

Explaining Changes in Child Poverty Over the Past Four Decades

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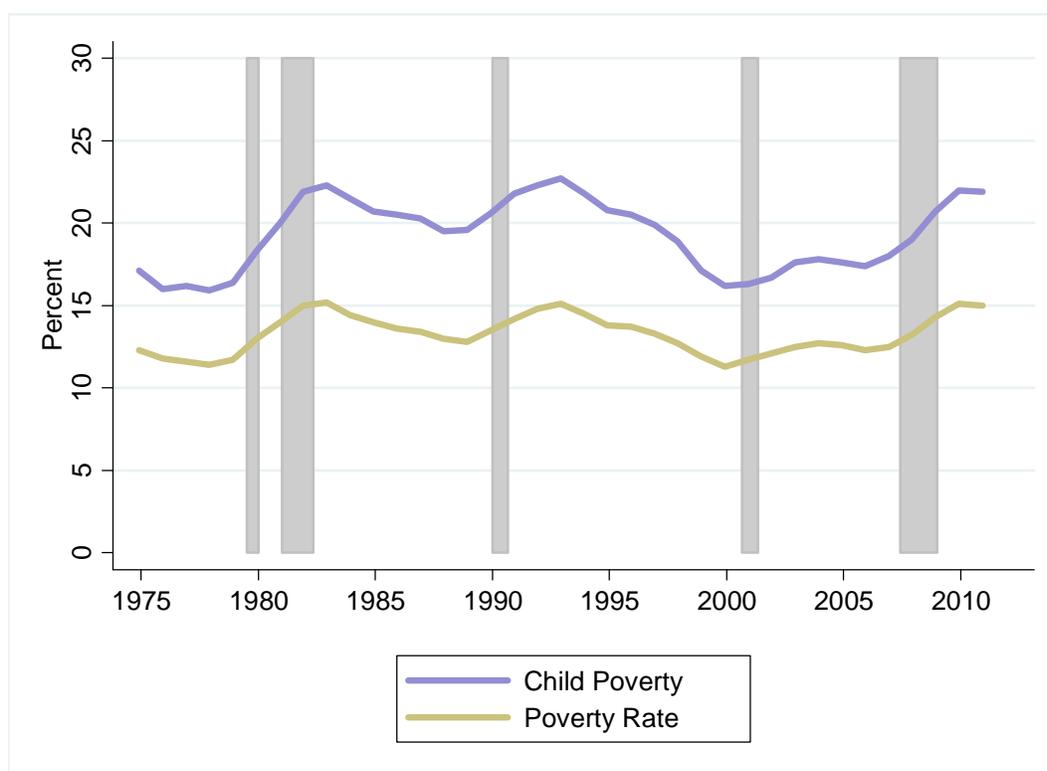
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Explaining Changes in Child Poverty Over the Past Four Decades

Child poverty rose between 1975 and 1993, then fell sharply for almost a decade until the 2001 recession. Since 2000, black and Hispanic child poverty rates have risen much more sharply than the white child poverty rate, after falling faster in the 1990s. These fluctuating child poverty rates over the last two decades (1993 to 2011) were due largely to changes in labor demand, in contrast to the earlier period (1975 to 1993), when changing family structure was the major driving force. Changes in labor demand seem to be much stronger determinants of parents' work effort than reactions to tax and transfer policy, suggesting that more generous government transfer policy may be called for.

Figure I. Child Poverty and Overall Poverty Rates, 1975–2011



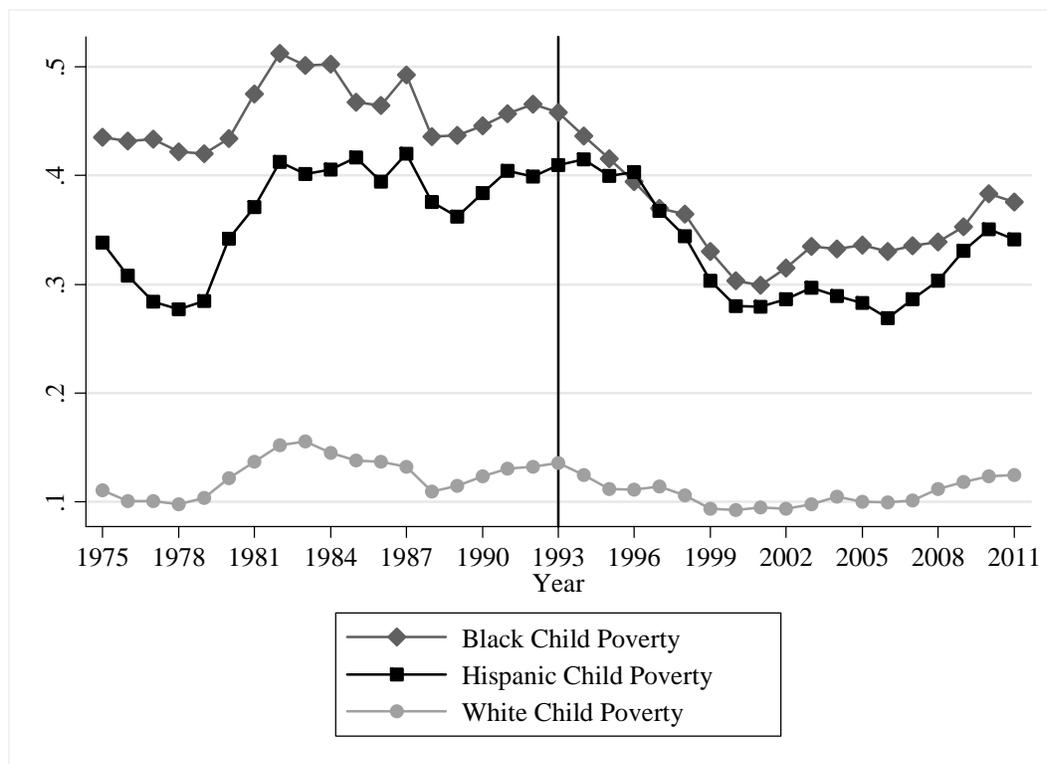
Note: Gray bars indicate recessions.

