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The case "against" social capital

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> She would have liked to tell them that behind Communism, Fascism, behind all occupations and invasions lurks a more pervasive evil and the image of that evil was a parade of people marching by with raised fists and shouting identical syllables in unison. But she knew she would never be able to make them understand. Embarrassed, she changed the subject.
>
> Milan Kundera, *The Unbearable Lightness of Being*

This essay is designed to call into question the current boomlet in policy and academic circles for social capital.[1] Social capital has become an explanation for an array of domestic problems in the United States as well as for understanding issues of third world development.[2] However, there is strong reason to ask whether the rise in interest in social capital is due to its demonstrated strength in elucidating socioeconomic phenomena or whether it is the intellectual equivalent of a stock market bubble. To be clear, analyses of social capital have highlighted an important aspect of socioeconomic behavior which has been underemphasized by economists—the role of nonmarket relationships in determining individual and collective behavior.[3] So, I do not question continuing research on this phenomenon. Rather, I ques-

Beginning with this issue of *Focus,* we plan to include selected articles examining the concept of, and research on, "social capital." Because it is by no means clear what the concept embraces, we open with a debate—perhaps more accurately, a discussion—between two scholars with long-standing interests in the influence of the community on individual behavior, and rather different perspectives upon it: Steven N. Durlauf of the University of Wisconsin–Madison and Samuel Bowles of the University of Massachusetts at Amherst.

tion both the importance which some have attributed to social capital and whether it is ultimately as benign a phenomenon as its advocates assume.

Conceptual ambiguity

One problem with the analysis of social capital is that it is ill-defined, with different authors attributing different meanings to the concept. Part of this ambiguity concerns whether social capital is defined in terms of its effects or in terms of its characteristics. The problem with a functional definition is that it renders analysis impossible since, as argued by Alejandro Portes, social capital becomes tautologically present whenever a good outcome is observed.[4] As a rhetorical device, one can see why this is effective. By defining the presence of social capital in terms of the presence of desirable outcomes, it is of course impossible not to treat social capital as an unalloyed virtue. Nevertheless, an alternative definition is appropriate if one is to make an assessment of social capital.

One possibility is to define social capital as "the influence which the characteristics and behaviors of one's reference groups has on one's assessments of alternative courses of behavior." The idea behind this definition is that social capital is present when a complete specification of how an individual makes decisions requires us to characterize what groups influence those decisions as well as to specify the causal mechanism by which this influence is transmitted. To take one case where this is true, consider James Coleman's famous example of wholesale diamond merchants in New York, in which bags of diamonds are lent for examination without any formal contracts or insurance, leaving the lender in danger of receiving counterfeits or lower quality diamonds when the diamonds are returned. Although opportunities for dishonesty are not rare, instances are virtually never observed. Here, social capital influences individual decisions on honesty because dishonesty by a given diamond merchant will induce responses by others which matter to his assessment of how to act.[5] This type of definition is consistent with Edward Laumann's and Rebecca Sandefur's idea that an individual's social capital "consists of the collection and pattern of relationships in which she is involved and to which she has access."[6]

To the extent that social capital is appropriately regarded as a set of mechanisms in which groups implicitly enforce certain behaviors among their members, it is clear that any presumption concerning its virtues is questionable. To see how social capital can lead to bad outcomes, consider the case of segregation in the South. One can make a plausible argument that social capital was important in perpetuating racial inequality. How? By creating enforcement mechanisms that precluded individual whites and blacks from deviating from the behavior which perpetuated Jim Crow laws and segregated social relations. Notice that just as diamond merchants in Coleman's example would be ostracized for contract violation, so would a white storekeeper who hired a black suffer from community reactions.

The example of the enforcement of segregation norms illustrates a more general principle: social mechanisms which enforce certain types of community behavior logically lead to correlated behaviors, but do not necessarily lead to socially desirable behaviors. Hence, discussions of social capital that do not specify how socially desirable versus socially undesirable behaviors are selected necessarily beg the question.

Social capital and social bads

The possibility that social capital can lead to undesirable behaviors is more than theoretical. Behaviors which enforce differential treatments of insiders and outsiders to a community are of course intimately linked to the nature of social capital; Portes and Patricia Landolt make clear how this distinction, when made in the context of zero-sum games such as hiring decisions, can lead to inequalities across groups.[7] Beyond this structural relationship, there is an attitudinal one. Strong group ties require members to think in terms of groups. Such a mindset will presumably carry over to contexts other than those in which group coordination is benign. Is it possible that an ethnic group with strong internal support mechanisms that insure members against economic dislocation exhibits its discriminatory behavior in other spheres, such as hiring or choice of residential neighborhood? Although it is conceivable that group identification along one dimension does not lead to such thinking along others, such compartmentalization seems very implausible.

The potential for group-based identification to lead to intergroup hostility has been well documented in the social psychology literature. In what has been called "the most successful field experiment ever conducted on intergroup conflict," Muzafer Sherif and colleagues studied the effects of group identification in the famous Robbers Cave experiment, named after the park where the experiment was conducted.[8] These experimenters studied the behavior of a group of teenage boys at an isolated retreat. The boys were broken into two groups that initially were not aware of the existence of one another. After one week, the groups were asked to assume names and chose Rattlers and Eagles respectively. A set of competitive activities was initiated between the two groups. Sherif documents in great detail how the two groups developed strong senses of group identity as well as differing internal behavior norms. Further, each group exhibited great animosity toward the other, animosity which carried over beyond the competitive activities. It became commonplace for the boys to attribute negative stereotypes to the other group; overt hostility bordering on violence emerged. The introduction of cooperative activities diminished the hostility, but the experiment clearly demonstrated that group identification can lead to intergroup hostility.

Related evidence abounds on the effects of group membership on perceptions and attitudes. Bernadette Park and Myron Rothbart found that sorority members tended to regard members of other sororities as less diverse than members of their own, an example of how strong intragroup relations can lead to stereotypical thinking about others.[9] In another classic set of experiments, individuals were randomly assigned to groups and asked to evaluate others along criteria for which no objective information was available. Subjects typically exhibited strong ingroup bias in these assessments.[10]

What sorts of groupings are likely to exist in environments that are rich in social capital? While there is no clear answer, again the psychology literature is very suggestive. Racial differences seem to be extremely salient in human cognition.[11] The research on race, and the case studies on social capital that have appeared, lead me to conjecture that ethnic homogeneity is a common feature of circumstances where social capital is strong.

It would be absurd to argue that parent teacher organizations, bowling leagues, and the like directly generate socially dangerous attitudes toward others. What does seem reasonable is the worry that, since those social structures in American society which promote community or group feelings are often (and possibly even typically) ethnically and economically segregated, they can help to reinforce group-based thinking with the attendant effect of exacerbating intergroup hostility. Such a concern seems especially serious given the increasing economic and social stratification of American (and indeed world) society.[12]

Indeed, I think it is no exaggeration to say that increasing egalitarianism in America has historically been associated with the breakdown of group identities (racial, ethnic, religious, regional) and so, one suspects, with a diminution of social capital, at least as conventionally characterized.

What leads to social capital?

A second lacuna in the social capital literature revolves around the reasons for its presence or absence. Although many social capital discussions have recognized that social capital formation is endogenous to a given socioeconomic environment, there has been relatively little attention to the implications of this for the interpretation of evidence or its overall social value.

To see how the endogeneity of social capital calls into question the sort of empirical evidence adduced to support its role in individual behavior consider, for example, a recent study by Frank Furstenberg and Mary Hughes.[13] In this analysis, the probabilities for a range of binary socioeconomic outcomes, including high school graduation and labor force participation, are shown to be related to community variables such as perception of a "strong help network" (which makes desirable outcomes more likely) and "child ever changed schools due to move" (which makes desirable outcomes less likely, presumably due to the attenuation of social connections).

The problem in interpreting these and other such social capital measures as causal is that each is a choice variable, subject of course to constraints, and therefore will reflect any omitted family characteristics in an empirical analysis. To be concrete, does the negative influence of childhood moves on socioeconomic outcomes reflect the importance of social capital, or does it reflect differences in the unmeasured characteristics of families that do and do not move? This is a problem that is endemic to the literature on group effects, yet seems to be generally ignored in the empirical studies of social capital.[14] Further, studies of social capital have yet to make a clear case for the direction of causality. Do trust-building social networks lead to efficacious communities, or do successful communities generate these types of social ties? As far as I know, no study has been able to shed much light on this question.

As for the implications of the sources of social capital for the interpretation of its value, consider the decline in membership in parent teacher organizations. Reduced participation in parent teacher organizations most likely occurred at least partially because labor market opportunities improved for women. Hence, in this case, the desirable effects of this social capital were purchased at the cost of restrictions on individual opportunity.[15] More generally, it seems plausible that, if the carriers of social capital are groups which are segregated by ethnicity, gender, or socioeconomic status, then increasing egalitarianism can cause social capital to decline.

