

# Lift Up the Poor

## How Rich Countries

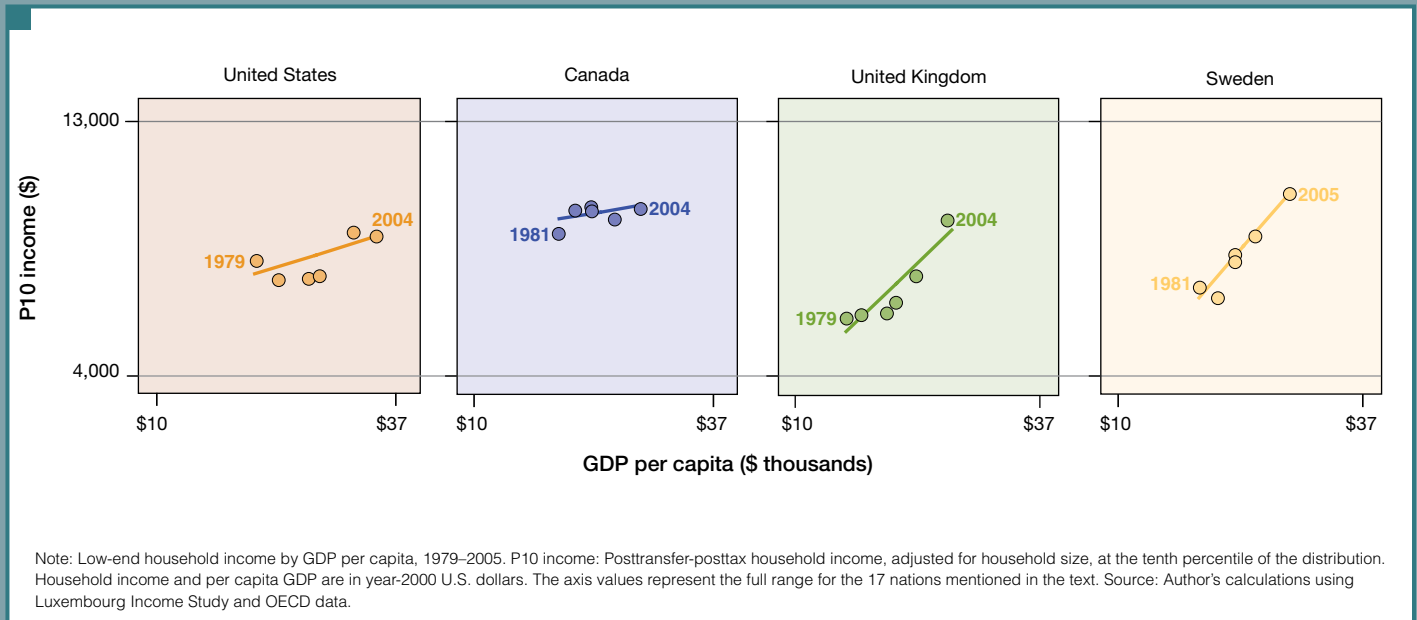
BY LANE KENWORTHY

As a nation grows richer, the living standards of its least well-off ought to rise. But one of the most striking features of late-industrial development is that the fruits of growth have—in some countries—been very unequally shared. Which countries have succeeded in lifting up the poor? And which have failed?

Figure 1 shows what happened from the late 1970s to the mid-2000s in four countries: the United States, Canada, the United Kingdom, and Sweden. The charts show the degree to which household income at the tenth percentile of the income distribution (vertical axis) improves as GDP per capita (horizontal axis) increases. Each of these countries experienced economic growth, moving to the right along the horizontal axis. But they varied markedly in the degree to which that growth reached the poor. In Canada, there was little or no rise in household income at the tenth percentile. In the United States, there was very little, and it occurred only in the late 1990s. The United Kingdom did much better, though also mainly during a particular period, the mid-1990s to the mid-2000s. In Sweden, economic growth yielded a consistent improvement in the incomes of those at the bottom.

In most advanced democracies—Austria, Belgium, Denmark, Finland, France, Ireland, the Netherlands, Norway, and Spain—the pattern during these years

FIGURE 1 Where have low-end household incomes risen with economic growth?



resembles Sweden's. But in others—Australia, Germany, Italy, and Switzerland—it looks more like the American and Canadian one. This raises the question: Why do the poor only sometimes reap some of the fruits of a growing economy?

