

Pathways

a magazine on poverty, inequality, and social policy

Summer 2008



CAN WE FIGHT POVERTY
DURING ECONOMIC DOWNTURNS?



Pathways

a magazine on poverty, inequality, and social policy

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Editors' Note

Downturn. Recession? Depression? The bad economic news has come in relentless waves: increasing food prices, ailing banks, rising unemployment, declining job creation, growing consumer debt, skyrocketing oil prices, a tidal wave of mortgage defaults and home foreclosures. And the poor, as always, are hurt the most. Although economic downturns can cause harm indiscriminately, the poor have the fewest resources to protect themselves.

It was just a few short months ago that the inaugural issue of *Pathways* boldly asked whether and how a new war on poverty might be fought. With budget dollars scarce and attention focused on the economy as a whole, that question might now seem quaint and Pollyannaish. We simply have to be realistic now and drop all that heady talk of eliminating poverty as we know it. Or so the conventional wisdom goes. But does a downturn instead provide, like the Depression did, an opportunity to step back and rethink how a modern market economy is best fashioned? Does it also provide an opportunity to reduce poverty in the course of delivering economic stimulus? These are the questions we asked our second issue's distinguished contributors to address.

The answers presented here are bold and wide-ranging. In some cases, our commentators suggest that downturns can indeed have silver linings, as they typically cast in sharp relief problems that were before concealed or papered over by prosperity. The unemployment insurance system is a case in point: The former chief economist at the U.S. Department of Labor, Alan Krueger, argues that we have too long lived with an antiquated unemployment insurance system, and that the system can and should be reformed to both meet the needs of the poor and steady our unsteady economy. The newly appointed director of economic policy for the Obama presidential campaign, Jason Furman, likewise suggests that a modern economy should be built on automatic stabilizers that could wean us from exclusive reliance on politically negotiated stimulus packages. And Dalton Conley, recent winner of the National Science Foundation's Alan T. Waterman Award, lays out a radical new vision of the ownership society, one that recasts all of us, poor and nonpoor alike, as investors and capital managers.

If some of our commentators find a silver lining in the downturn, others counsel realism and eyes-wide-open appreciation of the difficulties in fighting poverty and inequality in a downturn. The former senior advisor to the president for welfare policy, Ron Haskins, notes that conventional economic stimulus is a temporary poverty band-aid, while the former policy advisor to President Clinton, William Galston, suggests that a winning antipoverty program will have to be aggressively bipartisan and wide in appeal. And Benjamin Friedman, the William Maier Professor of Political Economy at Harvard University, reminds us that this broad-based support is difficult to secure in times, such as our own, in which so many people feel deprived of the fruits of economic progress.

Do these conversations matter? Absolutely. It is precisely such conversations that define our view of what's feasible and what's not—and ultimately determine what happens. Although there has been much useful (some would say endless!) debate about how to overhaul financial markets and otherwise strengthen the economy, the articles published here open new ground by referring to the disparate impact of the downturn and how and whether it might be redressed. We are committed to moving such conversations about winners and losers to the foreground. The objective of *Pathways*, as always, is to expose matters of distribution to the same open debate that is usually reserved for discussions of the economy and how to maximize total economic output.

—David Grusky & Christopher Wimer,
Senior Editors

Cause for Alarm?

Understanding Recent Trends in Teenage Childbearing

by Frank F. Furstenberg

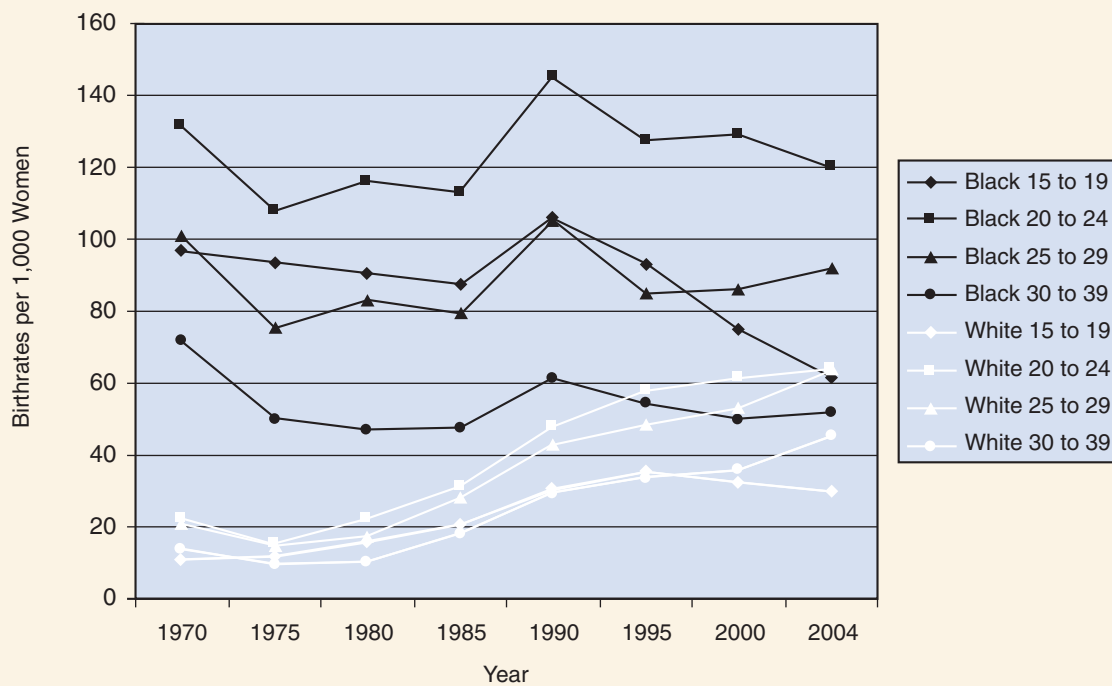
Teen pregnancy is back in the news. After 15 years of decline, the trend in teen birth rates ticked upward in 2006. Coupled with the ongoing media spotlight on the popular film *Juno* and the pregnancy of Britney Spears' younger sister, we're once again wringing our collective hands over kids having kids. But are these concerns really warranted? To what extent does teen pregnancy lead to mothers' and children's long-term poverty? Have policies adopted to deter early childbearing been effective in discouraging teens from having children before they are ready to shoulder the responsibilities of parenthood? To answer these questions, it's necessary to put the issue in proper historical context, and to cast a sober eye on existing policies that were employed to keep rates of teenage childbearing low.

Teenage childbearing first emerged as a public issue in the mid-1960s in the wake of the baby boom era. After the median marriage age for women dipped to 20 years in the late 1950s,

the trend reversed, and Americans began marrying later and later. By 2006, the median age at marriage had risen to nearly 26 years. The rise in median age was occasioned in part by the decline of well-paying manufacturing and union jobs that undercut the time-honored practice of "shotgun weddings." No longer were pregnant teens prepared to marry the fathers of their children when the men lacked good jobs or prospects of getting them in the immediate future. These weddings were partly responsible for the low median marriage age in the United States in the middle of the previous century. Today, shotgun weddings have become archaic; rather few teenage or even older couples now wed merely because of a premarital pregnancy.

While early marriage became less practical and desirable, sexual activity during the teen years continued, and younger women in the 1960s and 1970s practiced contraception poorly (if at all). The inevitable result of the decline in teenage marriage was a rising *proportion* of out-of-wedlock births among teenagers, especially among low-income minorities, even

Figure 1. Birthrates among Unmarried American Women by Race and Age, 1970 to 2004



Source: Centers for Disease Control and Prevention (2000); author's compilation of national vital statistics data from 2000 to 2004.

though the *rate* of non-marital births (per 1,000 unmarried women, ages 15–19) has fluctuated but not increased over the past several decades. (See Figure 1.) Driving the attention, then, was not an increase in the propensity of teens to become pregnant but a much lower likelihood of marriage when they did. Nonetheless, by the 1970s, teenage childbearing was declared by reproductive health advocates as an “epidemic” and by critics of more permissive sexual standards as a crisis for the American family.

In the clarity of hindsight, teenagers were merely the leading edge of a significant change in family formation—the decline of marriage and the rise of non-marital fertility in the United States and throughout much of the Western world, as Figure 1 shows. Over time, the trend first most conspicuous among black teens became increasingly prevalent among white teens and then among all women in their 20s and even 30s. Recent decades have seen declines in non-marital childbearing among blacks, especially black teenagers, while rates for white women have risen.

Nearly all observers, myself included, initially saw this trend in non-marital childbearing among teenagers as ominous. Across the political spectrum, social scientists and policymakers claimed on the basis of existing evidence that early childbearing contributed substantially to creating and sustaining long-term poverty and social disadvantage. Having a baby before social maturity, many early reports claimed, greatly increased the odds of dropping out of school and entering low-wage work or public assistance. In growing numbers, policy experts began to argue that reducing teenage childbearing was a powerful strategy for curtailing the cycle of social disadvantage. Sharp disputes have also emerged across the political spectrum over proper prevention strategies, and I’ll return to these differences later. But first I want to question the evidence underlying the conventional wisdom that childbearing early in life destines young women, their partners, and children for a life of disadvantage.

While it would be inaccurate to declare the conventional wisdom wholly wrong, a growing body of research indicates that it is surely exaggerated and increasingly disconnected from the policies that have been devised to curb early childbearing. Although teenage childbearing may contribute modestly to economic and social disadvantage, it is certainly not *the*, or even *a*, major cause of poverty for teenage mothers or their children. On the contrary, the main causal pathway likely works in the opposite direction: That is, persistent poverty is one of the primary causes of this nation’s high levels of teenage childbearing.

The Baltimore Study

Some 40 years ago, I began following the lives of several hundred teen mothers in Baltimore. The participants were mostly black, poor or near poor, and under 18 when they became pregnant. They all delivered their babies at a single hospital that drew from a broad catchment area including but not restricted to inner-city neighborhoods. As far as I could discern, their demographic characteristics closely matched the larger population of teen mothers in the city and generally fit the profile

of teen mothers living in other metropolitan areas. Over the decades, the women were interviewed seven times and, in the later stages of the study, I conducted in-depth conversations with a subsample of the participants.

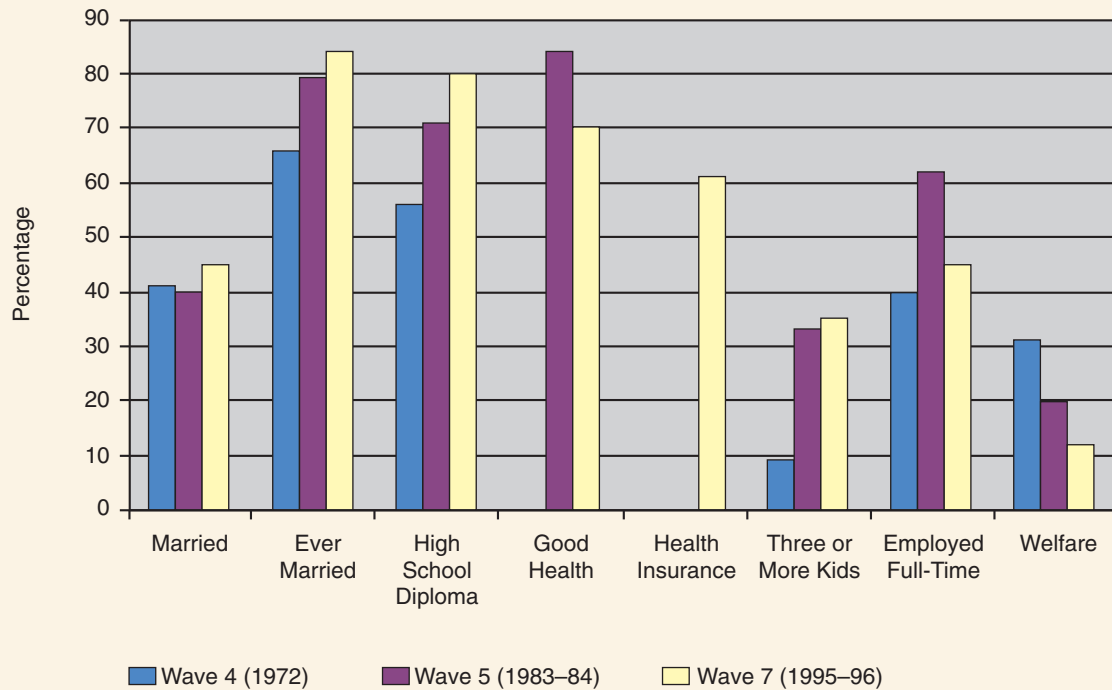
Predictably, in the early stages of the study, many of the women floundered. Many failed to graduate from high school in the early years of the study. Most had trouble gaining a foothold in the labor market, and nearly two-thirds had spells of relying on public assistance. Although a majority married in the first five years following the childbirth, usually to the fathers of their children, most of the marriages failed to survive. Only one in five of those who wed their children’s fathers remained married throughout the first-born’s childhood, and marriages contracted with non-fathers were even less stable. Despite their stated intentions and desires, most of the women had another child within two or three years of their first birth. Compared with their classmates, the women were experiencing distinctly more social and economic problems. So the profile of teen mothers derived from the early interviews gave every indication that most women and children were headed for a life of long-term disadvantage.

