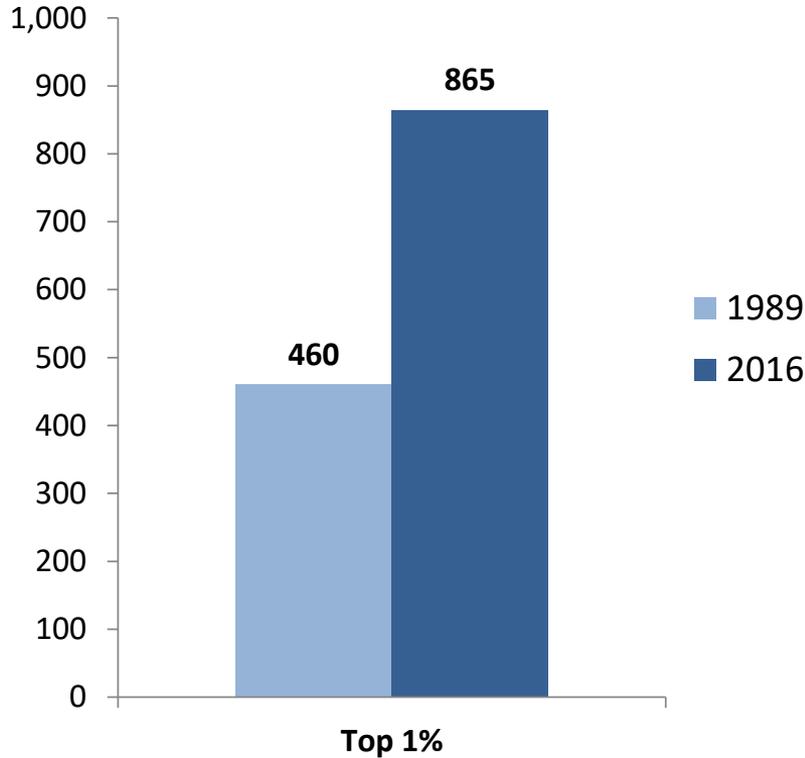


Source: Federal Reserve Survey of Consumer Finances and authors' calculations.

Very Top Experienced Phenomenal Gains

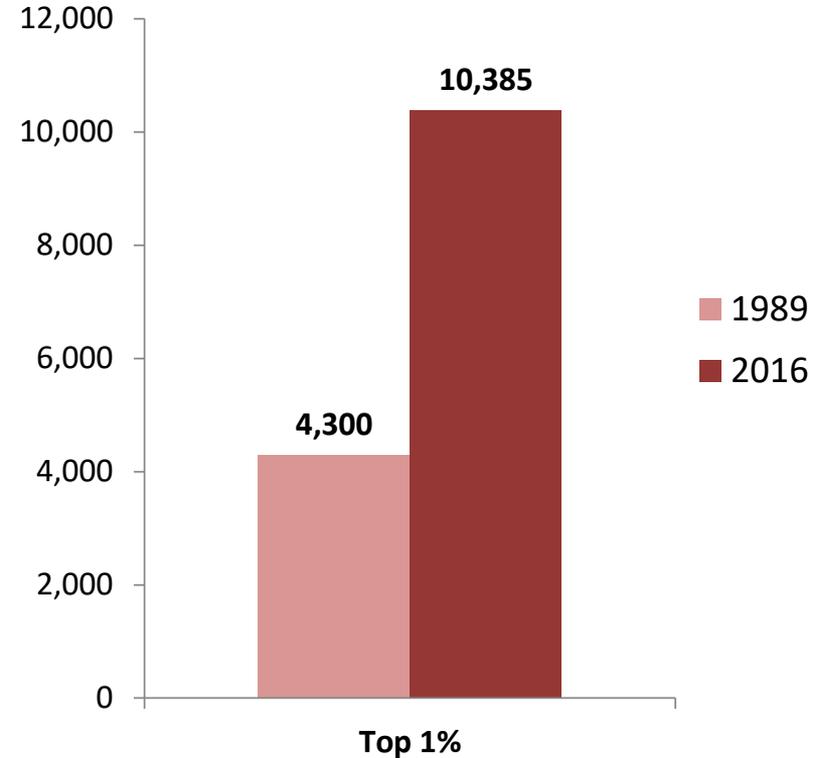
Income Distribution: Top 1 Percent

Thousands of 2016 \$



Net Worth Distribution: Top 1 Percent

Thousands of 2016 \$



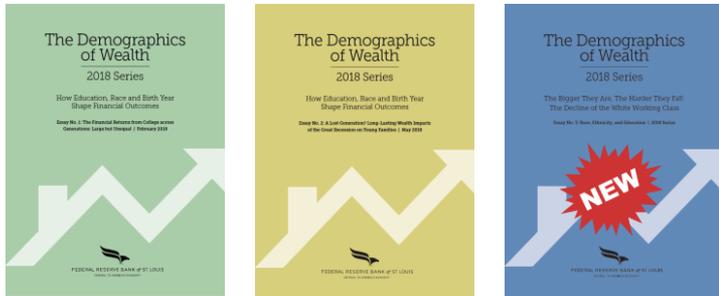
Rising Inequality for Both Wealth and Income

- Income and wealth gains have not been distributed equally; half of families have seen their share decline.
- At the same time, a very small share of families have accrued tremendous gains.
- In 2016, **10.9 percent** of families had *negative* net worth, up from **7.4 percent** in 1989.
- Given greater income instability and no assets to fall back on, these families live with even greater risk.