Finally, a better understanding of the determinants of social capital may imply policy remedies that can generate some of the benefits of social capital, without the adverse effects which I have suggested may arise. Specifically, social capital seems to arise in circumstances when there are socioeconomic "frictions," by which I mean circumstances where there is a need for some sort of collective action to overcome the failures of uncoordinated individual decisions. An example of this is the emergence of social norms which prevent overexploitation of a common resource or the existence of revolving credit associations among certain ethnic groups to facilitate economic advancement. To the extent that social capital emerges in environments with externalities of various types, we know from economic theory that it may well be possible for government policies to alter individual incentives and aggregate outcomes in ways which do not alter social relations per se. Put differently, although I do not think we have much idea how government policies can build social capital in impoverished communities, we do know a great deal about how different types of government programs can influence community outcomes.

It is easy to imagine ways in which government policies can obviate the need for social capital. Increased school funding may overcome the need for parental involvement in education in poor communities, just as targeted credit subsidies may overcome the need for revolving credit associations. Conversely, such a focus on causal determinants may well also illustrate cases where government policies cannot efficiently replace social capital. It may be that government credit programs cannot assess individual creditworthiness so well as private associations, so that such programs will suffer from substantial waste; similarly, the use of legal penalties to enforce ethical conduct among diamond merchants is clearly more costly than a strong social norm for honesty.

One critical feature of the substitution of government policy solutions for those that arise from intragroup social norms is that the former can be produced through democratic governance. Further, government policy solutions can address problems in intergroup relations, a topic I discuss next.

The implications for research

The specific concerns I have about social capital suggest an alternative direction in research. Social capital analyses focus on intragroup relationships. An equally important question is intergroup relations. Many of my concerns about social capital stem from the belief that although social capital might facilitate intragroup coordination, by enhancing group identity it promotes intergroup hostility. Such a worry is a long-standing one for students of racial relations; for example, a primary concern of Gordon Allport's classic study, *The Nature of Prejudice*, was the identification of conditions under which intergroup racial interactions reduced rather than increased racial animosity.[16]

Within social psychology (I have already discussed examples of intergroup hostility from that literature), studies of such issues fall into what Thomas Pettigrew calls intergroup contact theory.[17] This is a rich literature, with many suggestions about how to structure intergroup interactions so as to promote benign attitudes. In the Robbers Cave experiment, it turned out to be possible to at least partially overcome Eagle and Rattler animosities through the creation of common goals requiring intergroup cooperation (in this case pushing a truck!). By making intergroup and intragroup relations parts of a more general framework, social scientists will be far better equipped to understand the complexities which underlie group outcomes.

Social capital has proven a useful lightning rod for resocializing the analysis of individual behavior in the social sciences, notably in economics. I suspect that humans feel strong urges to form and identify with groups for evolutionary reasons, and so ignoring social organization necessarily handicaps the study of many socioeconomic phenomena. If for no other reason, by forcing social scientists to deal with the rich effects of social interaction on individual behavior, social capital enthusiasts have performed a valuable service. Certainly, further study is warranted.

This essay suggests that the nature and consequences of social capital are far more complex than is acknowledged in the popular and academic communities and that social capital is not likely to be the panacea its advocates often claim. Relative to the current research on social capital, I believe that new theoretical and empirical work is needed on (1) the meaning of social capital, (2) its net effect on societal welfare, with appropriate attention to the possibility of its generating negative outcomes, (3) its empirical significance in influencing individual decisions, and (4) a balanced assessment of intergroup as well as intragroup relations, so that the adverse effects of group identity on both members and others are properly assessed. These suggestions should not prove to be too onerous—after all, academics are a class of individuals who should be especially sensitive to the costs of enforced conformity.

So listen here, professor, with your head in the cloud.
It's often kind of useful to get lost in a crowd.
So keep your universities I don't give a damn.
For better or for worse it is the way that I am!

From "Little People," *Les Miserables*,
London Production Endnotes

■

[1]I thank William Brock, Donald Hester, John Knowles, Susan Nelson, and James Robinson for helpful conversations and the Romnes Trust, NSF, and the John D. and Catherine T. MacArthur Foundation for financial support.

[2]R. Putnam, "The Prosperous Community: Social Capital and Public Life," *The American Prospect* 13 (1993): 35–42, and "Bowling Alone: The Strange Disappearance of Civic America," *Journal of Democracy* 6 (1995): 65–78; P. Collier, "Social Capital and Poverty," mimeo, Social Capital Initiative, The World Bank, 1998.

[3]Interestingly, the social capital concept was originally introduced by an economist, Glenn Loury ("A Dynamic Theory of Racial Income Differences," in *Women, Minorities, and Employment Discrimination*, ed. P. Wallace and A. LaMond [Lexington: Lexington Books, 1977]). Loury's goal was to show how the introduction of factors such as social networks could lead to persistent differences in income levels across ethnic groups. As such, his analysis is immune to a number of the criticisms I make.

[4]A. Portes, "Social Capital: Its Origins and Application in Modern Sociology," *Annual Review of Sociology*, 1998, 1–14.

[5]J. Coleman, "Social Capital in the Creation of Human Capital," *American Journal of Sociology* 94 (1988): S95–S121. In the case of wholesale diamond merchants, Coleman argued that these types of cooperative behavior are sustained by the fact that the merchants are members of common religious and residential communities, and that dishonesty would break ties to those communities.

[6]E. Laumann and R. Sandefur, "A Paradigm for Social Capital," *Rationality and Society* 10 (1998): 481–95, quote, p. 498.

[7]A. Portes and P. Landolt, "The Downside of Social Capital," *The American Prospect* 26 (1996): 18–22.

[8]R. Brown, *Social Psychology*, 2nd ed. (New York: Free Press, 1986), quote, p. 535. M. Sherif, O. Harvey, B. White, W. Hood, and C. Sherif, *Intergroup Conflict and Cooperation: The Robbers Cave Experiment* (Norman: Institute of Group Relations, University of Oklahoma, 1961, reprinted by Wesleyan University Press, 1988).

[9]B. Park and M. Rothbart, "Perception of Out-Group Homogeneity and Levels of Social Categorization: Memory for the Subordinate Attributes of In-Group and Out-Group Members," *Journal of Personality and Social Psychology* 42 (1982): 1051–68.

[10]H. Tajfel, *Human Groups and Social Categories* (Cambridge: Cambridge University Press, 1981).

[11]L. Hirschfield, *Race in the Making* (Cambridge: MIT Press, 1997).

[12]D. Massey, "The Age of Extremes: Concentrated Poverty and Affluence in the Twenty-First Century," *Demography* 33 (1996): 395–412.

[13]F. Furstenberg and M. Hughes, "Social Capital and Successful Development Among At-Risk Youth," *Journal of Marriage and the Family* 57 (1995): 580–92. I single out this study because I regard it as among the best published on the role of social capital in influencing individual socioeconomic outcomes.

[14]W. Brock and S. Durlauf, "Interactions-Based Models," forthcoming as an IRP Discussion Paper, University of Wisconsin–Madison, 1999, and in *Handbook of Econometrics* 5, ed. J. Heckman and E. Leamer (Amsterdam: North Holland).

[15]This argument, which has been made by others such as Theda Skocpol ("Unravelling from Above," *The American Prospect*, 25 [1996]: 20–25), has been rejected by Robert Putnam ("Bowling Alone") on the grounds that the participation rate of fathers also went down. However, this objection only carries weight if mother and father participation is uncorrelated within families and if individual participation is not an increasing function of total participation. Neither seems plausible.

[16]G. Allport, *The Nature of Prejudice* (Reading: Addison-Wesley, 1954).

[17]T. Pettigrew, "Intergroup Contact Theory," *Annual Review of Psychology*, 49 (1998): 65–85.

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“Social capital” and community governance

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Once everyone realized that market failures are the rule rather than the exception and that governments are neither smart enough nor good enough to make things entirely right, the social capital rage was bound to happen.[1] Conservatives love it because it holds the promise that where markets fail—in the provision of local public goods and many types of insurance, for example—neighborhoods, parent teacher organizations, bowling leagues, in short *anything* but the government, could step in to do the job. Those to the left of center are no less enchanted because it affirms the importance of trust, generosity, and collective action in social problem solving, thus rejecting the idea that greed and other purely individualistic motives can be harnessed to public ends successfully enough to make civic virtue unnecessary.

