Preview
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12th Edition

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U.S. POVERTY RATES HIGHER, SAFETY NET WEAKER THAN IN PEER COUNTRIES

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Poverty rates in the United States increased over the 2000s, a trend exacerbated by the Great Recession and its aftermath. By 2010, just over 46 million people fell below the U.S. Census Bureau's official poverty line (according to data from the Current Population Survey). This preview of *The State of Working America, 12th Edition* puts the U.S. experience with poverty in an international context, comparing the lower end of the wage and income distribution in the United States with that of "peer" countries, largely countries within the Organisation for Economic Co-operation and Development (OECD) with roughly similar GDP per hour worked as the United States.

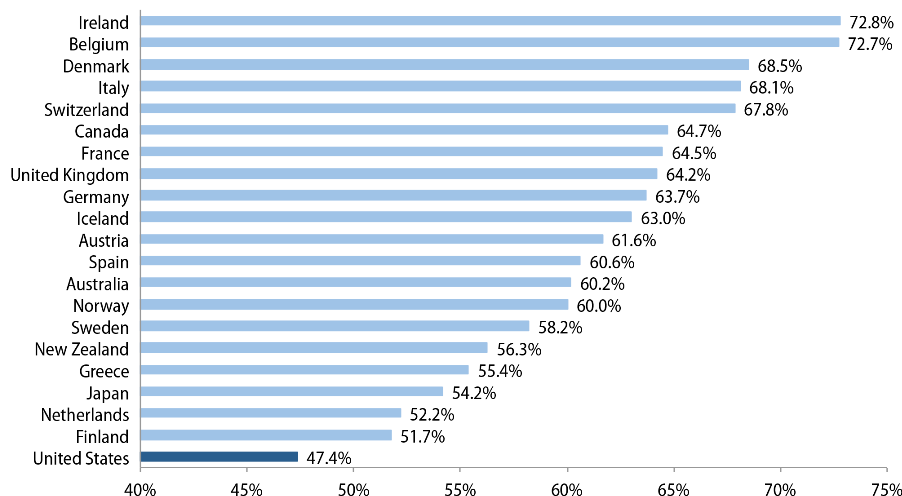
The first part of this preview provides a general comparison of poverty and the earnings distribution in the United States and peer countries. Next, it examines the extent to which resources go to the bottom, focusing specifically on the tax and transfer system that redistributes market income and provides a safety net to keep people out of poverty, or to help those who fall into poverty due to unexpected job losses or other reversals get back on their feet.

Poverty and the earnings distribution

One particular point of interest in international comparisons, shown in **Figure A**, is the ratio of earnings (wages) at the 10th percentile of the earnings distribution to earnings of the median worker. This measures how workers at the bottom fare in relation to the typical worker, with a lower number implying more inequality. As the figure shows, earnings at the 10th percentile in the United States

FIGURE A

Earnings at the 10th percentile as a share of median worker earnings in selected OECD countries, late 2000s



Note: Earnings is generally defined as gross earnings (wages prior to tax deductions or adjustments) for full-time, full-year workers.

Source: Authors' analysis of Organisation for Economic Co-operation and Development's *Distribution of Gross Earnings* metadata (data group labelled "late 2000s")

are less than half (47.4 percent) of those of the typical worker. This is the lowest share in the figure and is far below the (unweighted) peer average of 62.0 percent.

Figure A shows that earners at the 10th percentile in the United States are further from the U.S. median than 10th-percentile earners in peer countries are from their own countries' respective medians. However, median earnings vary across countries. Thus, the data in Figure A do not directly tell us how well-off workers at the 10th percentile in other countries are compared with U.S. workers at the 10th percentile.

Figure B directly compares the level of earnings (a measure of living standards) of low-earning workers in the United States with the living standards of low-earning workers in peer countries. The figure is scaled such that earnings at the 10th percentile in the United States equal 100 percent, making it easy to identify countries with higher relative earnings by their longer bars.