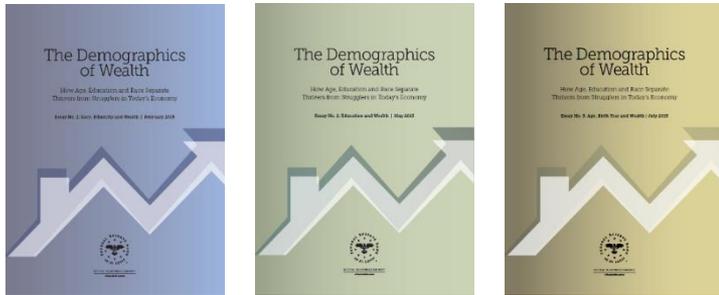
THE DEMOGRAPHICS OF WEALTH

The Demographics of Wealth Series

2018 Series



2015 Series



- This essay series studies wealth and other key outcomes according to a person's or family's:
 - Race/ethnicity
 - Education (own and parents')
 - Age and birth year
- Your race, education and birth year are strong predictors of your income, wealth, and well-being.



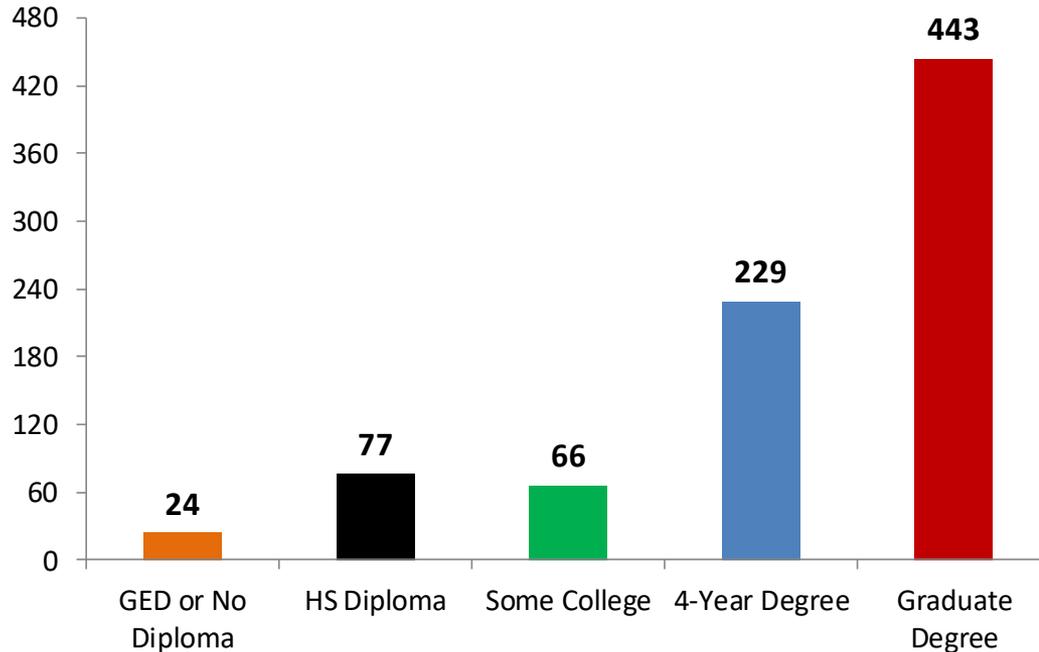
Education and Wealth

- Five groups based on highest educational attainment of the respondent:
 - Did not complete high school on-time (GED or no diploma)
 - High-school diploma
 - Some college, including degrees or certificates short of 4-year degree
 - Four-year college degree
 - Post-graduate degree

High Expected Returns to 4-Year Degree

Real Median Family Net Worth, by Education

Thousands of 2016 Dollars



Source: Federal Reserve Board's Survey of Consumer Finances.

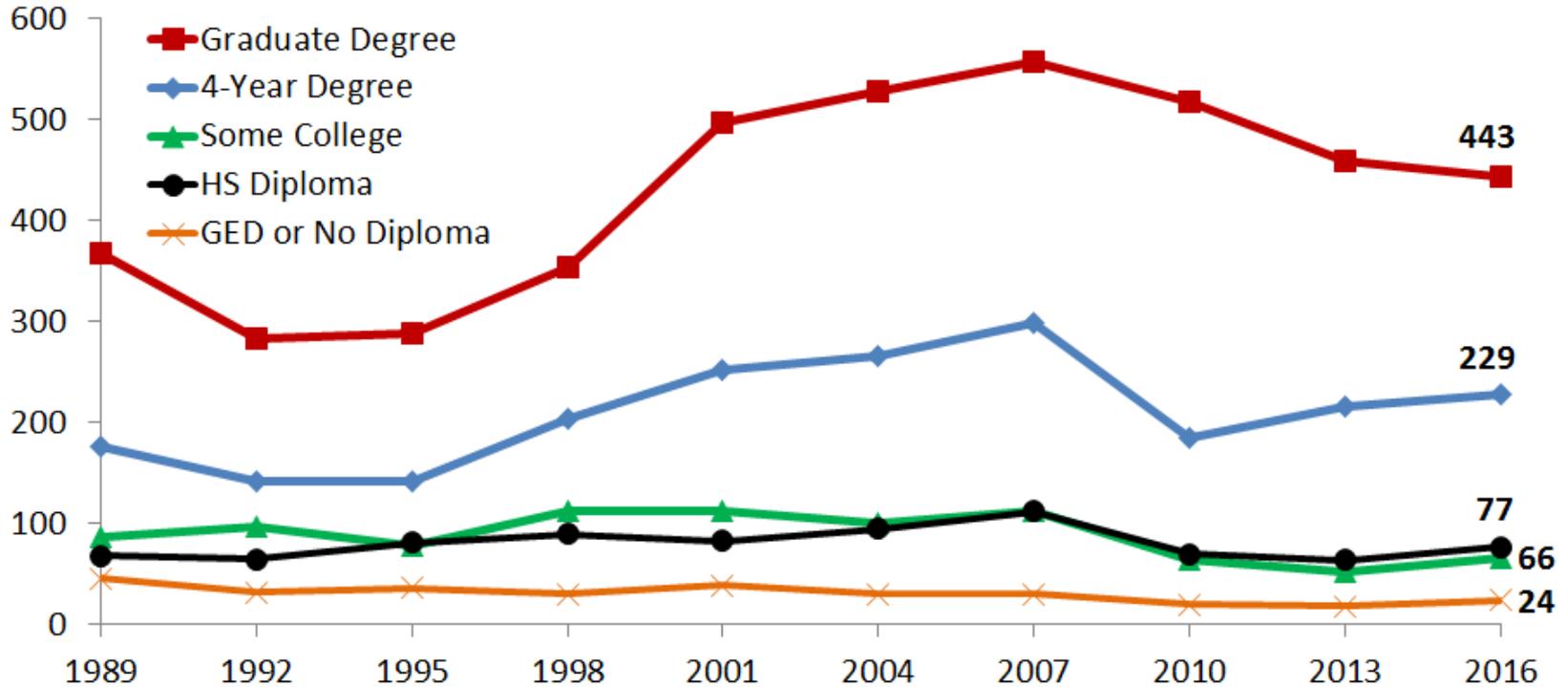
- There is an increasing wealth divide between families which have a college-degree and those that do not.
- Furthermore, expected returns associated with a graduate degree are increasing.