Conservatives might have been less avid if their favored institutions—unregulated markets and well-defined property rights—had fared better. But the utopian capitalism of the economics textbook has been tarnished in this century, ending as it is with growing inequality in the United States and the disastrous rush to privatization and deregulation in Russia. American liberals, along with social democrats and market socialists, might not have joined in, if the limits of governmental capacity and accountability had not been unmistakably and frequently demonstrated. Consider, in the United States, pork barrel subsidies for rich farmers, the bungled and costly attempt to impose nuclear power on the nation, and the failure to implement either effective medical insurance or electoral finance reform, both favored by large majorities.

The demise of these twin illusions of our century—laissez-faire and statism—thus cleared the intellectual and rhetorical stage for social capital's entry. And so, a decade ago, otherwise skeptical intellectuals and jaded policy makers surprised and impressed their friends with the remarkable correlation between choral societies and effective governance in Tuscany, the perils of a nation that bowled alone, and Alexis de Tocqueville on Americans as a nation of joiners. The social capital boom heralded a heightened awareness in policy and academic circles of real people's values (not the utility functions of *Homo economicus*), how people interact in their daily lives (locally, in families and work groups, not just as buyers, sellers, and citizens) and the bankruptcy of the ideologically charged planning versus markets debate.

Community governance

Perhaps social capital, like Voltaire's God, would have had to be invented even if it did not exist. It may even be a good idea. A good *term* it certainly is not. “Capital” refers to a thing possessed by individuals; even a social isolate like Robinson Crusoe had an axe and a fishing net. By contrast, the attributes said to make up social capital—such as trust, commitment to others, adhering to social norms and punishing those who violate them—describe relationships *among* people and would have been unintelligible to Robinson before Friday showed up. As with other trendy expressions, it attracts disparate meanings like flypaper. So many are now so firmly attached that it seems better to abandon the term in favor of something more precise.

“Community” better captures the aspects of good governance that explain the popularity of social capital, because it focuses attention on what *groups do* rather than what *individuals have*. By community I mean a group of people who interact directly, frequently, and in multifaceted ways. People who work together are usually communities in this sense, as are some neighborhoods, groups of friends, professional and business networks, gangs, and sports leagues. The list suggests that connection, not affection, is the defining characteristic of a community. Communities are part of good governance because they sometimes address problems that cannot be solved either by individuals acting alone or by markets and governments.

In some Chicago neighborhoods studied by Felton Earls and his colleagues, for example, residents speak sternly to youngsters skipping school or decorating walls with graffiti, and are willing to intervene to maintain neighborhood amenities such as a local firehouse threatened with budget cuts. These are all examples of what the authors term “collective efficacy.”[2] In other neighborhoods, residents adopt a more hands-off approach. Considerable variation in the neighborhood levels of collective efficacy exists; rich and poor, black and white neighborhoods exhibit both high and low levels. Remarkably, ethnic heterogeneity is considerably less important in predicting low collective efficacy than are measures of economic disadvantage, home ownership, and other markers of residential instability. Where neighbors express a high level of collective efficacy, violent crime is markedly lower, controlling for a wide range of community and individual characteristics including past crime rates. Chicago's neighborhoods illustrate the informal enforcement of community norms.

The Toyama Bay fishing cooperatives in Japan illustrate another aspect of community problem solving.[3] Faced with variable catches and the high level (and changing nature) of skills required, some fishermen have elected to share income, information, and training. One co-op which has been highly successful since its formation 35 years ago consists of the crews and skippers of seven shrimp boats. The boats share income and costs, repair damaged nets in common, and pool fishing information. Elder members pass on their skills, and the more educated younger members teach others the new high tech methods using Loran and sonar. The co-op's income- and cost-pooling activities allow its boats to fish in much riskier and higher-average-yield locations, and the sharing of skill and information raises profits and reduces productivity differences among the boats. Fishing, off-loading the catch, and marketing by individual boats are synchronized to increase the transparency of sharing and make opportunistic cheating on the agreement easy to detect.

The plywood workers who own their firms in Oregon and Washington benefit from both the peer monitoring of the Chicago neighbors and the risk pooling of the fishermen. They elect their managers and require, of their members, ownership of a share of the firm as a condition of employment and, of shareowners, employment in the firm as a condition for ownership. These co-ops have successfully competed with conventionally organized firms for over a generation, their success largely attributable to high levels of work commitment and savings on managerial monitoring of workers. Econometric analysis indicates that total factor productivity (output per unit of labor and capital combined) is significantly higher than in their conventional counterparts.[4] When faced with cyclical downturns in the demand for plywood the co-ops, unlike their competitors, do not fire or lay off workers, but rather elect to take cuts in wages or hours, thus pooling the cyclical risk among all members.

As these examples suggest, communities solve problems which might otherwise appear as classic market failures or state failures—namely, insufficient provision of local public goods such as neighborhood amenities, the absence of insurance and other risk-sharing opportunities even when these would be mutually beneficial, exclusion of the poor from credit markets, and excessive and ineffective monitoring of work effort. Communities can sometimes do what governments and markets fail to do because their members have crucial information about other members' behaviors, capacities, and needs. Members use this information both to uphold norms (work norms among the plywood workers and the fishermen, community behavioral norms in Chicago) and to make use of efficient insurance arrangements which are not plagued by problems of moral hazard and adverse selection (the fishermen and the plywood workers). Insider information is most often used in multilateral rather than centralized ways, taking the form of a kind word, an admonishment, gossip, or ridicule, all of which may have particular salience when conveyed by a neighbor or a workmate.

Communities thus may make an important contribution to governance where market contracts and government fiats fail because the information needed to design and enforce beneficial exchanges and directives is not effectively available to judges, government officials, and other outsiders. This is particularly the case where ongoing relationships among community members support trust, mutual concern, or sometimes simply effective multilateral enforcement of group norms. This idea long predates recent interest in social capital, even among economists. A generation ago, Kenneth Arrow (with Gerard Debreu) provided the first proof of Adam Smith's conjecture on the efficiency of invisible-hand allocations; but the axioms required by the Fundamental Theorem of Welfare Economics were so stringent that he stressed the importance of what would now be called social capital in coping with its failure:

> In the absence of trust . . . opportunities for mutually beneficial cooperation would have to be forgone . . . norms of social behavior, including ethical and moral codes (may be) . . . reactions of society to compensate for market failures.[5]

Communities are one of the ways these norms are sustained.[6]

Community failures

Like markets and governments, communities also fail. The personal and durable contacts which characterize communities require them to be of relatively small scale, and a preference for dealing with fellow members often limits their capacity to exploit gains from trade on a wider basis. Moreover, the tendency for communities to be relatively homogeneous may make it impossible to reap the benefits of economic diversity associated with strong complementarities among differing skills and other inputs. Neither of these limitations is insurmountable. By sharing information, equipment, and skills, for example, the Japanese fishermen exploited economies of scale unattainable by less cooperative groups, and reaped substantial benefits from the diversity of talents among the membership. But compared to bureaucracies and markets—which specialize in dealing with strangers—the limited scope of communities often imposes inescapable costs.

A second "community failure" is less transparent: where group membership is the result of individual choices rather than group decisions, the composition of groups is likely to be more culturally and demographically homogeneous than any of the members would like, thereby depriving people of valued forms of diversity. To see this, imagine that the populations of a large number of residential communities are made up of just two types of people easily identified by appearance or speech, and that everyone strongly prefers to be in an integrated group but not to be in a minority. If individuals sort themselves among the communities, there will be a strong tendency for all of the communities to end up perfectly segregated, for reasons that Thomas Schelling pointed out in his analysis of neighborhood tipping.[7] Integrated communities would make everyone better off, but they will prove unsustainable if individuals are free to move.

Economists use the terms "market failures" and "state failures" to point to the allocative inefficiencies entailed by these governance structures, and so far my discussion of these along with community failures has conformed to the canon. But like markets and states, communities often fail in other, sometimes more egregious ways. Most people seek out membership in a group of familiar associates and feel isolated without it; but the baggage of belonging often includes poor treatment of those who do not. The problem is exacerbated by the group homogeneity resulting from neighborhood tipping. When insider-outsider distinctions are made on divisive and morally repugnant bases such as race, religion, nationality, or sex, community governance is more likely to foster parochial narrow-mindedness and ethnic hostility than to address the failures of markets and states. This downside of community becomes particularly troubling when insiders are wealthy and powerful and outsiders are exploited as a result.

