ECONOMIC POLICY BRIEF

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SQUEEZING THE MIDDLE CLASS

Santa Clara County Families Lose Ground; Economy Shifting Towards Low Incomes, High Costs

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INTRODUCTION AND KEY FINDINGS

New statistics released today by the U.S. Census Bureau paint a disturbing picture of changes in Santa Clara County's economy since 2000. With lower income, an extraordinarily high cost of living, and a growing risk of falling into poverty, the average family remains worse off than before the crash. Unless new public policy initiatives explicitly confront the middle-class squeeze, these troubling conditions are likely to persist.

During the 1990s, Santa Clara County's unique position as the heart of Silicon Valley--the innovation center of the New Economy--brought extraordinarily fast, if uneven, growth. When the tech bubble burst, the county's economy came crashing down, precipitating a recession that went deeper and lasted far longer than in the rest of the country. Local employment and wages still have not recovered from this collapse; although recent signs indicate that the hemorrhage of jobs may finally be ending, tens of thousands of families still suffer from the recession's effects.

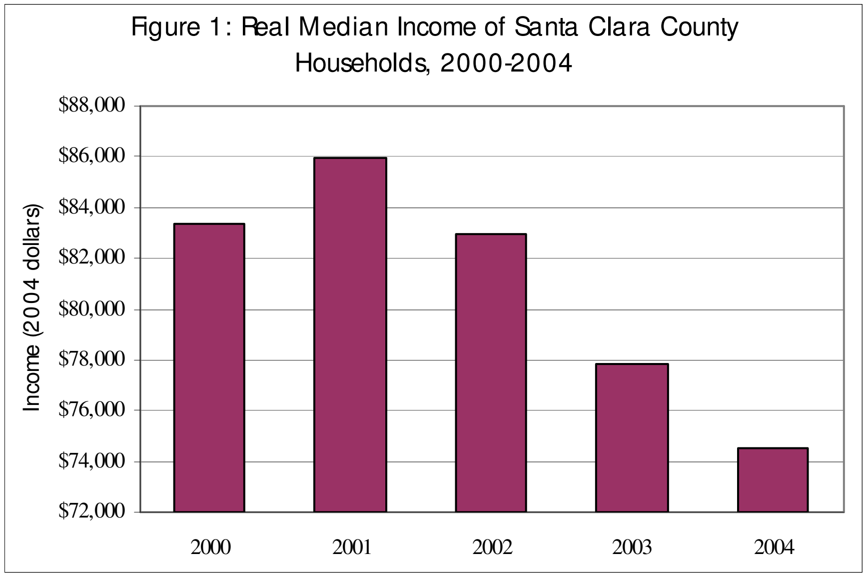
But our region's close ties to the high-tech globalized economy may also be bringing about a long-term shift away from the very type of shared economic growth that has made our families prosperous. The new Census data reveal that the distribution of household incomes is changing shape; the county's secure middle class is shrinking as more and more households fall into the lower income brackets. The middle class's continuing decline, three years after the end of the national economic recession, raises the concern that these trends may move beyond recessionary dips to produce a permanent transformation in our economy's structure.

This brief analyzes recent changes in median income, income distribution, poverty and cost of living in Santa Clara County.[1] It represents the beginning of an in-depth investigation by Working Partnerships USA into Silicon Valley's "post-crash" economy. Future publications will probe more deeply into families' experiences, the economy's new structure, forces driving the changes and what can be done to restore economic growth that benefits everyone in the Valley.

[1] Unless otherwise indicated, all data in this report is based upon the U.S. Census Bureau's American Community Survey. Working Partnerships USA is not affiliated with the Census Bureau.