Poverty Rates

Child poverty rates fell dramatically during the late 1990s but crept back up after 2000,¹ mirroring overall poverty rates (figure 1). The midpoint of the 37-year period from 1975 to 2011, 1993, was also the year with the highest child poverty rate, and it serves as a convenient comparison point. Poverty had been ratcheting up from the early 1970s until 1993, rising from 15 percent in 1970 to 23 percent in 1993, with shorter-run changes due to recessions and recoveries. Then child poverty fell dramatically during the economic expansion of 1993 to 2000, reaching 16 percent by 2000. That year begins another structural break, with an upward trend visible after 2000 even during recoveries, and child poverty reached 22 percent in 2011.

Some of the increase from 1975 to 2000 is explained by the increasing proportion of children from groups with higher poverty rates, notably blacks and Hispanics. But rates by race and ethnicity have also changed sharply since 1975. Poverty rates for black and Hispanic children fell much more steeply than rates for white children from 1993 to 2000 but have risen more rapidly since (figure 2; the vertical line marks the midpoint, 1993).

Figure 2. Child Poverty by Race and Ethnicity, 1975–2011



Since the official poverty definition depends on income received by the family and the number of adults and children in the family, substantial changes in the child poverty rate stem from changes in either income or family structure. Changing incomes are mostly attributable to changing work attachment (gaining or losing a job or working more or fewer hours) or changing wages, since earnings are most of cash income. Cash transfers have declined in importance as an income source, and tax credits and in-kind assistance, such as food stamps, have increased in importance. Though tax credits and in-kind assistance might improve family well-being, they are not counted as income when measuring poverty. Cash transfers are mostly too small to lift a recipient out of poverty, so they have little impact on the poverty rate. Changes in family structure and work have occurred over the last four decades that can explain much of the change over time in child poverty rates in each racial and ethnic category.

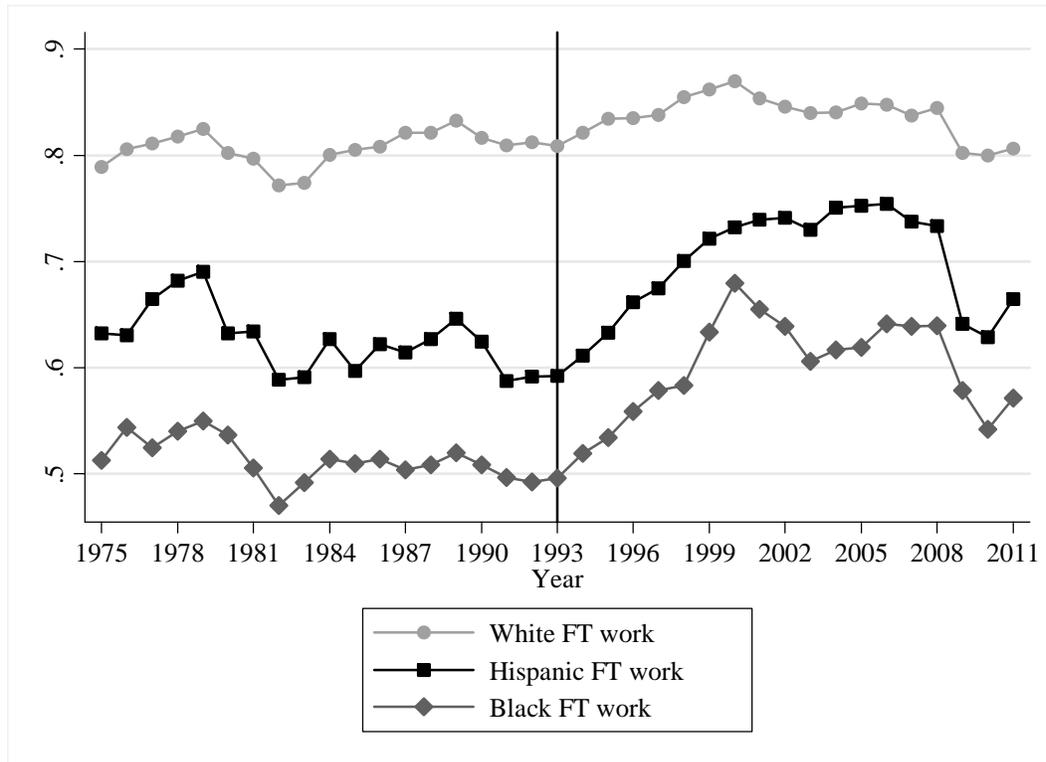
Family Structure and Work of Parents

Single parenthood is a frequently cited explanation of child poverty, and how much parents work is another. Essentially all the change in the child poverty rate between 1971 and 1989 can be explained by the increased share of families headed by single parents (Lerman 1996). Changes in family structure are particularly important when looking at how people become poor or escape poverty (Bane and Ellwood 1986). Changes in household composition (notably the birth of a child or the switch from a two-adult household to a female-headed household), employment, and disability status are the most important determinants of movements into or out of poverty (McKernan and Ratcliffe 2005).

Trends in work and marriage among parents are shown in figures 3 and 4. Figure 3 shows the proportion of children of different races and ethnicities who have at least one adult in their family working full time (at least 1,600 hours worked during the year, the equivalent of 40 weeks of 40-hour weeks or more than 30 hours per week for the whole year). The dramatic increases in these proportions in the mid- to late 1990s mirror the drop in child poverty during this time (the proportion of white children with no adult in the family working full time dropped by more than a quarter between 1993 and 2000). Other measures of work, including average hours worked or proportion working more than 1,000 hours, show similar patterns. Figure 4 shows the proportion of children of different races and ethnicities who live in a family with married parents. White and Hispanic children have been steadily less likely to have married parents over the entire period,