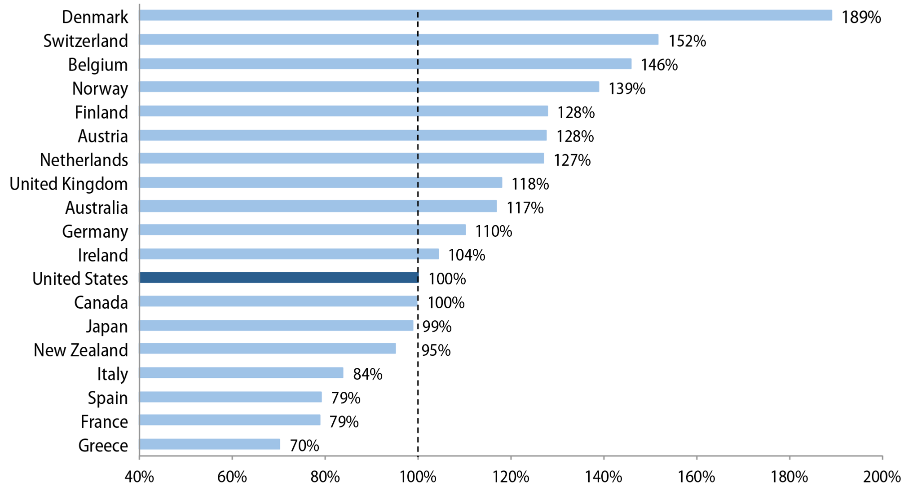
Despite the relatively high earnings at the top of the U.S. income scale (as illustrated in the forthcoming *The State of Working America, 12th Edition*), inequality in the United States is so severe that low-earning U.S. workers are actually worse off than low-earning workers in all but seven peer countries. As shown in the figure, the United States ranks 12th out of the 19 peer countries shown.

Turning to an international comparison of poverty rates, we examine the share of the population living below half the median household income in the United States and select OECD countries, a measure known as the relative poverty rate.

According to **Figure C**, in the late 2000s, 17.3 percent of the U.S. population lived in poverty—the highest relative poverty rate among OECD peers. The U.S. relative poverty rate was nearly three times higher than that of Denmark, which had the lowest rate (6.1 percent), and about 1.8 times higher than the (unweighted) peer country average of 9.6 percent.

FIGURE B

Earnings at the 10th percentile in selected OECD countries relative to the United States, late 2000s

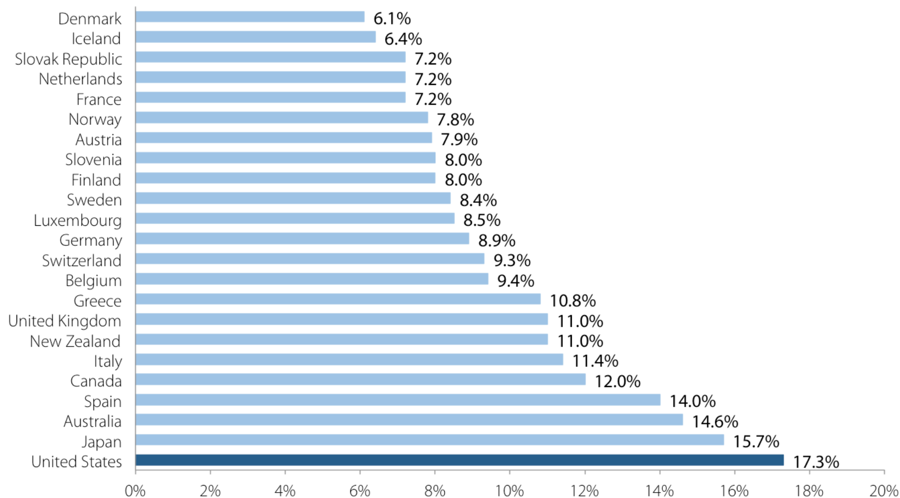


Note: Earnings is generally defined as gross earnings (wages prior to tax deductions or adjustments) for full-time, full-year workers.