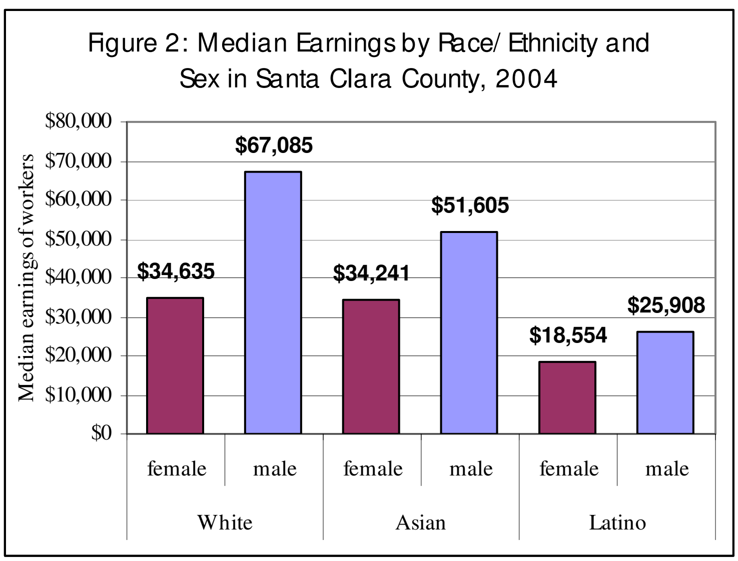
MEDIAN INCOME

- **The average family was worse off economically in 2004 than in 2000**
- **Latino workers still earn much less than white workers**



Real median household income has fallen for three consecutive years, meaning that most families are earning substantially less money, after inflation, than they did in 2001. From a high of $85,978 in 2001 (adjusted for inflation), in 2004 the average Santa Clara County household secured $74,509, as shown in Figure 1.

Families of all racial and ethnic groups are suffering the effects of the drop in income. Latino-headed households face a particular challenge because, on average, both individual earnings and household incomes of Latinos are significantly lower than those of other ethnic groups. Even in the best of times, Latino families are more likely to have to struggle to make ends meet. Latino wage earners aged 16 and over made, on average, only 44.2% of white workers' median earnings in 2004. And the average Latino household had a median income one-third less than the average white household in 2003.[2] Figure 2 displays the median earnings of Latino, white, and Asian workers aged 16 and over.



INCOME DISTRIBUTION

- **More households fall into the lowest income category, while the middle class stagnates and the affluent top is shrinking**
- **The "hourglass economy" of the 1990s replaced by a bottom-heavy "Victorian gown"**

A single measure like the median income shows us little of how individual families have fared. Looking at how income is distributed – how many households are low-income, how many are affluent, and how many in the middle – give a clearer picture of how households at varying income levels have experienced the recession. In Santa Clara County, this perspective reveals a disturbing image of an income distribution grown increasingly bottom-heavy.

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[2] Median household incomes by race/ethnicity are not yet available for 2004.

If we slice the income distribution into increments of $50,000, we find that the lowest bracket, composed of households earning $50,000 or below, is the only category showing substantial signs of growth. Between 2000 and 2003, 45,943 additional households found themselves falling into this category, an increase of 31%. At the same time, households earning between $50,000 and $100,000, who make up the bulk of Santa Clara County's secure middle class, saw their numbers drop by 9%, with 17,394 households falling out.

The number earning between $100,000 and $150,000 stagnated, adding just 834 households, a growth of less than 1%. Finally, the number of households at the top of the scale (largely the upper-middle class) declined, with 8,328 fewer households earning $150,000 to $200,000 and another 13,360 fewer earning $200,000 and above, respective falls of 15% and 23%.