Recession Interrupted Growing Returns to Ed.

Real Median Family Net Worth, by Educational Attainment

Thousands of 2016 Dollars

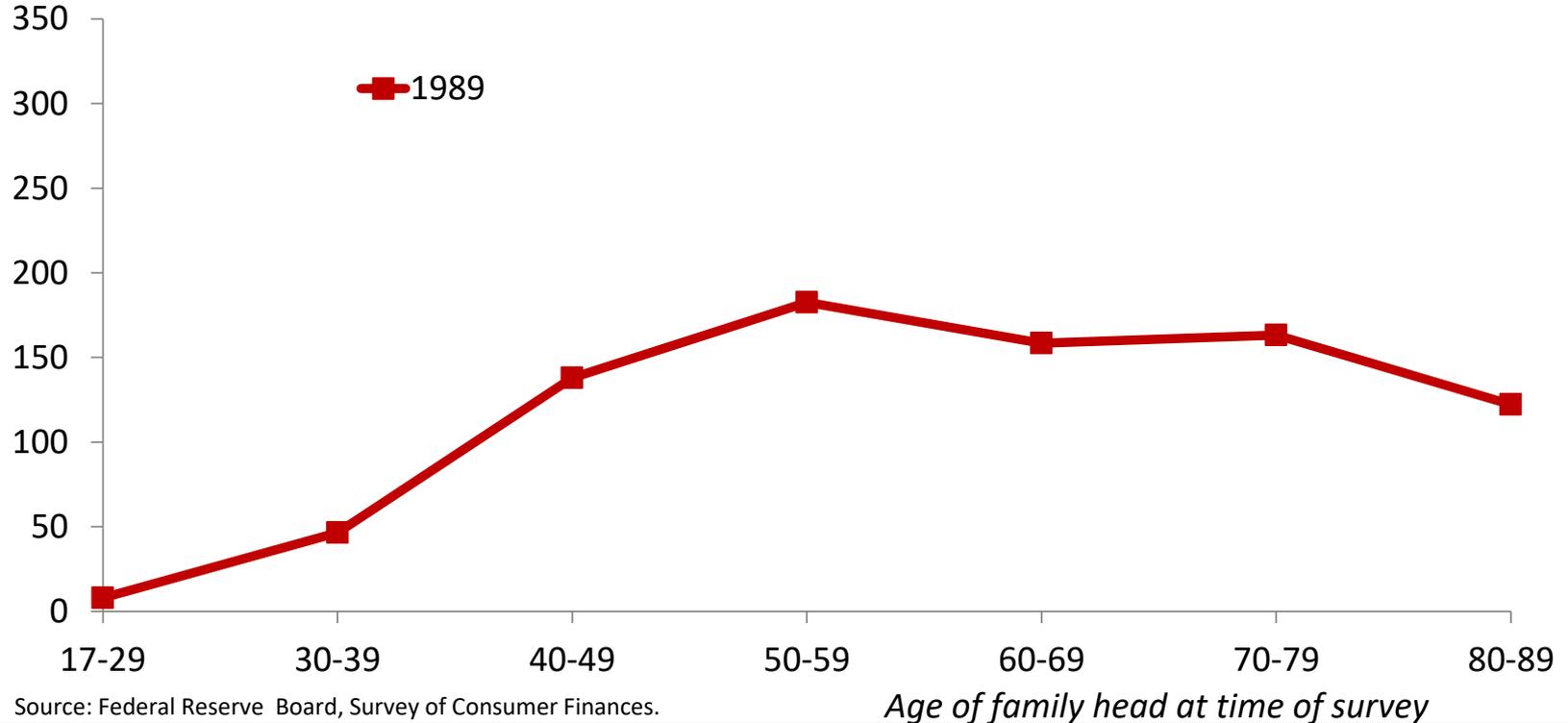


Source: Federal Reserve Board, Survey of Consumer Finances.