It was a something of a shock, then, to discover that this projection turned out to be largely inaccurate. Later interviews from the Baltimore study revealed that most of the teen mothers made substantial strides in their adult years (see Figure 2). Many returned to school either to graduate or earn a GED, and by their 40s, 10 percent had graduated from college. Most curtailed their fertility after a second or third birth. Over half became sterilized in their mid and late 20s, sometimes despite considerable opposition from the medical profession. Stable marriages continued to be elusive, but as single mothers, most of the women became self-supporting. Less than a sixth of the pool of women became chronic welfare recipients, and most of those who did suffered from serious cognitive, educational, physical or mental deficits, many of which predated the birth of their first child. Compared with a national sample of women with similar demographic and family characteristics, the teen mothers in Baltimore were only modestly worse off in later life than their counterparts who had begun childbearing after their teen years.

As for their first-born children, the picture is somewhat less clear. This much I can say. Slightly more than a third of the daughters became teenage mothers. Most of these daughters were faring surprisingly well by their late 20s. Compared with the daughters, the first-born sons were displaying many more problems in early adulthood. Close to half of the sons had dropped out of high school, and many had spent time in prison. What is more difficult to judge from this study and others like it is whether their mother’s age when they were born contributes at all to these struggles.

The results of my study are far from unique. The few other long-term longitudinal studies that exist reveal similar trajectories of recovery among teen mothers. All point to a high level of resiliency among early childbearers and, at least, their female offspring. This research seems to suggest that, while the short-term impact of childbearing can be highly disruptive to the lives

Figure 2. Characteristics of Teenage Mothers, 1972 to 1995–96 Across Time, Weighted for Attrition (N = 197)



of some women, teenage motherhood is not nearly as potent a source of disadvantage as many policy makers have believed. Apart from the remarkable determination of many teen mothers to get back on track, there is another reason some of the early studies on the consequences of teenage childbearing were misleading. They simply did not take adequate measure of the “selective recruitment” of unplanned parenthood—the distinctive characteristics of teenagers who have sex early in life, fail to use contraception reliably, and bring pregnancies to term. Prior to becoming pregnant, such teenagers are likely to have poor school performance, mental health problems, and the like.

Over the past decade and a half, economists, demographers, and sociologists have had a field day trying to measure the impact of early childbearing after taking account of selection. Disagreement remains in the literature on the precise magnitude of the impact, but almost everyone agrees that the size of the effect of the timing of first birth falls somewhere between minimal and modest depending on which outcome is examined. To put it differently, if young women from poor, minority communities delay their first birth by five years on average, it would do relatively little to change their economic fortunes in later life or to improve their chances of entering and maintaining a stable union. This is not to say that reducing teenage childbearing is not a worthy enterprise. Relatively few teens plan to become pregnant or are happy when conception occurs, but it turns out that reducing teenage childbearing is a rela-

tively blunt instrument for improving the economic or family fortunes of the disadvantaged.

Teenage Childbearing and Public Policy

In my recent book on this topic, I trace three lines of public policy that were predicated on the assumption that early childbearing was strongly implicated in the intergenerational transmission of social disadvantage: welfare reform, marriage promotion, and abstinence promotion. Welfare reform was in part justified as an approach to removing the “incentives” for early childbearing. Charles Murray, among many others, argued that the welfare system encouraged early and out-of-wedlock childbearing. Some proponents of welfare reform have pointed to the decline in teenage childbearing, especially among black women, as evidence of its success. However, the decline in early childbearing began fully five years before Temporary Assistance for Needy Families was passed (much less implemented). Evidence from state-level comparisons designed to reveal the impact of rules and restrictions on teen childbearing and out-of-wedlock parenthood either show no effects or very modest impacts. Qualitative data from my study and others that included interviews with young parents reinforce the impression that public assistance did not provide incentives for childbearing. What two researchers referred to years ago as “the myth of the brood sow” was, in fact, a fictitious account of why teenagers and poor women more generally have children out of wedlock.

Marriage promotion, a central policy of the current administration, seems unlikely to be very effective. The policy is predicated on the assumption that persuading couples to marry will improve their own prospects and the well-being of their children. Nothing from my study or the work of others who have tried to measure the impact of birth timing on marriage prospects seems to support this notion. The women who married and remained in stable unions—a very small percentage of all those who ever wed—certainly did better than those who did not, but that result occurred largely because they and their partners had more resources and commitment from the start. And, as I mentioned earlier, even among those who wed their child's father, only one marriage in five survived until the child was 18. Indeed, the likely breakup of these unions only created further flux in the family lives of the women and children.

I would not place high hopes on this nation's ability to counsel unwed couples with children sufficiently well to achieve stable and lasting marriages. At the margins, counseling couples may help, but it is difficult to imagine that such programs will be intense and long-lasting enough to make a sizable difference in the high rate of union dissolution. There are some ongoing experiments of programs designed to do just that, and we would be wise to await their results before pronouncing marriage promotion as a failure. However, I would be extremely surprised, pleasantly so, if this policy turns out to be an effective recipe for creating stable families and thereby reducing poverty.

A third direction of public policy has been to discourage early childbearing by promoting sexual abstinence during the teen years. Based on the premise that there is no effective way of preventing early childbearing except by getting teens to defer sexual activity, this approach has been one of the hallmarks of the conservative movement. Looking at all of the available information, it is probably not too soon to conclude that abstinence promotion is both retrogressive and a dismal failure.

According to data collected by the Guttmacher Institute, there has been a decline over the past decade in school-based sex education programs that explicitly discuss contraception. It appears that we have actually been back-peddling in providing preventive and reproductive health services to adolescents because many conservatives believe these services encourage promiscuity. However, virtually all the random-assignment evaluations of programs aimed at promoting abstinence have shown that they are unsuccessful in getting teens to postpone sexual activity. This finding is consistent with national data collected by the Centers for Disease Control (CDC) indicating that patterns of sexual activity have remained relatively stable during the past decade even as federal and state governments promoted the virtues of sexual abstinence. There has been a slight drop in the number of teens who have ever had intercourse, but the number of those who have had intercourse in the past three months remains unchanged. Moreover, a substantial number of teens continue to engage in unprotected sex. Recent data

released by CDC indicates that about a quarter of teenage girls who have ever had sex have an STD.

Our benighted approach to prevention—advocating abstinence while limiting exposure to contraceptive education—may also be implicated in the recent uptick in teenage childbearing. For the first time in 15 years, rates of teenage childbearing rose, and the increase was substantial, occurring among all ethnic groups. We cannot know for sure that the policies of the current administration explain this change or even that it is the beginning of a reversal of the long-standing decline in the rate of early childbearing. Nonetheless, we can conclude, I believe, that “abstinence only” has not worked to deter sexual activity, STDs, pregnancies, or childbearing. Whatever one believes about the costs of early childbearing or its link to long-term poverty and family instability, “abstinence only” programs have been a policy disaster.

None of the three approaches to pregnancy prevention among teens mentioned above appears to be a successful strategy for reducing either teenage childbearing or poverty. The apparent “causal” link between early childbearing and long-term poverty is questionable. If anything, the link probably mostly operates in the reverse direction: Persistent poverty may foster conditions that elevate higher levels of unintended childbearing, especially among teenagers.

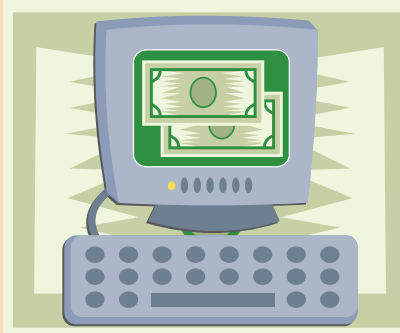
If we want to work on reducing teen childbearing—and I think we do—we should adopt a more realistic approach to preparing teens to make wiser decisions if and when they do enter sexual relationships. This is far from impossible. Most other countries in advanced economies treat this decision less as a moral dilemma than a public health problem. They actively promote safe sex through condoms and advocate reducing unwanted pregnancies by educating the young to use contraception and by making services readily available. Their levels of sexual activity among teens are no higher than the levels in the United States and, generally, they have lower rates of unintended pregnancies and abortions.

Strengthening reproductive health services for teens will help curtail the level of unintended pregnancy among young, unmarried women, but it will not help much to improve their fortunes in later life unless they are able to put the delay in parenthood to their advantage. This means that we must craft more effective policies at keeping youth in school, improving their educational attainment, and increasing the payoff of employment when they enter the workplace. Then, and only then, will we begin to see a connection between postponement of parenthood and the reduction of poverty. ■

*Frank F. Furstenberg is the Zellerbach Family Professor of Sociology and Research Associate in the Population Studies Center at the University of Pennsylvania. His new book, *Destinies of the Disadvantaged: The Politics of Teenage Childbearing*, was recently published by Russell Sage.*

Dollars and the Digital Divide

As the Internet becomes more important, some politicians have suggested that broadband Internet services should be considered a public good, the contemporary equivalent of telephone wires, electricity, or paved roads. The poor, so it is argued, are falling behind because they cannot access information or communicate as effectively as the better-off. But does differential access to the Internet indeed worsen the gap between the haves and have-nots? Is there an actual monetary payoff to Internet access?



This question has now been tackled head on. Using a national sample of U.S. workers, Paul DiMaggio and Bart Bonikowski found that those who used the Internet, either at work or at home, boosted their earnings at a faster rate than those who didn't. This result holds even when one adjusts statistically for other differences between Internet users and non-users that may affect future earnings (e.g., earnings in prior years). Why do Internet users do better? It is not just that Internet usage makes workers more productive on the job. Internet users have superior access to information about available jobs, inducing them to move more frequently and better chase high earnings.

It follows that the rise of the digital divide is indeed an inequality-generating development. In the new economy, being offline could mean being out of luck.

DiMaggio, Paul, and Bart Bonikowski. 2008. "Make Money Surfing the Web? The Impact of Internet Use on the Earnings of U.S. Workers." *American Sociological Review* 73: 227–250.

High Stakes but Low Risks?

Increasingly, firms are using standardized tests to measure the skills of job applicants, a development that might either (1) reduce racial and ethnic discrimination by minimizing opportunities for employer discretion, or (2) increase racial and ethnic discrimination insofar as minorities tend to do worse on standardized tests. Although an argument for either effect might be made, the answer is ultimately an empirical one. What impact do standardized tests actually have on minority hiring?

Using data from over 1,300 retail stores of a prominent national chain, David H. Autor and David Scarborough brought direct evidence to bear on this debate by examining minority hiring and job tenure both before and after testing procedures were implemented. The testing procedures appeared to increase the productivity of matches, given that job tenure rose by approximately 10 percent after testing was adopted. More surprising, perhaps, was that minority hiring was unaffected by the transition, and the productivity-enhancing aspects of testing accrued to minority and non-minority applicants alike. The rapid spread of skills testing, then, may not be as harmful to minority applicants as some feared.

Autor, David H., and David Scarborough. 2008. "Does Job Testing Harm Minority Workers? Evidence from Retail Establishments." *Quarterly Journal of Economics* 123: 219–277.

The Long March

The most recent research suggests that privilege *does* make you happier. The more highly educated are happier than the less educated, and whites are happier than members of other less privileged races. But are the privileged able to lock in such happiness advantages over their entire life course? Or do their happiness advantages tend to fade as they age?

Using a series of nationally representative samples from 1972 to 2004, Yang Yang found that all Americans tend to get happier as they age, as they settle into their roles and gain more satisfaction and self-esteem from them. However, the happiness advantage of the most privileged groups (in terms of class, race, and gender) tends to erode over time as they experience the stresses of aging, such as the death of friends and spouses and the associated loss of social support. Although the less privileged also face these same stresses as they age, such happiness-reducing effects are counterbalanced by happiness-increasing ones, most notably their retirement from especially stressful jobs and the associated access to age-related social welfare benefits (e.g., social security and Medicare). The happiness advantage of the privileged tends to dissipate as a result.

For all the Sturm und Drang of trying to get ahead, where happiness is concerned it seems we're all headed to much the same spot. So while inequality in quality of life remains persistent through much of the life course, old age may at least bring us all a bit closer to equality.

Yang, Yang. 2008. "Social Inequalities in Happiness in the United States, 1972 to 2004: An Age-Period-Cohort Analysis." *American Sociological Review* 73: 204–226.

A Big Texan Experiment

When the Supreme Court required universities to adopt race-neutral admissions policies in 2003, some state schools settled on so-called percent laws, which required them to offer admission to a fixed percentage of graduates within each of the state's high schools. These laws precluded state universities from admitting an especially large number of students from high schools that were presumed to be academically strong. Although it was initially unclear how these new policies would affect the diversity of incoming university classes, some intriguingly optimistic findings are beginning to emerge.

Using statewide data from Texas, which implemented a percent law guaranteeing state-school admission for the top 10 percent of any high school's graduating class, Kim M. Lloyd, Kevin T. Leicht, and Teresa A. Sullivan find that the top students who knew about this law were more likely to aspire to attend college, more likely to expect to attend college, and more likely to actually apply to state universities. This ratcheting up of aspirations, expectations, and applications was especially prominent among minority students in the top 10 percent of their class.

The great virtue, it would seem, of percent laws is that they reduce ambiguity and lay out a clear and well-specified pathway to entering state universities. This in turn helps promising minority students see higher education as a feasible path toward economic mobility.