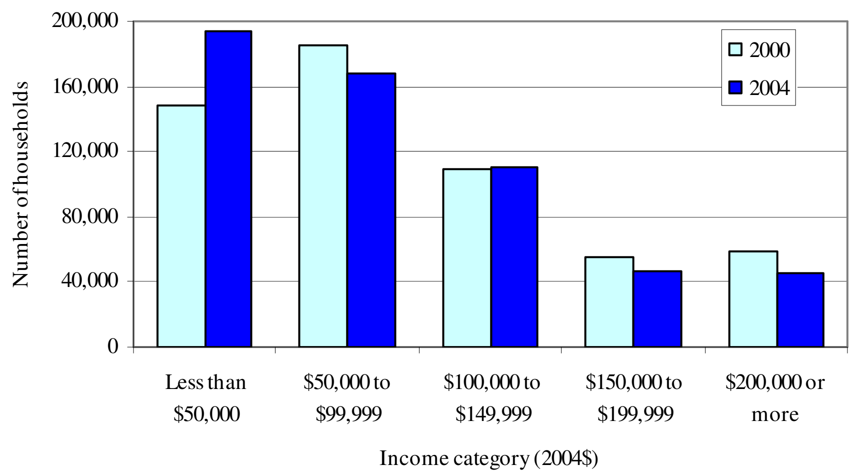
The household income distribution reveals a crucial, and worrisome, difference between Silicon Valley's economic trends in the 1990s and today. Between 1990 and 2000, the very lowest income category (below $10,000) increased dramatically, while the middle class shrank. These two trends have continued through 2004. But during the 1990s, the highest income categories ($100,000 and above) also saw substantial growth. In other words, the middle class was diminishing, but while some of those vanishing middle-class families would fall to the bottom, many stood a good chance of making it to the top.

No longer. From 1990 to 2000, the share of households earning $100,000 or more averaged a 2.9% annual growth rate, increasing by the impressive total of 32% for the entire decade. In contrast, from 2001 to 2004 the share of households in this category averaged a *negative* annual growth rate of -4.6%.

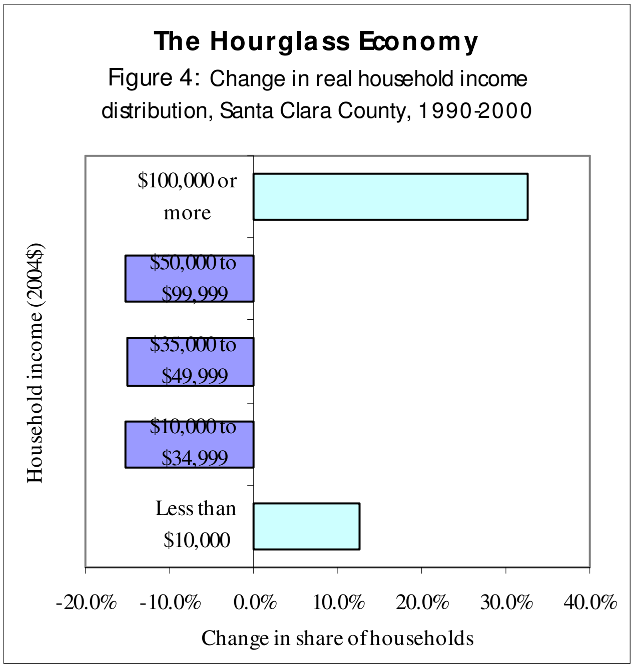
Figures 4 and 5 show trends in income distribution from 1990-2000 and from 2001-2004. Figure 4 exemplifies what came to be known as the "hourglass economy" of the 1990s: growth at the top and the bottom of the income distribution coupled with a decline in the middle class.