Source: Authors' analysis of Organisation for Economic Co-operation and Development's *Distribution of Gross Earnings* metadata (data group labelled "late 2000s")

FIGURE C

Relative poverty rate in the United States and selected OECD countries, late 2000s

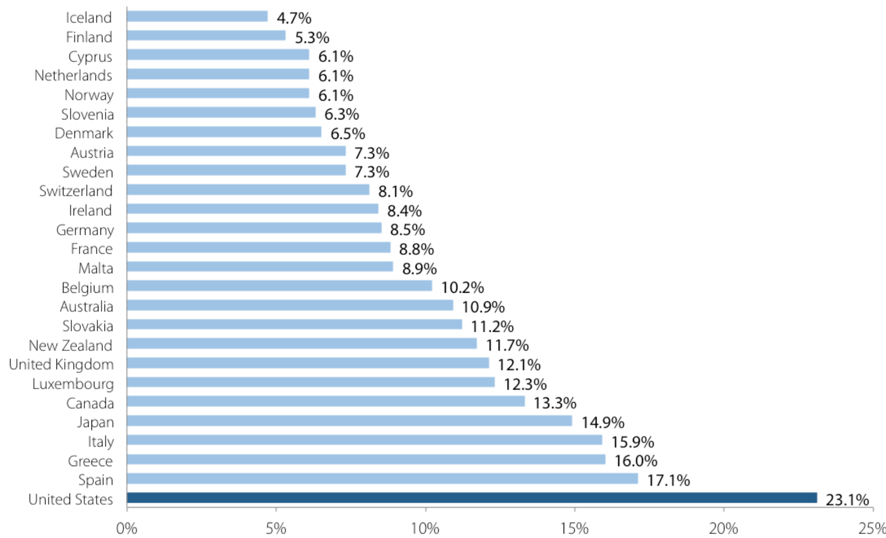


Note: The relative poverty rate is defined here as the share of individuals living in households with income below half of household-size-adjusted median income. Poverty rates are based on income after taxes and transfers.

Source: Authors' analysis of Organisation for Economic Co-operation and Development *Stat Extracts* (data group labelled "late 2000s")

FIGURE D

Child poverty rates in selected developed countries, 2009



Note: The child poverty rate is the share of children living in households with income below half of household-size-adjusted median income.

Source: Adamson (2012, Figure 1b)

While the overall relative poverty rate in the United States is higher than that of peer countries, the extent of child poverty is even more severe, as shown in **Figure D**. In 2009, the United States had the highest rate of child poverty among peer countries, at 23.1 percent—meaning that more than one in five children in the United States lived in poverty (as measured by the share of children living in households with household income below half of median household income). This level is almost five times as high as that of Iceland, which had the lowest level, at 4.7 percent, and over two times higher than the (unweighted) peer-country average of 9.8 percent.