Lloyd, Kim M., Kevin T. Leicht, and Teresa A. Sullivan. 2008. "Minority College Aspirations, Expectations and Applications under the Texas Top 10% Law." *Social Forces* 86: 1105–1137.

Trickle Up Spending

The government is often criticized for lavishing aid on programs that foster mobility among the poor while starving similar assistance programs directed toward middle- and upper-income citizens. Where does government spending on promoting upward mobility actually go? Is the federal government indeed spending most of its mobility-promoting money on the poor?

According to a new report by Adam Carasso, Gillian Reynolds and C. Eugene Steuerle, the government is not at all biased toward the poor in its mobility spending. The authors traced federal expenditures and tax subsidies aimed at promoting economic mobility in areas such as job training, savings and investment incentives, and small business development. It turns out that nearly three-quarters of this spending flows to middle- and upper-income households. Worse yet, the government programs directed toward lower- and middle-income households are rife with problematic disincentives, ones that frequently discourage rather than encourage work and saving. For example, because Temporary Assistance for Needy Families dissipates steeply when recipients work and earn more, they are less likely to use these programs for economic mobility.

The government, then, may be giving many people a "hand up" (rather than a "handout"), but the beneficiaries are often those who are already better off. If you're poor in the United States, the helping hand of the state is both hard to find and not as helpful as we tend to think.

Carasso, Adam, Gillian Reynolds, and C. Eugene Steuerle. 2008. "How Much Does the Federal Government Spend to Promote Economic Mobility and For Whom?" Washington, D.C.: Economic Mobility Project, an initiative of The Pew Charitable Trusts. Available at <http://www.urban.org/url.cfm?ID=411610>.

Minding the Gap

The No Child Left Behind law holds schools accountable for student performance and seeks to close persistent socioeconomic, racial, and ethnic achievement gaps that have long dogged proponents of equal opportunity. But what if the sources of those gaps lie outside the purview of the school system?

According to new research by Jacob E. Cheadle, a sizable portion of the achievement gap stems from activities and investments outside the regular school day. Using longitudinal data on a national sample of kindergartners, Cheadle found that much of the racial, ethnic, and socioeconomic gap in children's achievement was due to the types of learning materials that parents provided at home and to participation in organized after-school enrichment activities, such as arts, athletics, and dance.

It is possible, then, that only so much may be achieved by reforming schools. To close lingering achievement gaps, education reforms may have to reach well beyond the school's doors.



Cheadle, Jacob E. 2008. "Educational Investment, Family Context, and Children's Math and Reading Growth from Kindergarten Through Third Grade." *Sociology of Education* 81: 1–31.

An illustration depicting a group of businessmen in white shirts and ties standing on a yellow ledge that is part of a brown cliff. The cliff is eroding away from the right side, and several businessmen are shown falling off the edge, tumbling down a red and orange slope. In the background, a tall grey building with a red door and a red flag on top stands against a blue and orange sky. The overall style is a textured, painterly illustration.

Insuring AGAINST Recession

Alan Krueger

Although the economy may yet skirt a recession, there is no question that the labor market has turned down. And if this downturn is like recent ones, it will take a while for the job market to recover. A short-term economic stimulus package could speed the recovery and help reduce poverty. Unfortunately, the stimulus bill that the president proposed and Congress passed had different goals. But it is not too late for them to return to the drawing board for a second try.

A short-term economic stimulus program should have three goals. First, and most obviously, it should stimulate the economy. Second, it should provide relief to individuals whose economic situation was severely and unexpectedly hurt by the downturn—not just because these individuals need the most help but also because such targeting assists with stimulus. Third, the program should not weaken the government’s long-term budget position. The bipartisan stimulus plan that quickly passed Congress this spring was notably weak on the second criterion in that unemployed job seekers receive little relief from the enacted stimulus package.

We can build a better stimulus plan by retooling the unemployment insurance (UI) program. Before laying out this argument, some background information may be useful.

According to the Bureau of Labor Statistics (BLS), “Persons are classified as unemployed if they do not have a job, have actively looked for work in the prior 4 weeks, and are currently available for work.” The unemployment rate has been creeping up in recent months, rising from 4.5 percent in April 2007 to 5.0 percent in April 2008 (both seasonally adjusted). It is also worrisome that the average duration of ongoing unemployment spells has been rising for some time. In January 2001, the average duration of unemployment for an unemployed worker was 12.7 weeks; in January 2008 it was 17.5 weeks. Nearly one in five of those currently unemployed have been unemployed for more than six months. Data from recent Gallup Polls indicate that Americans, especially those in middle and higher income groups, are increasingly concerned that it has become more difficult to find a quality job. Workers are anxious about the job market, and they are reining in consumption.

Unemployment has serious economic consequences for the unemployed and the broader population. Jonathan Gruber of the Massachusetts Institute of Technology, for example, has found that consumption of food, clearly a basic necessity, falls for the unemployed. He further finds that receiving UI benefits reduces the drop in food consumption of the unemployed. And the very existence of unemployment implies that we are not getting the most out of our resources, which costs the economy output and tax revenue. In a very real sense, providing adequate UI and providing economic stimulus go hand in hand.

The unemployment insurance program provides automatic economic stimulus because benefits ramp up temporarily in a downturn and reach those most in need. For example, outlays for unemployment insurance soared from \$14 billion in 1989 to \$37 billion in 1992, when the jobless rate peaked, and fell to \$21 billion in 1995, when the labor market improved. By building

up reserves in prosperous times and spending them in weaker times, the program helps stabilize the economy. And unemployment insurance provides a measure of security for those who do not directly receive benefits. Just knowing that benefits are available in case of job loss inspires confidence. A strong safety net also makes it unnecessary to have industry-by-industry bailouts in response to adverse shocks.

The last two recoveries from recessions could be described as “jobless recoveries.” Unemployment lingered and job growth was painfully slow for months after the recessions officially ended. Although no one has a crystal ball—and it is unclear how long the current slowdown will last, or whether it will be declared a recession by the National Bureau of Economic Research’s Business Cycle Dating Committee—there are reasons to expect unemployment to linger after the current slowdown ends. In this environment, it is particularly appropriate to consider reforms to the UI program, both temporary and permanent. Undertaking these reforms would help both unemployed workers and the economy as a whole bounce back.

As with all insurance programs, UI involves several trade-offs. Paying benefits to the unemployed could induce some people to stay unemployed longer than they otherwise would. Economists have long noted that reducing the burden of unemployment increases the opportunity cost of work, leading some unemployed workers to delay a return to work. Such an incentive effect, however, is not a sign of the program’s failure. It simply means that the unintended consequences must be weighed against the desired effects of the program, and an appropriate balance struck. In addition, recent research by Raj Chetty of UC-Berkeley suggests that it may be desirable from society’s perspective to provide job seekers who have inadequate savings sufficiently generous UI benefits to enable them to stay out of work longer and search for an appropriate job. Longer spells of unemployment, to the extent they occur, are not necessarily undesirable if they enable workers to find jobs that use their skills fully. Thus, longer unemployment spells are not always an unintended consequence of UI. In a downturn, when good jobs are harder to find and spells of unemployment are longer, the balance of UI’s intended and unintended consequences shifts, and we should worry more during those times about cushioning the blow of unemployment.

Through a series of sensible reforms, UI could be a much more efficient and effective program. Four reforms in particular should be considered.

Automatic triggers: The automatic triggers that temporarily turn on extended benefits without Congressional action are no

longer set at realistic levels. The state triggers are connected to the insured unemployment rate, which is the fraction of covered workers who receive benefits. The insured unemployment rate must exceed 5 percent for extended benefits to be provided and must be 120 percent above the rate in the corresponding period in each of the prior two calendar years. Because insured unemployment has drifted down relative to the BLS's unemployment rate (which includes all unemployed workers, insured and ineligible), and because the natural rate of unemployment has declined, it is now very unlikely that a state will automatically trigger extended benefits. In practice, the automatic triggers have become irrelevant. These automatic triggers have not been modernized, and modernizing them would significantly improve the current system. If more reasonable automatic triggers are not put in place, a short-term fix would be to extend the maximum duration of benefits in the current economic slowdown, especially in those areas with high unemployment. Extended benefits are well targeted to a population that is very much in need of assistance, and that population is growing.

Making layoffs more costly: The financing of UI could do more to stabilize the economy and discourage layoffs. The federal government sets minimum standards for state unemployment insurance programs and has a history of encouraging “experience rating.” The practice of experience rating discourages employers from laying off workers because it assesses a higher UI contribution rate for employers with a worse history of layoffs. This unique feature of the American UI system may in part help to account for the relatively low unemployment in the United States compared with other economically advanced countries.

Unfortunately, the degree of experience rating has severely lapsed. Better experience rating could be accomplished by increasing the 5.4 percent maximum tax rate on high-layoff employers, and by requiring the states to have at least five different rates and to spread employers among the rates. Some states have only two rates. In addition, the per employee taxable earnings cap—which ranges from \$7,000 to \$10,000 in half of the states—should be raised, which would allow better experience rating at lower tax rates and make the financing of the program less regressive. Raising the caps and lowering the rates would also increase demand for less skilled workers. Improved experience rating would discourage employers from laying off workers, and help internalize the externalities layoffs impose on society. A study by David Card of UC-Berkeley and Phillip B. Levine of Wellesley estimates that the unemployment rate would decline by six-tenths of a percentage point if industries were fully experience rated—that is, if employers in an industry were required to pay the full additional costs of unemployment benefits for layoffs in that industry. These changes could be made in a way that is revenue neutral, so the tax on employers as a group would not change.

Eligibility for part-time workers: Third, unemployed workers who are otherwise eligible for UI but are searching for a part-time job (because of family obligations, for example) are ineligible for benefits in many states, a restriction in coverage that should be changed. These workers pay into the system, but are prevented from receiving benefits when they and their



LEO ROSALES

Alan Krueger chats with Senator Ted Kennedy (D, Massachusetts) after testifying before Congress on Unemployment Insurance reform in March, 2008.

families need them. States could be required to expand eligibility. Workers who would be made eligible for UI benefits as a result of this reform would be primarily single-parent, female, and low-income earners, all of whom are likely to be particularly hard hit by an economic downturn.

Addressing the credit crunch: Last, but not least, the credit crunch that the economy is experiencing presents a unique situation in which a temporary increase in the level of UI benefits may be particularly timely. Unemployment benefits help unemployed workers maintain a minimum level of consumption when their income drops. Benefits replace around 50 percent of lost earnings, but the replacement rate is typically less than that because benefits are capped, often at less than \$400 a week. The average weekly UI benefit as a percent of the average weekly wage of covered workers was only 34.5 percent in the third quarter of 2007 according to Labor Department data. Even with UI benefits, many of the unemployed are forced to borrow to pay their bills. But borrowing is difficult in the current credit crisis. In addition, many adjustable rate mortgages are resetting, requiring higher monthly payments. Even the short-term unemployed may face pressure meeting mortgage payments. A temporary increase in UI benefits can thus help forestall mortgage foreclosures for a vulnerable population.

This is not of course to suggest that UI reform alone is enough. A meaningful stimulus package should also assist workers who are not eligible for UI—for example, by improving food stamp eligibility and delivery. But UI reform should be a central part of any sensible stimulus package. In this most recent economic slowdown, the set of policy choices we've made does little to buffer harsh consequences for low-income workers. By helping those workers, we not only assist where need is greatest, but we promote economic stimulus by smoothing consumption and bolstering demand. The simple conclusion: A reformed UI would help not only those who find themselves out of a job but the rest of us as well.

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A Golden Parachute FOR EVERYONE?

Dalton Conley

In the standard, industrial society model of Keynesian economics, job growth drives the economy, and consumption, in turn, is what drives job growth. As a result, most politicians are obsessed with jobs as the main avenue to economic security—they push the idea that we need to create more and more jobs, and find people to fill those jobs. This obsession leads to a tilting at windmills on the part of political leaders, particularly during election years—and doubly so during recessionary election years such as this one.

Mainstream Democratic politicians are right about the fact that productivity gains are not equally distributed among workers. But they are mendacious in promising that they can fix the problem by scuttling trade deals or cutting tax rebate checks. In a globalized economy where wages are always lower somewhere else, keeping manufacturing jobs here is a losing battle. Instead we should focus on de-linking—to the maximum extent possible—economic security from the vagaries of the labor market by helping average Americans become part of an investor class. We Americans should be thinking about ourselves as an investor society, as global capital managers. Yes, this may take a feat of imagination to envision during a period of recession, but if we don't take stock of our fundamental policy strategies during a downturn, when will we?

With the current consumption-based approach to social and economic policy, there will always be a disconnect between the macroeconomic health of the U.S. economy and the fortunes of the typical American family. Productivity growth results in the shedding of jobs and a windfall for the few—the executives and major shareholders—instead of the many. By contrast, if everyone were an investor, productivity gains could instead be distributed in the form of dividends. When productivity increases, we could actually work less, taking more time off when our kids were born or our parents were ailing, for instance. Such a work-deemphasizing approach would represent nothing short of a whole new economic policy, one more appropriate for a post-industrial knowledge economy than the New Deal's vestigial, social insurance model.