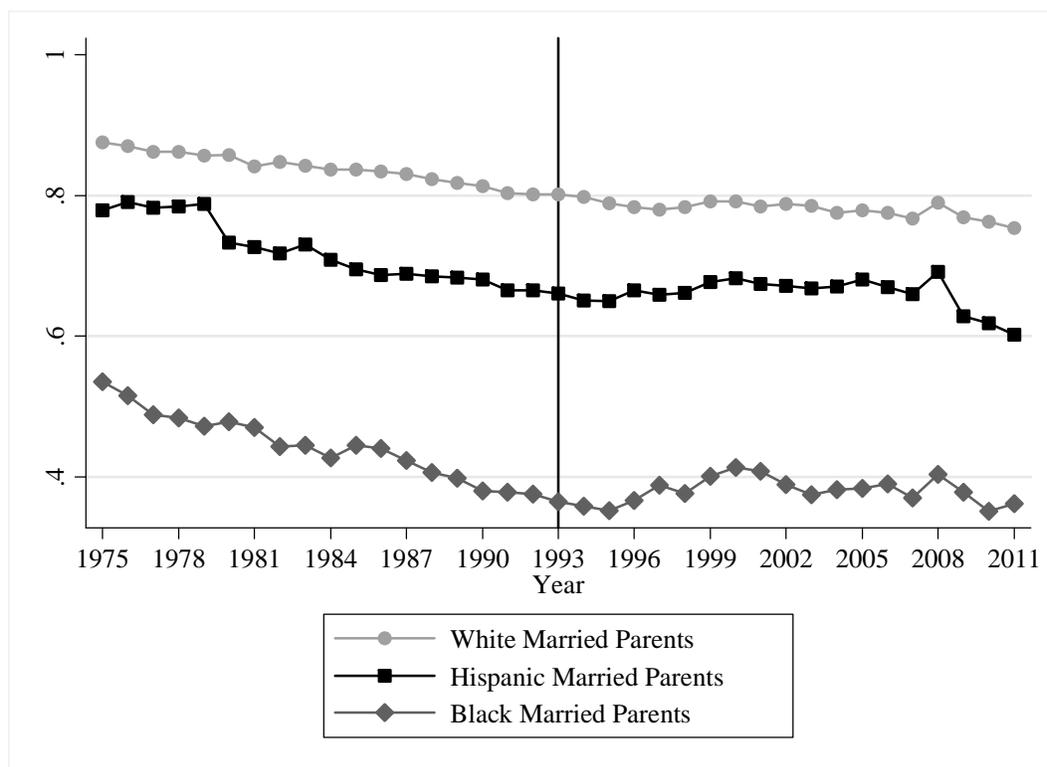
whereas 36 percent of black children had a married parent in both 1993 and 2011, with increases in that proportion between 1993 and 2011.

Figure 3. Proportion of Children with a Parent Working Full Time, by Race and Ethnicity, 1975–2011



Comparisons of figures 2, 3, and 4 indicate that secular increases in child poverty between 1975 and 1993 are related to changes in family structure. Full-time work exhibits no clear trend, while poverty trends up; at the same time, marriage trends down, indicating that shorter-run variation in child poverty is tied to work but longer-run trends are tied to family structure. While the relationship between family structure and poverty is still strong at each point in time after 1993, the changes in child poverty are not driven by family structure between 1993 and 2011. Instead, changes in child poverty track changes in parents' full-time work, and the long-term trend of increasing work explains lower poverty over the whole 18-year period. Meanwhile, the proportion married shows no such clear trend. We can formalize this observation by decomposing changes in the child poverty rate into changes due to child characteristics, such as whether they have married parents, and changes in the child poverty rates within subgroups, such as the poverty rate among children of married parents.

Figure 4. Proportion of Children with Married Parents by Race and Ethnicity, 1975–2011



Work and Family Structure Drive Changes in Child Poverty

To understand what drives a change in a measured rate such as child poverty, we can use a variety of decomposition methods, including a simple shift-share method, the related direct standardization method used by Lichter, Qian, and Crowley (2005), the Oaxaca decomposition method used by Nichols (2006), or a reweighting method called DFL decomposition (DiNardo, Fortin, and Lemieux 1996), which allows us to see the impact of many characteristics. The DFL decomposition reweights the data to take account of shifts in many characteristics at once, whereas we can only look at one characteristic at a time with the simple shift-share analysis, though shift-share analysis finds essentially the same pattern.² Essentially, the DFL method estimates what child poverty would have been, had the distribution of some set of characteristics not changed, and we are free to add any characteristics to the set.

The DFL decomposition results shown in figures 5 through 9 include controls for parent and child age categories, number of people in the family, complex families (not just parents and children), marital status of adults in the family, five categories of work attachment (adult working the most works 0–400 hours, 400–800 hours, 800–1,200 hours, 1,200–1,600 hours, or more), and four

categories of educational attainment of adults in the family (high school dropout, high school graduate, some college, or bachelor's degree or greater).

Figures 5 and 6 present results for two periods. Figure 5 shows changes from 1975 to 1993, when child poverty increased, and figure 6 shows changes from 1993 to 2011, with a large decrease in child poverty and subsequent increase, almost to 1993 levels. (Results comparing the 1993–2000 decrease and 2000–2011 increase, not presented here, lead to similar conclusions.) Consistent with findings based on a simple shift-share analysis, the DFL decomposition of changes ascribes a large fraction of the change in child poverty between 1975 and 1993 to changes in age and family structure (single parenthood, number of family members, multigenerational households), as shown in figure 5. Drops in child poverty between 1993 and 2011 are largely due to increased work effort by parents, as shown in figure 6.

Changes in the age and family structure of white children predict a 2.1 percentage point increase in child poverty, which is 85 percent of the 2.5 percentage point actual increase between 1975 and 1993. Changes in work among parents from 1975 to 1993 tended to operate in the wrong direction, shown as a negative percent of change in child poverty explained. In other words, among white children, we would have predicted child poverty would have fallen by 1.7 percentage points due to increased work by parents, holding other factors constant, which is shown on figure 5 as -67 percent of the actual change.

