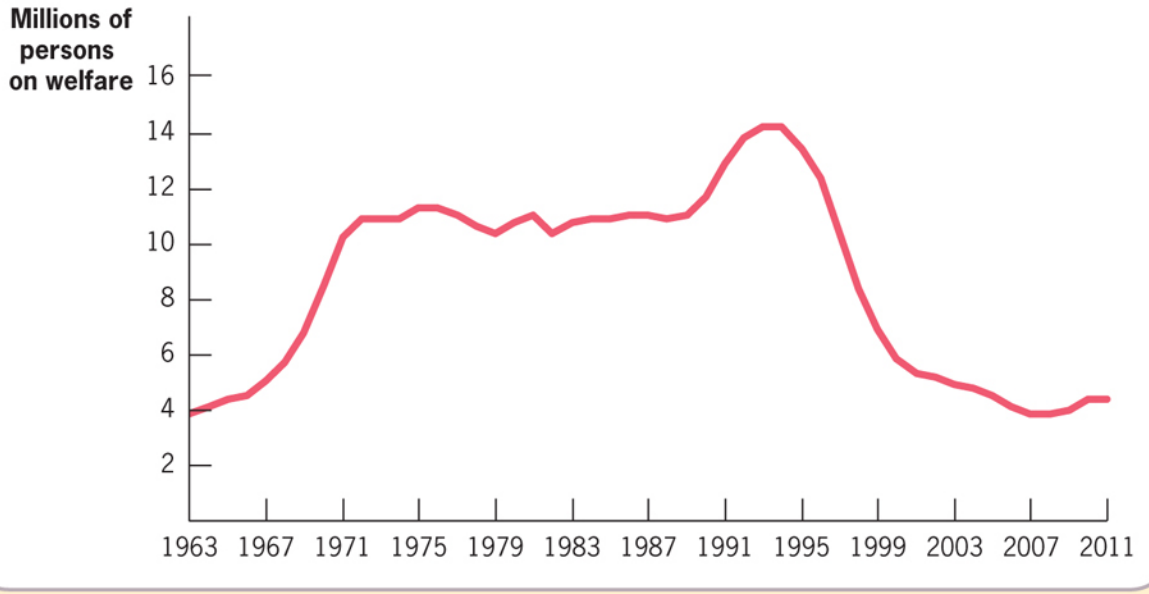
Jonathan Gruber

Public Finance and Public Policy

Fourth Edition

Chapter 17
Income Distribution and Welfare Programs

■ FIGURE 17–1



Welfare Caseloads in the United States, 1960–2011 • The number of persons on welfare rose rapidly in the 1960s, then was fairly constant until rising again in the recession of the early 1990s. Welfare enrollments fell dramatically after 1994; some of this reduction was due to the 1996 welfare reform law and related earlier state policy initiatives.

Source: http://www.acf.hhs.gov/programs/ofa/data-reports/index.htm.

Figure 17-1 Welfare Caseloads in the United States, 1960–2011
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■ TABLE 17–1

Share of Aggregate Income Received by Quintile, 1967–2010

Income	1967	1975	1980	1985	1990	1995	2000	2005	2010
Lowest 20%	4.0	4.4	4.3	4.0	3.9	3.7	3.6	3.4	3.3
Second 20%	10.8	10.5	10.3	9.7	9.6	9.1	8.9	8.6	8.5
Third 20%	17.3	17.1	16.9	16.3	15.9	15.2	14.8	14.6	14.6
Fourth 20%	24.2	24.8	24.9	24.6	24.0	23.3	23.0	23.0	23.4
Highest 20%	43.8	43.2	43.7	45.3	46.6	48.7	49.8	50.4	50.2
Top 5%	17.5	15.9	15.8	17.0	18.6	21.0	22.1	22.2	21.3

Source: *Income, Poverty, and Health Insurance Coverage in the United States* (2010), Table 3; accessed at http://www.census.gov/prod/2011pubs/p60-239.pdf; secondary source: "Striking It Richer: The Evolution of Top Incomes in the United States." N.p., 2, Figure 2, Mar. 2012. Web. 21 June 2012. Accessed at http://elsa.berkeley.edu/~saez/saez-UStopincomes-2010.pdf.