The problem is endemic: communities work because they are good at enforcing norms, and whether this is a good thing depends on what the norms are. The recent resistance to racial integration by the white residents of Ruyterwacht (near Cape Town) is as gripping an account of social capital in action as one can imagine.[8] Even more striking are U.S. regional differences in the relationship between violence and community stability. Dov Cohen and Richard Nisbett have described a "culture of honor" which often turns public insults and arguments into deadly confrontations among white males in the South and West, but not in the North.[9] Cohen's research confirms the finding that in the North, homicides stemming from arguments are less frequent in areas of higher residential stability, when measured by the fractions of people living in the same house and the same county over a 5-year period. But this relationship is inverted in the South and West: residential stability is *positively* and significantly related to the frequency of these homicides where the culture of honor is strong.[10]

Policy making and institutions

Many adherents of the liberal philosophical tradition—whether conservative advocates of laissez-faire or their social democratic and liberal socialist critics—have for the reasons above seen communities as anachronistic remnants of a less enlightened epoch that lacked the property rights, markets, and states adequate to the task of governance. In this view, communities are not part of the solution to the failures of markets and states, but part of the problem of parochial populism or traditional fundamentalism, according to one's lights. Many holding this view have long since rejected any dogmatic adherence to either pole of the planning versus markets opposition; but these anchors still moor the ship of good government as firmly as ever, debate now centering on the optimal location along the resulting continuum.

Those who advocate social capital or, as I would prefer, community governance, as an important aspect of policy making and institution building have come to be dissatisfied with this view, doubting (with Arrow) that states or markets (in any combination) can be so perfected as to make community redundant, and believing that the substantial drawbacks of this third form of governance can be reduced by adequate social policy. And many have pointed to cases where efforts to perfect the market or assure the success of state interventions have destroyed imperfect but nonetheless valuable community-based systems of governance, suggesting that policy paradigms confined to states and markets may be counterproductive.

Unlike the utopian capitalism of textbook neoclassical economics and the utopian statism of its sub-branch, welfare economics (which for most of this century imagined that governments had both the information and the inclination to offset market failures), there can be no blueprint for ideal community governance. Communities solve problems in a bewildering variety of ways with hundreds of differing membership rules, de facto property rights, and decision-making procedures.[11] But the cases I have noted earlier may suggest some of the elements which are frequently found in well-governing communities and which might form part of a public policy aimed at enhancing the desirable aspects of community governance.

Ownership

The first, and perhaps the most important element is that members of the community should own the fruits of their success or failure in solving the collective problems they face. The Japanese fishermen, skippers and crew alike, own shares in the output of their co-op and hence directly benefit from its success in a way that employees on fixed wages would not. Among the Chicago residents, communities in which home ownership is common exhibit much higher levels of "collective efficacy." The most likely explanation is that home owners benefit fully from their neighborhood improvement interventions—not only from the improved quality of life but from the enhanced value of their homes. This interpretation is consistent with the fact that U.S. home owners are more likely to participate in local *but not national* politics.[12] Finally, the plywood worker-owners' success would be inexplicable were it not that, as residual claimants on the income stream of the co-op, each owns the results of *the others'* efforts. As these examples suggest, in order to own the success of their efforts, community members must generally own the assets with which they work or whose value is affected by what the community does.

The legal and governmental environment

The cases above—and hundreds like them—suggest that well-working communities require a legal and governmental environment favorable to their functioning. The Chicago residents' success in reducing crime could hardly have been realized had the police not been on call. The Japanese fishing co-ops, numbering more than a thousand, work within national and prefectural environmental and other regulations which they are free to complement by locally made rules, but not to override. A comparison of Taiwanese and South Indian farmer-managed irrigation organizations shows that the greater success of the former is due to the effective intervention of national governments in providing a favorable legal environment and handling cases in which the informal sanctions of the community would not be adequate.[13] The fact that governmental intervention has sometimes destroyed community governance capacities does not support a recommendation of laissez-faire.

The face-to-face local interactions of community are thus not a substitute for effective government but rather a complement. Neglect of this point no doubt explains some of the popularity of the social capital concept. The Gallup Poll recently asked three thousand Americans whether it was better that the poor receive help from family, neighbors, and friends, or from the government; they also asked if inequalities in income and wealth were "acceptable" or "a problem that needs to be fixed." Although the sample was evenly split between the two approaches to helping the poor, those unconcerned about the level of inequality were almost three times more likely to support the family and friends approach than the government solution.[14] Those supporting the social capital option in this case were seemingly motivated more by the fact that it would shrink government than by the hope that it would reduce inequality.

Thus both a legal and governmental environment which complements the distinctive governance abilities of communities and a distribution of property rights which makes members the beneficiaries of community success are key aspects of policies to foster community problem solving. There is a third element in the community good-governance package: active advocacy of the conventional liberal ethics of equal treatment and enforcement of conventional antidiscrimination policies. It is not unrealistic to hope that communities can govern effectively without repugnant behaviors favoring "us" against "them"; there are many examples of well-working communities that do not exhibit the ugly parochial and divisive potentialities of this form of governance, including all of those above.

Other ways of empowering communities can be imagined, but some of them should be resisted, for they heighten the difficult tradeoffs between good governance and parochialism. For example, among U.S. localities, participation in church, local service and political groups, and other community organizations was found to be substantially higher where income was more equally distributed, suggesting that policies to increase income equality would enhance community governance. But racially and ethnically diverse localities—measured by the probability that two randomly selected members of the population would be of different racial or ethnic groups—had significantly *lower* levels of participation.[15] One may hope that procommunity public policy would not seek to increase the racial and ethnic homogeneity of groups for this reason. But simply resisting government policies which homogenize is not sufficient. If these findings (and others like them) suggest that successful communities are likely to be relatively homogeneous, then a heavy reliance on community governance—absent adequate counteracting policies—could promote higher levels of local homogeneity simply because the success of groups and their likely longevity will vary with how homogeneous they are.

The future of community governance

Dilemmas such as this are not likely to go away. Far from being an anachronism, community governance appears likely to assume more, not less, importance in the future. The types of problems that communities solve—and that resist governmental and market solutions—arise when individuals interact in ways that cannot be regulated by complete contracts or by external fiat because the interactions are complex or the information concerning the relevant transactions is private or unverifiable. These interactions arise increasingly in modern economies, as information-intensive team production replaces assembly lines and other technologies more readily handled by contract or fiat and as difficult-to-measure services usurp the formerly preeminent role of measurable quantities like kilowatts of power and tons of steel as both outputs and inputs. In an economy increasingly based on qualities rather than quantities, the superior governance capabilities of communities are likely to be manifested through growing reliance on the kinds of multilateral monitoring and risk-sharing exemplified above. The model of the Japanese firm as an information-sharing clan has already assumed importance for this reason.[16]

But communities' capacities to solve problems may be impeded by hierarchical division and economic inequality among its members. Many observers believe, for example, that the limited inequality between managers and workers in the Japanese firm is a key contributor to its success. Farmer members of irrigation organizations in Tamil Nadu, India, and Guanajuato, Mexico, are more likely to cooperate in making efficient use of water if status and class inequalities among them are limited.[17]

If I am right that communities work well where the tasks are qualitative and hard to contract for, but the conflicts of interest among the members are limited, the conclusion seems inescapable that highly unequal societies will be competitively disadvantaged in the future. Their skewed structures of privilege and material reward limit the capacity of community governance to facilitate the qualitative interactions which underpin the modern economy. ■

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A policy in Lampman's tradition: The Community Reinvestment Act

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When I first met Robert Lampman, nearly three decades ago, I was a young economist in the process of switching jobs from working on macroeconomics at the Federal Reserve Board to working on poverty problems at the Office of Economic Opportunity. Time has marched on, and I am now back at the Fed, working on both macro and poverty issues at the same time.

Bob Lampman used to promote his antipoverty agenda in two parts. The first was to ensure "high levels of employment and increasing average product per worker." This is, of course, one of the fundamental mandates of the Federal Reserve, and we are trying to achieve the objective daily. The second was "special private and public programs for those groups who do not readily share in the benefits of economic progress."[1] It turns out that the Fed administers a very important program of this type, the Community Reinvestment Act (CRA).

CRA began in 1977 as a little-known bank law, responding to reports of redlining and other credit market distortions. Based on the charters of savings and loan associations, which require them to meet the convenience and needs of the communities they serve, the CRA encourages these institutions to serve the credit needs of low- and moderate-income borrowers in their communities. The financial regulatory agencies grade institutions on their CRA performance, the grades are made public, and CRA records must be considered by regulators in assessing proposed mergers or acquisitions.

The actual number of mergers denied by the regulators because of CRA problems is small, but the act has acquired much more visibility than numbers alone would suggest. On the political side, it has become a major bone of contention in discussions about new financial reform legislation. On the economic side, it seems to have been responsible for about $120 billion annually in loans to low- and moderate-income homeowners, small businesses, small farms, and community development activities. Though some of these loans would no doubt have been made in the absence of CRA, and some may not benefit low-income groups disproportionately, $120 billion is a lot of money.

