

AEI poverty and income session, August 25, 2008
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Whether the 2007 poverty rate announced tomorrow by the Census Bureau goes up, down, or stays the same, it's a good bet that someone at the press conference will note that 2007 was last year and ask what the rate is now, in 2008. Because a year has to be over before the Census Bureau can ask people about their annual incomes, the latest official poverty rate is always at least a year old.

Although the Census Bureau issues the official poverty rates only once a year, we already have official data through June 2008 about factors that drive poverty, especially employment and earnings. Figure 1 uses a long historical series of these data in a simple statistical model. Each year's poverty rate over three decades is modeled based on the rate in the *prior* year and *changes* in employment, average weekly earnings, the Food Stamp Program caseload, and the number of single mothers. The solid line traces actual official poverty rates reported by the Census Bureau, and so runs out in 2006. The dotted line is generated by the model.

The fact that the dotted line stays very close to the solid line over more than a quarter century means that variation in employment, earnings, food stamps, and single parents from year-to-year correlates well with variation in the poverty rate. Based on these long-standing historical relationships, the model predicts that the 2007 poverty rate will be about .2 percentage points above 2006. *Caution Number 1* is that an apparent .2 percentage point increase may not be statistically significant, meaning that it could have occurred just by chance because the Current Population Survey used to gather these data is a sample. *Caution Number 2* is that, on average, the model is off the actual by a little less than .2 percentage points. So it would not be surprising if the model showed a small increase in poverty and the Census Bureau announced that there was no change. However, based on these historical relationships, it would be surprising if the Census Bureau announced that poverty had declined in 2007.

Maybe more interesting than what happened last year is what the model says has been happening in 2008. There's a lot of 2008 to go yet, and things may improve. But through June, the indicators the model uses weren't improving. The dotted line on Figure 1 predicts another .2 percentage point increase in the poverty rate for 2008.

In order to see why the model predicts higher poverty in 2007 and 2008, Figure 2 shows how several of the predictors in the model used in Figure 1 have been *changing* since the beginning of 2007, which is shown as zero. *Falling* employment and earnings tend to *cause* more poverty – so, for the *green* and *blue* lines on Figure 2, *down indicates more poverty*. Food Stamp Program participation is not a cause of poverty. In general, households must be poor in

order to receive food stamps. *Higher* food stamp caseloads are an *effect* of more poverty – so, for the *yellow* line on Figure 2 *up* indicates more poverty.

The ratio of employment to population (the dotted blue line) has been declining at a fairly steady rate throughout 2007 and the first half of 2008. By contrast, Food Stamp Program caseloads (the dashed yellow line) began to rise steeply at the beginning of the second quarter of 2007. The decline in average earnings (the solid green line) began only in the fourth quarter of last year.

From Figure 2, it is easy to see why the model predicts additional poverty increases for 2008. However, keep in mind that the official poverty rate is based on *pre-tax money income*. It does not count noncash government transfers, such as food stamps, or the effect of taxes. This is particularly important in 2008, because the official poverty rate will not reflect the economic stimulus payments distributed through the federal income tax system this year.

The next picture is drawn from last year's Census Bureau report on poverty and income in 2006. As interesting as poverty levels and trends are, what the Census Bureau reports about median household incomes may get a lot more attention tomorrow. Median incomes are not average or per capita incomes, that can be influenced by large gains among top earners. Median incomes represent the households in the middle.

On Figure 3 you can see that after each peak in the economic cycle, median incomes declined during recessions, but then gradually recovered again and eventually surpassed their previous peak before the next recession hit. Figure 3 illustrates that, not only has poverty not fallen back to its pre-recession level (on Figure 1), but, through 2006 at least, the middle of the distribution hadn't recovered fully yet either.

The share of householders who are *immigrants* increased by more than two percentage points over the short period on Figure 3. Could the poor showing of median income since 2000 be due to more immigrants with low earnings? Figure 4 shows similar patterns for median incomes among both householders born in the United States and those born elsewhere. Through 2006, neither group had recovered its pre-recession peak.