### Government Policy Matters

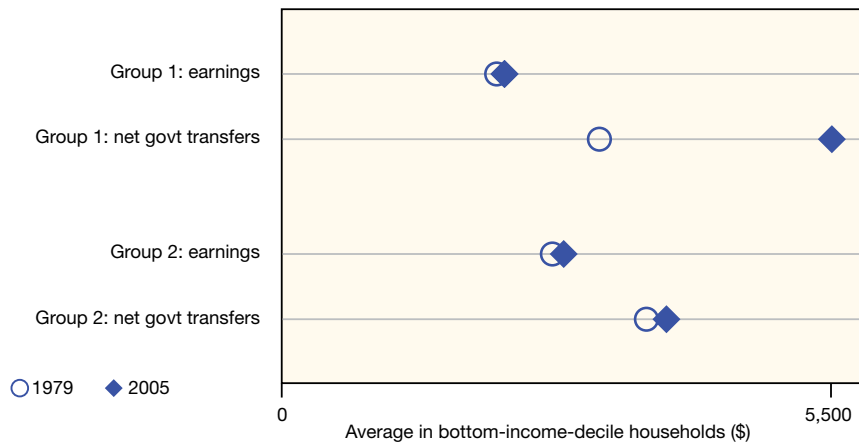
We often think of economic growth as a “trickle-down” process in which rising earnings are secured via more work hours and higher wages. But in almost all of these countries (Ireland and the Netherlands are exceptions) the earnings of low-end households increased little, if at all, over time. Instead, as Figure 2 suggests, increases in net government transfers—transfers received minus taxes paid—tended to drive increases in incomes when they occurred.

Governments in some of these nations did more to pass the fruits of economic growth on to the poor. For the most part, this didn't entail increasing the share of GDP allocated to public transfers. Such increases were common in the 1960s and 1970s. But in most of these affluent nations—even

the most generous ones, such as Denmark and Sweden—increases in the share of GDP allocated to public transfers largely stopped after the 1970s. In recent decades, the distinction has been between countries that kept transfers rising in line with GDP versus those that did not. Sometimes doing so requires no explicit policy change, as benefit levels tend to rise automatically as the economy grows. This happens when, for instance, pensions, unemployment compensation, and related benefits are indexed to average wages. Increases in other transfers, such as social assistance, typically require periodic policy updates. That's true also of tax reductions for low-income households.

In the United States, only one of the main government transfer programs, Social Security, is structured in such a way that benefit levels automatically increase when the economy grows. Social Security retirement benefits are indexed to average wages, so they have tended to rise more or less in concert with GDP. Unemployment benefit levels are determined by state governments. In many instances, the benefit level is

FIGURE 2 Government transfers and taxes have been the chief mechanism through which economic growth reaches the poor.



Note: Average income in the bottom decile of the posttransfer-posttax income distribution. Household income, adjusted for household size, in year-2000 U.S. dollars. Group 1: Denmark, Finland, Ireland, Netherlands, Norway, Sweden, United Kingdom. Group 2: Australia, Canada, Germany, Switzerland, United States. This calculation can't be done for Austria, Belgium, France, Italy, and Spain. Actual years vary depending on the country. Source: Author's calculations using Luxembourg Income Study data.

a “replacement rate,” which means the payment is a certain fraction of the unemployed person’s former wage or salary. Because real wages in the bottom half of the distribution have not increased in the past several decades, unemployment benefits for Americans in low-wage jobs have failed to keep up with growth in the economy. Other programs, such as the Earned Income Tax Credit (EITC), the Supplemental Nutritional Assistance Program (SNAP, formerly called Food Stamps), Social Security Disability Insurance (SSDI), and Supplemental Security Income (SSI), are indexed to prices. This means they keep up with inflation, but not with economic growth. Temporary Assistance for Needy Families (TANF, formerly AFDC) payments are determined by state policymakers; there is no automatic increase, not even for prices. AFDC-TANF benefit levels have fallen steadily in inflation-adjusted terms over the past several decades.

If most of the poorest Americans were elderly Social Security recipients, the U.S. pattern in Figure 1 probably would look more like Sweden’s. But in the United States, as in many other countries, most of those in the bottom 10 percent are not retirees. Many elderly Americans have no income from earnings, but Social Security benefits, payments from employer-based retirement programs (company pension or 401k), and other income (from the sale of a house, for instance) combine to keep them above the bottom decile. The fact that most of our other government transfers have only kept up with inflation rather than with the economy, coupled

with the decline in AFDC-TANF benefits, accounts for the slow income growth at the bottom in the United States.

Should we bemoan the fact that employment and earnings aren’t the key trickle-down mechanism? No. At higher points in the income distribution, they do play more of a role. But for the bottom 10 percent there are limits to what employment can accomplish. Some people have psychological, cognitive, or physical conditions that limit their earnings capability. Others are constrained by family circumstances.

