

## Chapter 4 – Labor Force Participation

### I. Income Sources

### II. Labor Force Status

### III. Subemployment

### IV. The Question of Causation

### V. Poverty Impact of Cyclical Unemployment

#### I. Income Sources

Labor force attachment is a key difference between poor and non-poor households – the fraction with earnings differs by 30 percentage points.

There are important differences in income sources for families with children compared with families without children. Moreover, among families with children, the patterns of income sources vary for two-parent families and single parent families.

Schiller's Table 4.1 - Income Sources of 2-Parent Families (with children under 18) 2001 March CPS		
	% of families receiving any income from source	
	Poor	Non-poor
Earnings	77.7	97.7
Interest, dividends	18.7	67.7
Pensions	1.5	4.5
Social Security	8.6	5.5
Welfare		
- Cash benefits	15.5	2.5
- Food Stamps	34.6	4.7
- Housing assistance	12.5	2.1

There are a number of features to take away from the above table.

First, “poor” and “non-poor” are defined over the course of the previous calendar year, and each of the sources means that the family did receive some amount of income from that source over the year. For instance, the first cell says that 78% of poor families received some amount of earnings over the previous year; it does not discuss the intensity of work however.

Second, a number of the comparisons are interesting.

- Virtually all non-poor families with children have earnings, while a substantial fraction of poor families do not.
- Non-poor families receive more income from assets (e.g., stock dividends, etc.). In the text, Schiller claims that “The *median* American family owns net assets of roughly \$90,000.” (Page 68). In the previous edition, he claimed \$100,000. According to a number of sources, including the Census, that number cannot possibly be correct for the entire U.S. population.

See the Census Bureau’s “Wealth and Asset Ownership” page – <http://www.census.gov/hhes/www/wealth/wealth.html>

The most recent information – although dated – comes from “Net Worth and Asset Ownership of Households: 1998 and 2000”.

The U.S. Census Bureau reported that “median household net worth increased from \$49,932 in 1998 to \$55,000 in 2000.” See <http://www.census.gov/prod/2003pubs/p70-88.pdf>, page 2.

Among all married households, including the elderly and childless households, median net worth was \$91,218 in 2000. Among all female headed households, median net worth was \$23,028. In many cases, virtually all of that net worth is in the form of home equity, not liquid assets. Excluding home equity, median net worth would be \$13,473 for all U.S. households (see page 11 of the Census document).

- Why exclude home equity? That’s a good question. Many people might think of home equity as an *illiquid asset* – meaning it is difficult to turn it into cash in a hurry. That’s certainly true if you were selling your house, but is less true if you obtain a home equity loan.
- To compute home equity (=value of the house minus liabilities), the government relies on the Survey of Income and Program Participation. This presents several problems, as is apparent from the survey instrument at [http://www.sipp.census.gov/sipp/core\\_content/1993/quests/sipp93w7.pdf](http://www.sipp.census.gov/sipp/core_content/1993/quests/sipp93w7.pdf) (starting on page 58). The questions on mortgages present no problems, but the question on the value of the home states:

“(Including rental properties attached or located on ...’s own residence), what is the current value of this property; that is, home much do you think

it would sell for on today's market if it were for sale?"

The reason this presents more of a problem than other questions (e.g., amount of wealth owned in the form of stocks, bank account balances, etc.), is that many people don't have a good idea of what their home is actually worth because they sell their homes only rarely. If the typical homeowner overestimated the value by 5% – that could make a dramatic impact on net worth. Also, home values are top-coded in the SIPP, which matters more in states with high housing values.

Additional note: Schiller's \$90,000 could not have come from the CPS, because the CPS does not report the value of assets (and liabilities).

- Pensions and social security are relatively small factors for families with children.
- A substantial fraction of poor married households receive food stamps, and a smaller fraction receive cash benefits or public housing. A small fraction of non-poor households (less than 3%) receive these different welfare benefits.

Why do any non-poor households receive welfare income? There are several explanations.