When You Were Born Matters

Median Family Net Worth by Age

Thousands of 2016 Dollars

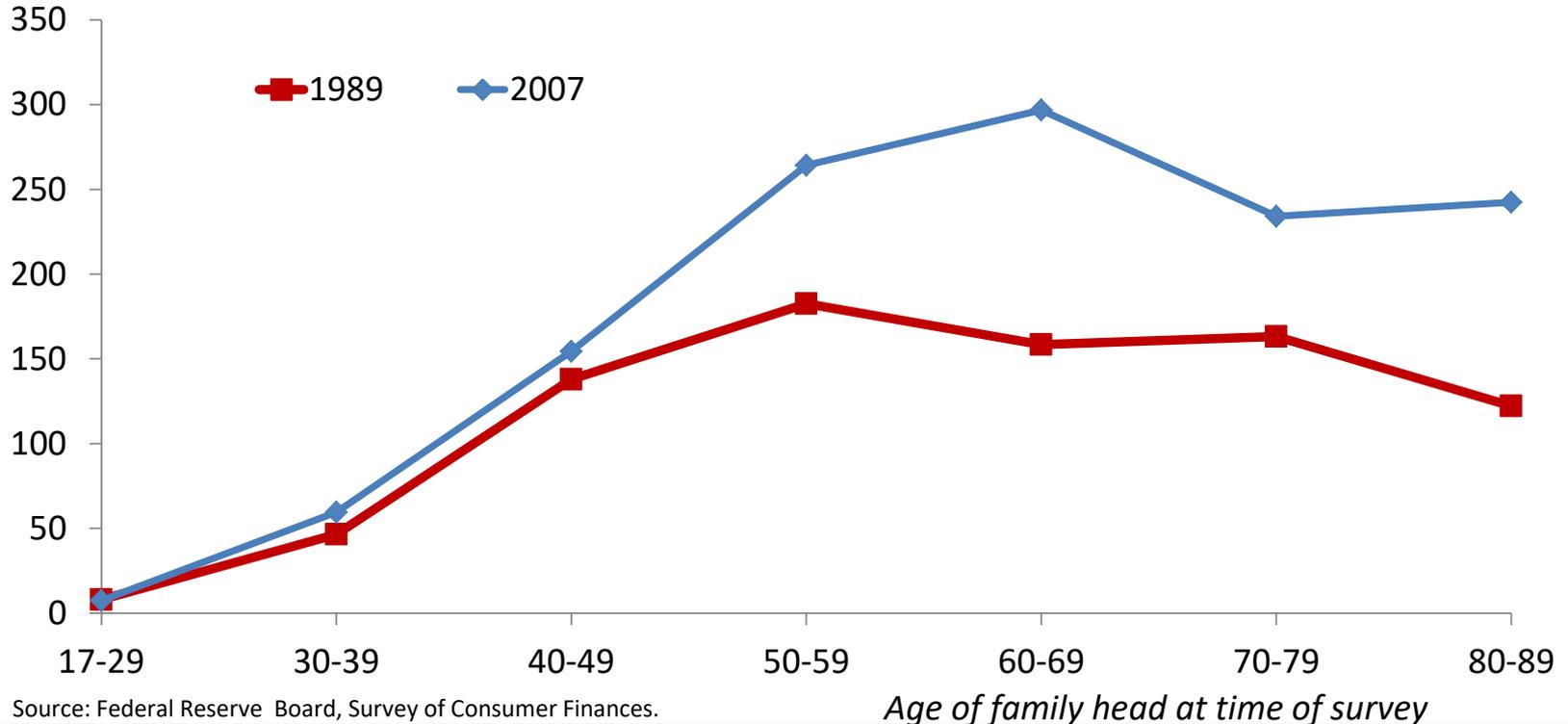


Source: Federal Reserve Board, Survey of Consumer Finances.