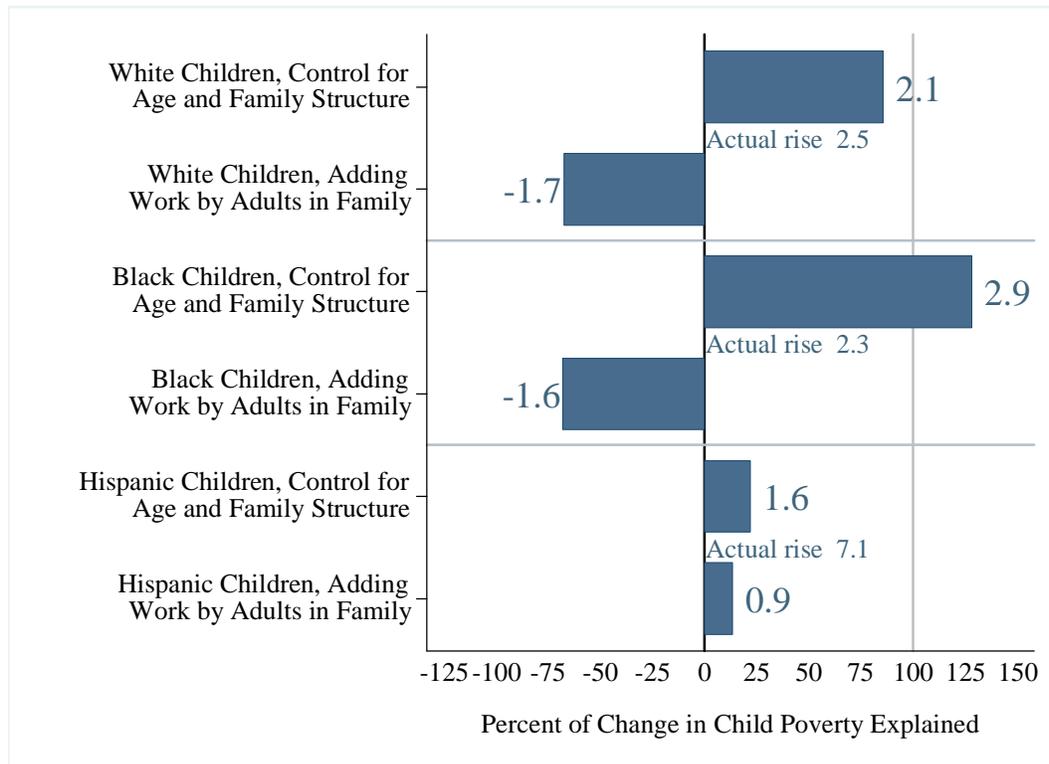
Changes in the age and family structure of black children predict a 2.9 percentage point increase in child poverty, which is more than the 2.3 percentage point actual increase between 1975 and 1993, and thus is shown as more than 100 percent of the actual rise explained on figure 5. Changes in work among parents of black children from 1975 to 1993 pushed down poverty 1.6 percentage points, holding other factors constant. Thus changes in work effort among these parents went in the wrong direction to explain the observed change in poverty, which is shown on figure 5 as -67 percent of the actual change explained.

Changes in the age and family structure of Hispanic children predict a 1.6 percentage point increase in child poverty, which is 22 percent of the actual 7.1 percentage point rise in child poverty among Hispanics. Changes in work among parents of Hispanic children from 1975 to 1993 pushed child poverty up another 0.9 percentage points, holding other factors constant, which is shown on figure 5 as an additional 13 percent of the actual change explained.

In short, changes in work among parents from 1975 to 1993 tended to operate in the wrong direction, shown as a negative percent of change in child poverty explained, whereas changes in the

age of children and parents and in family structure tended to explain a large fraction of the observed change in child poverty.

Figure 5. Explaining Increased Child Poverty from 1975 to 1993 Using DFL Decompositions



In contrast, changes in family structure do not explain changes in child poverty between 1993 and 2011 (figure 6), and changes in work explain most of the change in child poverty. Changes in the age and family structure of white children predict a 1.1 percentage point increase in child poverty between 1993 and 2011, but child poverty actually fell 1.1 percent, so those factors are shown on figure 6 explaining -96 percent of the actual change. Changes in work among parents from 1993 to 2011 pushed down poverty by 0.8 percentage points, shown as 69 percent of the actual change.

Changes in the age and family structure of black children predict a 0.6 percentage point decrease in child poverty, only 8 percent of the actual 8.2 percentage point drop between 1993 and 2011. Changes in work among parents of black children from 1975 to 1993 pushed down poverty an additional 4.6 percentage points, holding other factors constant, shown on figure 6 as 55 percent of the actual change explained.

Changes in the age and family structure of Hispanic children from 1993 to 2011 predict a 0.9 percentage point increase in child poverty, which is 14 percent of the actual 6.8 percentage point

drop in child poverty among Hispanics, but in the wrong direction, shown as -14 percent explained on figure 6. Changes in work among parents of Hispanic children pushed child poverty down 4.7 percentage points, which is shown on figure 6 as 69 percent of the actual change explained.

The comparisons year by year in figures 7, 8, and 9 show that controlling for parental work keeps poverty rates much more constant in the comparison of each year to 1993 for almost every year after 1993, by race and ethnicity. If the line marked “additionally control for work” were perfectly flat, then changes in work would account for all of the change in child poverty. Holding constant work effort by parents does more to explain changes in child poverty rates in every year since 1993 than controlling for age and family structure, or adding education controls. This is true for black and Hispanic children, at least, whereas among white children work is of primary importance in every year up to 2009, when educational attainment becomes necessary to explain changes in child poverty.

Not all changes are explained by changing work and family structure. Shifts toward lower educational attainment among parents appear to explain some of the increase in child poverty between 2000 and 2011, in every race and ethnicity, as seen in figures 7, 8, and 9. We can also see from figures 7, 8, and 9 that the changes in poverty around 1980 are not well explained by any of the candidate explanations, which suggests that changes in the real wages of parents were the dominant force driving changes in poverty at that time. In 1979, an inflation crisis drove down real wages and wages did not recover for most workers in the subsequent recessions of 1980–82. The opposite change in wages is observable in the late 1990s, when wage increases among parents drove the unexplained portion of falling child poverty, at the same time that increasing work explained a large part of the drop.