This need for a national family investment policy is made all the more pressing by recent trends in private savings rates nationwide. In 1984, the rate stood at 10.4 percent of national income. By 2006 it had slid into the red (–1 percent). We have the lowest savings rate among the world's largest economies, and the lowest domestic savings rate since the Great Depression. How is it possible that we had negative savings even in the early 2000s, a time of economic growth? Answering this question is key to understanding the recent disconnect between the macroeconomic health of the economy (as traditionally measured) and poll numbers showing an American public anxious about their economic prospects.

We need to do something drastic to raise our savings rates in this country—across the socioeconomic spectrum—or face a future in which we do not control our own financial destiny.

Obstacles to Savings

Today's relentless consumption and depressed savings is a relatively new development, not a long-standing feature of American culture. These outcomes may be understood as the result of outmoded social arrangements that depress savings in general and retirement savings in particular. The following four factors are especially problematic.

Over-reliance on employer-based plans: Like our health care system, our savings system is broken partially due to its historic link to employers. But today, in an era of flex time and frequent job change, only about half of all workers are covered by an employer retirement plan. And less than 30 percent of low-income workers (the bottom fifth of the income distribution) have the opportunity to take advantage of such plans. Just as it does not make sense from a competitiveness or efficiency standpoint for the United States to lean on employers to provide health care, the same can be said for savings policy. It is time to recognize that a system created in a previous labor market does not work in today's climate. Individuals should be able to enjoy all the tax and match benefits of savings regardless of who their employer may be or whether they are employed at all.

Overly complicated tapestry of plans: The number of savings plan types is truly dizzying: traditional IRAs, Roth IRAs, 401(k) plans, simple 401(k), 403(b) plans, 457 plans, thrift savings plans, simple IRAs. The list goes on and on. Worse yet, given the nature of politics and the policy-making process, legislators often just add to the existing smorgasbord of programs. As with tax reform, it comes time every so often to overhaul the system and simplify. That time has come. Why is less more? With a smaller number of clearly delineated plans, it becomes easier to explain which plans should be used for which purposes, and the public is accordingly less likely to abandon all hope of understanding.

Silo-ed savings plans: In addition to the various retirement savings options listed above, we also have savings plans for health and education (health savings accounts, Coverdell IRAs, 529 plans). However, an integrated, lifetime savings policy would create a single mechanism to incentivize savings for a variety of productive purposes. Of course, we would need to rethink bankruptcy and other laws to protect essential savings from creditors in much the same way that retirement savings currently enjoy a privileged position. In other words, if we were to link all tax-privileged savings plans into a single account, we would need new rules to protect some portion of those savings for retirement—in case, for instance, a family were devastated by medical bills.

We Americans should be thinking about ourselves as an investor society, as global capital managers. Yes, this may take a feat of imagination to envision during a period of recession, but if we don't take stock of our fundamental policy strategies during a downturn, when will we?

Lack of commitment mechanisms: We know from behavioral economics that future commitments to save are easier to make than current commitments, since people tend to discount the future more than they “should.” Yet we continue to have a policy that does not take into consideration this fundamental aspect of human nature. We need a policy that allows individuals to commit to future withholdings, even if they do not feel ready to contribute at a particular point in time. We also need to offer individuals the option of electing “covenant” savings plans. Borrowing from the covenant marriage movement, this election would stiffen rules for withdrawal and strengthen future contribution commitments.

If we were to achieve a consensus that traditional social insurance is simply not enough in a post-industrial economy, what would an investor society policy environment look like? An attractive approach is outlined below.

Toward an Investor Society Policy

The hard part of saving, everyone knows, is being able to forget about all the other seemingly endless needs and wants that arise each pay cycle and instead squirrel away part of our check. Those in the middle and working classes have it particularly rough in this regard. They have more financial pressures, and they frequently do not have an employer who is willing to match savings with company funds.

In fact, H&R Block recently conducted an experiment in which one group of income-tax filers was offered a 50 percent match to divert some of their tax refund to an individual retirement account. Only 14 percent took the company up on its offer (though this figure was lower for those who were offered no match or a smaller one). This relatively low figure may dumbfound some economists as irrational. But it makes complete sense to sociologists. Many of Block's clientele are folks who can barely make ends meet on a day-to-day basis. Plus, they are uncertain about the future, and rightly so. Will they hold onto their present jobs in an age of employment instability? Will they even live long enough to enjoy the fruits of their IRA? They may be figuring that \$500 in hand now is a lot more valuable than \$750, plus compounded interest, 20 or 30 years in the future.

But if it is true that future uncertainties combine with the financial stresses of today to put the squeeze on lower-income families' savings, then there is a silver lining, a way to provide these families an easy savings mechanism over the long haul: no-money-down, long-term matches (thereby using the logic of the balloon mortgage payment and other tricks of the sub-prime lending market toward better ends).

This is how it would work: Instead of having to make repeated “savings decisions” to fork over my tax refund year after year in order to qualify for a saver's credit (under the current IRS policy) or an IRA match (under the Block experiment or a similar policy), the individual would agree to set aside future wages—say 4 percent annually for 15 years. In return, the individual gets a \$1,000 initial deposit into a savings account, and a 50 percent government match for that 4 percent over the course of the next decade and a half. The key is that the government would be asking low-income savers to commit to squirreling away future earnings, not current tax refunds (as compared with the H&R Block experiment or the current U.S. saver's credit). This commitment structure gives savers something now while paying later—thus promoting savings by taking full advantage of what we know about human behavior.

Building on this idea, such a plan could borrow inspiration from the covenant marriage movement to strengthen the savings commitment even further. Here, penalties for non-qualified withdrawals would be more severe. We could use the future match rate as an incentive for individuals to commit to greater savings by offering, for example, a 50 percent match for the first 3 percent of earnings committed to savings; 55 percent for the next 1 percent; and 60 percent for the following 1 percent. This

creates the maximum incentive for everyone to put away 5 percent annually. Individuals could save more of their pretax income (up to, say, 10 percent) on this tax-preferred basis; however, the match would end at 5 percent. The entire system would be limited in the same way FICA is currently limited to the first \$102,000 of compensation in order to ensure some progressivity.

Less more stringent withdrawal penalties seem draconian, universal savings plans could be designed for lifetime use. In other words, we could have one tax-preferred asset account that would work as a 529 college savings plan, a health spending account, and a universal IRA. Thus, withdrawals (up to certain percentage limits for each category) could be made for a wide range of qualifying reasons at any point. Such a plan would be intended to replace all retirement savings plans—employer- or individual-based—as well as savings policies not intended for retirement (such as tax credits on savings).

Evidence from savings experiments also suggests that once the initial barriers to saving have been surmounted, individuals tend to save more. In other words, savings is addictive. I therefore propose that we create a series of universal “family savings accounts,” seeded with \$1,000 at birth, mimicking Tony Blair’s “baby bonds” policy that has been successfully implemented in the United Kingdom. Parents could then direct a proportion of their matched savings to their children’s accounts with no tax penalty. This will make every child grow up with an asset and savings orientation. A successful retirement security orientation must begin with the right policies from the cradle.

While I have focused on improving savings opportunities for low-income Americans here, such policies could (and should) be made universal. This ensures both fairness and political support. But it should be noted that, in general, it is lower-income Americans (and minorities in particular) who face a savings/assets crisis. This is most true in today’s recessionary economic climate, making action all the more urgent and necessary. Key to righting American savings rates as a whole is fixing the system for the poorest among us.



The Covenant Savings Plan

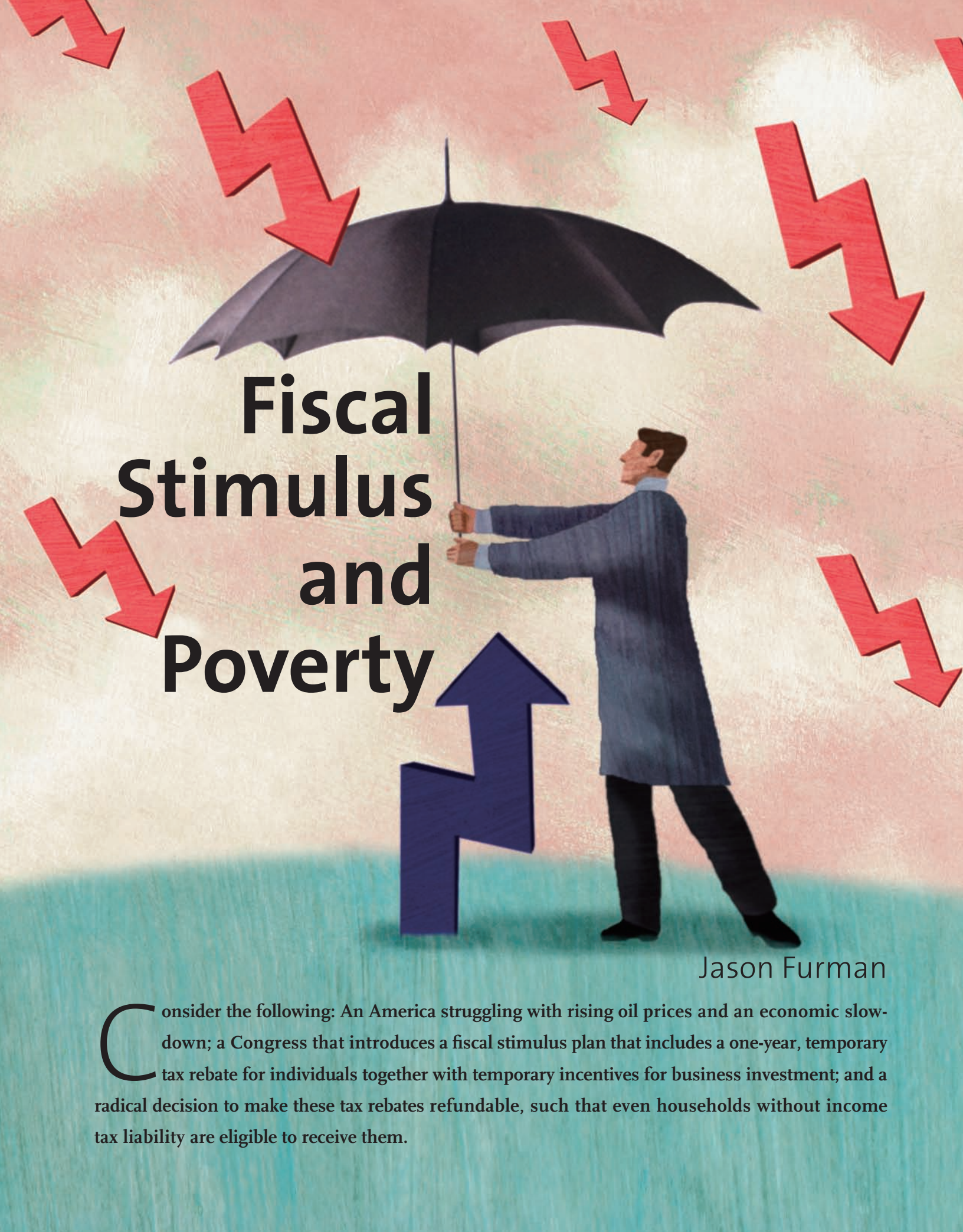
Last year’s Pension Protection Act takes a step in the right direction by encouraging (though not requiring) companies to make 401(k) deductions the default upon employment unless a participant does the paperwork to withdraw. But for the increasing numbers of Americans who are self-employed, temporarily employed, or who work for a company that does not offer a 401(k), we need to create the same structure of savings.

A “covenant savings plan” along the lines of what I’ve outlined here would do exactly that—

provide a mechanism by which those who don’t have the option of a 401(k) at work can check a box once and save for years. This family savings plan should garner appeal on both sides of the aisle. Republicans have long desired private savings accounts for all Americans. Democrats, meanwhile, want to protect Social Security and augment it for those at the bottom of the income distribution. This proposal accomplishes both goals.

Is now the right time to recast ourselves as an investor society? It might well be argued that, however attractive such a recasting might be, we haven’t the luxury of undertaking major reform in the context of dire economic circumstances. But economic history suggests otherwise: It was, after all, precisely the dire circumstances of the Depression that ushered in major institutional reform (in the form of Keynesian economics), reform that served us well for the bulk of the 20th century. Some 70 years later, difficult economic circumstances again cast in sharp relief the deficiencies of consumption-based approaches, shortcomings that can no longer be ignored. These circumstances, for all the short-term pain they cause, will be a long-term blessing insofar as they force us to chart a new and more productive course for the 21st century.

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Fiscal Stimulus and Poverty

Jason Furman

Consider the following: An America struggling with rising oil prices and an economic slow-down; a Congress that introduces a fiscal stimulus plan that includes a one-year, temporary tax rebate for individuals together with temporary incentives for business investment; and a radical decision to make these tax rebates refundable, such that even households without income tax liability are eligible to receive them.

You might think this describes 2008, and you would be right. But it also describes 1975, the birth year of the earned income tax credit (EITC), widely seen as one of America's most successful antipoverty initiatives. And so it follows that recessionary times, however painful, can serve as incubators for policies that reduce the incidence of poverty. I lay out below how we can ensure that the present economic slowdown will again serve as just such an incubator.