There's a good deal of talk about whether we're heading for, or are already in, a recession. If so, this could be the first economic cycle over which the middle appears to have lost ground. We'll see what the Census Bureau has to say tomorrow.

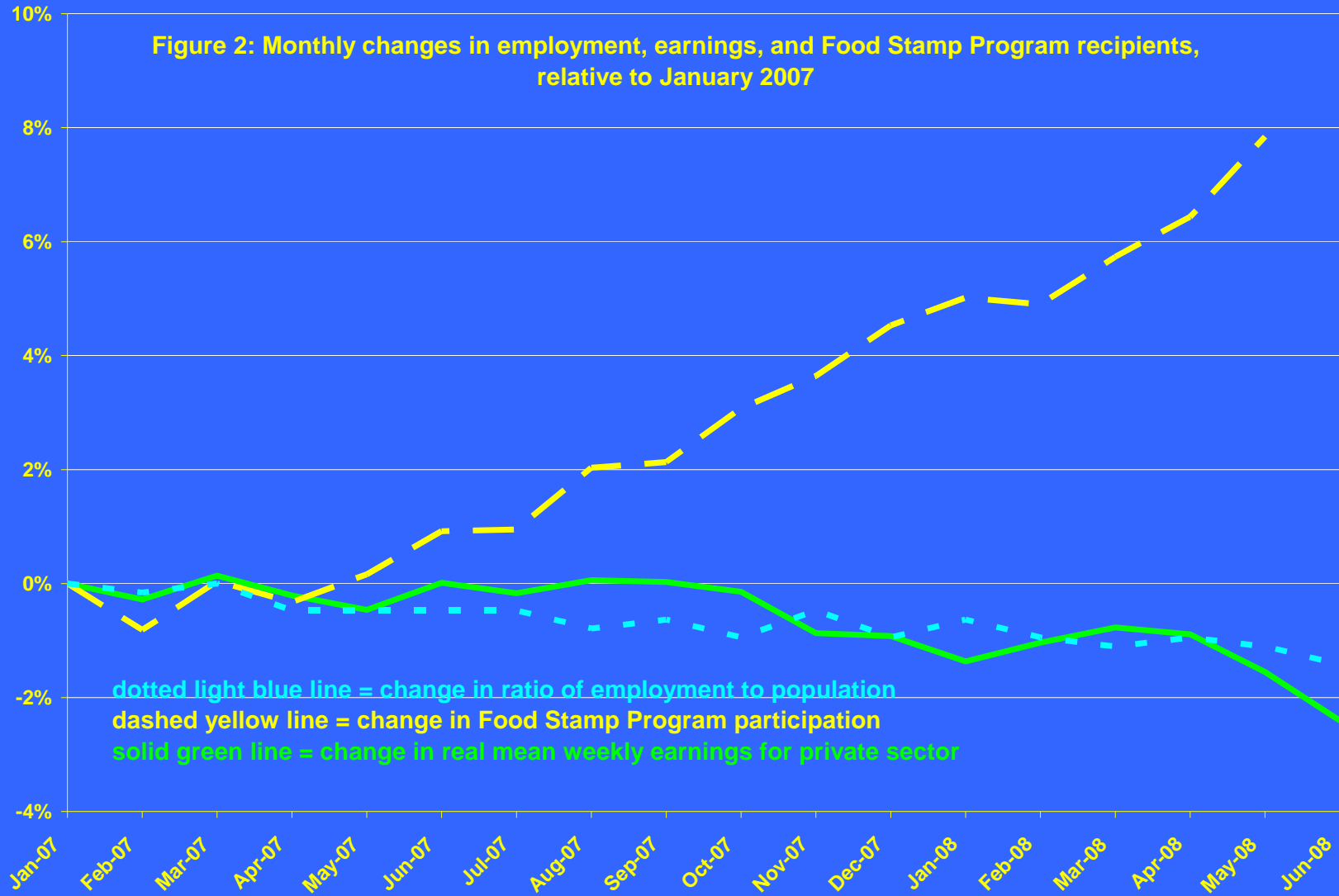
Figure 1: Poverty rate for all persons

Solid line = actual rate

Dotted line = rate predicted by model including previous year's actual as an independent variable along with changes in employment, mean weekly earnings, food stamp participants, and female family heads with children