Unlike many interesting public programs that are studied to death before they even get off the ground, CRA is well aloft, but has been very little examined. The impact of credit market programs such as CRA could be just as important as income support systems in influencing the long-term economic prospects of low- and moderate-income groups. It is time for social scientists interested in fields such as antipoverty policy, urban development, and social policy to focus research attention on these programs.

How CRA works

The CRA encourages financial institutions to make housing and business loans to low- and moderate-income borrowers in low- and moderate-income neighborhoods within their communities ("assessment areas," in the language of the law). Larger institutions must satisfy a lending test focusing on their mortgage, small business, and community development lending; an investment test focusing on their grants for and equity participation in community development activities; and a service test focusing on branch location and the availability of normal banking services to low- and moderate-income groups.

The law is administered by the federal regulatory agencies that already supervise financial institutions. For banks, these are the Fed, the Office of Comptroller of the Currency, and the Federal Deposit Insurance Corporation; for savings and loan associations, it is the Office of Thrift Supervision. These agencies examine and rate financial institutions every two or three years and meet frequently to try to standardize their CRA ratings criteria. At the present time, about 20 percent of institutions are ranked as outstanding, about 75 percent as satisfactory, and less than 5 percent as needing improvement. Only rarely is an institution found to be in "substantial noncompliance" with the law.

The biggest component of CRA loans is for mortgages to low- and moderate-income borrowers. There are detailed reporting requirements for mortgages made to these and other borrowers under the Home Mortgage Disclosure Act of 1975. In 1997, the 10,000 commercial banks and savings and loan associations subject to the act made about 1.1 million new loans to low- and moderate-income borrowers; the aggregate volume of these loans made under CRA in 1997 was about $58 billion, a total that has remained roughly stable throughout the 1990s.

The other large component of CRA lending is for small businesses and farms. Fed staff have estimated that in 1997 about $41 billion in new loans, a quarter of all new business loans, were made as a result of CRA. Community development loans amounted to another $18 billion, for an aggregate total of $117 billion in loans made under CRA in 1997.

Nobody has studied these totals carefully enough to generate counterfactual evidence—that is, what share of these loans would have been made in the absence of CRA. But the fears of redlining and other credit barriers that spurred passage of the law and the eagerness of financial institutions to receive CRA credit for their low-income lending both suggest that the loans probably would not have been made in the absence of CRA.[2] The econometrics are still unclear, but at the very least the act appears to have been responsible for a volume of new lending that dwarfs expenditure on any other poverty program of Lampman's day or today.

Perhaps as significant as the numbers themselves are the activities that take place. The prototype CRA project features a community group that supplies the entrepreneurship and organizational capability. This group may procure cheap vacant land from the city, obtain other grants or funds for the construction or rehabilitation of housing units, then sell the units to lower-income homeowners. The mortgages on the properties will be made by banks or savings and loan institutions, which get CRA credit for the loans. The community group will put funds from the sale of the homes into a revolving loan fund.[3]

The repayment experience with CRA loans has generally been very good. Fed staff estimate that annual losses on CRA loans between 1993 and 1997 are about one-third of 1 percent. The aggregate annual loss rate on the $191 billion in CRA small business loans over this period is .0035; on the $282 billion in CRA mortgage loans it is .0039. There is no evidence that the small business loss rate is any higher than the loss rate for non-CRA small business loans; the CRA mortgage loss rate is slightly higher than the extremely low loss rate on non-CRA mortgage loans.

These low loss rates, when combined with some slight loan subsidies to borrowers by many financial institutions, imply that CRA loans are nearly as profitable as other loans. In one survey of large residential mortgage lenders, 98 percent found them profitable, and 24 percent found them at least on a par with other loans.[4] Hard evidence is difficult to come by, but the profitability of CRA loans could be rising over time as lenders learn more about screening and credit-scoring for this segment of the population and as new opportunities arise for secondary market sales.

Given the rapid rise in bankruptcy filings in recent years, it is natural to wonder if CRA-induced expansions of credit are partly to blame. The evidence suggests not. Fed staff attribute at most 3–4 percent of overall bankruptcy losses to CRA loans. Moreover, the time patterns differ. Whereas overall bankruptcy filings and writeoffs for consumer credit cards and other loans have increased sharply since 1995, CRA loan losses have been low and stable throughout the 1990s.

Questions regarding CRA

Promoting programs that are popular with those actually trying to arrange credit for low- and moderate-income borrowers, CRA raises a number of interesting research questions, some concerning the law's operation and some its ultimate impact.

Structure of the law

Although institutions can be held liable for lending discrimination under the Equal Credit Opportunity Act, they cannot be held liable for poor CRA records per se. Because CRA records are examined in the merger process, this would, superficially, seem to encourage excessive scrutiny of merging institutions with good CRA records and insufficient scrutiny of institutions that might have poor CRA records but no plans to merge.

Because about 95 percent of institutions generally receive CRA passing grades, one would expect very few mergers to be denied. The Treasury Department reports that of the 86,000 merger applications filed since 1985, there were only 755 CRA protests. In these protested cases, 690 mergers were eventually approved.[5] From 1993 to 1997, the Federal Reserve considered an average of 1,100 merger cases a year in which the merging institution was subject to CRA. Only 70 cases a year, on average, raised issues serious enough to trigger a detailed CRA review. In general, the merger was denied on CRA grounds in only one case a year, but in another seven or so the merger application was withdrawn, perhaps for CRA-related reasons.

These numbers do not make the CRA test appear very formidable, but that impression is belied by other considerations. The simple amount of lending and the share of banks with good CRA records suggest that the CRA test is stronger than it looks, or that banks are increasingly finding it in their own interest to do CRA-type lending. Many banks also devote significant resources to their CRA regulatory submissions and lending efforts, creating special divisions to manage CRA projects. In addition to the formal, public CRA ratings, there is a public comment period for mergers and acquisitions, and in many cases a public meeting. Although mergers are rarely blocked because of low CRA ratings or negative public comment, such publicity is certainly not welcomed by banks.

Often, potentially merging banks make substantial prospective lending commitment agreements with community groups, even though the Fed and other regulatory agencies have repeatedly stated that they go only by the past record, not by any prospective CRA agreements. These agreements have evoked allegations that community groups “hold up” banks by threatening to file protests or speak against the banks at public merger meetings unless they sign CRA agreements. Given the stance of the regulatory agencies, it is puzzling that such threats, if indeed they have been made, should be effective.

Coming to a judgment about the structure of the CRA is difficult. On one side, the present structure does seem to have been effective in prompting a wide range of financial institutions to pay serious attention to low- and moderate-income credit needs, buttressed by government examinations but not by a costly legal enforcement process. The law has certainly opened up dialogue between financial institutions and community groups and has created profitable new lending opportunities that financial institutions may not have discovered without the push of federal legislation.

On the other side, there may be more focus than is socially optimal on banks in a position to merge, as opposed to those in a position to improve lending practices for the benefit of low- and moderate-income groups. There may also be gaps in coverage—not all markets may be served by financial institutions subject to CRA. Scholars interested in financial institutions should study CRA to see what can be learned about desirable ways to regulate financial activities.

Predatory lending

Many businesses have their less than noble side, and the subprime lending business does as well. Many new loans are now being made to low- and moderate-income borrowers, but competition in providing credit to such borrowers is limited, and there have been numerous reports of predatory or fraudulent lending practices. Loans for home repairs or debt consolidation might give cash up front but carry high interest rates and fees, unnecessary insurance, and difficult repayment terms. Loan sales people are reported to search neighborhoods for low-income but high-equity borrowers, often elderly, not financially literate, and quite vulnerable to deception. Borrowers can be unwittingly led to rapid turnover of home equity loans (a process known as “loan flipping”) with high finance charges every time. As borrowers pay the fees and become even more cash-starved, the equity they have built up in their homes over many years erodes.

How to deal with the problem is a major public policy challenge. Often the reported abuses revolve around refinancing of homes and balloon payments (large lump sum payments on the principal of the loan at specified times). Because many borrowers benefit greatly from such credit arrangements, it makes no sense to outlaw the practices altogether. Laws against usury may cause credit to dry up when general levels of interest rates rise. Disclosure forms are already complex with much fine print, and some borrowers can neither read nor understand them.

In response to earlier reports of fraudulent lending, Congress in 1994 passed the Home Ownership Equity Protection Act, which prevented balloon payments in the first five years of a loan, limiting early loan flipping but perhaps taking even further advantage of myopic borrowers. It also defined a class of “high cost” loans for which it established thorough disclosure requirements and prohibited some practices that often led to abuses. But many lenders have skated just below the requirements, subprime lending is still growing rapidly, and predatory lending has apparently continued.