- First, the income limits for some welfare programs is greater than the poverty line. For example, a household can receive food stamps if their income is under 130% of the poverty line (though their actual food stamp benefit is fairly small). Public housing income limits are tied to the median income limit within a county, which can be greater than the poverty line. (See <http://www.huduser.org/datasets/fmr/fmrs/index.asp?data=hist> and <http://www.huduser.org/DATASETS/il/fmroid/index.html> ). In Lexington, the Fair Market Rent was \$784 for a three bedroom apartment, and the "low" income limit for a family of four was \$30,550.
- Second, actual welfare eligibility is often based on monthly income, not annual income as in the CPS and used in the tables. Suppose that a middle-class married couple was unemployed for several months during the calendar year, so that their monthly income was transitorily low. In that case, the family would be eligible for welfare benefits and may decide to collect it. But once the family becomes employed again, their income goes up and they are ineligible. For some of these families, over the course of the calendar year, the monthly earnings in the months that they were employed would lift the family out of poverty, yet they still collected some benefits.
- Third, the CPS defines family status as of the March interview date (where the survey-taker asks about the previous year). Family status can change during the year; suppose, for example, that a female headed household with children got married. When the household was unmarried (for part of the year), they were more likely to be poor and on welfare, but they show up as married (and

non-poor) here.

Figure 4.1, on the next page, shows the relative importance of SOME income sources for poor and nonpoor married families. The most important fact to take away from the table is that for both groups, earnings comprise the overwhelming majority of income. For poor families, earnings comprise 84% of total annual income, and for non-poor families, 93%.

- These pie-charts exclude in-kind income such as food stamps and housing; both of these would diminish the importance of earnings, especially for poor households. They also exclude tax credits like the Earned Income Tax Credit, which could be as high as \$4,500 in 2006.

Nevertheless, earned income is clearly a dominant factor in annual income for married households with children.

#### Single Parent, Female Headed Families

Schiller's Table 4.2 - Income Sources of Female Headed Families (with children under 18) 2001 March CPS		
	% of families receiving any income from source	
	Poor	Non-poor
Earnings	66.3	95.3
Interest, dividends	10.8	44.7
Pensions	2.1	5.6
Social Security	9.2	13.9
Welfare		
- Cash benefits	37.4	9.3
- Food Stamps	58.5	12.2
- Housing assistance	32.6	8.2

As can be seen by this second table, there are a number of contrasts between poor married households and poor female-headed households. There are also a number of comparisons between non-poor households.

- As with married households, there is a large gap in fraction who report

earnings for female headed households who are poor and non-poor.

- Both poor and non-poor female heads are less likely to have asset income than their married counterparts.
- Both poor and non-poor female heads are substantially more likely to participate in welfare. The same kind of reasons outlined above explain why non-poor female heads may participate in these programs. More than one-third of poor female heads participate in cash welfare, food stamps, and public housing. Many participate in all three.

Figure 4.2 shows the relative importance of SOME income sources for poor and nonpoor female headed families. Relative to married couples, earnings is a less important income source. Again, if in-kind income was included in these numbers, earnings would be dramatically less important.

## II. Labor Force Status

### Participation and Poverty

The definition of labor force participation includes not only all people who are working for pay, but also people who are actively looking for jobs. Both employed persons and unemployed persons are counted as labor force participants.

Non-participants are people who are neither working for pay nor actively seeking paid employment. Figure 4.4 shows that poverty rates double in most cases in 1998 when the household head did not participate in the labor force for the entire year. Poverty rates went up from 3% to 16% for two-parent families, and from 18% to 53% for female headed families.

Several questions arise from these statistics:

- Why are poverty rates *so low* among two-parent families, even with non-participation? For example, poverty rates for married households, regardless of work attachment, seem to lower than for female heads.

The most obvious point to make here is that we look at the household head in making these tabulations. The household head is often defined as the person who is responsible for paying the rent or mortgage; when more than one person is responsible, there is no clear rule on which of them is the head. Suppose that the head is the husband, as is often the case. If the wife was working during the year, this may help keep the married household out of poverty.