But first let's recall in more detail how the EITC came about. The economy had just gone into recession in 1973. It was not until March 1975, however, that Congress finally enacted a fiscal stimulus plan—ironically the same month that the recession ended. The stimulus plan included rebate checks that were partially refundable for low-income households and that were phased out for high-income households. Overall, 6 million households received an average benefit of \$201, yielding a total of \$900 million in refundable credits. That is the equivalent of \$700 per household in today's purchasing power. Scaled as a size of the economy, the refundable credits are equivalent to \$8 billion today.

The idea of work-related tax credits predated the recession, and such credits were supported by President Richard Nixon and many others. But the stimulus bill provided a convenient pretext for enacting them. These work-related refundable credits were extended annually for several years, ultimately made permanent, then expanded in several rounds of tax legislation over the following decades. It wasn't until 2008 that another fiscal stimulus plan explicitly included a refundable component. (The 2001 tax rebate, by contrast, was limited to households that had taxable income before any credits.) It is this refundable component of the stimulus plan that has much poverty-combating potential.

The 2008 Fiscal Stimulus

The mantra that guided the 2008 package was that stimulus should be timely, temporary, and targeted—principles endorsed by figures as diverse as Ben Bernanke, Nancy Pelosi, Martin Feldstein, and Lawrence Summers. All three principles have important economic rationales. Recessions tend to be short-lived, so it is critical that stimulus be delivered in a timely manner. Moreover, fiscal stimulus can boost consumption almost immediately, helping fill in the time before the Federal Reserve's interest rate reductions can affect the economy, a process that takes about one year.

These same factors motivate the temporary nature of stimulus—we would not want to substantially increase the long-run budget deficit to combat a short-term recession. If we did that, we could be doing more harm than good.

Finally, it is important that fiscal stimulus be targeted by impact as well as need. By impact-targeting, I refer to the objective of generating, for every dollar added to the short-run deficit, the largest possible increase in gross domestic product. In other words, if we want stimulus spending to produce the maximum stimulus, we need to target that spending where it is most likely

to be spent by recipients. By need-targeting, I refer to the simple objective of assisting those households that need it most. In all recessions, some people experience large reductions in their income as they lose their jobs or face major pay cuts, while others continue to do fine. And even a small income loss can be very painful for a household living on the edge. A stimulus package is thus need-targeted to the extent that it goes to households experiencing job loss, major pay cuts, or even smaller pay cuts that might nonetheless push them over the edge.

These two senses of targeting are complementary. High-income households can save or borrow to smooth temporary shocks in their income. As a result, a temporary rebate has little impact on that household's consumption, as the rebate is likely to just go into savings. It follows that such poorly targeted rebates will have no expansionary macroeconomic effect. In contrast, as Federal Reserve Chairman Ben Bernanke testified earlier this year, "If you're somebody who lives paycheck to paycheck, you're more likely to spend that extra dollar." This is why the Congressional Budget Office and Moody's Economy.com both gave temporary increases in food stamps the highest rating of any fiscal stimulus policy.

The fiscal stimulus of 2008 did a much better job on the timely, temporary, and targeted dimensions than pretty much any fiscal stimulus that preceded it. It was enacted just as the economy was slipping into recession (if indeed the current episode is ultimately classified as an official recession). The provisions of the stimulus are all slated to expire, and it is my expectation that they actually will. And, finally, the majority of the stimulus was very well targeted, including \$40 billion in refundable tax credits—five times larger as a share of the economy than the pioneering 1975 refundable tax credits.

Steps for Future Fiscal Stimulus Bills

This stimulus package might therefore be viewed as a template for future bills. But it was the product of compromise and, as such, it inevitably includes items that should be changed. Although some of these changes should occur this year, others should be borne in mind for stimulus bills in future recessions. There are three changes, in particular, that merit singling out.

Extended unemployment insurance. First, the fiscal stimulus bill should have extended unemployment insurance to cover long-term unemployment—a problem that should be remedied immediately. This is especially pressing because the long-term unemployment rate is not just higher than it was going into either of the last two recessions, but is in fact even higher than it was when President Bush proposed extended unemployment insurance benefits in 2002.

Medicaid protection. Second, the fiscal stimulus should aim to protect poor people not just from direct financial hardship but also from the other consequences of recessions, particularly from state cutbacks in critical safety net programs like Medicaid. This protection could be fostered by temporarily increasing the federal match for Medicaid, a step that was taken in 2003.

This will help ensure that much or all of the additional money is used for this purpose, both because the increase would require states to maintain a specified level of financial effort, and because the increase would effectively lower the price of state provision of Medicaid services.

More low-income targeting. Finally, although it is too late to reopen this year, future fiscal stimulus bills should do more for low-income households. The \$40 billion in refundable tax credits was an impressive negotiating accomplishment for House Democrats, but it should not be the template for future fiscal stimulus bills. The final legislation limited low-income households to receiving as little as half as much money as middle-income households. The governing principle in future bills should be a flat, refundable tax credit—phased out for high-income households. In addition, other mechanisms like temporary expansions in food stamps, SSI, or Social Security benefits are an administratively simple way to quickly get money into the hands of the households that are most likely to spend it.

Beyond an Ad Hoc Approach

Passing timely, targeted, and temporary fiscal stimulus bills every time there is a recession would be a major policy accomplishment. But one would not want to rely on such an ad hoc approach. One reason the stimulus passed so quickly this year was the accident of election-year timing. Can we ensure that poverty-reducing stimulus is applied even when the business cycle happens to play out in a less timely way? I review below four structural reforms that would assist in meeting that objective.

Automatic stabilizers. We should improve the “automatic stabilizers” that supply fiscal stimulus as it is needed. For example, when the economy turns down, an automatic stabilizer boosts unemployment insurance benefits and reduces tax revenues, both of which act as automatic fiscal stimulus. As a general principle, the more progressive the tax and transfer system, the more potent are the automatic stabilizers. Unfortunately, policy has been moving in the opposite direction, and the current automatic stabilizers are less effective than they were in the 1960s and less effective than those found in most European countries. The automatic stabilizers would be strengthened if people automatically got more money when their incomes fall and paid more money when their incomes rise. For example, increasing the EITC, expanding eligibility for food stamps, or shifting to a more progressive tax system are all steps that would help make the economy more recession-proof by automatically injecting money to the households most likely to spend it when their incomes fall.

Better indexing. Recessions often coincide with commodity price increases, yet relief is not indexed to those increases. The food stamps program, for example, is not indexed for food price inflation. Thus, when families most need money and when the economy most needs stimulus, food prices and the value of food

stamps move in the opposite direction. Indexing food stamps in this manner could help protect the poor against the worst of macroeconomic maladies: stagflation.

Rainy day funds. Recessions often lead states to cut back on essential services. To avoid this, states should refrain from extensive spending and tax relief in good years, instead setting aside revenues in “rainy day funds.” The federal government could also help more given its superior ability to borrow in a downturn and pool risks across states. One helpful reform would be to index the federal government’s Medicaid matching rates to a national or state indicator of economic activity.

Modernizing unemployment insurance. Unemployment insurance is desperately in need of modernization. The system has been essentially unchanged since its creation in the 1930s. It does not cope well with intermittent workers, temporary workers, the self-employed, or multiple job holders—many of whom are poor. Also, the triggers in place to automatically extend unemployment insurance benefits are badly designed and almost never employed, even in a severe downturn. A number of steps could help remedy these problems, including federal standards for state eligibility rules that make it easier for part-time and low-income workers to qualify for benefits, voluntary accounts to help workers smooth their income during spells of unemployment, and updated rules to trigger extended unemployment benefits based on the actual unemployment rate in states.

Minimizing a Recession

Advocates of antipoverty policies generally stress complementarities with other policy objectives, often rightfully so. In the case of economic stimulus this complementarity has been verified by a substantial body of research and is broadly accepted. Putting money in the hands of the poor can help reduce the severity of a recession. And reducing the severity of the recession is the most important step we can take to mitigate any increase in poverty.

Although the current stimulus package is in many ways a template for the future, there is no guarantee that future downturns will again occur at precisely that time in the election cycle when legislative action becomes viable. I have thus outlined how we might build in automatic stimulus and poverty-reduction via stabilizers and indexing. While we should take as many steps as we can, both on an ad hoc basis in terms of better fiscal stimulus policies and on a permanent basis by improving antipoverty programs and the automatic stabilizers, ultimately we should recognize that we can no more legislate the business cycle out of existence than we can eliminate the link between economic activity and poverty. The poverty-inducing effects of the business cycle can in this sense be dampened but not eliminated.

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Killing Two Birds with One Stone

HARDER THAN YOU THINK

Ron Haskins

The bipartisan stimulus package enacted in February 2008 was, like most stimulus packages, a straightforward application of Keynesian fiscal policy: Spend your way out of recession. To the extent that recessions involve declines in consumption, convincing people to spend more money might prevent a recession or make a recession shorter and shallower than it might otherwise have been. Given that consumer spending comprises 70 percent of the nation's GDP, stimulating consumer spending as an antidote to recession has face validity.

Thus, policymakers have long responded to evidence of an approaching recession by increasing government spending in ways designed to increase consumer spending. In fact, programs like unemployment insurance, food stamps, cash welfare, and a number of others are said to be automatically countercyclical because as a recession sets in people lose jobs and qualify for unemployment insurance and welfare. As a result, they have more money than they would have had without the government benefits and they are—given their financial condition—likely to spend it, thereby achieving the desired end of increasing economic activity.

On those unfortunate occasions when Congress is looking for ways to spend additional money to stimulate the economy and avoid recession, advocates concerned with the rise of inequality in America over the past two or three decades might wonder whether it would be possible to design a stimulus package that would also have the long-term effect of reducing inequality or—the other side of the same coin—increasing economic mobility. Personally, I'm skeptical about whether a stimulus package, even the stimulus package passed on a bipartisan basis in February, will achieve its major goal of getting the economy back on track, let alone killing two birds with one stone by simultaneously having an impact on inequality. Sending a \$150 billion stimulus package out to boost a \$14 trillion economy strikes me as tantamount to sending a tugboat into a hurricane to rescue an ocean liner. Even so, let's ignore whether a stimulus package might actually stimulate something other than the federal deficit, and reflect on how stimulus packages differ from reforms designed to reduce inequality and promote mobility.

According to Doug Elmendorf and Jason Furman of the Brookings Institution, there is substantial agreement among economists that a good stimulus plan must be timely, targeted, and temporary. Timeliness is difficult to gauge. Policymakers want to boost the economy just as it is about to nosedive by boosting spending and consumption. But if we think we're entering a recession and we're not, stimulating the economy is inflationary. So the emergency spending both adds to the deficit and boosts inflation. But if policymakers wait too long, the spending package could come after the recession is already well under way or nearing its end. In either case, policymakers' attempt to help the economy could increase both inflation and the deficit without producing much good.

Even if the timing is right, and Congress acts in timely fashion as it did earlier this year, the money must arrive quickly in the hands of people who will spend it. As Elmendorf and Furman put it, the targeting must be right. If the money—\$1,200

for couples and \$600 for individuals in the current case—is sent to middle class households, as more than half of it was under the current plan, the households may save a substantial fraction of the money or use it to pay off debt, thereby defeating the purpose of the stimulus. Similarly, the provision in the package allowing rapid expensing of equipment and thereby increasing the cash available to businesses does not come with a guarantee that businesses will spend the funds on new equipment or new hires. In large part, the economy is in the doldrums because of excessive borrowing for lousy investments, so there may be reason to question whether individuals or businesses will suddenly make sound investments—especially given that good investments are relatively difficult to find during a recession. Still, it must be granted, if many of the credit-constrained businesses use their savings to hire or make productive investments in equipment, there will be some economic boost.

Finally, a good stimulus package must be temporary. Historically, the American economy has been the most innovative and productive in the world, characteristics that most economists believe result in part from low taxes and decisions by risk-taking individuals and corporations who operate without major government interference. If a stimulus package gets the economy back on track, it is important to quickly restore the level of government spending and government interference in the economy to the status quo ante. In fact, under Keynesian theory, after the economy recovers the government should tax more than it spends to maintain fiscal balance. In any case, by sending out one-time checks, making income from the stimulus checks that is spent within two months tax free, and allowing one-time expensing of equipment, most of the spending in the stimulus package meets the criterion of being temporary.

Tallying the score of the stimulus package on the three criteria of timely, targeted, and temporary, the package earns high marks—with the possible exception of being well targeted. The payments do have the effect of helping some families struggling with unemployment, but better-off families are less likely to spend their money. Certainly they are less likely to spend it than other groups that might have been targeted—such as unemployed workers, poor and low-income workers, and welfare recipients.

As a number of critics have observed, it is curious that Congress and the president did not spend more of the stimulus package money on the unemployed or on the poor and near-poor by sending money to households receiving food stamps or the earned income tax credit (EITC). There is good evidence that unemployed workers would spend most of any such money.

Studies show that the consumption of households drawing unemployment insurance falls by only about a third of the dip in consumption experienced by similar households that do not receive unemployment payments. Especially if the money were given as a one-time bonus to all recipients of unemployment benefits, it seems likely that most of the money would be spent quickly. This type of targeting would not only stimulate the economy, which is the prime goal of any stimulus package, but is additionally attractive because it gives money to people who need it to achieve at least some relief from the problems caused by the very recession policymakers are trying to fight.