The connection between CRA and predatory lending is potentially quite interesting and at this point quite unclear. There may be very little connection. Or CRA may inadvertently foster predatory lending because institutions subject to its provisions receive credit for lending to low- and moderate-income people, regardless of the terms of the loan. Or it may limit such practices, by bringing to the low- and moderate-income credit markets real competition from banks that are subject to regulation, use standard loan packages, have working relationships with community groups, and have a CRA service test.

This whole set of issues has been little studied. How widespread are predatory practices? The only remotely quantifiable information now available is from data on legal actions.[6] It would be helpful to understand the low- and moderate-income lending process better, to determine the conditions under which predatory lending thrives. What is the role of competition, or lack of it, in predatory lending? Study of different geographic areas, with different concentrations of vulnerable borrowers and different intensities of CRA activities, would help answer some of these questions.

The overall impact of CRA

The ultimate importance of the CRA lies in its social effects. With something as complicated as a credit program, there could be many such effects. Here are a few possibilities.

First, and relatively straightforward, is the impact of CRA on low- and moderate-income lending. CRA seems to have had a large effect, but perhaps not so much as the gross figures would indicate. The growth of subprime lending by institutions not covered by CRA suggests that some of this lending would have taken place anyway.[7] Yet having been shown the way by banks, a number of nonfinancial corporations are now entering the community lending business, a factor that might count in favor of CRA. How much new lending is truly due to CRA? Has CRA inspired nonbank lending, or has nonbank and subprime lending grown for similar reasons? What are the properties of this lending, and what is the impact of CRA on underserved segments of the credit market?

A second question is the impact of CRA on lending discrimination. It is now more than 20 years since CRA was passed in response to allegations of discrimination, redlining, and unequal access to credit, and four years since CRA rating criteria were fine-tuned to focus particularly on low- and moderate-income lending in low- and moderate-income areas. Is there evidence that lending discrimination has been reduced, or that neighborhoods are more integrated?[8]

A third question is the impact of CRA on financial evolution. Many CRA arrangements are very elaborate, with either outright gifts of urban properties from the city or city funds for land acquisition and development, funds from foundations and private developers, and CRA-type lending from financial institutions. Community groups have become financial entrepreneurs, putting together deals, working with city bureaucracies and banks. City bureaucracies have learned how to work with these groups, and many banks now have community development divisions. This sort of financial institution-building would seem to be profoundly important, but at this point the changes and their effects are largely observed anecdotally. Putting rigorous form on such developments is a challenging but potentially very fruitful research task.

A fourth question is the impact of CRA on credit markets. Lenders are now perfecting analytic techniques, such as credit-scoring, to facilitate the identification of good credit risks among the low-income population. Fannie Mae and Freddie Mac have developed their own financial models to provide a functioning secondary market for the mortgage loans, without which the primary lenders would do much less lending. Researchers have already begun to understand the effects of these changes on credit markets, but there is much still to do in understanding and improving credit-scoring.[9]

The fifth question seems the most important of all—the impact of CRA on economic development. As one tours the country and visits projects partially or fully funded under CRA, there are clear suggestions of success—visual differences between neighborhoods with and without CRA projects—but these impressions are superficial and unsystematic. Formal comparison studies of CRA and non-CRA areas in the same city, or activities before and after CRA, ought to be feasible. Many of these projects are now old enough that differences in property values, home ownership, school attendance, crime rates, and other indicators of neighborhood quality ought to be showing up. The law is ultimately designed to improve urban and rural life along these dimensions, and scholars should take on the task of ascertaining whether it really does so. ■

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[1]Both quotations are taken from R. Lampman, *The Low Income Population and Economic Growth*, Study Paper No. 12, U.S. Congress, Joint Economic Committee (Washington, DC: U.S. Government Printing Office, 1959).

[2]Suggests, but does not prove. There is a developing debate on the issue. J. Gunther, K. Klemme, and K. Robinson, in “Redlining or Red Herring,” *Southwest Economy,* Federal Reserve Bank of Dallas, no. 3 (May/June 1999): 8–13, argue that credit market barriers to low-income lending have been breaking down anyway, and that CRA has not played much of a role. In contrast, D. Evanoff and L. Segal, in “CRA and Fair Lending Regulations: Resulting Trends in Mortgage Lending,” *Economic Perspectives*, Federal Reserve Bank of Chicago, Nov./Dec. 1996: 19–43, found evidence that the increase in mortgage lending to low- and moderate-income groups was due to CRA.

[3]The mortgage will often be sold to a secondary buyer, often a government-sponsored enterprise such as the Federal National Mortgage Association (Fannie Mae) or the Federal Home Loan Mortgage Corporation (Freddie Mac). But these transactions take place roughly at market prices, so it makes sense to give the originating unit the CRA credit for the loan.

[4]L. Meeker and F. Myers, “Community Reinvestment Act Lending: Is It Profitable?” *Financial Industry Perspectives*, Federal Reserve Bank of Kansas City, 1996: 13–45; R. Avery, R. Bostic, P. Calem, and G. Canner, “Credit Risk, Credit Scoring, and the Performance of Home Mortgages,” *Federal Reserve Bulletin*, July 1996: 621–48.

[5]Treasury Department release, May 5, 1999.

[6]Luxman Nathan, “Borrower Beware: Equity Strippers Are Preying on Elderly Homeowners,” *Communities and Banking*, Federal Reserve Bank of Boston, Spring 1999, pp. 6–18.

[7]Gunther, Klemme, and Robinson, “Redlining or Red Herring.” The Shadow Committee on bank regulatory policy is also skeptical; see G. Benston, “Discrimination in Mortgage Lending: Why HMDA and CRA Should Be Repealed,” *Journal of Retail Banking Services* 19, no. 3 (Autumn 1997): 47–57.

[8]H. Ladd, “Evidence on Discrimination in Mortgage Lending,” *Journal of Economic Perspectives* 12, no. 2 (Spring 1998): 41–62, summarizes recent evidence.

[9]Avery and others, “Credit Risk.”

In the midst of reform: Wisconsin in 1997

Michael Wiseman

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It is common to gauge the success of welfare policy by the reduction in the number of families receiving assistance. If caseload reduction were genuinely the barometer of achievement, the sensible strategy would be to abolish cash assistance altogether. But when polled, voters consistently affirm support for social assistance for those in need, especially if aid is made conditional on work or other strategies leading to self-support. Many have voiced suspicion that smaller caseloads may have been purchased at the cost of greater family distress.

The real concern of poverty policy is with families in or at risk of poverty, regardless of welfare status. Are families at risk of poverty more secure now, and are their children better off, than they were before the 1996 Personal Responsibility and Work Opportunity Reconciliation Act, when access to cash assistance was an entitlement? New data from the Urban Institute's National Survey of America's Families (NSAF), fielded in 1997 (see box, p. 16), permit us to move toward this wider perspective. Because the NSAF is a "snapshot" of family circumstances at a point in time, it cannot be used to evaluate the net effects of welfare reform, but it can be used to look at the circumstances of the poor and near-poor and to look for evidence that state policy may have left holes in the safety net through which children and families have fallen.[1]

The NSAF reference year for assessing poverty, 1996, was a year of precipitous caseload decline, 1997 even more so, especially in Wisconsin (Figure 1). The inception of the Wisconsin welfare reform program, Wisconsin Works (W-2), has been accompanied by a dramatic drop in cash transfers, greater than that experienced in any other state or in the country as a whole. The importance of the state's role in welfare policymaking and the lead it has taken in implementing a work-oriented reform make the emerging consequences of W-2 a subject of particular interest. The NSAF data gathered so far put Wisconsin in a favorable light. But the fundamental questions are, not how well Wisconsin appears in 1997, but how much change will be evident when the 1999 NSAF data become available, and how change in Wisconsin compares to change in other focal states. This

