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A Loss of Focus in the Fight Against Poverty

by Robert N. Stewart

Over the years, class warfare has become as basic to American elections as tacos are to a Taco Bell menu. Left-wing politicians and interest groups have made bashing the rich a hobby. Phrases such as "tax cuts for the rich" and "the rich are getting richer while the poor are getting poorer" are heard frequently in their stump speeches. That some make more than others is a violation of their ideas of "social justice."

Fueling the class warfare is the Census Bureau's annual report on income in the U.S. Within this report are statistics on the country's income distribution. These statistics are reported using three primary measures: percentiles (especially quintiles), ratios thereof, and the Gini[1] coefficient. In 2004, the year for which data is most recently available, households in the top 20% (referred to hereafter as quintiles) earned 50.1% of the nation's income.[2] The second-richest quintile earned 23.2%, the middle quintile earned 14.7%, and the second from the bottom earned 8.7%.[3] The poorest quintile of Americans earned 3.4% of this nation's income.[4] Looking at ratios, the 90th percentile (lower limit for the top 10%) earned \$11.07 for every dollar earned by a household in the 10th percentile (upper limit for the bottom 10%).[5] Households in the 95th percentile (lower limit for the top 5%) earned \$3.56 for every dollar earned by a household that earned the 2004 median income of \$44,389.[6] By contrast, a household at the 20th percentile (upper limit for the bottom quintile) earned \$0.42 for every dollar of median income.[7] Finally, the Gini coefficient, which measures income inequality on a scale of 0 to 1, with 0 being perfect equality and 1 being perfect inequality, was 0.466 in 2004.[8]

From an international standpoint, a study recently published in *Social Science Quarterly* found the following: The U.S. has the highest degree of income inequality among "rich" nations; the U.S. has experienced the greatest increases in income inequality among "rich" nations over the past 20-30 years; and the poor in the U.S. are worse off than the poor in these other countries, while the rich in the U.S. are better off than the rich in other nations.[9] The rich nations with which the U.S. was compared included, among others, the United Kingdom, Ireland, Australia, Japan, France, Germany, Italy, Israel, Finland, Sweden, and Norway.

In the utopia of the left, where no one makes more or less than anyone, such data would be unfathomable. But before the next stump speech that blasts the rich, it is important to note that the Census Bureau data makes income inequality look higher than it really is. According to researchers at the Heritage Foundation, the Census tends to overstate the income inequality statistics in four ways: They omit various forms of cash and non-cash income, they do not take taxes into account, they contain an unequal number of persons in the different quintiles, and they don't account for differences in the amount of work performed in each quintile.[10] These researchers found that when these four variables were accounted for, the 2002 income distribution statistics — at the time, the most recent available — changed dramatically. The income share of the richest quintile dropped from 49.7% to 35.8%, and the income share of the poorest quintile increased from 3.5% to 12.3%.[11] Fixing for the first three variables, the ratio of top-quintile income to bottom quintile income dropped from \$14.30 to \$4.21.[12]

More fundamental, however, is the role of income inequality in the economy. In a paper for a symposium sponsored by the Federal Reserve Bank of Kansas City, economists Jason Furman and Joseph Stiglitz claimed that

> The sense that the political system is one in which, while each person may have one vote, some votes count more, or are at least more effective in determining outcomes than others, leads to disillusionment with the democratic process and a decrease in participation by those who are effectively partially disenfranchised.[13]

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In other words, income inequality leads to an imbalance in political power, and in turn, disenfranchisement of the poor. But most recent example of disenfranchisement of the poor — the rioting of Muslims in poor neighborhoods — took place in France, where income inequality is lower than in the U.S.[14]

Income inequality is a problem if the rich are getting richer at the expense of the poor. But according to Martin Feldstein, a Harvard Economics Professor and former Chairman of the Council of Economic Advisors, that is not the case. Income inequality has grown because of factors such as increases in productivity, entrepreneurial success, increased work by high-wage earners, and lower capital costs.[15] According to Feldstein, "…if the material well-being of some individuals increases with no decrease in the material well-being of others, that is a good thing even if it implies an increase in measured inequality."[16]

The real problem in the U.S. is poverty and not income inequality. Rather than enacting policies that redistribute income, the government should fight poverty through policies that promote school choice, work, and strong families. As the British publication *Economist* stated, "helping the poor, the truly poor, is a much worthier goal than merely narrowing inequalities. If the rich get poorer thanks to high taxation…few are better off. If the poor get richer, however, the whole country will benefit."[17]

ENDNOTES

[1] Developed by and named for Italian statistician Corrado Gini (1884-1965).
[2] Carmen Navas-Walt, Bernadette D. Proctor, and Cheryl Hill Lee, "Income, Poverty, and Health Insurance Coverage in the United States: 2004," United States Census Bureau, August, 2005, < http://www.census.gov/prod/2005pubs/p60-229.pdf > (December 16, 2005).
[3] *Ibid.*
[4] *Ibid.*
[5] *Ibid*
[6] *Ibid.*
[7] *Ibid.*
[8] *Ibid.*
[9] Timothy M. Smeeding, "Public policy, economic inequality, and poverty: the United States in comparative perspective," *Social Science Quarterly*, Supplement to Vol. 86, December 2005, page number.
[10] Robert Rector and Rea S. Hederman, Jr., "Two Americas: one rich, one poor? Understanding income inequality in the United States," Backgrounder No. 1791, Heritage Foundation, August 24, 2004, < www.heritage.org/research/taxes/bg1791.cfm > (January 5, 2006).
[11] *Ibid.*
[12] *Ibid.*
[13] Jason Furman and Joseph E. Stiglitz, "Economic Consequences of Income Inequality," *Income Inequality and Policy Options*, Papers and proceedings of a symposium sponsored by the Federal Reserve Bank of Kansas City, Jackson Hole, WY, August 27-29, 1998.
[14] Smeeding, p. 958.
[15] Martin Feldstein, "Overview: Is income inequality really a problem?" *Income Inequality and Policy Options*, Papers and proceedings of symposium sponsored by the Federal Reserve Bank of Kansas City, Jackson Hole, WY, August 27-29, 1998.
[16] *Ibid.*
[17] *Economist*, "Does Inequality Matter?," June 14, 2001, < http://www.economist.com/PrinterFriendly.cfm?story_id=655998 > (January 4, 2006).

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