Many other determinants of parental earnings in turn affect child poverty rates, including differential fertility patterns by wage and education, and immigration. Immigration and fertility can change the composition of parents not only by changing their racial and ethnic makeup, and education and family structure, but also by changing the wage distribution. Much of the change in fertility and immigration has been concentrated in Hispanic families, with smaller changes in black and white families. Successive waves of Hispanic immigrants have tended to have lower wages (Borjas 2005). Immigrants tend to have wages that reflect the economic development of their birth country (Favreault and Nichols 2011), and this is true in Hispanic, white, and black families. However, more immigrants have come from less-developed countries during the entire period of

study, meaning that the drop in poverty from 1993 to 2000 and rise from 2000 to 2011 is not well explained by changes in the composition of immigrants.

Figure 6. Explaining Decreased Child Poverty from 1993 to 2011, Using DFL Decompositions

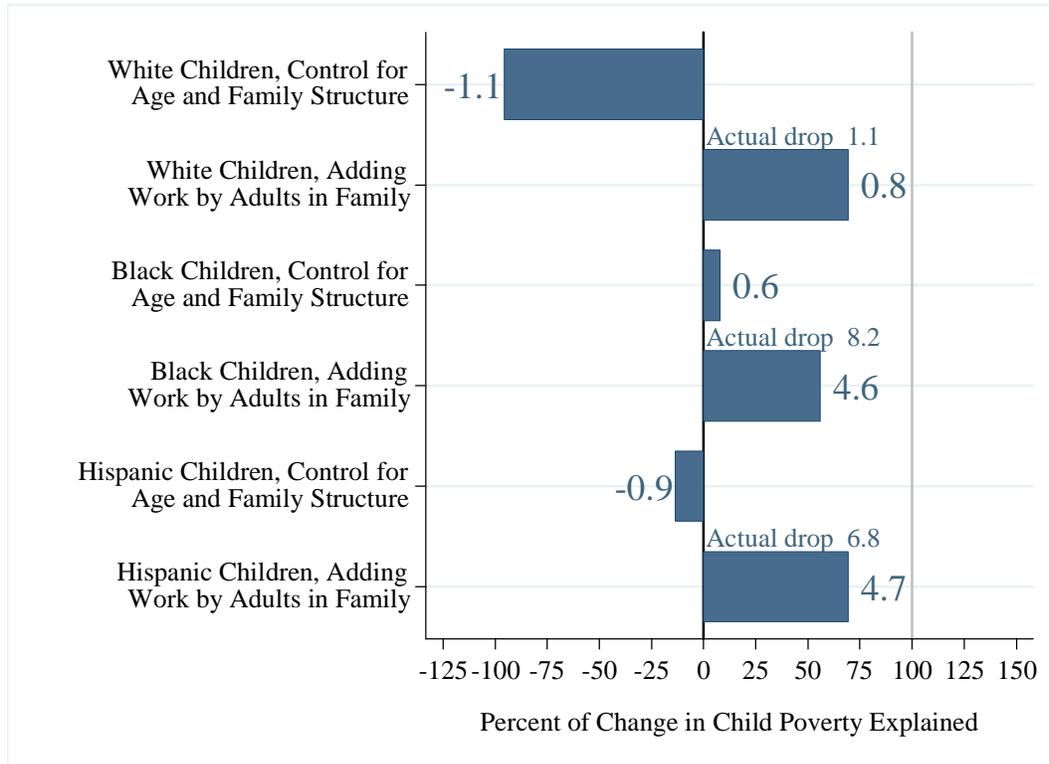


Figure 7. DFL Decomposition Results for Black Children, Each Year Compared to 1993

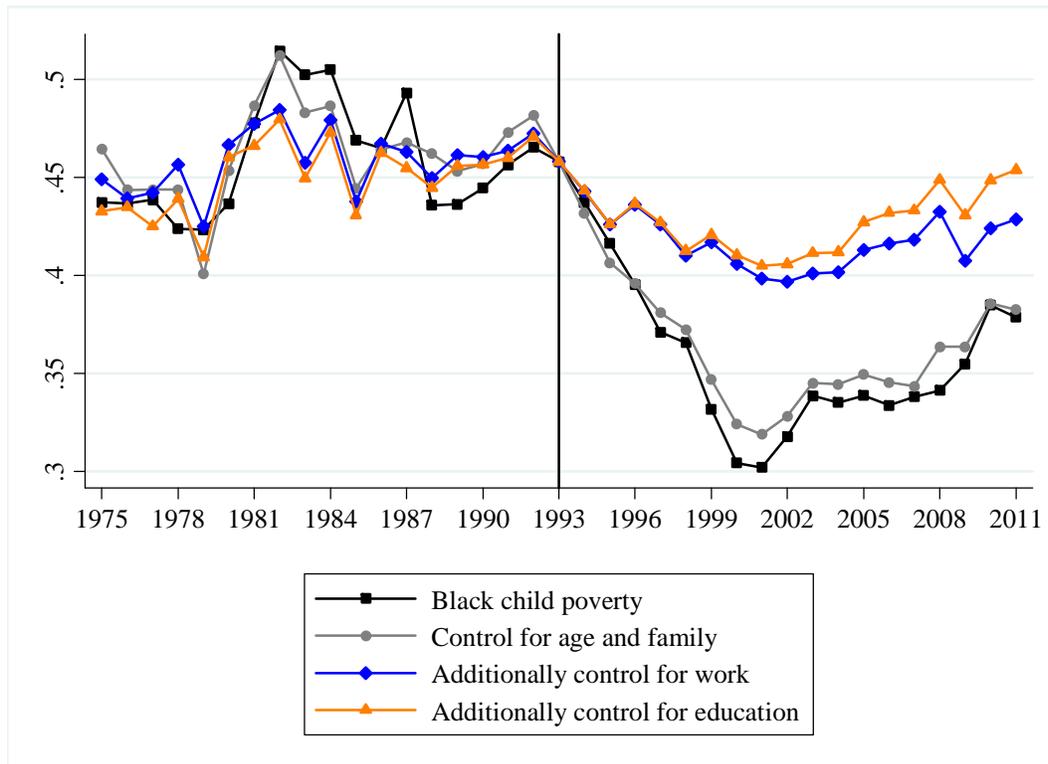


Figure 8. DFL Decomposition Results for Hispanic Children, Each Year Compared to 1993