- Why are poverty rates *so high* for female heads, even for those who do participate in the labor force?

Labor force participation means working at any time during the previous year. Thus, a temporary, part-time job would count as being "in the labor force," but

the earnings from such a job would probably not move the household out of poverty. "In the labor force" includes those who are unemployed but seeking work. Such labor force participants have no earnings when unemployed.

## Nonparticipants

In the year 2000, the U.S. population was about 285 million. About half of the population did not participate in the labor force. This group included:

- Children – defined as age 15 or younger
- Retired individuals (mostly the elderly)
- Full time students over age 16
- Institutionalized, disabled, or sick people
- Homemakers – Many women with children actually do work, however. Over 70% of women with pre-school children work.
- "Other" – they may be "dreamers and drifters"

## Unemployment

Those who aren't working but are actively looking for a job are counted as unemployed, but in the labor force. The duration of unemployment is important for poverty. Many unemployed (around 40%) are unemployed for five weeks or less – a relatively short period of time.

### The Process of Economic Deterioration

People rely on different sources of income during their unemployment spell.

Unemployment Insurance (UI) benefits are only available to those who have a history of employment and have been laid off (rather than fired or quit). There is often a short waiting period before you can start collecting. These benefits often replace about one-third of wages, and are often restricted to 26 weeks.

- Schiller notes that 9% of long term unemployed recipients were poor prior to taking up UI, but 19% were poor while on UI and 34% were poor when UI ran out.
- It would be incorrect to infer from the first two numbers, 9% and 19%, that collecting UI causes poverty. Rather, economic circumstances are changing over the course of the unemployment spell – for example, a family may draw down on assets, and the deterioration in these other factors is increasing poverty rates.

## III. Subemployment

In addition to those who are employed and unemployed, there are other classifications of job behavior.

- Discouraged workers - individuals who are not actively seeking work because the prospects of find a job are so bleak. They are classified as being out of the

labor force. They cite job market reasons for not looking.

- Marginally attached workers - individuals who are not actively seeking work because of personal reasons such as child care.
- Underemployed - individual who is at work, but not working to capacity, for example working at a menial job or a part-time job.
- Subemployment - the whole grouping of these three concepts – discouraged workers, marginally attached workers, and the underemployed.

## **IV. The Question of Causation**

Do the Poor Really Try?

The explanations from chapter 1, which related to flawed character, restricted opportunity, and big brother, come into play here. Those who claim restricted opportunity would point to the fact that the stated reasons for being unemployed are legitimate – illness, disability, child care, etc. Those who would claim flawed character would argue that it is more socially acceptable to claim those reasons – illness, disability, etc., than the true unstated reason – laziness or personal choice. Less than 10% of those who spent time outside of the labor force say it was because they “couldn’t find work” – rather other elements that involve personal choice.

Macroeconomic Forces

Economy’s state obviously has effect on work opportunities. During the great depression, unemployment was 25%. In the early 1980s, it reached 10.8%. These forces lead to several issues limiting the opportunities of the poor.

- The Hiring Queue – Employers are likely to hire the most-skilled first. This suggests that those with the least skills have an even more difficult time finding a job during a recession when labor demand is low.

One implication of the hiring queue is that the average skill of both the employed and unemployed goes up during a recession; employers take a more select group of employees, so the average skills of the employed goes up. Moreover, some good people with skills who used to be employed are now unemployed, raising up the average for the unemployed.

- There are four distinctions in unemployment: cyclical (varying with the economy), frictional (time off when moving from one job to another), seasonal (time off as the seasons change, for example in agriculture), and structural (varying with occupations or areas – such as declining industries).

## **V. Poverty Impact of Cyclical Unemployment**

Unemployment and poverty rates follow similar patterns. Poverty among married

households is very responsive to changes in the unemployment rate, while female headed households are less responsive (recall that female heads rely less on earnings than married couples).