When You Were Born Matters

Median Family Net Worth by Age

Thousands of 2016 Dollars

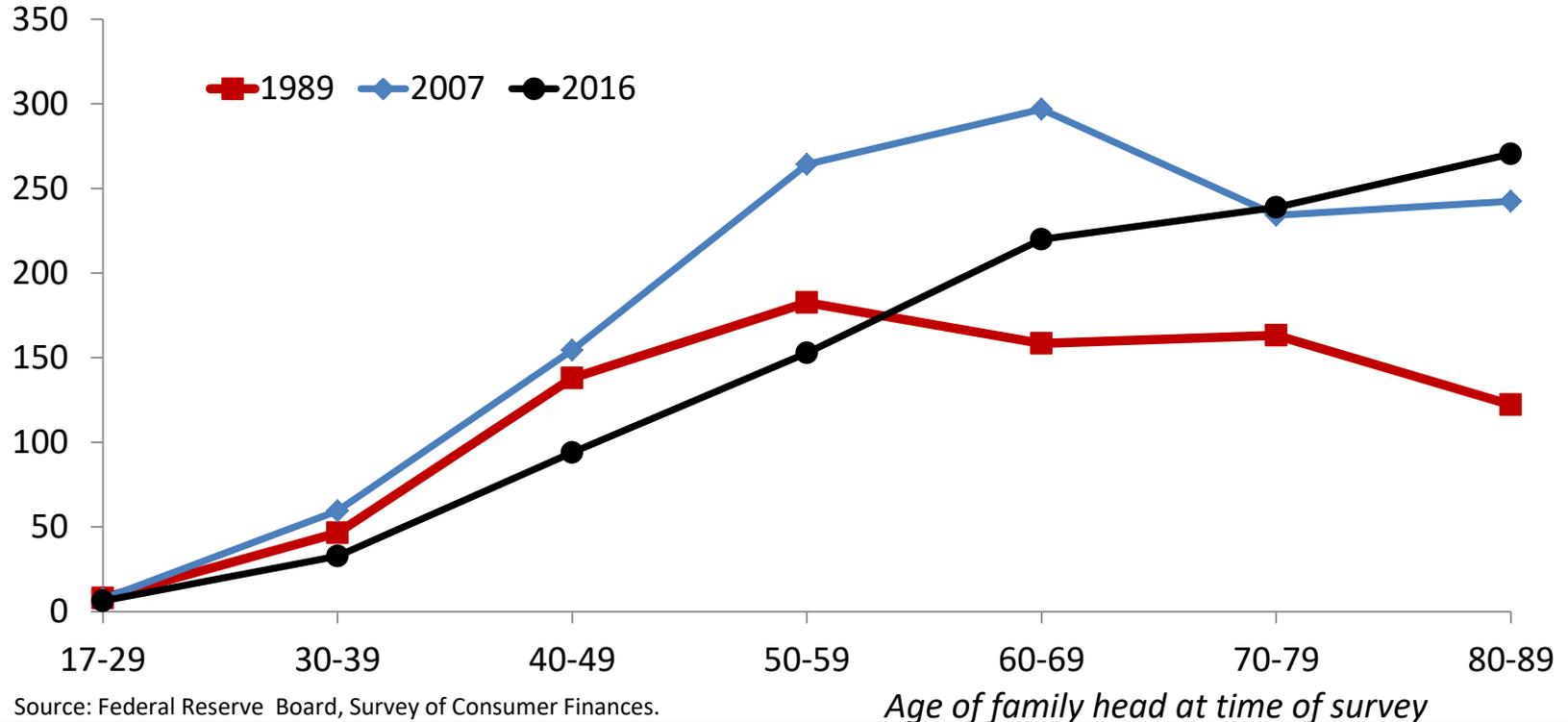


Source: Federal Reserve Board, Survey of Consumer Finances.

When You Were Born Matters

Median Family Net Worth by Age

Thousands of 2016 Dollars



Source: Federal Reserve Board, Survey of Consumer Finances.

Age of family head at time of survey



The Lasting Impact of the Great Recession

- The Great Recession of 2007-09 inflicted deep and widespread losses to wealth across American families.
- While wealth losses occurred across the age spectrum, the extent of the damage has been unequal.
- Younger families suffered the most and have rebounded slowly.

Can Families Recover What They Lost?

- For the families that lost the most wealth, how likely are they to recover in time for major goals?
 - First home purchase
 - Tuition for their children
 - Retirement
- Will young or middle-aged families at the advent of the recession become part of a “lost generation” that struggles to achieve life’s financial milestones?

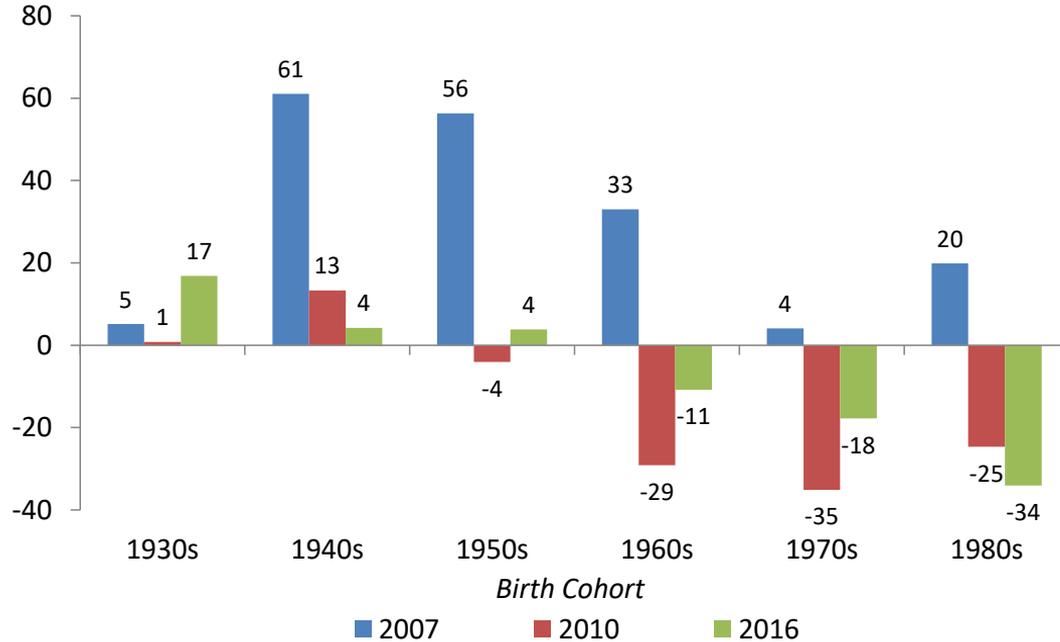
Generational Wealth Outcomes

- For a wealth benchmark, we estimate the typical life-cycle using all households in our survey.
- To understand how members of particular birth years have fared, we track six decade-long cohorts over time:
 - Household respondents born in the 1930s, 1940s, 1950s, 1960s, 1970s and 1980s.
- To be clear, we don't track individual families across time; instead, we track “quasi-panels” of families.

Which Generations Have Recovered?

Deviation of Birth Cohort Median Wealth from Predicted Value

Percentage Points



Sources: Federal Reserve Board's Survey of Consumer Finances and authors' calculations.