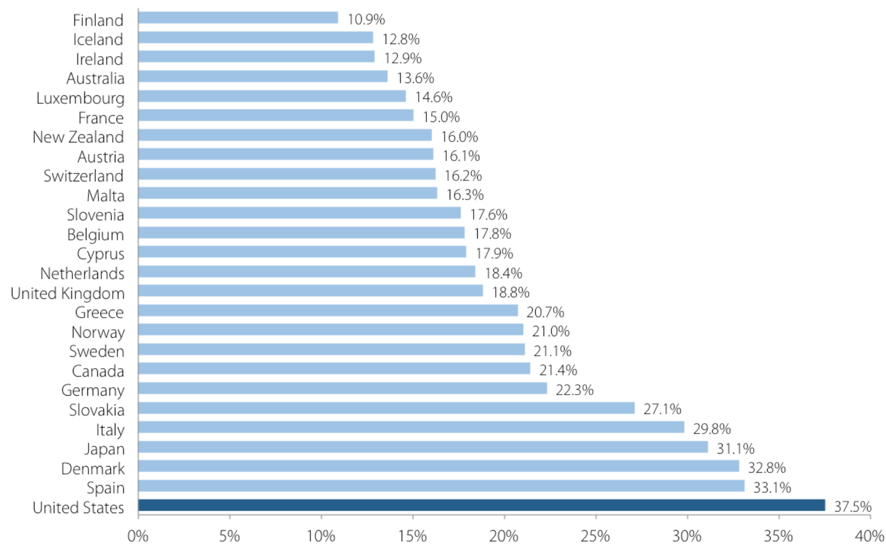
Another useful way to look at the extent of child poverty in the United States relative to other countries is to examine the child poverty gap: the distance between the poverty line (defined here as half of median household income) and the median household income of children below the poverty line, expressed as a percentage of the poverty line. A smaller value means that the median household income of children below the poverty line is relatively close to the poverty line, while a larger number means their median income is further below the poverty line, i.e., that they are relatively more poor. **Figure E** shows that the child poverty gap in the United States is 37.5 percent, the highest among peer countries. Therefore, not only is the incidence of child poverty greater in the United States (Figure D), but U.S. children living in poverty also face higher relative deprivation than impoverished children in other developed countries.

Resource allocation

To show how taxes and transfer income affect poverty rates, we can compare poverty rates based on income calculations that include taxes and government transfers (Figure C) with rates based on income calculations that exclude them ("pretax and transfer" poverty rates). While differences in the latter can be attributed to differences in market outcomes (such as the domestic economy but also a country's minimum wage, level of unionization, and other labor market institutions), the former reflects both

FIGURE E

Child poverty gap in selected developed countries, 2009



Note: The child poverty gap is the gap between the poverty line and the median income of children below the poverty line, taken as a share of the poverty line. The poverty line is defined as half of household-size-adjusted median income.

Source: Adamson (2012, Figure 7)

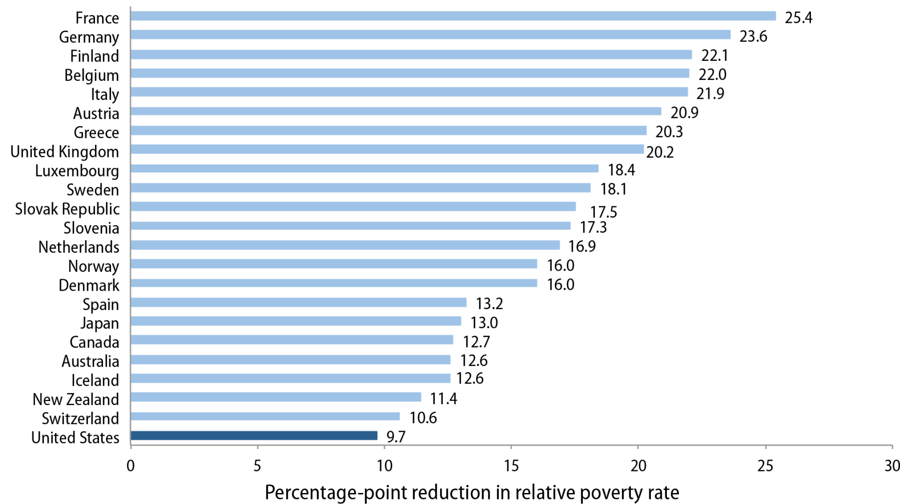
market outcomes and variations in the extent of tax and transfer programs for low-income households. Differences between the two poverty rates are solely due to the government safety net.