Table 17-1 Share of Aggregate Income Received by Quintile, 1967–2010
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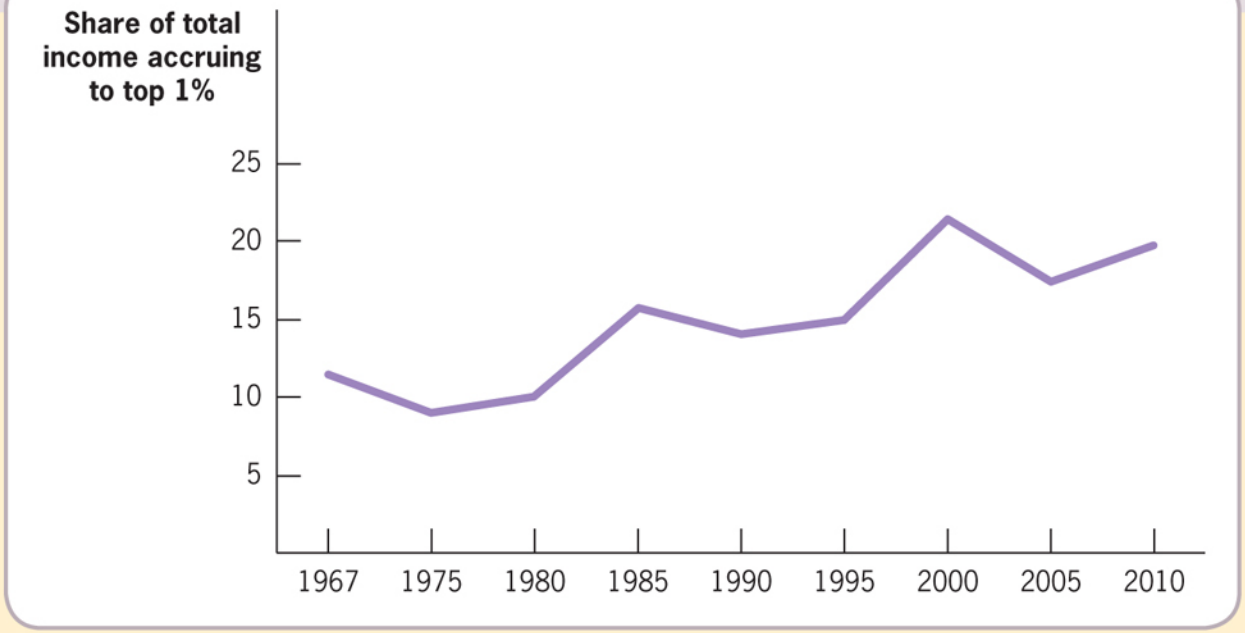
■ FIGURE 17-2



Share of Aggregate Income Accruing to the Top 1% • The share of income accruing to the top 1% fell in the years 1967 to 1975 and grew thereafter, more than doubling since 1975.

Source: Income, Poverty, and Health Insurance Coverage in the United States (2010), Table 3; secondary source: "Striking It Richer: The Evolution of Top Incomes in the United States." N.p., 2, Figure 2, Mar. 2012. Web. 21 June 2012. Accessed at http://elsa.berkeley.edu/~saez/saez-UStopincomes-2010.pdf.