- Cohorts born before 1960 were above benchmark levels in 2016.
- Cohorts born in 1960 or later were below predicted wealth levels.
- The 1980s cohort slipped noticeably further behind between 2010 and 2016.

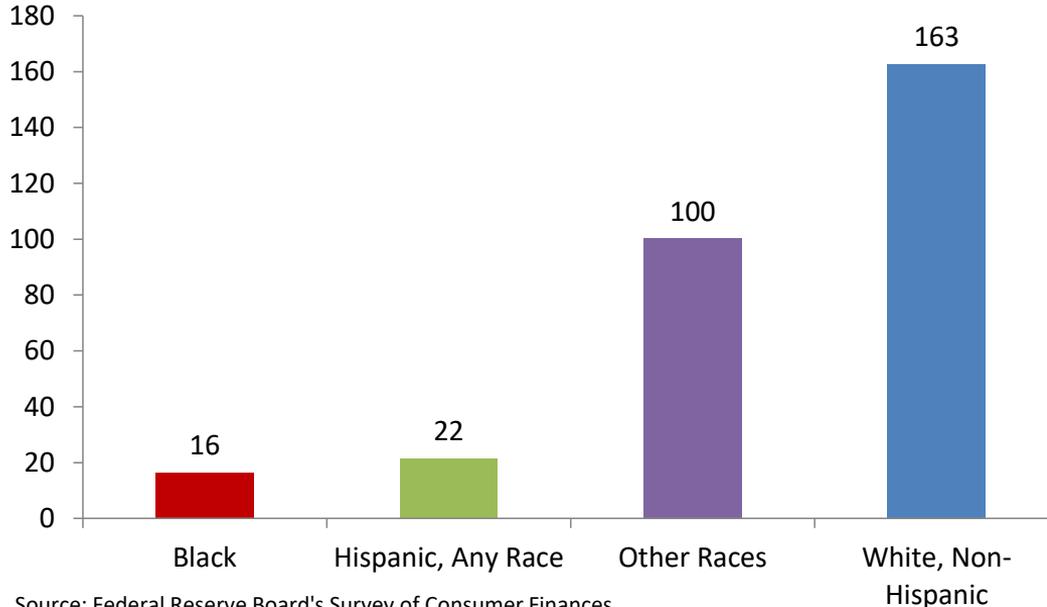
Race, Ethnicity and Wealth

- Four groups based on race or ethnicity of the survey respondent:
 - Non-Hispanic white
 - Non-Hispanic black or African-American
 - Hispanic of any race
 - Other or multiple races (Asian, American Indian, Alaskan Native, Native Hawaiian, Pacific Islander, other race, identifies with more than one race)

The Racial Wealth Gap is Wide...

Median Household Net Worth, by Race/Ethnicity of Respondent, 2016

Thousands of 2016 \$



Source: Federal Reserve Board's Survey of Consumer Finances.

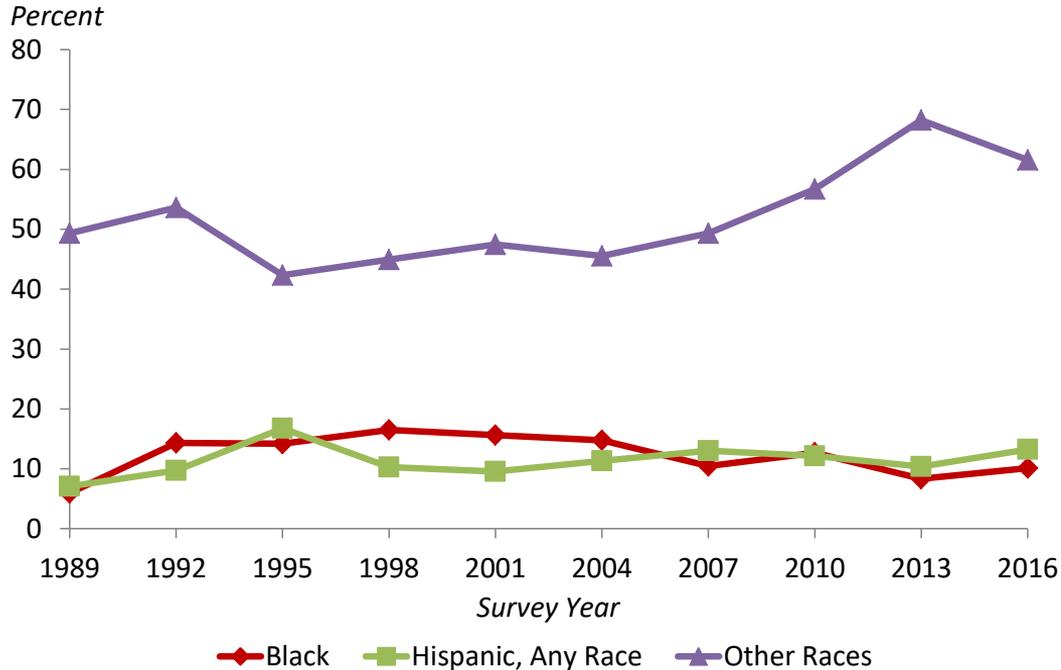
Note: "Other Races" includes Asians, Native Alaskans, Pacific Islanders, Native Americans, and families identifying with more than one race or ethnicity.

- The racial wealth gap in the U.S., observed at the aggregate, is wide and most severe for black and Hispanic families.
- As of 2016, the median black family had 10 cents per dollar that the median white family owned.



And It Has Been Persistent

Median Real Net Worth, Relative to Non-Hispanic White Families



Source: Federal Reserve Board's Survey of Consumer Finances.