At any given point in time, some will be out of work due to structural or cyclical unemployment. And in all rich countries, a large and growing number of households are headed by retirees. We surely can do better at helping able adults get into (or back into) employment, but we shouldn’t pretend that paid work is a realistic route to guaranteeing rising incomes for everyone.

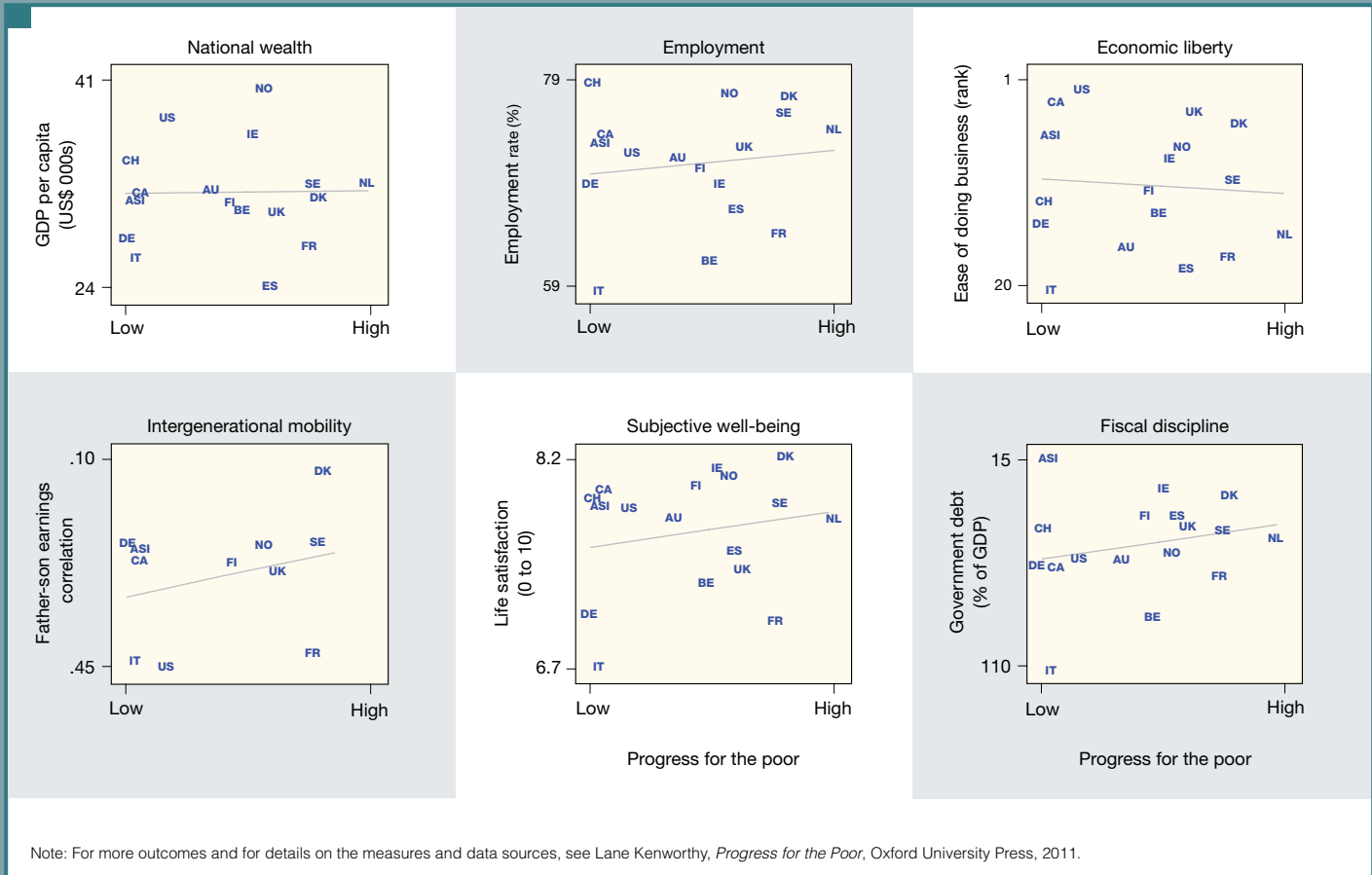
Income isn’t a perfect measure of the material well-being of low-end households. We need to supplement it with information on actual living conditions, and researchers and governments now routinely collect such data. Unfortunately, those data aren’t available far enough back in time to give us a reliable comparative picture of changes. For that, income remains our best guide. What the income data tell us is that the United States has done less well by its poor than many other affluent nations, because we’ve failed to keep government supports for the least well-off rising in sync with our GDP.