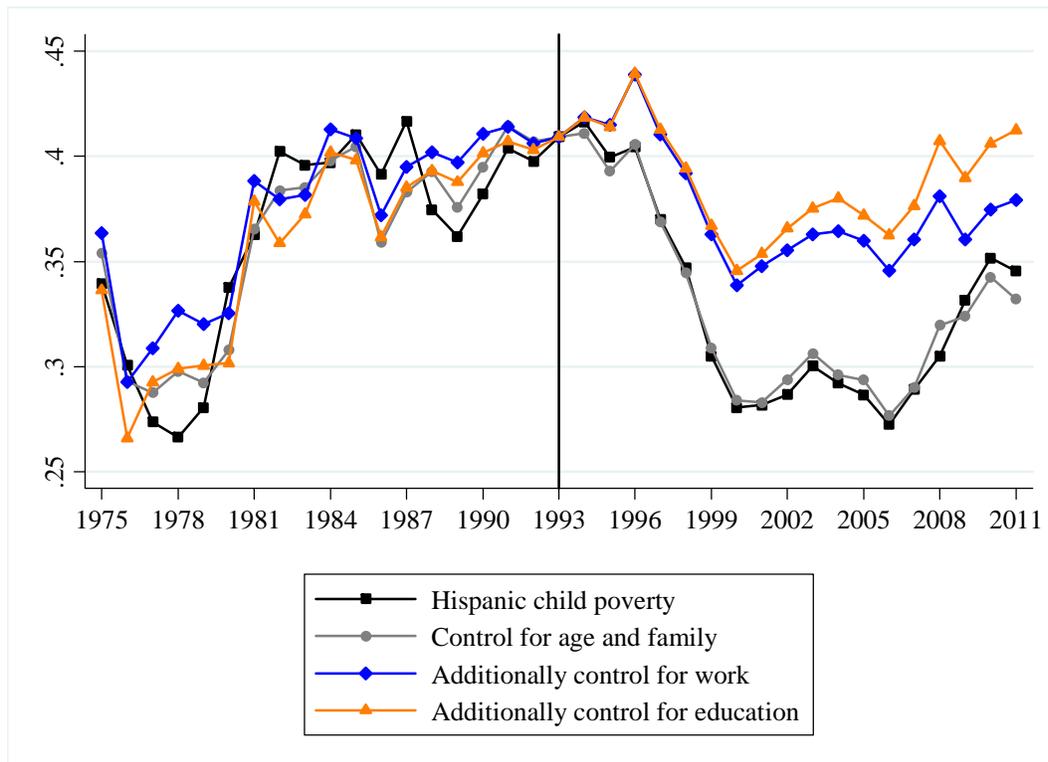
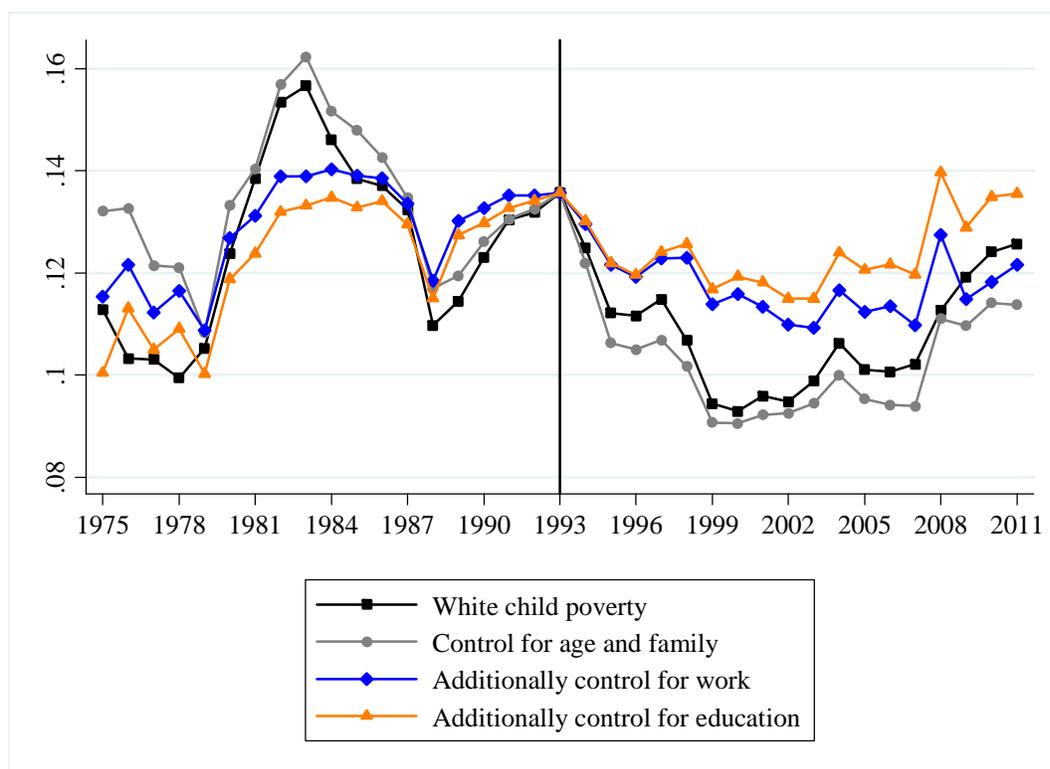


Figure 9. Decomposition Results for White Children, Each Year Compared to 1993



Tax and Transfer Policy Affects Work by Parents

Having found that child poverty rates in the past 20 years were driven largely by changes in parental work, it is natural to ask what drives these changes. There are several explanations for changes in parental work patterns over 1993–2011, including changes in tax policy, changes in transfer policy, demographic changes and immigration, and changes in the demand for workers. Because the focus here is on poverty, we care less about what happens in the upper half of the income distribution, which leads to the focus on tax and transfer policies targeted to low-income households.