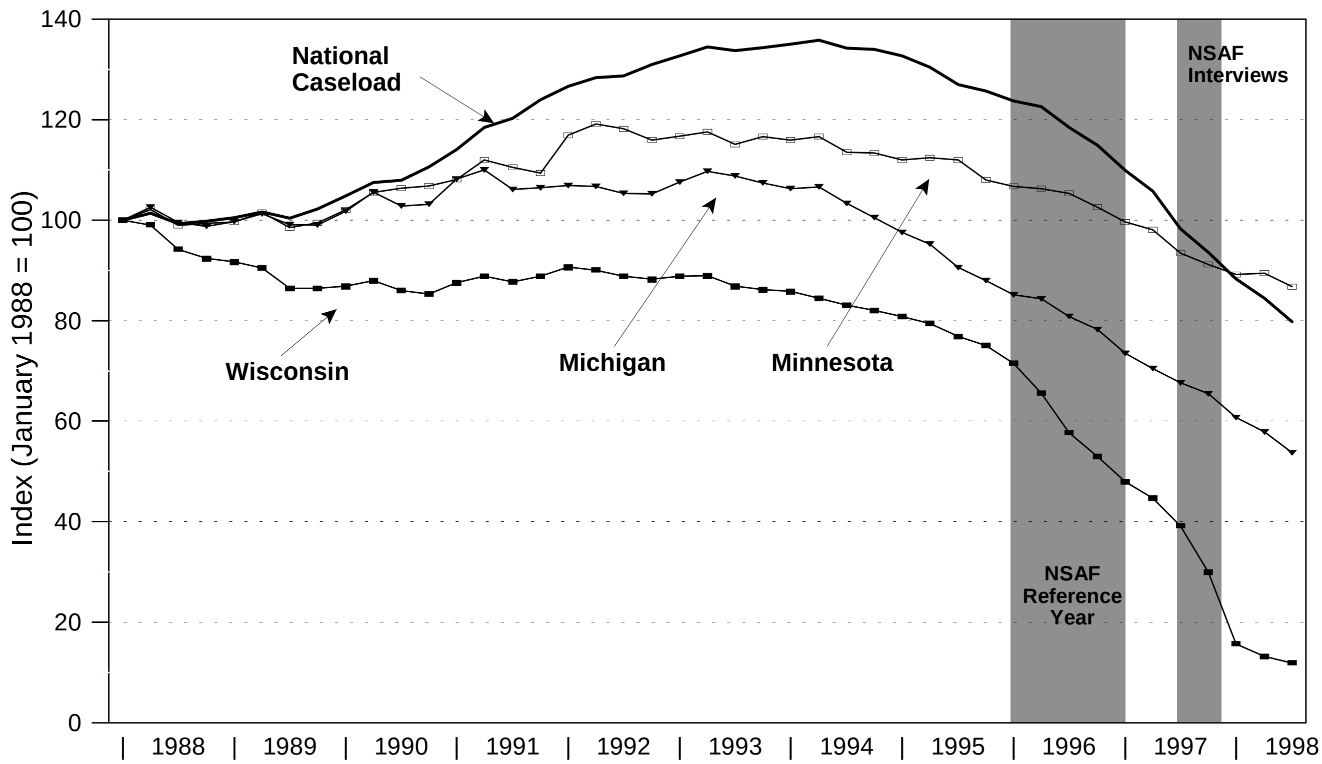

Figure 1. AFDC/TANF caseloads, Michigan, Minnesota, Wisconsin, and U.S., 1988–98.

Source: U.S. Department of Health and Human Services, Administration for Children and Families, welfare caseload data.

The National Survey of America's Families

The National Survey of America's Families (NSAF) is one of the primary data collection efforts of Assessing the New Federalism, a multiyear Urban Institute research project intended to analyze the devolution of responsibility for social programs from the federal government to the states. A primary goal is to obtain social and economic information about the well-being of children in low-income households likely to be most affected by changes in welfare and health policies.

A telephone-based survey of almost 50,000 households in 13 focal states as well as the nation as a whole, the NSAF oversamples low-income families, those with incomes less than twice the official poverty standard. In 1997, when the survey began, this low-income cutoff amounted to about $25,000 for a single-parent family of three or $32,000 for a two-parent family of four. The states surveyed are Alabama, California, Colorado, Florida, Massachusetts, Michigan, Minnesota, Mississippi, New Jersey, New York, Texas, Washington, and Wisconsin.

The survey is designed to provide national estimates of various indicators of family and individual circumstances and well-being as well as reliable state-specific estimates. Wisconsin's sample is almost twice as large as the average sample for the other focal states (this was made possible through fund-raising by the Wisconsin Works Management and Evaluation Project). The NSAF has 5,800 interviews from Wisconsin, 42 percent of them from Milwaukee County—an oversample sufficient to support separate analysis for the county.

The first round of the NSAF was fielded between February and November 1997. The national response rates were 65 percent for interviews about children and 62 percent for interviews about all nonelderly adults. Response rates in Wisconsin were among the highest in the survey: 68 and 65 percent in Milwaukee County and 75 and 69 percent in the rest of the state.

The survey is being repeated in 1999. The NSAF, including the Wisconsin supplement, will eventually be released for public use.

cross-cutting review of the state's families in 1997 sets a baseline for answering that question.

To place the data that follow in context, three things about Wisconsin are worth noting. First, population growth in the state has been slow relative to the nation, though comparable with other states in the upper Midwest; this is one of the factors underlying slower caseload growth. Second, except for Minnesota, Wisconsin has the smallest minority population of the states that are included in the NSAF. To the extent that minorities face a higher incidence of poverty and greater labor market problems, Wisconsin faces fewer difficulties in mounting an effective welfare-to-work policy than, say, California. Third, the Wisconsin labor market has been tight, but there are other states with lower unemployment rates—Minnesota, for one. Unemployment in Milwaukee County has been high relative to the rest of the state, and the county, especially the inner city, has regularly been cited as an area in which job supply may be inadequate to support employment-oriented welfare reform.

Welfare policy in three Midwestern states

The tables in this article include comparisons especially with two other Midwestern states, Minnesota and Michigan. The three states have in common geographic contiguity, a significant share of employment in manufacturing, and very tight labor markets occasioned by robust economic growth in the 1990s. They suffer in similar ways from climate and cholesterol, and on a number of dimensions (size, share of children in the population, population growth rate, and unemployment), Wisconsin falls between the other two. In 1996–97, welfare benefits in all three states were among the most generous in the nation.

At the time of the survey, all three had Republican administrations, yet welfare policy differed substantially.

The NSAF interviews in Wisconsin were largely completed before formal implementation of Wisconsin Works (W-2), the state's current welfare program, in September 1997. Many of the features of W-2 had, however, already been implemented in the state's Work First, Self-Sufficiency First, and Pay for Performance initiatives. This package promoted diversion of assistance applicants to employment, immediate job-taking as the principal object of assistance policy, and aggressive sanctioning of those who failed to comply. In December 1995 the state established the criteria for "right of first selection" for county social service agencies interested in becoming operating agencies for W-2. In order to qualify, counties had to reduce caseloads under Aid to Families with Dependent Children (AFDC) by 25 percent between September 1, 1995, and August 30, 1996.[2] Thus the NSAF covers an interval of extremely active welfare-to-work effort.

Michigan had been actively involved in welfare reform efforts since at least 1992. The Work First program introduced in 1994 required participation in a welfare-to-work orientation program as a condition of eligibility for assistance and until a job was found, and penalized nonparticipating families. Michigan's Family Independence Program (FIP) federal waiver allowed relatively generous disregard of earnings. In 1996, the state began experimenting with Project Zero, a demonstration in six sites designed to lower the incidence of unemployment to zero among AFDC/FIP participants required to work. Michigan was the second state, after Wisconsin, to submit its state plan for Temporary Assistance for Needy Families (TANF) once Congress substituted TANF for AFDC.

Table 1
The Families of Wisconsin's Children
(Percentage distribution of children by family circumstance)

State figures in **bold** are significantly different from the national average;
Milwaukee (MKE) figures in **bold** are significantly different from the balance of Wisconsin (BW)

	Comparison States		Wisconsin			
Family Type	MI	MN	All	MKE	BW	U.S.
Two-parent: The child lives with two biological or adoptive parents	64.2	**72.3**	**66.6**	**50.3**	70.1	62.6
One-parent: The child lives with one biological or adoptive parent who may or may not be living with another adult (or adults).	25.7	**20.0**	**23.4**	**38.8**	20.1	26.7
Blended: The child lives with one biological or adopted parent who is married to a step-parent who has not adopted the child.	7.7	**5.9**	7.7	6.0	8.1	7.6
No-parent: The child lives with adults other than his or her parents.	**2.4**	**1.7**	**2.3**	**4.9**	1.7	3.2

Source: National Survey of America's Families.

During the NSAF survey, the most significant difference between welfare reform strategies in Michigan and Wisconsin lay in the way work was pursued. In Wisconsin, the emphasis was on getting people off cash assistance, and that focus is dramatically evident in the criterion of caseload reduction established for right of first selection. The state made no changes in the time-limited financial work incentive incorporated in AFDC. In contrast, Michigan's policy emphasized work over closure: Project Zero was about zero cases *in which adults were not contributing to family income*. The state's work incentive incorporated in FIP allowed working recipients to keep the first $200 of earnings with no impact on benefits; thereafter earnings reduced benefits by 80 cents for every dollar—hardly much incentive for pushing on to self-sufficiency. The $200 plus 20 percent initiative had no time limit.

