SENATE REPUBLICAN STAFF COMMENTARY

Income Inequality: Low Income Families with Children Fare Better than Most and the Middle Class is Doing Better than Recent Reports Suggest

May 31, 2007

Two recent Washington Post articles ("The Rise of the Bottom Fifth: How to Build on the Gains of Welfare Reform"[1] and "Fair to Middling in the Middle Class"[2]) highlight components of income inequality recently addressed in a study[3] released last week by Senator Brownback, the Joint Economic Committee's (JEC) Senior Republican Senator.

The first article, "The Rise of the Bottom Fifth: How to Build on the Gains of Welfare Reform," rebutted the notion that low-income families have suffered disproportionately in recent years. Instead, it revealed that between 1991 and 2005, low-income families with children achieved larger real income gains (35%) than all groups but the very highest. In terms of earnings, low-income families with children outpaced gains made by all other groups (see Figure 1).

The second article, "Fair to Middling in the Middle Class," dispelled notions of an alleged downfall of the middle class, stating that, "Rumors of the demise of the American middle class are greatly exaggerated…to the degree that the middle class is shrinking, it is because more people are rising out of it than falling from it."

Senator Brownback's study drew many of the same conclusions. In particular, the JEC Senate Republican Staff study highlighted the importance of work, education, and family structure in helping Americans achieve real income gains, and pointed out imperfections in how inequality is measured.

Further detail of the articles' main points and findings from the studies they reference are included below.

The first Washington Post article drew from a CBO study[4] that attributed an increase in work and earnings as the primary contributor to an above-average increase in real incomes of low-income families with children. Family structure also played an important role as female-headed households experienced lesser income gains (30%) than non-female headed households (35%).[5]

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[1] Haskins, Ron. "The Rise Of the Bottom Fifth: How to Build on the Gains Of Welfare Reform." The Washington Post. 29 May, 2007; p. A13.
http://www.washingtonpost.com/wp-dyn/content/article/2007/05/28/AR2007052801056.html

[2] Pearlstein, Steven. "Fair to Middling in the Middle Class." The Washington Post. 30 May, 2007; p. D01.
http://www.washingtonpost.com/wp-dyn/content/article/2007/05/29/AR2007052902001.html

[3] The Joint Economic Committee Senate Republican study, entitled "Income Inequality: Education, Marriage and Work Play a Defining Role," can be found at:
http://jec.senate.gov/republicans/_files/IncomeInequality_EducationMarriageandWorkPlayaDefiningRole_20070522_.pdf

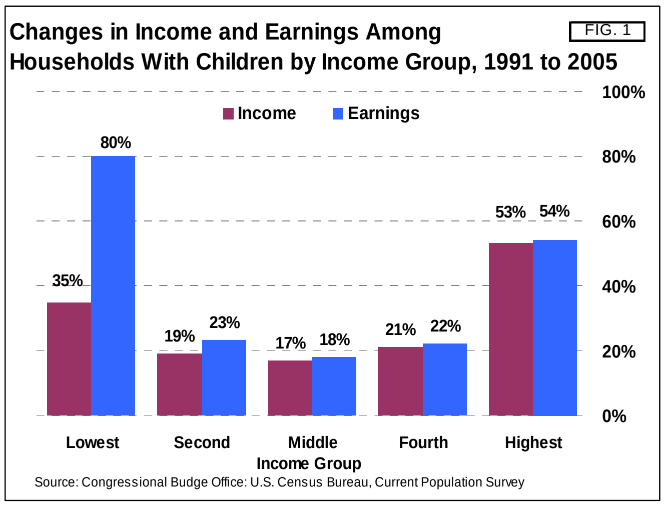
[4] "Changes in the Economic Resources of Low-Income Households with Children," May 2007, http://www.cbo.gov/ftpdocs/81xx/doc8113/05-16-Low-Income.pdf.

[5] Non-female headed low-income households with children consist of those headed by either a married couple or single male. Single males made up about 12% of the non-female headed group.

Like the Brownback JEC study, the CBO study reveals how income mobility alters the composition of low-income households over time. When individual families with children in the bottom fifth in 2001 were tracked until 2003, the average household income increased by 45%. However, when the bottom fifth of households with children in 2001 was compared to the bottom fifth in 2003 (as was done for the overall study), the average household income actually declined.