Received wisdom about increasing labor force participation in the 1990s is that most of the expansion among single mothers stemmed from a more generous earned income tax credit (EITC) and increasing labor demand, with welfare reform and other policy changes have a smaller impact (Meyer and Rosenbaum 2001). There are many studies on the effect of the EITC and welfare reform. Work on the EITC (such as that by Eissa and Hoynes 2006) tends to show that while the EITC expansions should theoretically increase work at lower levels but discourage work at higher income levels as the credit is phased out, the only effect on behavior seems to be on the extensive margin (whether people work or not); the hypothesized reductions in hours of work at higher

income levels are not observed in the data. Effects on fertility and marriage are also not seen in the data.

Work on the effects of welfare reform tends to show that policy changes reducing effective tax rates on earnings increased labor force participation only modestly (Blank 2002). Those labor force participation increases also seem to have produced no change in pretax wages (e.g., Grogger 2003), suggesting labor demand also increased. Some studies even estimate a positive slope to the labor demand curve for women (Borjas 1986), which implies either a very strange labor demand story or that labor demand was shifting outward during the 1980s, leading us to mistakenly conflate supply and demand changes.

There is some evidence that single mothers most affected by EITC expansions experienced increased employment and higher pretax wages as a result of the subsidy, though one would expect pretax wages to fall as participation increases due to lower effective tax rates (Eissa and Nichols 2005). This is also consistent with a positively sloped labor demand for that group, though estimates differ as to the incidence of the EITC (Leigh 2010; Rothstein 2010). Certainly, wages rose for groups induced to work in the 1990s by tax and transfer incentives, suggesting labor demand was increasing faster than labor supply. The increase in labor supply in 1994–2000 came mostly after welfare reform and the EITC, especially during 1998–2000, while subsequent reductions in effective tax rates do not seem to have further increased labor force participation.

Important recent changes in tax and transfer policy are not counted toward child poverty, in particular tax credits and food assistance. Food assistance would not affect poverty by itself, even if it were counted, because it is worth too little to lift many children out of poverty. Tax credits such as the EITC and the refundable portion of the child tax credit would have an impact on child poverty if they were counted as income, but the impact would be focused on the year or two when poverty fell due to increased work, so poverty would appear to fall even faster during the mid-1990s were tax credits counted. There would be little change over the post-1993 period, however, as the amounts have not changed enough to change the proportion of children moved into or out of poverty since then.

The importance of tax and transfer policy on levels of work among parents is paramount, as tax and transfer policy is the main lever available to affect work decisions. Clinton ran on a platform of ending welfare as we know it primarily because of concerns about the impact of work creating a culture of poverty in low-income families. Conditional on the government promoting economic expansion and job creation as much as it can, the government also wants to promote work by low-

income parents in part to avoid social costs associated with paying transfers to people who would work were the transfers not available (incurring deadweight losses) and in part to encourage a habit of work that might be transmitted to the next generation. In general, the social cost of transfers is tied closely to how responsive parents are to transfer policy; if a small decrease in transfers induces many more people to work then the social cost of the transfer is high, but if people are unresponsive to transfer amounts then the social cost of the transfer is low (Chetty 2008).

One way to summarize impacts of tax and transfer policy on parental work is to regress full-time work by at least one parent on effective tax rates (due to income and payroll taxes and welfare policy) and minimum wages (a higher minimum wage lowers employment in the long run but increases it in the short run). Over a long period, work by parents increased in response to policy changes lowering the disincentives to work (table 1). However, there were numerous changes in incentives to work after 1993, yet the regression shows no evidence of substantive changes in labor force participation caused by the substantial changes in tax and transfer policy after 1993. This could be because people became less sensitive to changing tax and transfer policy, or because other changes were simply so much more important that they swamp the effects due to policy.³

Table I. Regressions of Parental Full-Time Work on Work Incentives (Factors Affecting Take-Home Earnings)

	All Children			Single Parents		
	White	Black	Hispanic	White	Black	Hispanic
Data drawn from 1977 to 2009						
Real minimum wage	-0.0106*** (-4.53)	-0.00598 (-1.71)	-0.0112* (-2.33)	-0.0117** (-2.82)	-0.00276 (-0.58)	-0.0156* (-2.67)
Income and payroll tax rate on part-time minimum-wage work	-0.0929*** (-5.02)	-0.0743** (-2.88)	0.0741 (1.36)	0.00459 (0.19)	-0.0405 (-1.48)	0.0567 (1.10)
Welfare effective tax rate on part-time minimum-wage work	-0.00536 (-0.37)	-0.0711* (-2.45)	0.0131 (0.37)	0.0565 (1.63)	-0.106* (-2.34)	0.0140 (0.31)
Observations	2,078,042	384,179	532,996	388,486	226,643	167,362
Data drawn from 1994 to 2009						
Real minimum wage	-0.00718* (-2.27)	0.00334 (0.51)	-0.0209*** (-4.32)	-0.0171* (-2.08)	0.000674 (0.07)	-0.0206* (-2.08)
Income and payroll tax rate on part-time minimum-wage work	0.120*** (6.57)	0.169*** (5.93)	0.296*** (4.70)	0.0892*** (4.36)	0.134*** (4.03)	0.184*** (4.37)
Welfare effective tax rate on part-time minimum-wage work	0.00771 (0.31)	-0.0156 (-0.43)	-0.0237 (-0.39)	-0.0455 (-1.17)	-0.0125 (-0.22)	-0.0701 (-0.98)
Observations	964,497	187,330	306,372	207,783	114,688	101,446

* $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$; t statistics in parentheses robust to clustering on state

Notes: Regressions include state fixed effects and controls for ethnicity, family size, age and family structure, and educational attainment of parents. CPS data do not identify state before 1977, and explanatory variables are not available for all states after 2009.

Higher minimum wages result in lower rates of work in most regressions. If we split this into short-run and long-run impacts as in Baker, Benjamin, and Stanger (1999), this is due to a positive short-run impact on work and a larger negative long-run impact as employers substitute away from minimum-wage workers.