Figure F plots the differences between pre and post tax and transfer poverty rates in the United States and peer countries. (As with Figure C, the measure used here is the relative poverty rate, the share of the population below half of median household income.) For example, the pretax and transfer poverty rate in the United States in the late 2000s was 27.0 percent, while the post-tax and transfer rate was 17.3 percent. The difference, 9.7 percentage points, is how much the U.S. tax and transfer system reduced the poverty rate. Among the peer countries in Figure F, the United States' tax and transfer system does the least to reduce the poverty rate. In contrast, tax and transfer programs reduced the poverty rate in France by 25.4 percentage points (from 32.6 percent to 7.2 percent post tax and transfer). France's redistributive programs lowered poverty by about 2.5 times as much as those of the United States. The (unweighted) average effect of peer countries' tax and transfer programs is a poverty-rate reduction of 17.4 percentage points—an effect nearly two times greater than that produced by such programs in the United States.

While Figure F shows the effect of taxes and transfers on poverty rates, it does not show levels of social spending (for example, government expenditures on Medicare and Social Security in the United States). **Figure G** shows total social expenditure as a share of GDP for the United States and select OECD countries plotted against their post-tax and transfer poverty rates (from Figure C), providing a clear picture of the relationship between social spending and poverty. Of these countries, the United States stands out as the country with the highest poverty rate and one of the lowest levels of social expenditure—16.2 percent of GDP, well below the vast majority of peer countries, which average 21.3 percent (unweighted). The figure sug-

FIGURE F

Extent to which taxes and transfer programs reduce the relative poverty rate, selected OECD countries, late 2000s

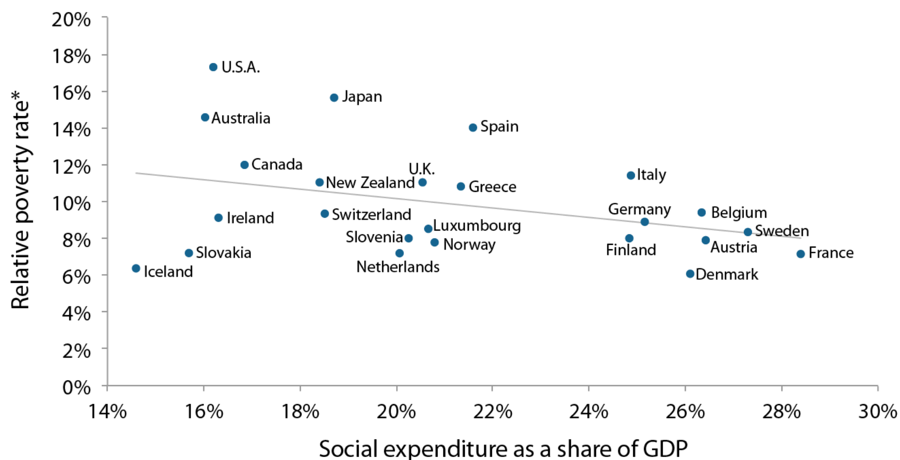


Note: This figure plots the differences between each country's pre- and post-tax and transfer relative poverty rate, where relative poverty is the share of individuals with income below half of household-size-adjusted median income.

Source: Authors' analysis of Organisation for Economic Co-operation and Development Stat Extracts (data group labelled "late 2000s")

FIGURE G

Social expenditure and relative poverty rates in selected OECD countries, late 2000s



* The relative poverty rate is the share of individuals with income below half of household-size-adjusted median income. Poverty rates are based on income after taxes and transfers.

Note: Social expenditure is government expenditure on social programs, such as Social Security and Medicare in the United States. The equation for the trend line is $y = -0.2559x + 0.1528$ and the $R^2 = 0.1266$.

Source: Authors' analysis of Organisation for Economic Co-operation and Development *Stat Extracts* (data group labelled "late 2000s")

gests that relatively low social expenditures are at least partially implicated in the high U.S. poverty rate.

Together, Figures F and G demonstrate that peer countries are much more likely than the United States to step in where markets and labor policy fail in order to lift their most disadvantaged citizens out of poverty.

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