As with unemployment insurance, providing a one-time payment to food stamp and EITC households would result in poor and low-income families receiving additional money. These households are likely to be even worse off on average than households receiving unemployment insurance and therefore all the more likely to spend most or all of the money as soon as they get it. Yet Congress and the president are sending checks worth \$120 billion or so to around 130 million Americans, many of them richer and in less need of cash than the households drawing unemployment insurance, food stamps, or EITC payments. These wealthier households need the money less and will almost surely be less likely to spend it quickly.

We ought not, however, exaggerate the inequality-reducing effect of such targeting. After all, using the stimulus to boost payments to the unemployed or to EITC and food stamp recipients would not address long-term inequality; it is temporary relief of hardship—worthy policy in its own right, but not necessarily a useful step in reducing long-term inequality. Now, as compared with the three criteria of a good stimulus package, consider the major characteristic of a good program to promote mobility and reduce inequality in a more enduring way. The foremost criterion for a program to promote economic mobility is investment in human capital. The American economy, and the economies of most modern nations, feature many jobs that pay well and provide good benefits, such as health insurance and retirement savings. However, these same economies, especially the American economy, also generate jobs that pay poor wages with few or no benefits. Oversimplifying somewhat, the good jobs require post-secondary education or long-term, structured training and work experience; the low-wage jobs require a high school education or less. In the last three decades the returns to post-secondary education have increased, while the economic situation of school dropouts and high school graduates have stagnated or declined. It follows that if a greater share of Americans were to attend post-secondary institutions, more young people would qualify for decent jobs, and economic mobility would rise while inequality falls. There will always be workers at and near the bottom of the wage distribution, but if they have greater skills they can command higher wages. More skilled workers at the bottom, in other words, would boost the entire bottom of the wage distribution.

It is not necessary to attend a four-year college to realize a sizeable boost in skills and earnings. Harry Holzer and Robert Lerman of the Urban Institute in Washington, D.C., have recently called attention to what they label “middle-skill jobs”

that include clerical, sales, construction, installation/repair, production, and transportation/material moving positions. About half the jobs in the American economy fall into this middle-skill category. Equally important, the Bureau of Labor Statistics projects that about 45 percent of all job openings over the next decade will be in these middle-skill categories. Overall, occupations requiring a postsecondary vocational award or an associate degree are projected to grow by over 20 percent in the next 10 years, and many of these middle-skill jobs fall into this category. Furthermore, wages for many of these middle-skill occupations, such as registered nurses, speech and respiratory therapists, radiological technicians, and electricians, have improved over the past decade and can be expected to continue improving in the years ahead.

Government has done a great deal to enhance the economic well-being of those at the bottom of the income scale. Workers who take jobs at wages of around \$8 per hour would earn perhaps \$12,000 per year if they average 30 hours a week for 50 weeks. But these families do not live by earnings alone. A single mother with two children earning that \$12,000 would be eligible for about \$1,500 in food stamps and a payment of nearly \$4,500 from the EITC. Although wages at the bottom of the distribution have stagnated for three decades, government policy has not. Workers at the bottom are better off as a result, but most of them remain in low-wage jobs and do not advance to better jobs. The stagnation of this group of Americans and their wages is the principle reason the nation has only modest economic mobility compared with many other nations with modern economies. Government subsidies for low-wage workers can improve their economic circumstances and help them avoid poverty, but subsidies do little to increase economic mobility. Similarly, if an economic stimulus package gives more money to this group, they will in all likelihood spend it quickly, but their economic mobility will not increase. Directing money from a stimulus package to families at the bottom (or headed in that direction), as Congress could have done in the 2008 stimulus package by expanding payments to families receiving unemployment insurance, food stamps, or the EITC, would provide them with a temporary boost that would only slightly reduce income inequality. Even so, as soon as the temporary program ends, so would the already slight reduction in economic inequality.

The two key differences between a good economic stimulus policy and a good mobility policy are timeliness and permanency. Stimulating the economy requires an immediate spending boost that ends quickly; increasing economic mobility requires investments in human capital that must be more or less permanent features of public policy and that require at least two years to mature. There is no short-term fix to increase economic mobility. The nation needs a long-term strategy to increase economic mobility—a strategy that focuses primarily on investing in human capital. Policy that boosts human capital cannot and should not be enacted or implemented on the fly.

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Widening Inequality Means a Democracy at Risk

Benjamin M. Friedman



The recent slowing of economic growth in the United States threatens not just financial markets, but also the livelihoods of millions of Americans. The aftermath of even the fairly mild recession of earlier this decade increased the number of families living in poverty by 22 percent (from 6.4 million families to more than 7.8 million). The impact of the previous recession in the early 1990s, likewise only a mild one, was slightly greater. As the economy's pace of expansion continues to slow—from 3.6 percent in 2004, after allowing for rising prices, to 3.1 percent in 2005, then 2.9 percent in 2006, 2.2 percent in 2007 and now perhaps nothing at all in 2008—the important questions that the national debate about economic policy will have to confront will include not just how to restore the economy's growth but also how to think about those whom this newest slowdown will inevitably place under harsher stress.

That debate will be more difficult because of the recent widening of inequality. Even when an economy is growing, as America's has been over the past six years, the interaction between economic growth and changes in distribution governs the extent to which the majority of a country's citizens enjoy rising living standards. A rising standard of living, for the broad bulk of the citizenry, is normally a crucial condition determining whether any society also makes progress in a variety of other dimensions that Western thinking has traditionally regarded as positive in explicitly moral terms: generosity toward the disadvantaged, to be sure, but also tolerance, openness of opportunity, and commitment to democracy, among others. The broader question, therefore, is what measures U.S. public policy can and should take to address not just the immediate economic slowdown but the ongoing combination of modest growth and widening inequality that has resulted in declining incomes for the majority of Americans throughout the current decade.

Rising Incomes and Improving Living Standards

The experience of many countries suggests that when a society experiences rising standards of living, broadly distributed across the population at large, it is also likely to make progress along a variety of dimensions that Western thinking has long held to be not merely positive but morally positive. Experience also demonstrates that when a society is either stagnating economically or, worse yet, suffering a pervasive decline in living standards, it is unlikely to make much progress on these social, political, and moral dimensions.

The reason that economic growth and inequality matter for these positive goals is that most people evaluate their living standards primarily on a relative basis. When asked whether they are well off, most people's normal reaction is to think: relative to what? But at the same time, most people typically have in mind two distinct benchmarks for comparison. Their sense of well-being depends both on how they live compared with how they have lived in the past and on how they live compared with others around them. If these two sources of satisfaction with

one's life are substitutes for one another, as mostly appears to be the case, then getting ahead by either benchmark diminishes the urgency that people attach to getting ahead by the other one. Whenever economic circumstances allow most people to live better than in the past, therefore, the effect is to diminish the importance that people attach to living better than everyone else. Hence resistance to movements that allow others to get ahead is softened.

In America in particular, eras in which economic expansion delivered ongoing material improvement to the majority of the country's population have mostly corresponded to eras when opportunities and freedoms broadened, political institutions became more democratic, and the treatment of society's unfortunates became more generous. But when incomes have stagnated or declined, reaction and retreat have been the order of the day. On one issue after another—not just generosity to the poor, but race relations, religious prejudice, attitudes toward immigrants, even such basics as who gets to vote and under what circumstances—the historical record makes clear that America has made progress mostly when living standards for the majority of the nation's citizens are advancing. With the notable exception of the Depression of the 1930s, the opposite has been true when incomes have stagnated or fallen. And as I argue more fully in my recent book on the subject, this pattern is also characteristic of many other long-established Western democracies.

Consequences of Widening Inequality When Economic Growth Is Limited

When the fruits of an economy's growth accrue disproportionately to only a few people, aggregate growth is not always sufficient for others to get ahead as well. This is especially true in America today, where the labor force is highly heterogeneous (perhaps increasingly so as a result of trends in education and immigration), the economy's large investments in information technology are leading to ever wider differentials in what workers with differing skills are able to earn, and the economy's already-advanced status means that its aggregate growth is likely

to be modest even under the best of circumstances.

Since 2000, the median income among American families (that is, the income of the family just in the middle of the country's distribution) has consistently lagged behind rising prices. Only those who are already at the very top of the income scale have experienced any improvement. In 2006, the latest year for which information is available, the income of the median family was \$58,400. But at the beginning of the decade, the median family earned \$59,400 in 2006 dollars.



It is not the case that there was no aggregate economic growth over this period. Total economic output in the United States expanded on average by 2.4 percent per annum between 2000 and 2006, even after allowing for higher prices, while the population grew by a bit less than 1 percent per annum. The mean per capita income therefore rose in real terms. But widening inequality overwhelmed these gains, preventing any increases, and actually resulting in small decreases for a majority of the nation's families.

This situation differs sharply from what America had experienced throughout most of the nation's past. At times when productivity gains were strong, and the economy as a whole moved forward rapidly—for example, the middle of the 19th century, the early decades of the 20th, the quarter century immediately following World War II and, most recently, the mid to latter years of the 1990s—the bulk of the population likewise enjoyed rising incomes and improving living standards. Conversely, when productivity gains slowed, or the economy faltered for other reasons—in the late 19th century, during much of the period between the two world wars, and for roughly two decades

running from the early 1970s to the early 1990s—the public at large naturally saw little increase. What is different today is that the link between the U.S. economy's aggregate productivity gains and output growth and the increase in incomes and living standards that they deliver to the great majority of American citizens has been severed. The reason is that widening inequality has meant that the fruits of our economic growth have accrued to only a minority of Americans at the top.

What Should Be Done?

With the economy slowing and perhaps entering a recession, much of today's discussion of economic policy revolves around the need to resolve the impasse in the financial markets left by the implosion of subprime mortgage lending and, at the same time, add short-run impetus to economic activity. The Federal Reserve System has already acted forcefully, both to lower interest rates and to provide additional liquidity to banks, and even to investment banks, via several new lending facilities. Congress has enacted a \$164 billion economic stimulus package, of which roughly two-thirds consists of cash transfers mailed directly to individuals and one-third new benefits to businesses from additionally accelerated depreciation of their capital investment.

So far—unlike in most recent recessions—Congress has failed in its effort to extend unemployment benefits beyond the standard 26-week limit. Nor has there yet been any serious consideration of expanding the existing federal antipoverty programs, like food stamps and subsidized housing, nor of incremental public works programs (at either the federal or state-local level) to provide employment directly to those whom the weakened economy puts out of work. Although rising joblessness and reduced income growth inevitably create calls for the former, the success or inadequacy of the nation's poverty programs is more properly a matter for decision with longer horizons in mind. And except for the Depression of the 1930s, when public works programs like the WPA and the CCC made a major contribution to economic recovery by putting millions of Americans back to work, the record of public-sector job creation as an anti-recessionary device is not good; in most cases, by the time the jobs are created the recession is over.

The more important policy discussion, which would have been important even without the current economic slowdown, is what to do about increasing inequality. The principal force acting to widen income gaps in America in recent decades is a technological revolution that has sharply increased the demand for some kinds of skills while reducing the demand for others. As a result, workers who have those newly scarce skills (computer programming, for example, or certain forms of organizational management) have been able to command increasing premiums in the labor market, while those whose skills are in lesser demand (more basic industrial disciplines, or even brute-force manpower) have seen their wages decline and good jobs requiring such skills become harder to find.

Once the technological basis of production has stabilized, systematic economic forces are likely to work in the opposite

direction and counteract further increases in inequality. On the demand side, larger wage premiums for workers with certain skills lead business to innovate in yet further ways, so as to economize on the use of what has now become high-wage labor. At the same time, the larger wage premiums give workers an increased incentive to acquire the skills that are scarce, thereby introducing a supply response as well. Over time, therefore, the widening of inequality brought on by the recent technological revolution is likely to turn around. But this process may be a lengthy one, and along the way the wider inequality remains a fact with which the society must deal.

Public policy can play an important role in accelerating this dynamic response to skill-biased technical change. Education in America is largely the responsibility of the public sector. Numerous public education programs—ranging from improving the basic education that nearly everyone receives, to making college more affordable, to providing vocational training or retraining—could be included in our policy response. The evidence suggests that programs focused on the very young, such as Head Start for preschool children at risk of underperforming in the early grades of elementary school, offer the greatest prospect of success. Such programs simultaneously serve the objectives of rendering the distribution of skills and therefore wages more equal, and of improving the average productivity of the labor force as a whole, hence increasing aggregate economic growth.

There is evidence that other influences are at work too. For example, the skill mix among new immigrants to the United States (particularly legal immigrants) is in part the consequence of immigration policies, adopted in the 1960s, that give priority to immigrants seeking permanent admission to this country for purposes such as family unification or political asylum. From time to time, supplementary policies have sought to redress the resulting skill bias in a limited way. The H-1B temporary visa program, for example, allows up to 65,000 highly skilled immigrants per year to work in the United States for a maximum of three years before returning home. A larger-scale and more comprehensive shift in U.S. policies on permanent immigration would blunt at least some of the effect of skill-biased immigration in compounding the effect on wage differentials due to skill-biased technical change.

Presumably Congress had reasons for setting the immigration priorities that it did, a half a century ago, and objectives like family unification and political asylum are not to be dismissed lightly. But the economic condition of the United States is different today—specifically, economic growth on average is slower and incomes are becoming more unequal, so that the majority of families are no longer enjoying an increase in their standard of living—and so a reasoned assessment may plausibly lead to different choices now than what seemed appropriate then.