The impact of higher taxes on small amounts of earnings (measured as income and payroll tax rates on part-time, minimum-wage work by state and year) is negative for the whole time period, but positive in the latter half of it. The effect of higher effective tax rates on work due to welfare policy (which change as maximum benefits and earnings disregards change by state and year) is negative only for black children over the whole period, and statistically indistinguishable from zero in the latter half of the period examined.

Changes to tax and transfer policy can also induce changes in family structure, but marital status and fertility decisions have reacted very little to changes in policy from 1993 to 2011 (Crump, Goda, and Mumford 2011; Ellwood 2000).

The absence of impacts on work by parents of the changing incentives to work embodied in tax and transfer policy from 1994 to the present supports the idea that a substantial part of the large changes in work observed in recent years stemmed from fluctuations in labor demand, not shifts in labor supply due to changing incentives.

Conclusions

Child poverty rates have fallen during the 1990s and risen since 2000 mostly because of the changing labor market experiences of parents, in contrast to earlier decades when changes in family structure played a larger role. Increased labor force participation in the 1990s was caused less by policy changes reducing effective tax rates on earnings and more by increasing labor demand. This suggests that more generous transfer policies targeted at children might not drive down labor supply among parents but could improve child well-being.

The benefits of small reductions in child poverty are high. Holzer and colleagues (2008) suggest that a 1 percentage point increase in child poverty might cost the economy an extra \$28 billion a year in the future, partly because children who grow up poor earn less. If the social costs of lowering child poverty rates are lower than commonly thought, more generous tax and transfer policy for parents is in order.

Notes

1. The source for all reported findings are author's calculations using Current Population Survey March supplement data, 1976 to 2012, now known as the Annual Social and Economic Supplement, augmented with state-specific data from Nichols and Kassabian (2012). The CPS data are the source of official poverty statistics reported by the Census every September for the prior calendar year. While there have been many criticisms of the official poverty definition for not counting some resources (tax credits and in-kind assistance) and some costs (child care, out-of-pocket health spending, and housing), poverty remains the official measure that guides policy decisions, so we will examine changes in child poverty using the official poverty threshold. We define black throughout as non-Hispanic black and white as non-Hispanic white, which limits us to 1975 and later data, when reliable indicators of Hispanic ethnicity are available.

2. The simple shift-share analysis takes a change in poverty rates between two years, call them 0 and 1, and ascribes part to changes in shares or parents working or married and part in changes in poverty rates in each subgroup. If we call s_1^m the share married in year 1 and s_0^m the share married in year 0, and s_1^u the share unmarried in year 1 and s_0^u the share unmarried in year 0, with p_1^m the poverty rate of children with married parents in year 1 and p_0^m the poverty rate of children with married parents in year 0, then the change in poverty Δp (p_1 minus p_0) can be written

$$\begin{aligned}\Delta p &= (s_1^m p_1^m + s_1^u p_1^u) - (s_0^m p_0^m + s_0^u p_0^u) \\ &= (s_1^m p_1^m - s_0^m p_1^m) + (s_1^u p_1^u - s_0^u p_1^u) \\ &\quad + (s_0^m p_1^m - s_0^m p_0^m) + (s_0^u p_1^u - s_0^u p_0^u) \\ &= (\Delta s^m p_1^m + \Delta s^u p_1^u) + (s_0^m \Delta p^m + s_0^u \Delta p^u)\end{aligned}$$

Thus, the change in poverty is algebraically due to a change in shares s weighted by poverty rates, and a change in poverty rates p weighted by shares.

Using this shift-share method, more than 100 percent of the rise in child poverty between 1975 and 1993 can be explained by changes in family structure among black and Hispanic children (implying changes in within-group rates have a negative contribution, meaning that they work to push poverty in the direction opposite to the way it actually changed over that period). Instead of marriage, we can examine the share of children with at least one parent or guardian working full time, to conclude that changes in work explain about half of the change in child poverty between 1975 and 1993 among black and Hispanic children. Among white children, changes in family composition explain about a quarter of the observed change, while changes in work explain negative one-quarter of the observed change.

To better understand proportions explained, consider white children in 1975 and 1993. White child poverty rose from 11.1 percent to 13.6 percent, a 2.5 percentage point increase. The share with married parents fell 7 percentage points, and the poverty rate among those with married parents was lower than that among children without married parents (12 percent versus 21 percent in 1993). The latter group increased by 7 percentage points. The shift away from married parents pushed up the overall rate by 0.6 percentage points (-0.07 times 0.12 plus 0.07 times 0.21), about a quarter of the actual 2.5 percentage point increase. Hence the “unexplained” portion due to changing within-group poverty rates accounted for three-quarters of the change in child poverty by this measure.

In contrast, the share of white children with a parent working full time rose 2 percentage points, and the poverty rate in the full-time group was about 7 percent in 1993. The share without a working parent dropped 2 percentage points, and the poverty rate in that group was about 41 percent in 1993. The shift toward having a parent working full time pushed down the overall rate by 0.6 percentage points (0.02 times 0.07 plus -0.02 times 0.41), about a quarter of the actual 2.5 percentage point increase but in the wrong direction—that is, white child poverty would have decreased 0.6 percentage points due to increased work had within-group rates not changed. The increased in poverty rates within group drove up child poverty 3.1 percentage points, for a net increase of 2.5 percentage points.

Changes in white child poverty between 1993 and 2011 are explained by neither changes in the proportion of parents working full time nor changes in proportion married, according to shift-share analysis (both work and marriage have a negative percent explained). In contrast, increased full-time work explains 63 percent of the change for black children and 82 percent of the change for Hispanic children, while changes in proportion married works in the wrong direction. So the shift-share analysis tends to support the notion that family structure changes explained more of the change in child poverty during the first half of the period we examine, and work more in the second half. However, shift-share analysis is a blunt method of ascribing explanatory power.

3. The observed connections between changes in full-time work and changes in policy affecting incentives to work could also be partly attributable to states increasing tax credits or changing welfare policy when employment falls. But, if we assume policy changes are responding to parental work, we can ascribe the changes in work to changes in state policy.

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