Figure 17-2 Share of Aggregate Income Accruing to the Top 1%
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■ TABLE 17–2

Share of Aggregate Income Received by Quintile of Household for OECD Nations

Country (year)	Income Quintile					
	Lowest	Second	Third	Fourth	Highest	Highest 10%
Austria (2005)	8.4	12.4	16.8	22.3	40.1	13.6
Belgium (2005)	9.4	13.1	17.1	21.8	38.5	13.2
Canada (2005)	8.2	12.1	16.2	21.6	42.0	16.2
Czech Republic (2005)	10.0	13.1	16.3	21.2	39.4	14.5
Denmark (2005)	10.7	14.4	17.8	21.6	35.5	11.1
Finland (2005)	9.6	13.2	16.8	21.3	39.1	14.3
France (2005)	9.4	12.9	16.3	21.0	40.4	15.2
Germany (2005)	8.7	12.8	16.5	21.7	40.4	14.2
Greece (2005)	7.9	12.0	16.0	21.5	42.6	16.4
Hungary (2005)	9.3	12.4	15.8	20.4	42.0	17.4
Italy (2005)	7.6	10.8	15.0	20.2	46.5	21.7
Korea (2005)	8.0	12.7	16.9	22.4	40.0	13.1
Luxembourg (2005)	10.1	13.6	17.0	21.5	37.8	12.4
Mexico (2005)	4.6	7.8	11.6	18.3	57.6	32.3
New Zealand (2005)	7.9	11.1	16.0	22.3	42.8	15.9
Norway (2005)	9.8	13.2	16.0	19.5	41.6	19.3
Poland (2005)	6.8	10.7	14.6	20.6	47.4	20.9
Portugal (2005)	6.6	10.1	13.7	19.3	50.2	24.5
Slovak Republic (2005)	9.7	13.5	16.8	21.2	38.7	13.7
Sweden (2005)	10.7	14.4	17.6	21.5	35.7	10.9
Turkey (2005)	5.5	9.1	13.1	19.1	53.4	28.7
United Kingdom (2005)	7.9	11.2	15.0	20.6	45.4	19.8
Unweighted average	8.5	12.2	16.0	21.1	42.2	16.7
United States (2010)	3.3	8.5	14.6	23.4	50.2	21.3

Source: OECD - World Bank, World Development Indicators; Income distribution and poverty in OECD Countries (2008), Table 1.6, accessed at http://www.oecd.org/document/4/0,3343, en_2649_33933_41460917_1_1_1_1,00.html; Income, Poverty, and Health Insurance Coverage in the United States (2010), Table 3, accessed at http://www.census.gov/prod/2011pubs/p60-239.pdf.

Table 17-2 Share of Aggregate Income Received by Quintile of Household for OECD Nations
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■ TABLE 17-3

Poverty Lines by Family Size (2012)

Size of Family Unit	Poverty Line
1	$11,170
2	15,130
3	19,090
4	23,050
5	27,010
6	30,970
7	34,930
8	38,890
For each additional person, add	3,960

Source: U.S. Department of Health and Human Services (2012).

Table 17-3 Poverty Lines by Family Size (2012)
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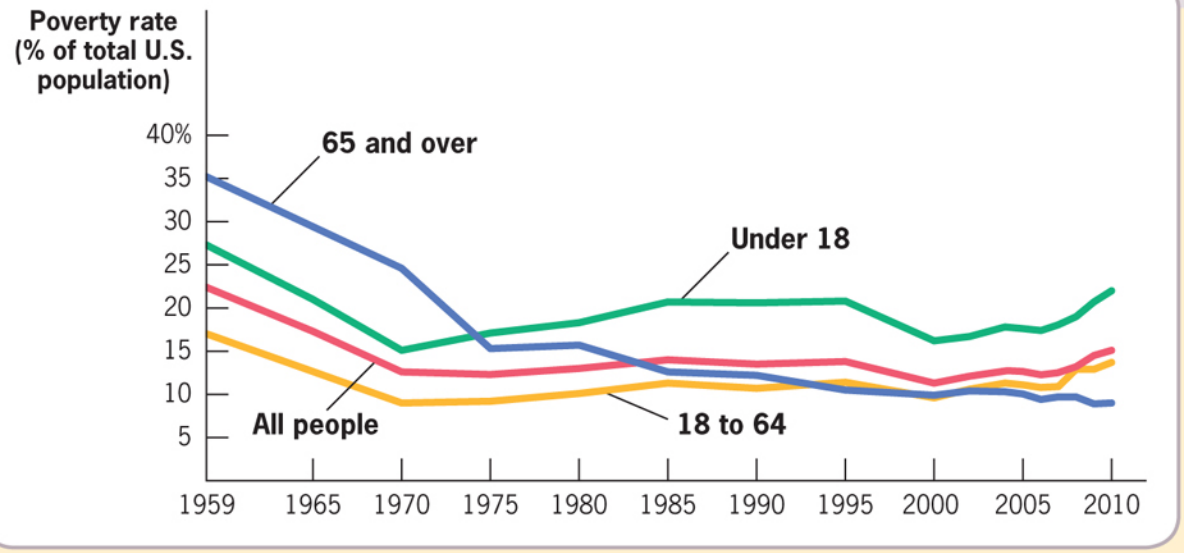
■ FIGURE 17-3



