

One Economist's Thoughts on Welfare Programs
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Cash transfer programs - like Food Stamps or Temporary Aid to Needy Families (TANF) - are highly controversial even or perhaps especially amongst economists. Although the research questions are far from answered, we can say, with some confidence, that these programs distort markets and individual choice. There is evidence that the old AFDC program reduced labor force participation. It also appeared to have some impact on marriage and possibly out of wedlock birth rates. Most of the evidence is mixed and most economists would agree that the effects are smaller than one might fear. Indeed, it is quite clear that many other factors have a much larger impact on an individual's labor market, marital, fertility and other choices and outcomes. Indeed, we find mostly, that the stuff we don't and can't measure (tastes and preferences among them) appear to be the most important.

As an economist, I firmly believe that the role of government in the economy is to move markets toward the efficient social equilibrium where marginal social costs equal marginal social benefit. In most cases, the market does this pretty well without any help. Only when there are externalities - costs borne by those outside the market (like pollution) or benefits accrued by those not participating (public goods like police or national defense) - should the government play a role. Welfare programs are usually not seen as solving an externalities problem. So, as an economist, I should probably consider them to be "bad" and generally be opposed to them.

I'm not though. Indeed, I think it crucially important that these programs be continued and supported. The reason is simple and has nothing to do with economics. It is simply a moral stance. It is my personal belief that we in society have a moral and ethical obligation to provide basic necessities like food, clothing and shelter for those who for some reason are unable to do so. I'm not picky about the reason either. I can go into more detail, quote scripture, tug at the heart strings, all that stuff - but I'm not going to. It is what I believe.

There are costs to taking this stance. It costs money to provide these programs (for the economists, I recognize deadweight loss as well). It is my preference (that's economist talk again) to pay these costs in order to meet this moral obligation. I understand them. I don't discount them or ignore them. To me the benefit is bigger than the costs.

I also think the Federal government, in conjunction with state governments, is in a unique position to provide these services. I know a great many people who agree with my general statement of moral obligation, but would prefer that it be undertaken at a private level through religious and other organizations. While I support these organizations as well (both in principle and financially), there are two economic reasons why the government can and should be the primary instrument. There are other reasons as well, having to do with "fairness" but I won't tackle them here. I'm sure you've heard the arguments.

The primary reason why the government can and should do this is geographic. Economic downturns are most often very local phenomena. A great example is Flint, MI in the 1980's and contrasting that with Silicon Valley at the same time. In 1978, General Motors employed over 80,000 people in Flint directly. Indirect employment was also huge with suppliers of everything from parts to toilet paper. As GM closed

those plants and GM employment fell over the next decade, Flint suffered dramatic unemployment and the social and economic problems associated with that situation.

In 1980, Apple Computers opened in Silicon Valley and the "high tech" boom began. As personal computers and all that has gone with them proliferated, Silicon valley experienced dramatic economic growth (both population and income).

If we relied on local organizations to handle welfare, Flint would be in terrible trouble. With the economy there drying up, and those that could leaving, there is little economic base from which to draw. However, at the same time, there was an area with little local unemployment and very high incomes. The federal government is in the unique position of being able to transfer resources widely within the country. This provides a certain amount of efficiency that is difficult (perhaps impossible) to achieve through other organizations.

Given that I support transfer or welfare programs, as an economist I want to see (or help design) programs which accomplish the goal of providing this aid with the least distortion to the markets and the most efficient allocation of the money. This is complicated and difficult and I won't go into detail here. I will acknowledge that there is a great deal of work to be done in this direction and that there have been significant positive changes over the years as well (I would point especially to the rise of the EITC for example).

I think the most difficult aspect of designing welfare programs is to clearly identify goals. It is easy to say "I want to help poor people." It is much harder to define exactly what that means. Indeed in order to "help" you need some indication of what is wrong in the first place. Economists (and others) have spent lifetimes trying to ascertain the problems which lead to poverty. It is easy to spout things like "no one should go hungry" or "we want to break the cycle of poverty" or even "we want to help people to stand on their own feet." It is much more difficult to determine why people go hungry, how the cycle of poverty works and why people don't stand on their own feet. But to design programs which will help, we do need to understand the answers to these questions. And, they are not simple.

A second problem is "targeting." How to design programs that help the people who most need it. The minimum wage is actually a very poorly targeted program. In many ways Food Stamps is a pretty well targeted program (don't get me wrong, it's not perfect). So anytime I look at welfare programs, targeting is crucial to me. I am in support of these programs because of a particular preference, so I want the money to do the most good there.

Designing programs with minimal distortion is also important. Designing programs that keep incentives for labor force participation is tough. If you give money, but then take it back as they earn more, you are effectively taxing them at a very high rate (indeed at one point, the effective tax rate for AFDC participants was 100%). Economists have long worked carefully to address these issues and we have had some success. The EITC program and various aspects of other programs appear to be a direct result of a huge body of literature dating back at least to the mid 1970's. It has taken us a long time to understand how best to design welfare programs. And we are not through yet.