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# Notes on Inflation and Paid Care Services in the U.S.

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# **Notes on Inflation and Paid Care Services in the U.S.<sup>1</sup>**

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This paper offers a number of reasons why increases in average wages among the lowest deciles of the population are not likely to significantly buffer the effects of rapid inflation on families with incomes below the poverty line. It also raises a number of specific questions for future research.

Much of the discussion on tradeoffs between inflation and unemployment in the U.S. focuses on a comparison between increases in wages and average increases in consumer prices, not surprising given the history of macroeconomic preoccupation with the Phillips Curve. However, serious consideration of the relative impact of these two scourges requires a wider lens, considering uneven and variable impacts not directly related to wage trends.

My comments today are prompted by Paul Krugman's op-ed in the *New York Times* on November 29, 2022, entitled "[Does Inflation Disproportionately Hurt the Poor?](#)" to which he answers, basically, "No." I have many disagreements with his casual analysis but will focus on one here: he seems to assume that most poor people are wage earners and that consideration of wage trends in lower quantiles is sufficient to make his case.

This assumption is incorrect. Even 2021, a year when the unemployment rate was quite low by historical standards, adult poverty was concentrated among non-wage earners. According to the latest Census Report on Poverty in the U.S. (Creamer et al. 2022) 20,982,000 adults ages 18-64 lived in poverty in the U.S. in 2021. Of these, 13,793,000, or about 66%, did not work (for pay) for even 1 week. Many of these were probably engaged in unpaid care and pooling income with a wage earner, but the poverty rate was much higher among those in this "non-work" category—30.0%, compared to 4.7% among those who worked for pay either full or part time. Many of these "non-working" adults faced constraints on their ability to work for pay: The poverty rate of adults 18-64 with a disability was 24.9% (Creamer et al. 2022: Table A.1). The poverty rate of all those living in

a household with a female householder with related children under age 6 was 44% (Creamer et al. Table A.2).

Furthermore, the contributions that wages make to family income are mediated by many factors, including hours of paid employment, the relative contribution of public benefits such as TANF and SNAP benefits, effects on savings, *and* out-of-pocket costs for services such as health care, childcare, eldercare and care of disabled family members. A substantial share of poor and low-income families include young children and include parents (especially mothers) whose employment is constrained by childcare responsibilities. Public childcare services are unevenly and inadequately subsidized, and childcare shortages resulting from the closure of family daycare centers during the pandemic have been exacerbated by a shortage of childcare workers who have moved to better paying jobs (Goldstein 2022).

My hypothesis is that families with dependents (whether young children, elderly, or individuals experiencing illness or disability) have been and remain particularly hard hit by inflation. A cruel paradox is that increases in wages at the bottom of the distribution for employees in childcare and eldercare can have the effect of raising costs and/or reducing the employment hours of low-income families that rely on these services. This paradox emerges from the heavy reliance on market-based paid care provision in the U.S., which, in effect, pits low-wage workers against low-income consumers. One telling example: mortality rates in U.S. nursing homes appears to go up when unemployment goes down, because reluctance to pay higher wages leads to reduction in the quantity and quality of the care services provided (Stevens et al. 2015; Konetska et al. 2018).

I cannot test this hypothesis regarding the incidence of inflation or explore its possible implications here. What I can do is a) describe what we know (and don't know) about trends in the U.S. Consumer Price Index relevant to care services b) discuss some distinctive features of care services that could help explain these trends and c) raise plenty of questions for further research.

### **Trends in the Price of Paid Care Services**

Through its Data Finder, the Bureau of Labor Statistics publishes data on the Consumer Price Index for Urban Consumers (CPI-U) and the CPI-U for Day Care and Preschool, Nursing Homes and Adult Daycare and Medical Care Services. As can be seen from Figure 1 (at the very end of this document), prices from these care services have increased at an especially rapid rate since 1998. Also, trends in prices for these services overlap rather closely.<sup>2</sup>

Purchases of these care services represent a relatively small share of total expenditures compared to those on food, energy and rent, but are nonetheless substantial for those families that do spend money on them. Analysis of data from the Consumer Expenditure Survey (CE) and the Survey of Income and Program Participation (SIPP) could provide more details regarding their relative importance. However, little attention has been devoted to empirical analysis of “care services” as a category; both data resources and secondary analysis remain slim. (Folbre et al. 2022).