Poverty Rates over Time in the United States • The poverty rate for all, and especially for children, fell substantially during the 1960s, then rose steadily until the mid-1990s, fell in the last half of the 1990s, and then rose again early in the 21st century. In contrast, the poverty rate for the elderly fell steadily during this entire period.

Source: U.S. Census Bureau, Income, Poverty, and Health Insurance Coverage in the United States (2005– 2010).

Figure 17-3 Poverty Rates over Time in the United States
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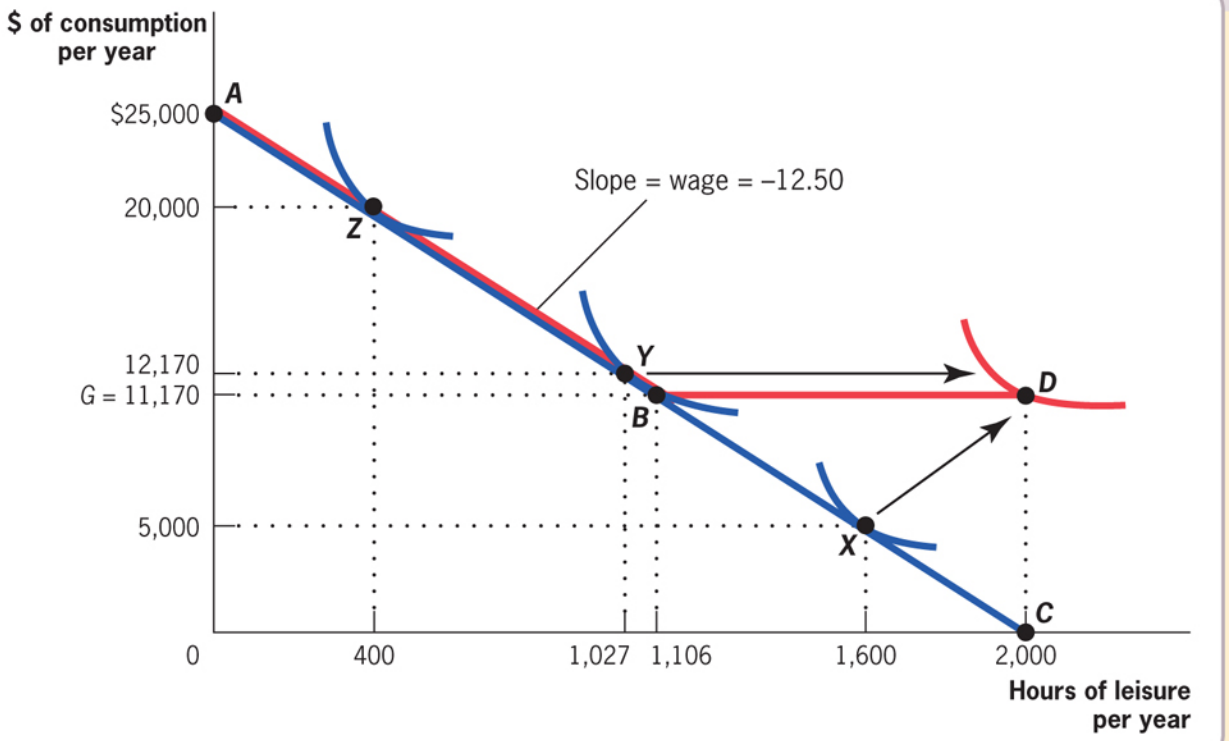
■ FIGURE 17-4