Figure 2: Monthly changes in employment, earnings, and Food Stamp Program recipients, relative to January 2007



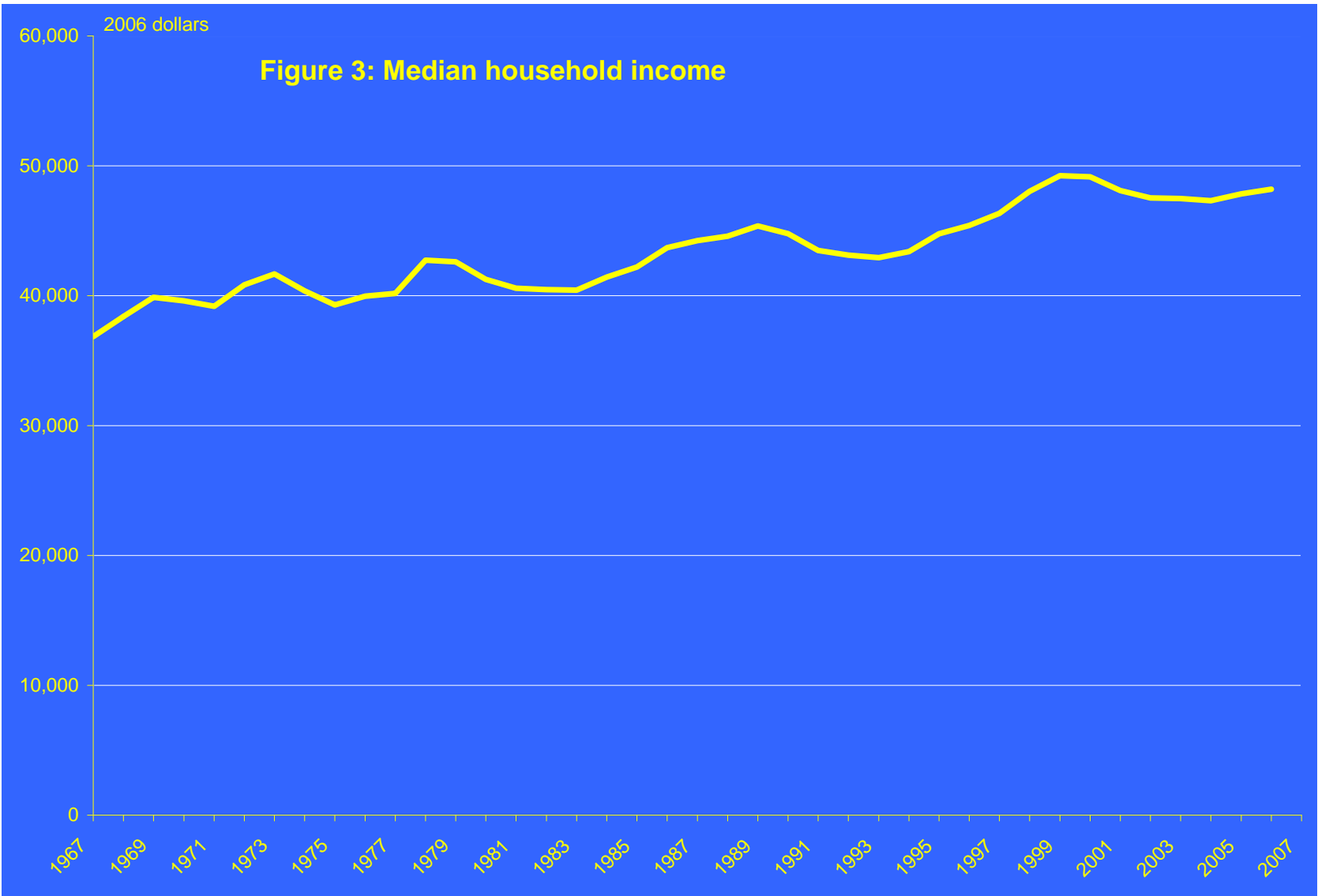


Figure 3: Median household income