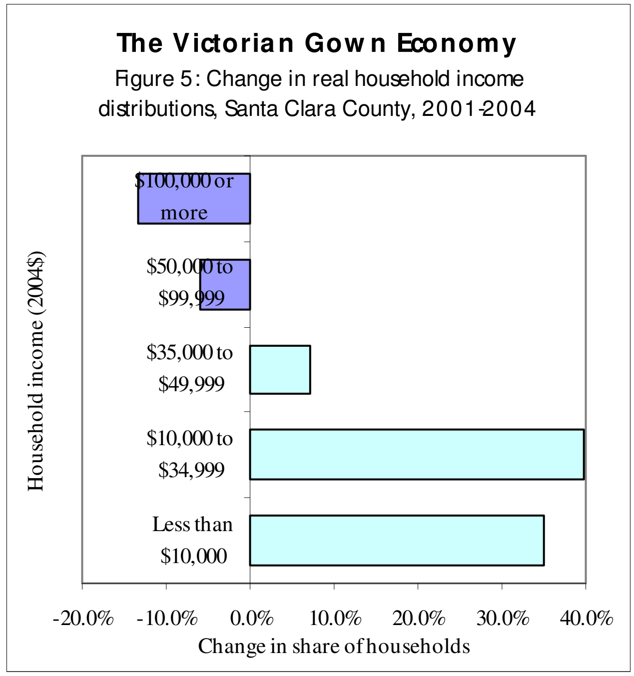
Figure 5 highlights the changes in the hourglass economy since the crash. The top income brackets are shrinking and the middle class remains largely stagnant, while growth at the bottom has accelerated. Rather than an hourglass, the new post-crash economy brings to mind an old-fashioned Victorian gown: small on top, cinched down to nearly nothing in the middle, and ballooning out at the bottom.[3]

Figure 3: Change in Real Household Income Distribution from 2000 to 2004, Santa Clara County



[3] Table 4 is drawn from American Community Survey data, while Table 5 is drawn from the U.S. Decennial Census in 1990 and 2000, adjusted for inflation. Data from the two surveys cannot be directly compared.





POVERTY AND COST OF LIVING

- **The high cost of living, especially housing prices, makes it difficult to make ends meet**
- **Adult poverty is up sharply; the poverty threshold does not accurately reflect the cost of living**

Compared to the rest of the country, Santa Clara County incomes still appear quite high; our median household income is the tenth largest in the nation, even after three years of sharp declines. But the numbers mask the region's extraordinary cost of living – also among the highest in the nation. Even as incomes have dropped, the costs of essential goods and services, particularly housing, health care and transportation, has remained high, creating hardships for the Valley's families.

More and more of households' shrinking incomes are being swallowed by the high cost of housing. Although the rental market has cooled since 2000, Santa Clara County renters paid the highest median monthly housing costs in the nation in 2004.

Meanwhile, the cost of buying a home in the county is soaring in defiance of falling family incomes. Median home sale prices break new records every month: by June 2005, the price in Santa Clara County had reached $760,000, an 18% jump in a single year and an explosive 41% growth since 2001.[4] Prices dropped slightly in July, but whether that decline represents a cooling-off or just a blip remains to be seen. As a result, where in 2000 36.7% of homeowners with mortgages paid more than thirty percent of their income for housing, in 2004 45.7% of homeowners were paying this excessive price.

Renters had it somewhat better, with median rents falling slightly from $1,310 in 2000 to $1,181 in 2004. But rents did not fall nearly as fast as renters' incomes, with the result that renting families too are paying a larger percentage of their income for housing than they did in 2000. 47.8% of renters put more than thirty percent of their income towards housing in 2004, an increase from 40.0% in 2000.

In short, nearly half of both renters and owners with mortgages now see over thirty percent of their dwindling income sucked into housing, leaving families with less each year to pay for food, health care, child care, and transportation.

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[4] California Association of Realtors

Poverty Levels: The growing cost of basic necessities combined with falling incomes has pushed more individuals over the edge into poverty. The percentage of all Santa Clara County residents in poverty has jumped by 34% since 2000, and adult poverty has grown even faster, seeing a 50% increase. These proportionately huge increases in poverty place a strain upon our region's social services. 7.9% of adults and 8.7% of all residents fell below the federal poverty line in 2004, compared to 6.5% and 5.3% respectively in 2000.

But the poverty numbers do not tell the whole story. Federal poverty standards, along with income eligibility standards for most safety net programs, do not take into account the true cost of living. is leaves many families stranded as their incomes fall below the cost of living, but above the poverty line.