In addition, the increase in rewards paid to top executives has absorbed a sizeable share of American corporations' total compensation budgets during the last decade or two. For example, since the early 1990s, the compensation of just the five highest-paid executives at U.S. public companies doubled

compared with their companies' earnings. This trend may be in part due to market forces. But it is also the consequence of corporate governance practices affecting how pay is set, and those rules are, in turn, partly set by public policy. Congress has recently acted to require greater disclosure of executive compensation, and tighter enforcement of existing laws has cut back on some of the patent abuses that contributed to soaring compensation in the past (for example, backdating of options granted to purchase company shares, or falsifying the reported earnings on which incentive pay is often based). Other steps, such as requiring "plain English" shareholder approval of certain forms of executive compensation, are also possible. Here too, redressing widening inequality is hardly the only concern in shaping such policies. But there is no reason to assume that the specific rules of corporate governance inherited from the distant past are the best ones under today's circumstances.

Other changes in public policy, directed not at income distribution but at improving the economy's aggregate growth prospects, are important in this context as well, and not just because the economy may be in a recession. Here many of the answers are already familiar. The U.S. government's again-chronic budget deficits (after a brief respite at the end of the last decade) are sapping the economy's ability to invest in new factories and up-to-date machinery. America's failing schools are not equipping the nation's young people with the skills they need. The country's tax policies are increasingly designed to preserve the position of whoever has already done well (or whose parents did well), rather than create new opportunities for those willing to work and able to contribute. While there is much to debate in the details, the warranted directions in which to move are well known. The faster the economy's aggregate growth, the more room there is for increase in incomes and living standards more broadly.

Whatever actions public policy might take to spur additional economic growth, the implications of today's ongoing increase in inequality in America are sobering. If part of what matters for tolerance and fairness and opportunity, not to mention the strength of a society's democratic political institutions, is that the broad cross-section of the population have a confident sense of getting ahead economically, then no society—no matter how rich it becomes or how well-formed its institutions may be—is immune from seeing its basic democratic values at risk whenever the majority of its citizens lose their sense of forward economic progress. This risk is not just a matter of the current cyclical slowdown. Experience suggests that if the combination of modest growth and widening inequality persists, once the slowdown is over, many of the social and political pathologies that have emerged in the past, both here and elsewhere, are likely to reappear.

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The Politics of Fighting Poverty in Faltering Economies



William A. Galston

The next president has a real chance to reduce poverty and increase opportunity in this country. Indeed, the way forward on those two objectives has seldom been clearer, and the only question is whether the president will be able to frame such an initiative in a way that mobilizes broad-based public and congressional support.

There are two main constraints within which the next president will operate that will affect whether an antipoverty and pro-opportunity agenda succeeds. The first and most obvious constraint is that the president will likely be taking over an economy in the midst of a downturn. Because government revenues decline in a downturn, there will be limits on the number and size of any new initiatives, and such discretionary spending as does occur will be most easily justified in the Keynesian language of economic stimulus. In this article, I will argue that the Keynesian framing lends itself to antipoverty initiatives rather than anti-inequality ones.

The second main constraint is that, despite increased polarization in the electorate, raw partisanship is increasingly unpopular. A premium will be placed, therefore, on crafting an agenda around which a bipartisan consensus can be built. The two main presidential candidates recognize both the need for and public taste for more bipartisanship than has been on display during the Bush administration. This need is magnified, moreover, in an economic downturn because the fiscal constraints that downturns generate create an automatic bias against any costly new initiatives. If that bias is to be overcome, a bipartisan consensus will likely be needed.

I will attempt to lay out the types of antipoverty and pro-opportunity initiatives that might work well in light of these two constraints. The constraints lead us toward many of the same policies and are therefore quite conveniently complementary, which is precisely why I claim that the way forward has seldom been clearer. Although I cannot lay out a comprehensive list of initiatives here, I attempt to identify the three main principles around which such initiatives might be built.

Principle I: Emphasize Poverty Not Inequality

The initiative must be carefully framed to speak to shared commitments. And the winning framing will likely involve a focus on poverty rather than inequality. Whereas poverty is typically defined as *absolute deprivation* (relative to some agreed-upon baseline), inequality does not necessarily imply any deprivation at all, only that some groups are relatively better off than others.

Why should the next president focus on poverty and not inequality? An initiative built on reducing inequality alone is bound to be politically divisive, as it is an initiative that only liberals could embrace. For the most part, what liberals regard as a matter of fairness and social justice, conservatives call envy and class warfare; and conservatives, unlike liberals, are also quite committed to the incentive-generating effects of inequality. There is simply no percentage in this context for liberals to push, almost lemming-like, an anti-inequality initiative when so much headway on an antipoverty initiative might instead be made. If one asks, for example, which of the proposals proffered in this issue of *Pathways* are likely to be implemented and which are not, the simple litmus test of whether they take on poverty or inequality would no doubt serve us well.

In an economic downturn, the rationale for focusing on poverty rather than inequality becomes stronger, and not just because a downturn tends to increase the number of poverty

stricken and hence foster a bipartisan interest in assisting them. Democrats and Republicans alike are perforce interested in delivering stimulus during a downturn, and it is well known that stimulus measures targeted toward the poor are especially efficient because the poor are more likely than the rich to spend that extra cash. The implication is that downturns are tailor-made for antipoverty initiatives but not necessarily for anti-inequality initiatives.

Beyond the steps already taken in this spring's first stimulus package, the particular programs that might in this context be undertaken are well known. There is no compelling reason, for example, why the minimum wage should not be indexed for inflation. And increasing the Earned Income Tax Credit would not only increase work-related income, but also enhance work incentives and strengthen families. We should increase the participation of single workers in the program and reduce the steep marriage penalty now built into its structure.

We could also reduce poverty by strengthening the bridge from welfare to work. The 1996 reform bill worked much better than its critics predicted, but we could improve it by further weakening two key barriers to full-time employment—child care and health care. We should expand the child care tax credit for poor families. Also, while we are debating whether and how to achieve universal health insurance coverage, surely we can agree on a federal-state program that funds and achieves universal coverage for poor children.

All other things being equal, there is a relation between poverty and family structure. At the very least, the federal government could throw its spotlight on what some have called the “sequencing strategy”: If you finish high school, get married, and have children—in that order—both you and your children are much less likely to live in poverty. As part of this push, the government could put new emphasis on reducing teen and unwanted pregnancies, which often disrupt the optimal sequence.

These proposals are for the most part well known. As a general policy, we should build on what works, look skeptically at what has not worked, and experiment only in those areas where we don't know enough to act boldly on a large scale.

Principle II: Means-Testing Has Its Place

The next president should likewise recognize that there is growing support across party lines for means-tested programs. Increasingly, conservatives understand that the market does not cure all social ills and that there is a place for carefully targeted public programs. For their part, most liberals no longer believe, as the saying went, that “programs for poor people are poor programs.” To the contrary, a fair number of means-tested programs have not only survived but thrived, even in adverse political circumstances. The social democratic strategy of garnering widespread support for antipoverty initiatives by including everyone in them is not and likely never will be attractive in the United States.

The rationale for means-testing is yet more compelling in the context of an economic downturn. As I mentioned above,

the most efficient way to spend out of a downturn is to target the poor, as the poor will quickly spend much of their stimulus check. The stimulus package of February 2008 is not as targeted as some might want, but it may well presage more aggressive targeting in the future.

The initiatives laid out under “Emphasize Poverty Not Inequality” are, for the most part, means-tested; hence there is no need to rehearse them again here. These initiatives don’t, however, address the pressing problem that many poor and near-poor families find themselves living from paycheck to paycheck without ever accumulating savings. This makes it difficult for them to buffer themselves against financial reverses, and it either precludes home ownership or makes it possible (as we now see) only on terms that cannot be sustained. To turn this around, we need a means-tested savings match—for example, two public dollars for every dollar saved by poor families, a one-to-one match for near-poor families, and fifty cents on the dollar for the working class.

These types of means-tested programs are usefully contrasted against those that single out a given neighborhood and pour resources into improving opportunities for all neighborhood residents. Because neighborhoods comprise residents of varying economic circumstances, a place-based strategy of this sort is quite poorly targeted, with all the consequent inefficiencies that entails. The evidence on the effectiveness of place-based strategies is scanty at best. We would do better to invest in means-tested strategies that allow hard-hit urban areas to benefit in proportion to the number of residents who meet the test.

Principle III: Facilitate Opportunity

The third, and final, principle that should inform the next president’s program is to foster opportunities rather than guarantee mobility outcomes. Opportunity is typically understood as a set of enabling conditions that allow all children, regardless of family background, to compete fairly for those jobs or occupations to which they aspire. We have sought to increase opportunity in this country by strengthening primary and secondary education, by providing information and resources needed to take advantage of post-secondary education and training, and by building an economy that offers jobs to all willing workers. By contrast, mobility pertains not to opportunities but to outcomes, and it is accordingly measured by comparing the occupations (or income) of parents to the occupations (or income) of their children. It may be understood as the realization of the opportunities to which individuals are exposed as well as their decisions whether to “take up” those opportunities.

While liberals often argue that family background should have no impact on how children fare later in life, conservatives are less sure that this is an appropriate ideal because it necessarily interferes with the prerogative, indeed responsibility, of parents to assist their children. Moreover, they are concerned that perfect mobility could not be achieved without massive social disruption, perhaps even a dismantling of the family itself. The implication, again, is that bipartisan support is best achieved by focusing on equalizing opportunities, an objective that is surely in itself sufficiently daunting.

How might opportunity be equalized? Our most urgent and important task is to mount a comprehensive assault on the shortcomings of our educational system. We know, for example, that fully half of the “achievement gap” between white and minority students at age 18 is attributable to differences that children bring with them to the first day of public school. So we need measures to ensure that children arrive at school ready to learn, including a federal-state partnership to make pre-kindergarten education universal for all 3- and 4-year-olds. Based on state-level programs, it appears that means-tested subsidies to families are efficient and effective.

There are other important gaps in our education system that we must fill. For example, because they have fewer opportunities for enriching activities outside school, poor children are more likely to lose ground during the summer. “Opportunity vouchers” for summer school would help them retain what they learned during the previous year.

We have also recently learned that we have been fooling ourselves for decades about high school graduation rates. In major urban areas, the real rate of on-time graduation with a regular high school diploma barely reaches 50 percent. The Department of Education has recently required all states to adopt a uniform system of accounting and reporting for dropouts. That’s a sensible and long-overdue step, but it’s only a start.

In today’s economy, young people without a diploma are all but doomed. This is especially true when the labor market they enter is weakened by an economic downturn like the one we are currently experiencing. To avoid losing another generation to the streets and prisons, we need a crash anti-dropout plan. Starting in middle school, every student at risk of dropping out should be paired with an adult mentor who monitors progress, offers assistance and advice, provides information and encouragement about post-secondary opportunities, and warns teachers and administrators when a student seems to be veering off the path.

Finding Political Common Ground

The next president should build on areas of agreement across partisan and ideological lines. Because reducing poverty, assisting those in need (means-testing), and enhancing opportunity are themes that resonate through most of the political spectrum, they should constitute the foundation for his efforts. In an economic downturn, the task of developing political common ground is even more critical, as one must overcome real fiscal constraints that make it difficult for all but the most strongly supported initiatives to succeed.

I do not mean to suggest that my proposals—none of which is original—represent an adequate response to the difficulties we face. But they do offer three key advantages: They have already been tested, they can achieve support across party lines, and they are well-suited to an economy entering a downturn. A skillful and determined president of either party could, I believe, create broad agreement on such proposals without squandering scarce political capital.

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Creating Second Chances

BY DEVAH PAGER

With more than 2 million individuals currently incarcerated in the United States, and more than 12 million who have prior felony convictions, integrating the large and growing population of the formerly incarcerated has become an urgent priority. Because steady work reduces the incentives

that lead to crime, making sure ex-offenders find employment is crucial. But ex-offenders face bleak prospects in the labor market, in part because a criminal record makes it difficult to find work. Indeed, survey estimates suggest that more than 60 percent of employers would not knowingly hire an applicant with a criminal background.

These problems were revealed in a recent experiment I carried out using an audit methodology that sends pairs of job applicants to apply for entry-level jobs. The pairs were carefully matched in all respects (such as education and training) except that one presented evidence of a criminal record and the other did not. I found that employers use the “negative credential” of a record as a screening mechanism, weeding out ex-offenders at the outset. As a result, ex-offenders were only one-half to one-third as likely to receive initial consideration from employers, as compared with equivalent applicants without criminal records. Given these stark differences, the problem of finding steady work for the large numbers of ex-offenders returning to communities each year is clearly a challenge.

Of course, it is important to keep in mind that the employment of ex-offenders is not necessarily without cost. Employers bear the burden of workplace theft and workplace violence as well as the more mundane problems of unreliable staff and employee turnover. A criminal record is arguably a relevant signal. Indeed, to the extent that the past is a strong predictor of the future, a conviction conveys some information about the likelihood of future illegal, dangerous, or debilitating forms of behavior. Employers thus have good reason to be cautious about hiring individuals with known criminal pasts. Any policy designed to promote the employment of ex-offenders must address the risks employers face when they hire individuals with criminal records.