### **Distinctive Features of Paid Care Services**

Paid care services differ from other services in significant ways, with implications for relative price trends, industrial organization, and political alignments. Paid provision of health, education, and social services tends to be labor-intensive and person-specific,

involving close interactions between provider and recipient that are often sustained over time. This specificity contributes to information problems, including difficulty ascertaining service quality before purchase. Consumer sovereignty is limited. Institutional factors such as third-party payment complicate transactions, and positive externalities imply that social benefits often exceed private gains.

Not surprisingly, both public and non-profit enterprises play a prominent role in care service provision. Regardless of institutional form, however, the “output” of care services is seldom measured directly: The value of improved health cannot be assigned a clear market value, much less be attributed to specific inputs of time and money. Likewise, the value of educational services that may pay off in higher earnings over an entire lifetime, or social services helping reduce the risk of hunger or homelessness cannot easily be parsed. Because care services are often person-specific, requiring effective cooperation from the care recipient (and, often, their family and friends), it is difficult to measure their quality and their productivity often remains opaque.

Most economic analysis of care services has focused on their resistance to labor-saving technical change. In the early 1990’s, William Baumol deplored the “cost disease” of services, warning that the share of Gross National Product devoted to health, education, and social services was destined to calamitous increase (Baumol 1993). In later years, he softened his diagnosis somewhat, arguing that productivity gains elsewhere in the economy could facilitate increased consumption of services with a high income elasticity of demand (Baumol 2012). Victor Fuchs and others elaborated on these concerns, suggesting that childcare, education, medical care, and long-term care represent a distinctive

subcategory of the larger service sector (Fuchs 2008). It is time to follow up on this suggestion.

William Nordhaus summarized data supporting Baumol's argument that lagging labor productivity in many service industries was associated with increasing relative prices (Nordhaus 2008). However, the categorization of service industries has remained somewhat vague. It includes very disparate components, including typically poorly paid retail services, lucrative business services, and care services aimed at improving health, education, and social welfare. Patterns of technological change and industrial organization obviously vary considerably across these product categories (Baumol himself was most interested in the peculiarities of in-person performance arts).

One early effort to disaggregate service employment broke it down into four subsectors: 1) Distributive Services (transportation, communication, wholesale and retail trade, except eating and drinking, 2) Producer Services (financial, insurance, engineering, law and business services) 3) Social Services (health, education, welfare and government) and 4) Personal Services (domestic, lodging, repair and entertainment) (Browning and Singelmann 1976; Singelmann and Browning 1980). However, U.S. statistical agencies largely rely on more disaggregated categories. The Standard Industrial Classification (SIC) system, developed in the 1930s when manufacturing was ascendant, utilized 12 basic categories, where generic services include primarily personal services, health, and education and other differently named categories (still generally considered services) including wholesale trade, retail trade, public administration, finance/insurance and real estate/ and transportation/communications/electric, gas and sanitary services). Dissatisfaction with these categories led to the development of an alternative system in

1997, the North American Industry Classification System (NAICS), which includes five mainly goods-producing and fifteen mainly service-providing industries.

Categorization matters, because it provides the context for analysis of comparative trends in prices, productivity, and industrial organization. The Browning and Singelmann categorization is more consistent with attention to “Care Industries” than the disaggregated SIC or NAIC codes, although its “Social Services” rubric also includes all government-funded activities, including, presumably, military spending. Victor Fuchs (2008) does not explicitly use the term “care service industries,” but the thrust of his analysis is consistent with this term. Categorical ambiguities are both cause and consequence of theoretical disinterest—especially compared to the manufacturing sector.

Official collection and analysis of price data in the U.S. takes two basic forms. The Bureau of Labor Statistics utilizes data from the Consumer Expenditure Survey and other sources to analyze out-of-pocket expenditures by households to construct Consumer Price Indices. The Bureau of Economic Analysis collects data on personal expenditures that includes expenditures made by institutions (such as corporations and the government) on services destined for household consumption (Jansen et al. 2020). While it is difficult, as previously indicated, to parse specific trends, both series suggest that care industries follow a distinctive pattern.