Labor Supply Decisions with a 100% Benefit Reduction Rate (BRR) • If workers are subject to a welfare system with a 100% BRR, then their budget constraint changes from ABC to ABD. Persons such as Mr. X (earning below $11,170 without welfare) will no longer work (he takes 2,000 hours of leisure). Some persons earning just above $11,170 without welfare, such as Ms. Y, may also be induced to drop out of the labor force and join welfare. Here, Ms. Y moves from point Y to point D. Persons such as Mr. Z will be unaffected.

Figure 17-4 Labor Supply Decisions with a 100% Benefit Reduction Rate (BRR)
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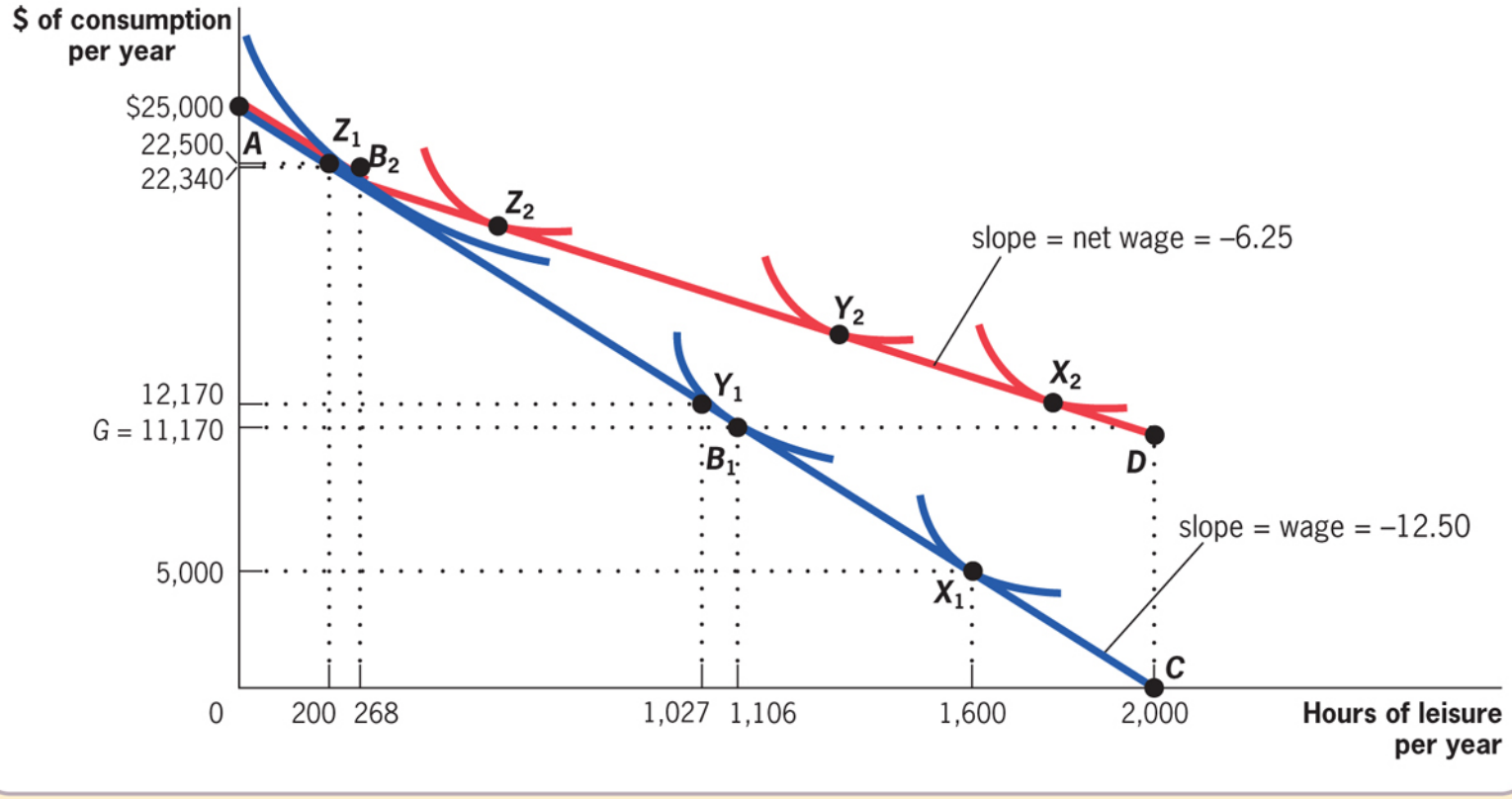
■ FIGURE 17–5