In 2004, the federal poverty threshold for a two-parent, two-child household was $19,157, meaning that only families earning below this amount are considered poor. But this cutoff is calculated using outdate methods, and without accounting for Santa Clara County's high cost of living. The true income needed for a family to fulfill its basic needs without assistance is much higher.

For two adults with two teenaged children, the 2004 self-sufficiency standard – based upon the actual costs of food, housing, transportation, health care, and other essentials in our region – is $47,329 annually, nearly two-and-a-half times the poverty threshold. Roughly a quarter of Santa Clara's residents do not earn enough to reach self-sufficiency.[5] For most of them, the public safety net no longer provides real protection, because their incomes are too high to qualify for services intended to help families pull themselves up.

THE GLOBAL ECONOMY AND POLICY IMPLICATIONS

A portion of the hardships now faced by Silicon Valley families is, of course, caused by the aftermath of the 2001 recession. But three years later, the data indicate that our region's economy did not merely suffer a temporary slowdown, but has jumped tracks. We have now begun to move in a persistent direction typified by lower incomes, increasing inequality, and heightened economic insecurity.

Santa Clara County's economic strength – its close ties with tech and global networks – has also become its weakness, as we are being hit first and hardest by globalization's trends. Among them:

- The replacement of permanent employment by temps, contractors, and domestic outsourcing
- International outsourcing ("offshoring") of formerly well-paying jobs
- The flight of manufacturing, eliminating millions of secure middle-class jobs for workers with a high school education
- Loss of upward mobility within companies, as necessary training and education becomes harder to obtain
- Increased productivity funneled into profits rather than hiring or wages

Cumulatively, these trends are generating a qualitative change in the organization of work. More and more jobs offer low pay, few if any benefits, and no job security. They are dead-end positions, requiring relatively little education and lacking career ladders through which increased skills yield increased compensation. Secure middle-class jobs that can support the average family are becoming rarer. Another set of jobs, accessible to those with advanced education and the right experience, pay very well indeed; but post-2001, even these high-paying jobs are disappearing. For Santa Clara County families, the future of the high-tech global economy looks increasingly grim.

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[5] Self-sufficiency standard calculated for Santa Clara County by the National Economic Development and Law Center. Working Partnerships USA calculations estimate that 25% of households fall below self-sufficiency. A study by United Way Silicon Valley independently produced the same estimate.

To avoid a continuing decline of the middle class and polarization of our region, Silicon Valley will have to redefine its relationship to the global economy and its notion of economic progress. Three key principles can be drawn from our experience over the past several years:

- While healthy businesses are essential to a shared prosperity economy, business growth alone does not necessarily benefit Santa Clara County's workers. The post-crash era has seen productivity, stock prices and profits soar, with no increase in jobs or wages. An explicit public policy goal must be not just economic growth, but growth that will fulfill the needs of both our region's businesses and its working families,

- By the same token, economic development must focus on the creation of quality jobs, not simply quantity. A continued shift to low-paying, insecure jobs without health coverage will ultimately harm our communities and overwhelm our public services.

- Alongside an emphasis on quality job growth, we need to recreate a social safety net that sustains households facing economic upheaval in Santa Clara County and across the country. A key first step is restoring access to healthcare for working adults and their families.

The time to reverse the trends of falling income and growth at the bottom is now – before they become permanent. If we succeed, Santa Clara County can provide a model of an economy that leads the world in innovation <u>and</u> spreads the benefits of innovation to all of its residents.

ABOUT US

Working Partnerships USA was formed in 1995 as a collaboration among community-based organizations to develop institutional and public policy responses to the negative impacts of the Silicon Valley's new economy on working families. We endeavor to accomplish our mission both by bringing a wider range of voices to the table in discussions of economic development, workforce development and employment policy, and by designing programs to reduce inequity and improve security and quality of life for working families in the New Economy.

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