The construction of price indices is both conceptually and empirically demanding since price changes affect the composition of the average basket of goods and services purchased. In general, the construction of such a basket is based on the average consumer, considered a kind of representative agent. In other words, the composition of the basket of purchased does not vary according to consumer characteristics. Darren Rippy (2014) puts



it this way in his history of the Consumer Price Index, “in reality, each consumer unit (be it a household or an individual) purchases a unique mix of goods and services, and uniquely responds to changes in the relative prices of the goods and services in this basket.” The U.S. Bureau of Labor Statistics has repeatedly considered the issue of whether low-income households are more adversely affected by inflation (Garner et al. 1996; Klick and Stockburger 2021). Recent research suggests that they tend to purchase goods subject to higher price increases (Jaravel 2021; Klick and Stockberger 2021).

This pattern may be partially driven by differences in the composition of households in the lowest quartile, especially the presence of young children, adults with disabilities, or elderly persons, whose needs are likely to affect the consumption basket. These differences are significant since the CPI is used to adjust both Social Security payments and the official U.S. poverty line for inflation. Heterogeneity in the impact of inflation on living standards is not limited to differences in family income or individual wages.

Age is another salient factor. For instance, the Bureau of Labor Statistics has developed an experimental version of the Consumer Price Index for Urban Consumers (CPI-U) for households with members over age 62, labeled the CPI-E, which shows that these households generally experience a higher rate of inflation than indicated by the overall CPI-U (largely as a result of out-of-pocket medical and care expenses). However, the CPI-E is a simple re-weighting of data collected for the entire population; a more accurate measure would be based on a larger sample of older households (Munnell and Hubbard 2021).

Concerns about the applicability of the CPI-U to measurement of poverty trends has intensified as utilization of paid childcare services has increased over time (Sherman and

Van de Water 2019). Child-care costs significantly increase the inequality of family market income, in part because they discourage maternal employment (Gonalons-Pons and Marinescu 2022).

### **Questions for Further Research (a partial list)**

*Regarding trends:* How have the CPI-U trends described in Figure 1 moved in more recent months and how do they compare to personal consumption expenditure data? What factors might explain the convergent trends in the prices of three different types of paid care services, given significant differences in wage trends in health care, childcare, and eldercare? Has increased regulation on the federal and state level played a role? Covid-19 had a crippling effect on small family-based childcare providers, who received relatively little federal pandemic aid.

What has been the impact of increased investment by private equity? Two out of three of the largest childcare center-based companies, KinderCare and the Learning Group, are private equity firms; Bright Horizons is publicly traded; their large size made it easier for them to survive the health challenges and financial stresses of the Covid-19 pandemic (Aspan 2013). The growing role of private equity and associated financialization of the elder care industry have sparked considerable concern (Walker et al. 2022; Harrington et al. 2017). When consumer sovereignty is limited, market pressure to lower the cost of paid care provision may well threaten the quality and quality of services provided.

*Regarding consumption baskets:* How do paid care services (within the industrial categories of health, education, and social service compare (and interact with) with unpaid care services provided within households and communities and those provided by the public and non-profit sector? (Increased utilization of volunteer food banks has been noted

in the media—how extensive are these in the aggregate?). Public policies such as Temporary Assistance to Needy Families (TANF) and the Earned Income Tax Credit (EITC) have increased the paid employment of low-wage mothers, but we know relatively little about the hourly cost of childcare (which could be usefully compared to hourly market wages of mothers) because most surveys collect information on total expenditures but not on hours utilized.

Over the last decades some states have expanded Medicaid-financed access to home and community based care for the elderly and people with disabilities, but regional variation is significant. Such policies are rare in Southern states). How has public spending on the Supplemental Nutrition Assistance Program (SNAP), energy bill and housing assistance been affected by inflation? What do we know about unmet needs for food, housing, heat, and care services, beyond anecdotal accounts?

*Regarding models of the distributional impact of inflation vs. unemployment:* What percentage of total family income, by decile, comes from earnings? How is income from capital (including capital gains) affected by inflation (profits seem quite significant in some sectors, such as energy). What is the impact of inflation on public transfers and services? How do consumption baskets among households differ by demographic composition and number of dependents, as well as by market income?