Labor Supply Decisions with a 50% Benefit Reduction Rate • Reducing the BRR to 50% changes the budget constraint with welfare to AB_2D. This leads persons such as Mr. X and Ms. Y to reduce their leisure (increase their labor supply) relative to a 100% BRR, moving from D to points X_2 and Y_2. But persons such as Mr. Z are now brought into the welfare program and reduce their labor supply as a result, at point Z_2.

Figure 17-5 Labor Supply Decisions with a 50% Benefit Reduction Rate
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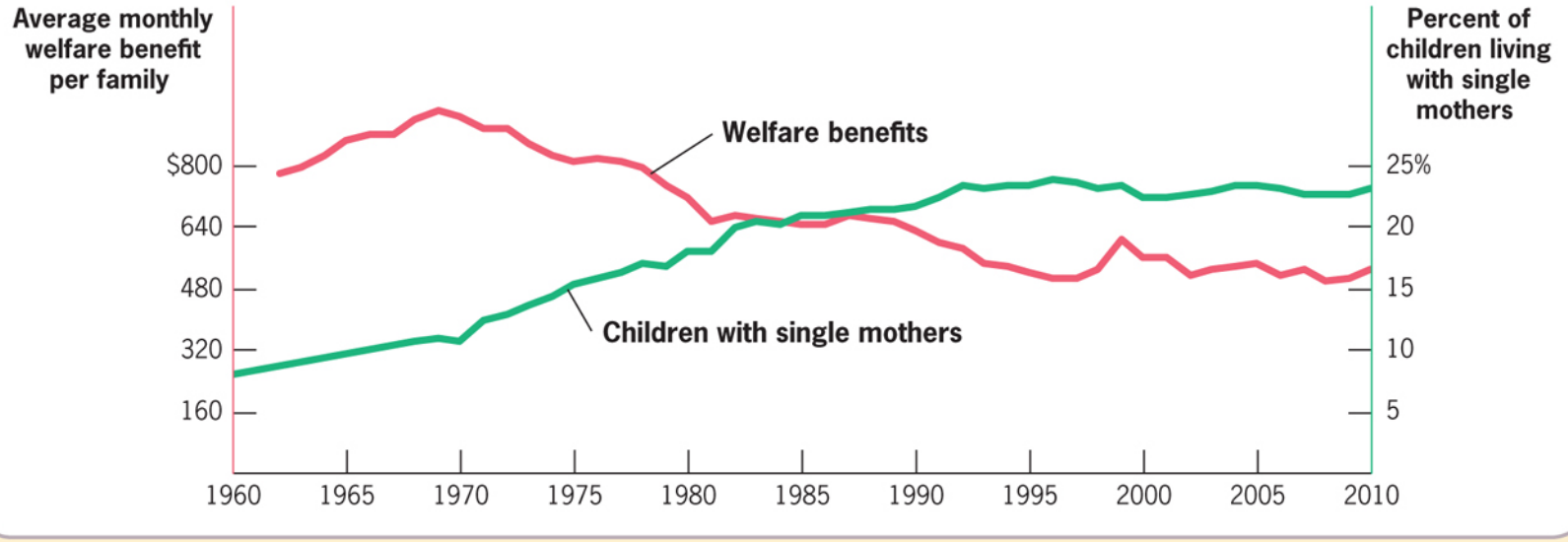
■ FIGURE 17-6



Welfare Benefits and Single Motherhood, 1960–2010 • The average monthly welfare benefit per family rose along with single motherhood in the 1960s, but single motherhood has continued to rise even as welfare benefits have fallen over the past three decades.