- Per dollar of white wealth, the median black family had between a low of 6 cents in 1989 to a high of 17 cents in 1998.
- Median net worth for Hispanic families has similarly been stagnant over the past 27 years.

Why Are Demographics So Powerful?

- Education
 - More education is *correlated* with many good outcomes:
 - More desirable occupation/profession.
 - Better household financial management.
 - More likely to be married.
 - Better health, longer life expectancy.
 - Higher income and wealth.
 - But *correlation isn't necessarily causation*—how important is education *per se*?

Why Are Demographics So Powerful?

- Research shows that educational attainment reflects:
 - True value added.
 - Signaling of your innate abilities.
 - Investments made in you by your parents and grandparents.
- One of our new essays uses parents' education to predict outcomes.
 - Wealth is associated with parents' educational attainment.
 - It appears that some people enjoy a “head start.”

Why Are Demographics So Powerful?

- Age and Birth Year
 - Income and wealth outcomes follow a life-cycle.
 - But timing appears to matter as well.
 - Conditions in the broader economy differ when different generations reach specific age-related milestones.
 - For example, purchasing a home versus selling a home at the peak of the housing bubble.

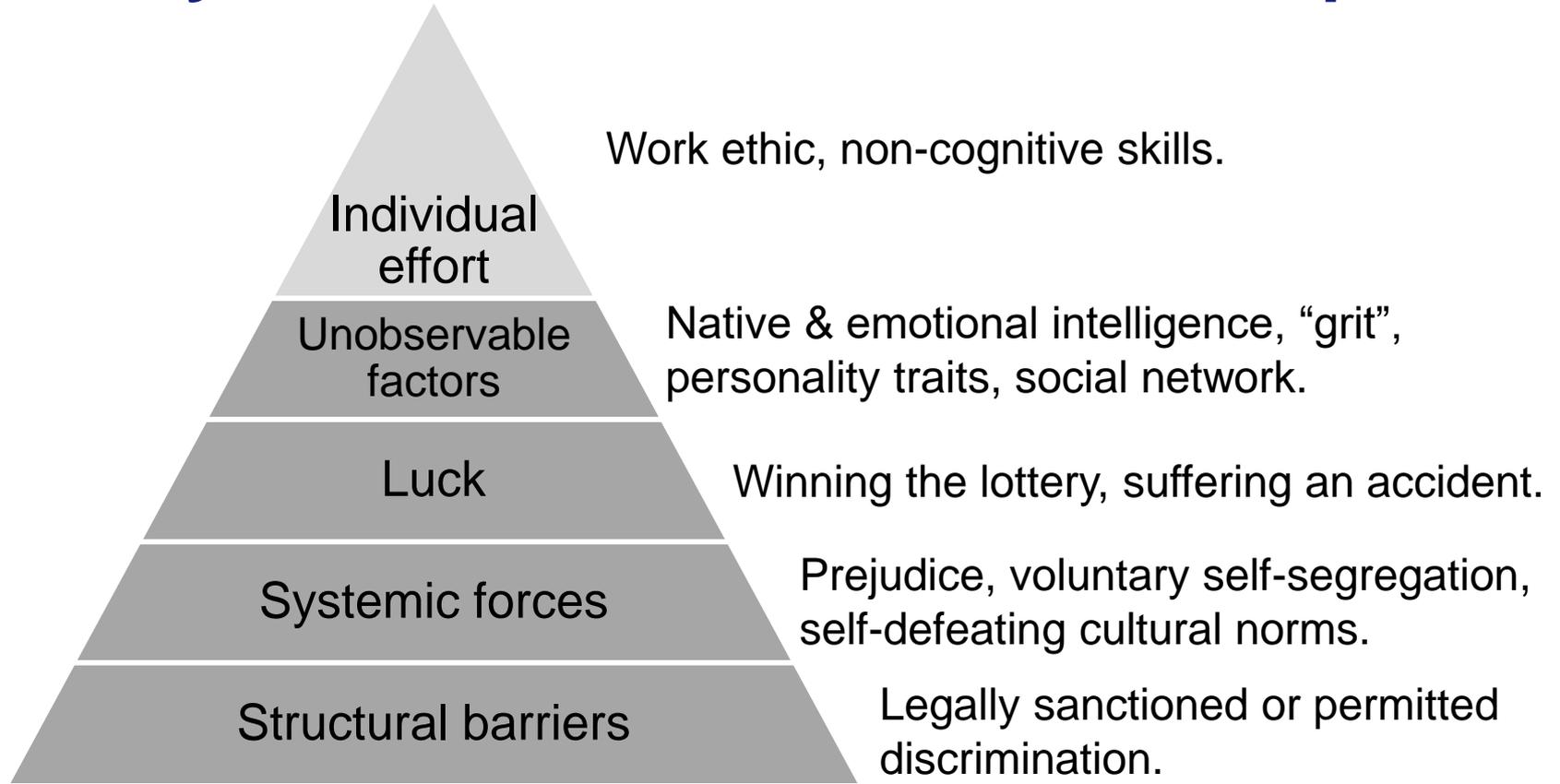
Why Are Demographics So Powerful?

- Race and ethnicity still matter—a lot.
 - Historical discrimination and disadvantage created large wealth gaps in the past, which profoundly affect today’s children and adults.
 - Continuing discrimination and disadvantage hamper full participation and achievement.
 - Ongoing structural and systemic barriers make it difficult to narrow wealth gaps.