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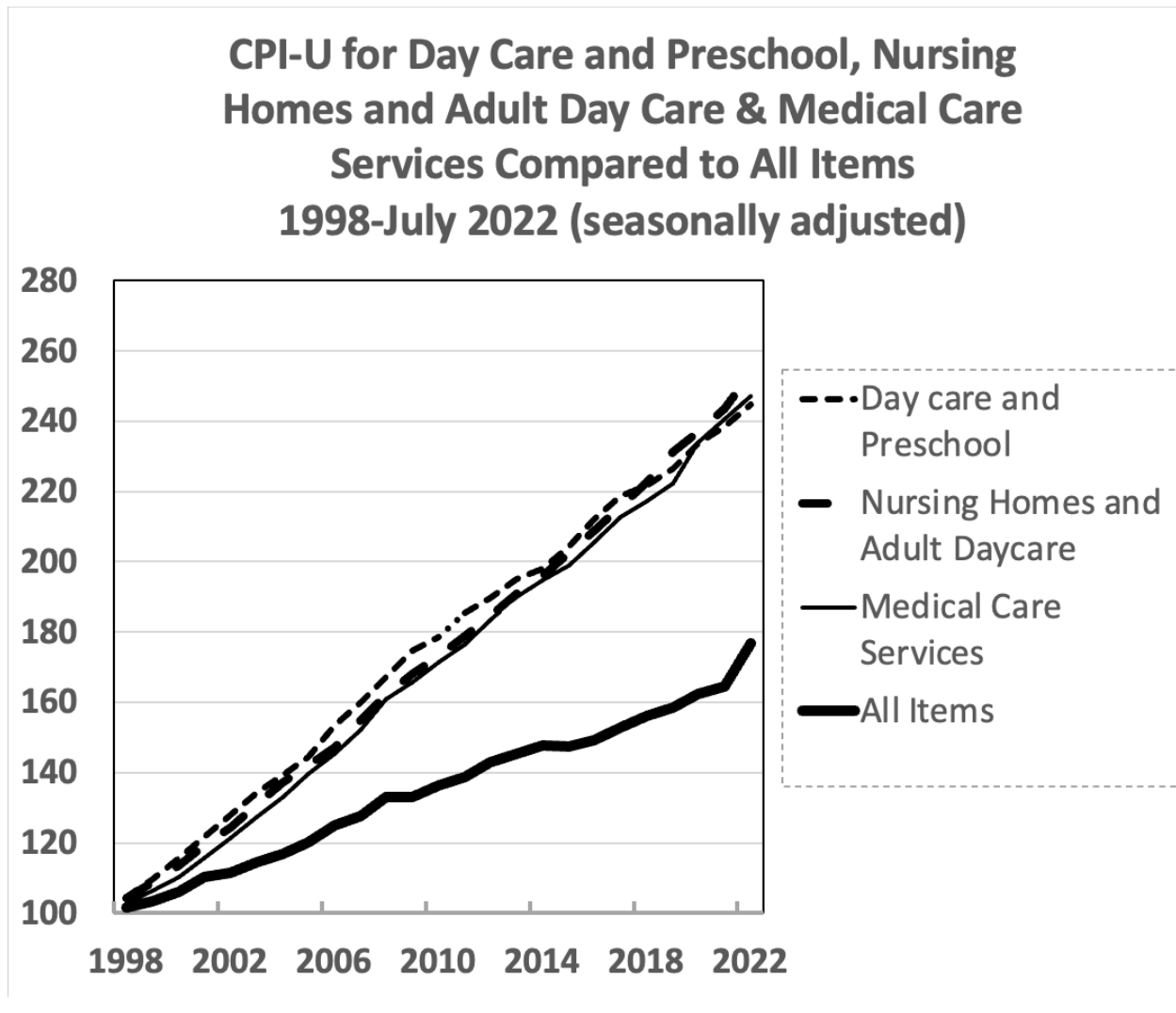
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**Figure 1.**



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## Notes

<sup>1</sup> These brief comments represent a jumping-off point for future research on the prices of paid care services. They are primarily drawn from a draft report, *Measuring Care Provision in the US: Resources, Shortfalls, and Possible Improvements*, coauthored by Nancy Folbre, Shawn Fremstad and Pilar Gonalons-Pons. They also benefited from email exchanges with Isabella Weber and Gregor Semieniuk.

<sup>2</sup> I have tried to find similarly disaggregated series for Personal Consumption Expenditures but have been unable to do so--any advice on this more than welcome!