Source: Welfare benefit data come from the U.S. Department of Health and Human Services (2011), Table TANF 6. Data on children with single mothers come from the U.S. Bureau of the Census (2011), Table CH-1.

Figure 17-6 Welfare Benefits and Single Motherhood, 1960–2010
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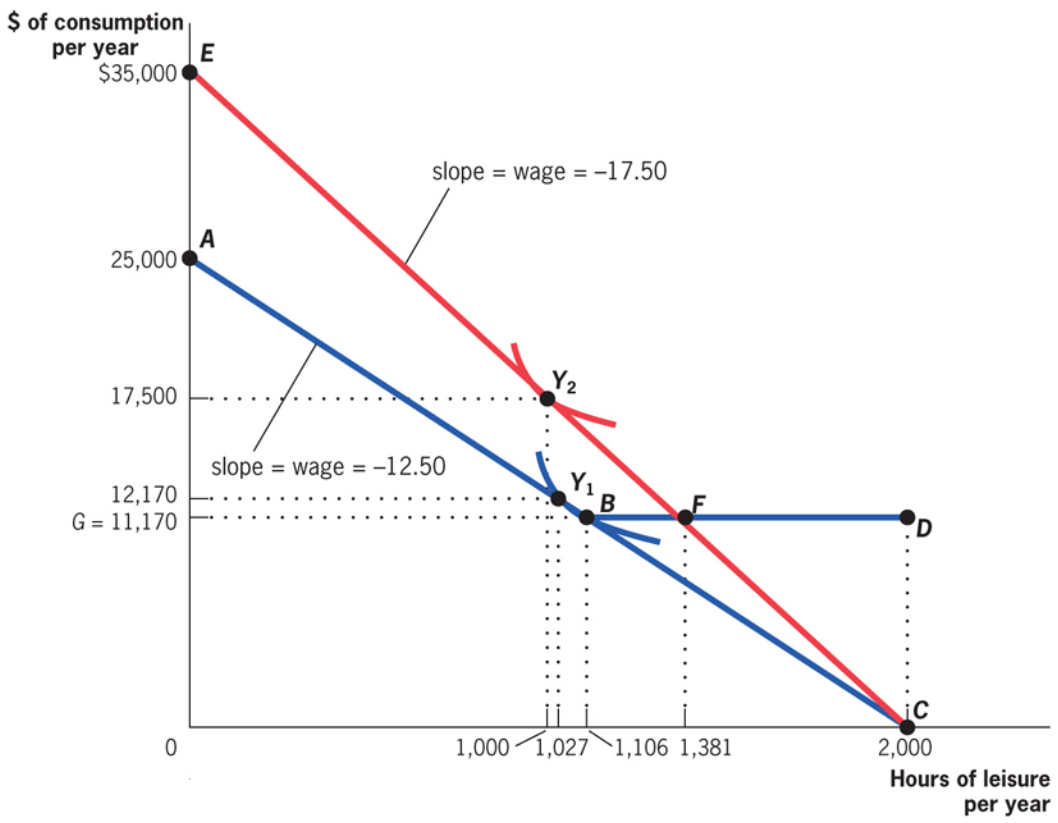
■ FIGURE 17–7



Increasing the Cash Welfare Opportunity Set • One way to reduce use of welfare without changing the benefit reduction rate (and thus running into the iron triangle problem) is to increase the outside opportunities of single mothers so that they can literally "work their way off welfare." By raising the single mother's wage to $17.50, we move her budget constraint with welfare from ABD to EFD. With this new budget constraint, she will no longer choose to be on welfare.