This article will consider how we might reform prisoner re-entry interventions and policy in light of the evidence of what works, what doesn't, and why. The current political environment points to some optimistic signs for significant policy reform in this area. The Second Chance Act, passed recently with broad bipartisan support, authorizes a range of programs and services in support of a more integrated and proactive model of prisoner re-entry. Though this bill remains limited in scope, it signals a willingness among politicians on both sides of the aisle to confront this pressing matter.

Avoiding the Mark

Current estimates suggest that nearly 700,000 inmates will be released from prison this year. Given ongoing prison expansion, the problem of prisoner re-entry will only continue to grow. Over much of the past three decades, the expansion of the criminal justice system received widespread support from politicians and the public. The nearly universal call for stricter enforcement and harsher penalties largely muted consideration of viable alternatives to incarceration.

Now, however, there is some indication that the tide is turning. After a decade of falling crime rates and an expanding economy through the 1990s, public sentiment became more receptive to alternatives, emphasizing longer-range solutions to the problems of crime and delinquency. Fully three-fourths of Americans surveyed in 2002, for example, approved of sentencing nonviolent offenders to probation or treatment instead of prison. Whereas Americans were more evenly split in 1990 over the goals of prevention versus punishment, more than two-thirds now believe that more money should be spent “attacking the social and economic problems that lead to crime through better education and training” as opposed to “detering crime by improving law enforcement with more prisons, police, and judges.” Furthermore, the majority of Americans now favor eliminating mandatory sentencing laws and returning discretion to judges.

At the same time, as the economy slows and states face tightening budgets, legislators are also looking for more cost-effective ways to manage crime. By 2003, more than a dozen states had made significant changes in their sentencing or corrections policy, including the repeal or reduction of mandatory sentencing laws for drug offenders, changes in approaches to technical violators of parole, increased investments in rehabilitative services, and the expansion of treatment alternatives to incarceration. If sustained, these changes could have long-term effects on the rate of incarceration and on the total number of individuals behind bars. There exists a glimmer of hope, then, that the rapid 30-year expansion of the criminal justice system may at last be slowing its pace.

As states consider moving away from imprisonment, there has been a renewed emphasis on finding alternatives to incarceration. Although still representing only a small fraction of criminal justice expenditures, many states are experimenting with programs that place an emphasis on restorative justice, community service, treatment, or intensive community supervision. Evaluations of these programs have found that certain alternatives to incarceration can in fact have sustained positive effects. Indeed, despite the pessimistic reviews of prison rehabilitation from the early 1970s, there is more recent evidence to suggest that well-targeted programs can have lasting effects on drug abuse, employment, and recidivism.

Given ongoing prison expansion, the problem of prisoner re-entry will only continue to grow

One model that has spread quickly in recent years is the drug court, a set of proceedings that runs parallel to, but independent of, the criminal court. Drug courts recognize that users and first-time offenders can often benefit from treatment, mental health services, and close supervision rather than confinement. These diversion programs allow minor offenders the opportunity and assistance to go straight before harsher sanctions kick in. In many cases, those who successfully complete the treatment program authorized by the drug court avoid altogether the formal markings of a criminal conviction.

The research on such issues reveals that reduced rates of recidivism among drug court participants and the savings relative to traditional court interventions are indisputable. These results provide support for the notion that well-targeted, sustained interventions can complement, and in some cases replace, incarceration with more lasting positive results. If federal and state governments are willing to invest in the development and evaluation of prison alternatives, the long-term costs of crime and incarceration could be substantially reduced.

Easing the Transition

A second strategy for easing the problems of prisoner re-entry—and for reducing the extraordinarily high rates of recidivism—emphasizes assistance in the transition from prison to home. One particular approach that has received little attention in the evaluation literature, despite its growing popularity in practice, involves intermediaries who facilitate employment of returning inmates. Intermediaries function as liaisons between employers and ex-offenders, often making first contact with employers, discussing the employer’s staffing needs and evaluating the possible fit between the employer and particular ex-offender job seekers. Intermediaries can help reduce employers’ concerns about hiring ex-offenders by vouching for the individual in question and by providing additional supervision capabilities through the initial employment transition. In this process, intermediaries also serve as staffing agents for employers, particularly those not large enough to have a human resources division and those who lack the time to screen many applicants from the open market. Furthermore, intermediaries can address the job-readiness needs of ex-offenders, including simple issues such as attire and interview skills as well as more complicated concerns about job skills and substance abuse. Several model programs in New York, Chicago, and Texas have been recognized for their success, each showing strong improvements in the employment outcomes of ex-offenders and significant reductions in recidivism. For example, an independent evaluation of the Texas-based project found that participants were nearly twice as likely to find employment relative to a matched group of parolees (60 percent versus 36 percent), and rates of re-arrest and re-impris-

onment were likewise significantly reduced. More evaluations employing careful experimental designs would strengthen our understanding of what works and point us toward successful models for a national program.

Although re-entry policy has emphasized employment for keeping ex-offenders out of crime, little has been done to safeguard those employers who stand at the front lines of our re-entry initiatives. Currently, only one resource, the Federal Bonding Program, provides some relief for employers who suffer loss or damages caused by an employee. The bonding program insures ex-offender employees (at no cost to the employer) for between \$5,000 to \$25,000 for a six-month period. This sum, however, is woefully inadequate relative to the size of negligent hiring lawsuits, which can reach 100 times that amount. We need to think more carefully about the necessary incentives to encourage employers to hire ex-offenders. At a minimum, an effective policy would impose limits on liability, or assume federal responsibility for a larger share of damages. If we believe that the employment of ex-offenders is an important step toward criminal desistance (and therefore relevant to public safety overall), employers should be encouraged, not punished, for providing this population with a much-needed second chance.

Erasing the Mark

The criminal credential does not fade with time. With no mechanism for removal, the information remains prominently displayed in background checks, coloring the reception even of those most indisputably rehabilitated. Several years ago, for example, I received a letter from a 43-year-old man in Missouri. He had been laid off from his job as a carpenter/contractor about six months before, and had been searching for work ever since. A felony conviction from 10 years earlier kept coming up in job interviews and, in the slow-growth economy, no employer seemed willing to take him on. He talked about his three young children, and his frustration in not being able to provide for them. He said his heart broke each morning when his 6-year-old daughter would leave for school and say to him, “Good luck in your job search, Daddy!” knowing that he would have to face her later that day with nothing more to offer.

Criminal records have been distributed ever more widely in recent years. Even those states prohibiting discrimination on the basis of criminal background continue to allow employers full access to information about criminal backgrounds, despite the fact that in most cases they are not supposed to use it. This policy is somewhat incongruous, especially given that other protected categories place corresponding restrictions on access to “incriminating” information: Employers are not permitted to ask the age of applicants, nor their marital status; and information about

the race of applicants, while often collected for Equal Employment Opportunity Commission reporting requirements, is always optional.

In my earlier review of job applications, I noted that a few large national employers had modified the questions on their application forms to respond to specific state law. For example, one employer’s application form asked about prior convictions for theft or embezzlement but did not seek information about other types of criminal convictions. These employers took it upon themselves to limit exposure to information that could taint their evaluation of candidates for reasons unrelated to the job, or in ways sanctioned by the state. Nevertheless, it is unrealistic to expect all employers to adopt such sophisticated and variable screening procedures. Rather, state governments could far more effectively govern when and where criminal record information is made available.

The United States is unique in privileging access to information over other social and political priorities. Many other countries, by contrast, place significant restrictions on access to information about the private experiences of individual citizens with the law. In France, for example, information about individual criminal backgrounds is carefully safeguarded within a single centralized and government-controlled database. Certain employers have the right or are even required to obtain criminal background information on prospective employees, while the vast majority of employers and other private citizens have no grounds for accessing this information. Indeed, it would scarcely occur to most French citizens to think of such information as relevant to the employment process. In the U.S. context, there are twelve closed-record states in which criminal record information is limited and regulated by centralized state agencies and provided to employers only when a reasonable case can be made for direct relevance. There is a strong argument for mandating such a system throughout the country.

Another approach is to place time limits on access to information about an individual’s criminal history.

The risk of re-offending declines precipitously following the first three years after release, and after five years without arrest, the rate of re-offending is extremely low. The public safety rationale for identifying an individual’s criminal history beyond this point thus becomes steadily less compelling. Simultaneously, the possibility of expungement (or the sealing of records) offers a tangible incentive for ex-offenders to stay out of crime. If an offender feels he will be relegated to unemployment or dead-end jobs for the rest of his life as the result of a prior conviction, the lure of the illegal economy becomes all the more powerful. If, on the other hand, this individual knows that buckling down for just a few years will earn him the opportunity to escape his past and build a better future, the incentives to stay

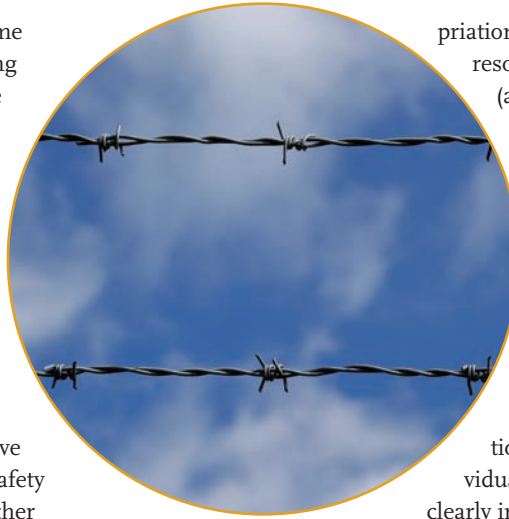
**The
Second Chance Act
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clean increase. The case for imposing time limits on the distribution of incriminating information has direct precedence in the case of credit checks. According to the Fair Credit Reporting Act of 2002, breaches of credit worthiness must be wiped clean after seven years. The law implicitly acknowledges that, while lenders and financial agents must be aware of the credit risks of prospective clients, individuals must be granted an opportunity for a “second chance” at financial solvency. Time limits on credit blemishes allow individuals to move beyond past mistakes. So, while public safety concerns mandate that employers and other members of the public retain the ability to identify those engaged in criminal activity, for individuals who have left their criminal past behind them (as the vast majority of young offenders eventually do), the opportunity for a fresh start should be granted. At the time of this writing, seventeen states allow certain convictions to be expunged or sealed. Many of these laws limit expungements (or sealing) to first-time offenses or grant them after an individual has remained crime-free for a specified amount of time. Federal policy could help make such expungements more widespread and uniform for reasonable types of employment and offenses.

Toward a Comprehensive Policy for Prisoner Re-entry

Fortunately, there are some signs of progress in re-entry policy. After winding its way through Congress over a period of more than five years, the Second Chance Act was passed in April 2008 with broad bipartisan support. The act authorizes \$300 million in grant programs to facilitate successful re-entry, including funding for local re-entry demonstration programs; grants to provide job training, mentoring, and transitional services; new funding for re-entry courts; funding for substance abuse treatment and drug courts as alternatives to incarceration; and grants for research and evaluation of re-entry policy and practice. The act sets a broad and ambitious agenda by providing integrated services and alternatives to conventional crime control techniques. Departing from recent decades, when reincarceration was the primary tool used to manage re-entry failures, this policy approach recognizes that the transition from prison to home is fraught with roadblocks, and that goals of reducing recidivism can be reached only by developing realistic alternatives and support along the way.

At the same time, the Second Chance Act represents only a first step in this direction. The \$300 million authorized at the time of this writing (albeit not yet cleared through appro-



priations) is a relatively small commitment of resources for such a huge social undertaking (and trivial relative to the overall annual corrections budget of \$56 billion). Moreover, there are critical components that have been left out of the final legislation. One of the key legal barriers facing ex-offenders, for example, is pervasive restrictions on occupational licensure, barring many ex-offenders from public sector employment and a growing number of private occupations.

In certain cases, the logic of these occupational restrictions is straightforward—individuals with a history of violent crime are clearly inappropriate candidates for employment in child care institutions or schools. In many other cases, however, legal restrictions on ex-offenders have far less connection to apparent safety concerns. In some states, for example, ex-offenders are restricted from jobs as septic tank cleaners, embalmers, billiard room employees, real estate agents, plumbers, eyeglass dispensers, and barbers. Currently, fewer than half of states offer standards for the use of criminal record information in making decisions about employment and licensure. Federal guidance on this question is much needed.

The current legislation also offers no strategy for the expungement or sealing of records for ex-offenders who have shown clear evidence of rehabilitation. Fortunately, this may be remedied soon. A second bill (the Second Chance for Ex-Offenders Act of 2007) has been introduced into the House of Representatives by Congressman Charles Rangel. This bill, which is still pending, would amend the federal criminal code to allow an individual to file a petition for expungement of a record of conviction for certain nonviolent criminal offenses.

Overall, policy development in prisoner re-entry shows some promising signs of change. No longer is the provision of services to offenders immediately viewed as “soft on crime,” and the broad support for the Second Chance Act suggests great potential for moving beyond traditional partisan lines. But there is still a long way to go. Re-entry capacity at the state and local level remains woefully inadequate relative to the hundreds of thousands of individuals re-entering communities each year. The Second Chance Act sends a strong message about the importance of a coordinated and proactive approach to prisoner re-entry. The task of achieving this goal remains for the future.

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