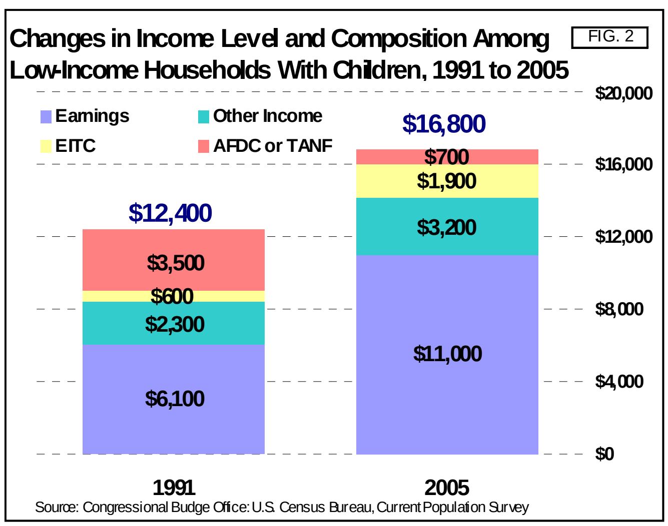
Highlights of the CBO report include:

- In addition to more favorable job market which benefited all income groups, the lowest-income households with children benefited from three policy changes:
  - Replacement of Aid to Families with Dependent Children (AFDC) with Temporary Assistance to Needy Families (TANF). The stricter work requirements and time-limits under TANF appear to have increased work and earnings among previous AFDC recipients.
  - Expansion of the Earned Income Tax Credit (EITC). The expansion helped encourage work among low-earners by supplementing wages with a larger tax credit.
  - Creation of the State Children's Health Insurance Program (SCHIP) and expansion of Medicaid. These programs increased the availability of health insurance and made it more likely for children to retain coverage even if their parent's income increased.



- From 1991 to 2005, the real average annual income of the poorest households with children (those in the bottom 20 percent, or bottom quintile) increased 35%. This increase was larger than the gains made by all but the highest income group. In terms of earnings, the poorest households achieved by far the largest gains of any group (see Figure 1).

- Low-income households with children achieved above average income gains despite significant reductions in welfare assistance primarily as a result of increased earnings (see Figure 2).

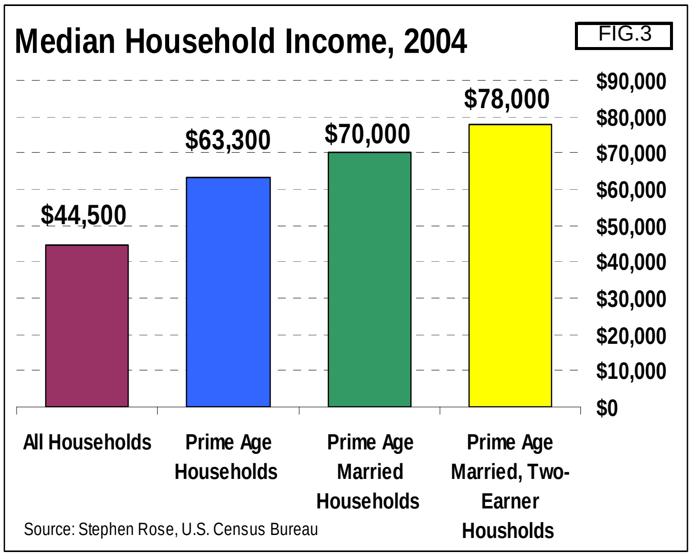


The second Washington Post article drew from analyses, conducted by economist Stephen Rose, that reveal how inequality can be distorted by comparing households of unequal sizes and ages. Additionally, Rose fully attributed the recent decline in middle-class households (defined by him to be households making between $30,000 and $90,000) to upward ascent, and disputed claims that middle class families are drowning in debt.

Highlights of Stephen Rose's analyses include:

- After adjusting the data for household size and excluding households headed by people under 29 or older than 59, median household income rose from $44,500 to $63,300 for the "typical American family" in 2004 (see Figure 3).

FIG.3



- Among married couple families in their prime working years (ages 29-59), median household income was $70,000 (and nearly $80,000 for two-earner households).

- From 1979 to 2004, the percentage of middle class households (those making between $30,000 and $90,000) fell by 8 percentage points while the percentage making more than $90,000 rose by 9 percentage points (the percentage making less than $30,000 remained about the same).

- Families are not "drowning in debt":
  - A majority of households (in 2004) held no credit card debt, and among the 46 percent who did, the median balance was $2,100.
  - Middle-class assets are up: median net worth for all households rose from $69,000 in 1989 to $93,000 in 2004.
  - Most household debt is mortgage debt, which, as a share of total debt, has increased by 8 percentage points (from 71 to 79 percent) from 1989 to 2004.
  - While the cost of some items, such as housing and healthcare, has risen faster than inflation, the cost of other items, such as food and computers, has declined in real terms.

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