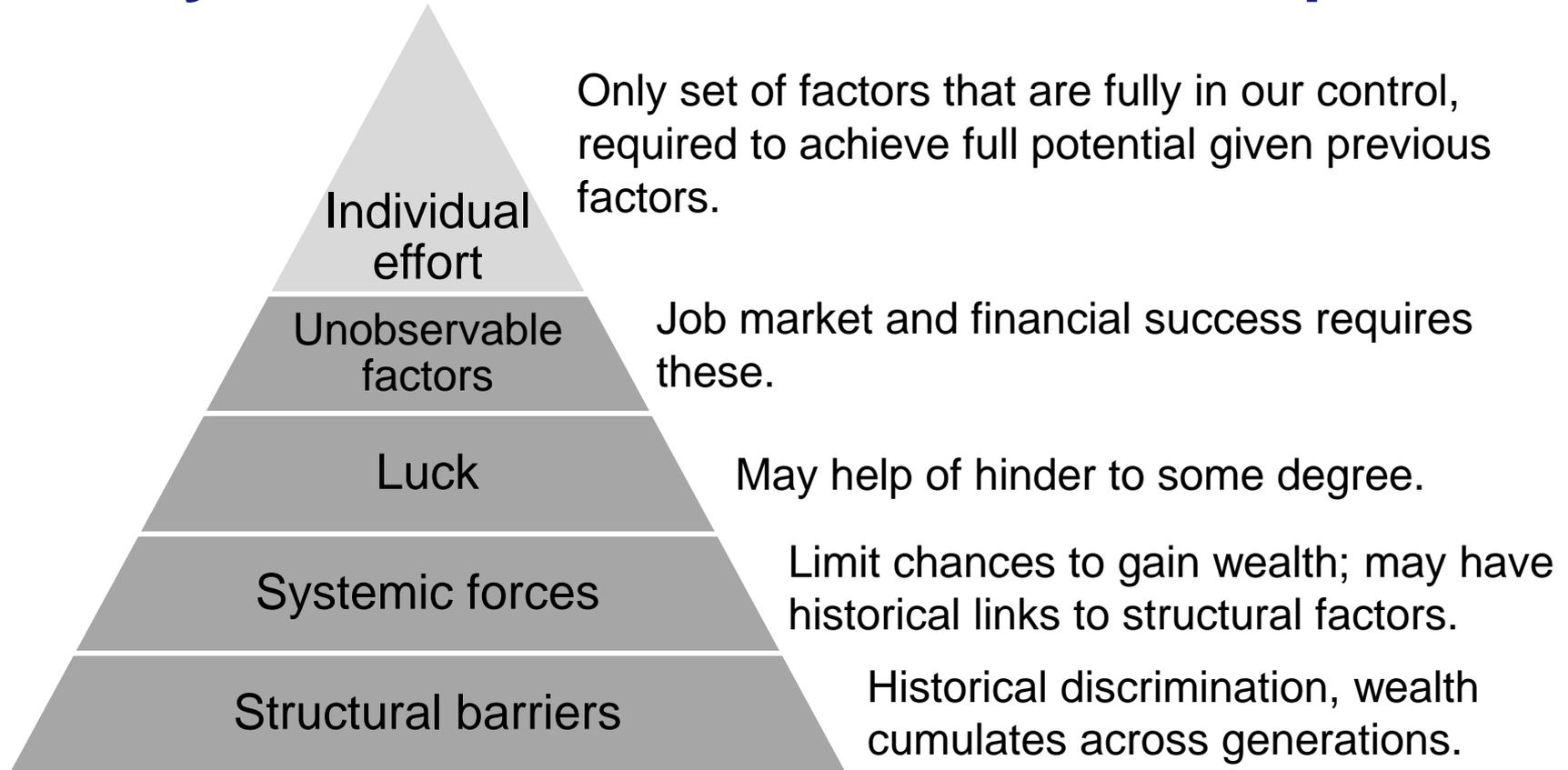
Why Are Wealth Outcomes So Unequal?

- Basic demographic characteristics are strongly related to typical income and wealth outcomes.
- This framework helps us *predict* but it doesn't *explain* everything.
- Our research suggests that *structural, systemic or other unobservable factors* related to race and ethnicity may be important drivers of wealth inequality.

Why Are Wealth Outcomes So Unequal?



Why Are Wealth Outcomes So Unequal?



IDEAS FOR MOVING FORWARD

Conversation One vs. Conversation Two

(Jackson 2017)

- **Conversation one** outlines expedient, small-scale interventions aimed to solve tightly defined problems or improve existing institutions.
- **Conversation two** involves a deeper discussion about where wealth gaps come from and what larger-scale changes might close them.
- Both conversations are necessary but often in social sciences the first is preferred or crowds out the second.

Conversation One

- Child Development Accounts / College Savings Accounts
 - Established at birth or when child enters kindergarten.
 - Universal (for all kids) and progressive (more for the poor)
 - Over 40 programs/policies in the U.S., some state- and city-wide.
 - Research shows positive impacts on child development, maternal health, and college outcomes.

Conversation Two

- **Not** endorsing any specific policy but conversation two involves bold proposals such as:
 - Renewed pursuit of desegregation of primary and secondary schools.
 - Disassociate school funding from neighborhood wealth.
 - End residential segregation (by race and income).
 - Universal higher education.
 - Wealth redistribution.

Conclusion

- While income and wealth poverty have improved from worst of the recession, inequality continues to grow.
- The families experiencing the most hardship fall along demographic fault lines.
- Reducing inequality, eradicating poverty and closing wealth gaps is no small task given complex, deep-rooted causes.
- Realistic proposal needs big ideas along with proven interventions.

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