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Stagnating Economic Well-Being Amid Rising Government Support

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Discussions of the 1 percent and the decline of the middle class have rightly played a growing role in US debates, but they have depended on rough measures of recorded market income that mask other changes in economic well-being taking place in people's lives. The Levy Institute Measure of Economic Well-Being (LIMEW) provides a way to look behind the curtain of monetary income to see the broader trends affecting household living standards. The LIMEW combines the following measures of access to the "necessaries and conveniences of life," to borrow Adam Smith's phrase: base income (mainly money earnings); income from wealth (gross imputed rent of owner-occupied homes and imputed income from nonhome wealth); net government expenditures that support household consumption (cash and noncash transfers from all levels of government, plus public consumption, minus taxes paid); and the value of household production (measured by multiplying hours of household work by their replacement cost).

Our latest research covers trends in the LIMEW over the 2000–13 period. The overall picture is one of historic stagnation in the growth of economic well-being for US households. Beneath the surface, there was a major shift in the composition of well-being. The post-2000 period saw a growing dependence on the government to sustain living standards, with rising net government expenditures offsetting a sharp drop in base income. That is, without government support, most US households would have seen a decline in their measured well-being, rather than "mere" stagnation. This stagnation (falling base income offset by rising net government expenditures) was not just a function of the Great Recession—it began well before, and continued well after—and it affected all quintiles of the LIMEW distribution.

Contrary to popular prejudice, the vast majority of the US population is directly supported by net government expenditures: the bottom 80 percent of households in the distribution of pre-fiscal income (LIMEW without net government expenditures) were net beneficiaries in 2013 (up from 70 percent in 2000). Post-2000, this support became increasingly vital for maintaining living standards. For middle-income households, the rise in net government expenditures ($8,000) over the 2000–13 period was composed almost entirely ($7,000) of an increase in transfers. It is notable that this increase was not solely a consequence of the swollen ranks of the unemployed due to the Great Recession. Although a 2007–10 jump in unemployment insurance and disability payments (Social Security) contributed to the overall growth of transfers, transfers rose in 2000–07 and 2010–13 as well—and the largest component of the entire post-2000 increase in transfers was represented by government medical expenditures (Medicare and Medicaid). Although tax payments tend to be positively correlated with base income, taxes barely changed for the middle-income group over this entire period, despite plummeting earnings.

The story is different for the most well-off households. Although their overall LIMEW was likewise supported by changes in net government expenditures, this mainly took the form of decreases in taxes. Households in the top 20 percent of the pre-fiscal distribution are, on average, net payers: their tax payments exceed the government expenditures that augment their household's consumption. However, these net payments shrank over 2000–13 for the richest households—they fell by more than the net benefits increased for any other quintile. In other words, if we look at the changes in net government expenditures that took place over this period, in absolute terms the richest households benefited the most. Although net government expenditures have an overall progressive structure—providing the greatest boost to the poorest, and then dwindling as one climbs the distribution—this progressivity eroded post-2000 (the progressivity of net government expenditures is almost entirely a function of taxes, as transfers and public consumption combined tend to be relatively equally distributed).

The overall stagnation in the growth of well-being affected all quintiles of the LIMEW distribution. The poorest quintile experienced the slowest LIMEW growth of all—a mere 0.07 percent average annual growth (ten times slower than the 1989–2000 period)—and the richest quintile experienced the steepest drop in LIMEW growth relative to the prior period (from 3.1 percent per annum to 0.25 percent). During the 1990s, a significant gap in the LIMEW growth rate between the top quintile and the rest of the population occasioned a historic rise in the inequality of well-being, as measured by the Gini coefficient. By contrast, 2000–13 saw the inequality of LIMEW remain high but relatively stable: LIMEW inequality narrowed somewhat in the early part of the twenty-first century, remained constant during the Great Recession, and then widened between 2010 and 2013, leaving it roughly where it began the period.

A broad-based stagnation in economic well-being amid stubbornly high inequality suggests something is badly amiss with the manner in which the combined institutions of the market, state, and household are delivering material progress, particularly to those who are most in need. Policymakers must take into account the expanding role of net government expenditures in buttressing living standards for a growing share of the US population.

A more detailed discussion of the issues can be found at levyinstitute.org/publications/stagnating-economic-well-being-and-unrelenting-inequality-post-2000-trends-in-the-united-states.

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