Figure 17-7 Increasing the Cash Welfare Opportunity Set
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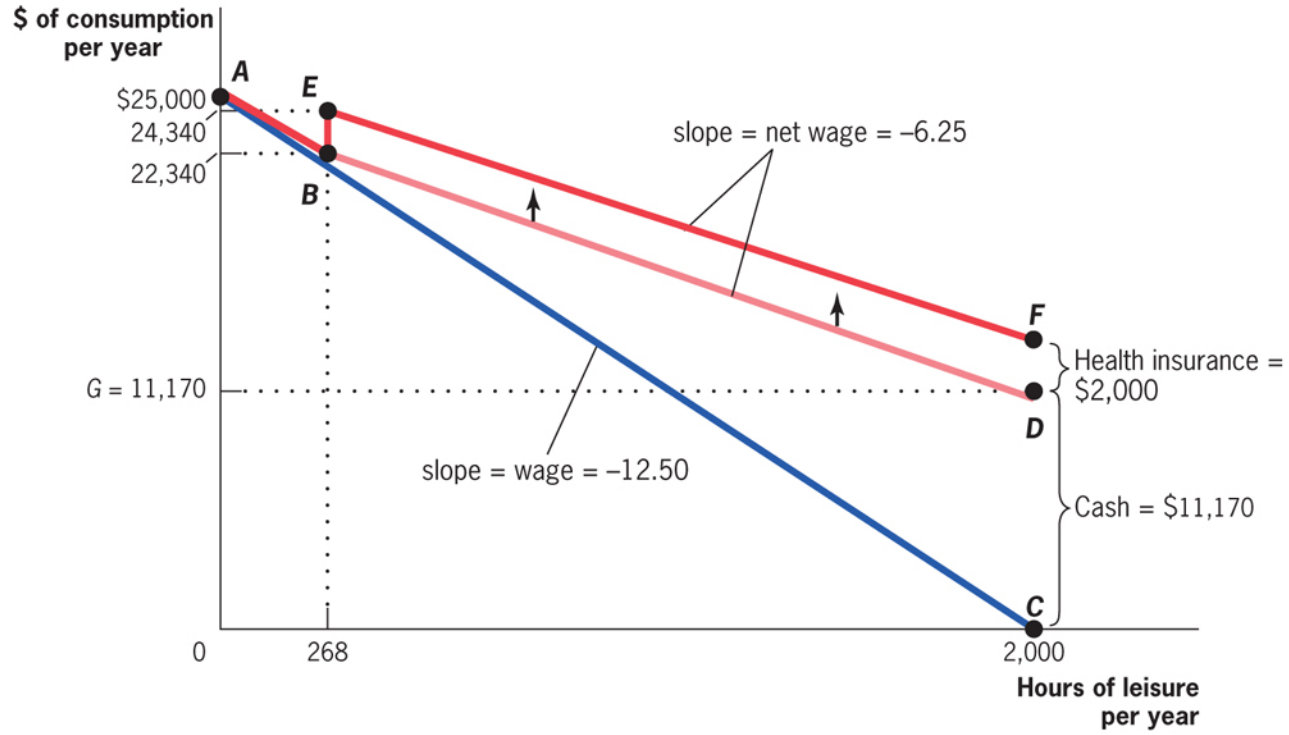
■ FIGURE 17–8



Tying Health Insurance to Cash Welfare • The linking of health insurance coverage through Medicaid to cash welfare creates an additional large disincentive to leave welfare. The budget constraint with the welfare program moves from *ABD* to *ABEF* when insurance is tied to welfare, with an extra portion (*BEF*) that reflects the value of Medicaid, but that ends when the individual leaves welfare. Thus, when Medicaid is linked to welfare, it is never sensible to leave welfare for a job that pays only slightly more, unless that job offers health insurance.

Figure 17-8 Tying Health Insurance to Cash Welfare