### Tradeoffs?

It often is said that there is no free lunch, that generosity comes at a cost. If we commit to improvement in the absolute living standards of the least well-off, must we sacrifice other desirable outcomes?

Here, too, the experiences of rich nations over the past several decades can offer some insight. I begin with a measure of “progress for the poor”: the slope of each country’s line in charts such as those shown in Figure 1. This is an

FIGURE 3 Are there tradeoffs between progress for the poor and other desirable outcomes?



indicator of the degree to which low-end household incomes rise as the society gets richer. Figure 3 displays a number of scatterplot graphs, each of which has this measure on the horizontal axis. Countries positioned to the right have been more successful at boosting the incomes of poor households. On the vertical axes are indicators of economic health, liberty, mobility, happiness, and fiscal discipline. These are measured at the end of the period, around the year 2007 (before the economic crash). Each of the outcome measures is arrayed so that it is better to be higher on the vertical axis. Evidence suggestive of a tradeoff would therefore appear in the form of a negatively sloped line.

The conclusion from these charts is straightforward: There is little or no indication that improvement in the incomes of the poor entails a sacrifice of other valued outcomes.

### Prospects for Progress in America

Modest, regularized increases in the inflation-adjusted benefit levels of existing social programs—the Earned Income

Tax Credit, unemployment compensation, social assistance (TANF and SNAP), housing assistance, and disability benefits—would yield significant improvements in the incomes of America’s least well-off.

Recent developments just across the pond have shown us the way. One of the most successful recent antipoverty efforts in affluent countries was that of the New Labour governments in the United Kingdom from the late 1990s through the late 2000s. Though Tony Blair and Gordon Brown’s governments focused much of their rhetoric and policy reform on improving employment and economic opportunity, they also increased net government transfers to low earners, single parents, and pensioners. Benefit and tax changes between 1997 and 2005 increased real disposable income for lowest-income households by about 20 percent. This increase was one of the largest in any of the rich countries for which reliable data are available.

Unfortunately, apart from a few exceptions such as the EITC, movement in this direction here in the United States has been halting. In most other cases, the politics of helping

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America's poor have proved quite difficult.

Is public opinion the obstacle? Most Americans support capitalism and business. Many believe hard work, rather than luck or help from others, is the key to success. Many feel they have opportunity to get ahead. At a general level, many are skeptical about the government's ability to help. Yet many believe income inequality is too high and that high inequality is not necessary for the country's prosperity. There is only limited support for enhanced redistribution as a remedy for high inequality, but Americans do support increased government spending on programs perceived to enhance opportunity and economic security. And a majority consistently favors increased government expenditure on the poor.

Social scientists' research on the determinants of social policy generosity tells us that what matters most are institutions. Given America's political institutions—the lack of a social democratic political party, a privatized system of cam-

paign financing, a majoritarian electoral system, a federal government structure, extensive separation of power across the three branches of government, a bicameral legislature, and the filibuster practice in the Senate—it is not surprising that we are a laggard among the rich countries in public safety net generosity.

Yet the world of social policy is not a deterministic one. Structures and institutions constrain, but they don't dictate outcomes. For instance, over the past century, center-right Christian democratic parties have been nearly as important as social democratic ones in promoting generous social programs. Government support for child care and early education in continental Belgium and France rivals that in social-democratic Denmark, Norway, and Sweden. In recent years, EITC-type policies have been implemented and expanded in widely diverse institutional settings and by governments at all ends of the partisan spectrum.

It was not foreordained that the United States would institute public health insurance programs for its elderly and its poor in the 1960s and enhance them in subsequent decades; expand its social assistance programs in the 1960s (AFDC) and 1970s (food stamps); create an employment-conditional earnings subsidy in the 1970s (the EITC) and expand it in ensuing years; implement severe time limits on receipt of a key social assistance benefit (TANF) in the 1990s; or fail to adopt government support for near-universal health care coverage in the 1970s and 1990s but then pass it in 2010.

The possibilities for American social policy surely are not endless, but neither are they as limited as a focus on America's political structure might lead us to presume. Over the course of the past century, U.S. policymakers sometimes have been able, even at unlikely moments, to fashion compromises that helped boost the incomes and material well-being of America's low-end households. When new or expanded programs have worked reasonably well, Americans have tended to like them. They then become difficult to remove. This staying power is aided by the array of veto points in the U.S. policy-making process.

The trajectory of American social policy has therefore tended to be one of advance—slow and halting advance, but advance nonetheless. To me this suggests reason for optimism about prospects for the future.

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