Minnesota's policy was different still. Under the Minnesota Family Investment Program (MFIP), initiated in 1994 and in operation in eight counties by the end of 1996, the state promoted work and poverty reduction but placed less emphasis on reducing the caseload than did Wisconsin. Work was promoted in part by a more generous financial incentive than that incorporated in federal law: food stamps and TANF were combined in a single cash benefit that was reduced by 36 cents for every dollar of earnings. Single parents were not required to participate in MFIP training and job placement programs until they had received AFDC for two years.

Thus by the time of the NSAF interviews all three states had well-defined welfare strategies in place. Wisconsin's strategy might have been anticipated to lower the caseload faster than Michigan's, and Michigan's to produce a higher incidence of work among recipients than policies followed in Wisconsin and in Minnesota. Since cross-sectional data cannot be used to infer causality or relate state-to-state variations in outcomes with any great confidence, I have tried to resist the temptation to do so. But it is perhaps surprising that there has been so little difference in outcomes, given what appears to be considerable difference in reform strategies.

Wisconsin families in 1997

This first foray into the use of NSAF data reflects the priorities of W-2. Employment is considered first, then income, then consequence, including children's outcomes.[3] The indicators discussed are broad-based and simple; over time, and as multiple surveys are accumulated, the analysis will be refined.

One consequence of caseload decline for Wisconsin was a substantial shift in the geographic focus of the state's public assistance policy. At the end of 1995, 53 percent of Wisconsin's AFDC cases were located in Milwaukee County. By August 1997, this share had risen to 67 percent.[4] Because of this overwhelming predominance, in Tables 1–4 data for the county are presented separately from the rest of the state.

Adults may be the focus of W-2, but concern about children is central. "[A]ll policies must be judged in the light of how well the policies strengthen the responsibility of both parents to care for their children," states the third of eight principles guiding the program.[5] Thus Table 1 provides a baseline for the discussion of indicators of the well-being of children, reporting their distribution by the type of family in which they live. Almost exactly two-thirds of Wisconsin's children live with both parents. By this measure, as by a number of others, Wisconsin as a whole does rather better than the U.S. average, though not so well as Minnesota. In Milwaukee, however, almost half of all children live with only one parent, and one in 20 lives with neither. The consequences of W-2 and other programs for this distribution will be of considerable policy interest.

Table 2
Low-Income Adults Employed Full- or Part-Time, 1997
(Percentage of adults not enrolled in school and reporting that they are "employed at a job or business")

State figures in **bold** are significantly different from the national average;
Milwaukee (MKE) figures in **bold** are significantly different from the balance of Wisconsin (BW)

	Comparison States		Wisconsin			
Family Status	MI	MN	All	MKE	BW	U.S.
Adults Aged 25 to 54						
Married[a] fathers	86.6	86.4	85.9	**76.9**	87.6	84.8
Married[a] mothers	**57.0**	**56.9**	**57.4**	48.6	58.8	45.3
Single parents	69.2	68.8	**77.5**	**71.6**	79.9	62.9
Other adults	59.9	**67.5**	**68.7**	**60.5**	71.0	56.5
Adults Aged 18 to 29						
Married[a] fathers	86.6	83.8	84.4	**58.2**	91.4	87.8
Married[a] mothers	**53.8**	**50.2**	**60.1**	**41.5**	63.7	36.7
Single parents	**67.1**	60.9	**69.4**	**57.9**	74.8	55.4
Other adults	68.8	**75.4**	**76.3**	68.5	78.2	65.4

Source: National Survey of America's Families.

[a]I.e., living in two-parent households as defined in Table 1. "Low-income" defined in the text, note 3.

Employment

Table 2 shifts the focus to the employment status of adults. The definition of employment is very broad, and adults are counted as holding jobs if they are working full or part time. The table restricts its attention to low-income adults aged 25–54—those most likely to be out of school, independent, and economically active. In effect, it asks, "Do the poor work?"

The evidence in Table 2 is that they do, and Wisconsin's low-income married mothers, single parents, and other adults are exceptional in this regard. For single parents, Wisconsin's employment rate exceeds the national rate by almost 15 points and is significantly greater than the rates for Michigan and Minnesota. Welfare policymakers are particularly interested in employment among younger single parents, and when we narrow the focus to adults aged 18 to 29 we find, once again, extremely high rates of employment. Rates are lower in Milwaukee County, but are still modestly higher than the national average. Perhaps the most distressing number in the table is the employment rate for young married fathers. In Milwaukee, more than one in three young fathers living with their families was without a job.

The striking employment figures in Table 2 have many implications. Nationally, Wisconsin is an outlier, and the labor market in the state was clearly even tighter in 1997 than unemployment data taken alone indicate. Other states had lower unemployment rates, but they also had lower employment rates, at least among adults in low-income families. To use a term common in European social policy, Wisconsin had a smaller yet-to-be-"activated" employment reserve than other states. Only Milwaukee County retained such a reserve, and efforts at raising employment there, especially among young married men, are very important both to strengthening families and to continuing state economic growth.

Table 2 also offers a caution against imputing causality to welfare reform. Low-income adults living in households without children ("other adults" in the table) are unlikely to be much affected by welfare reform. Yet the employment rate for this group is also exceptionally high in Wisconsin, suggesting that factors other than welfare reform—perhaps cultural, perhaps related to economic incentives—are likely to be involved in the high rate of employment for Wisconsin single parents.

Poverty

Wisconsin's high employment rate in 1996 translated into a low poverty rate, as Table 3 shows. The question asked here is simple: "Does pretax, post-transfer cash income exceed, for the family, the relevant poverty standard?"

The Wisconsin poverty rate of 8.9 percent is significantly below the national average and lower than the rate in Michigan and Minnesota, though not significantly so. The rate in Milwaukee is, as the employment statistics would imply, significantly higher than that for the rest of the state. And even in Wisconsin, we learn from Table 3, almost 17 percent of Wisconsin's nonelderly population is near-poor, living in families with incomes between 100 and 200 percent of the poverty level. This underscores the significance to the state of income support and services for families that are living above poverty, but not by much.

The focus of W-2 is on enabling parents. The second panel of Table 3 switches focus from the overall poverty

Table 3
Poverty Rate among Nonelderly Adults and Children, 1996
(Percentage living in households with incomes that fall below either the poverty level or 200 percent of the poverty level)

State figures in **bold** are significantly different from the national average;
Milwaukee (MKE) figures in **bold** are significantly different from the balance of Wisconsin (BW)

	Comparison States		Wisconsin			
Family Income	MI	MN	All	MKE	BW	U.S.
Children and Nonelderly Adults						
Below poverty level	**10.8**	**9.6**	**8.9**	**15.4**	7.5	14.8
Below 200% of poverty	**26.8**	**24.2**	**25.5**	**33.2**	23.9	33.2
Children in Poverty Only						
One-parent	**34.7**	**34.8**	**29.2**	**46.4**	22.1	44.1
Two-parent	**5.5**	**6.3**	**5.1**	**7.3**	4.7	10.5
All families	**13.7**	**12.5**	**11.4**	**23.9**	8.7	20.5

Source: National Survey of America's Families.

rate to the poverty rate of children. Wisconsin has the lowest child poverty rate of all the states studied, but its poverty rate of 11.4 percent is hardly a basis for complacence. Over 153,000 of the state's children—60,000 of them in Milwaukee—are poor.[6]

Material well-being

Even with adjustments for food stamps and the Earned Income Credit, the official poverty standard bases its assessment on a family's current income, not consumption. Just as it is important to look beyond caseload change as a measure of policy success, so it is important to look beyond income to family circumstance. Are people able to translate their incomes and other resources into adequate food, shelter, and medical care?

One reason for the lack of attention to consumption has been lack of agreement over appropriate indicators.[7] I use simple measures here, as a first step toward a more comprehensive assessment of the material aspects of family well-being (see Table 4).

Food problems

The standard here is quite low; we count families as having experienced a food problem if they *worry* that food will run out, if food has run out just once, or if an adult has gone without a single meal to provide food to a child during the preceding year.

Nationwide, almost one-third of children lived in families that reported some food problems during that time. This was true for over half of children in low-income families. Wisconsin has the lowest incidence of food problems of any of the states in the NSAF, but almost a third of children in Milwaukee County lived in families reporting such experiences.

It would be a mistake to think that such problems result from low incomes alone—about 12 percent of higher-income Wisconsin families report the same problem. Nevertheless, the incidence of food problems is almost four times as high in lower-income families.

Shelter problems

The national economic recovery from the 1991–92 recession has tightened housing markets and raised housing costs. The result, according to the U.S. Department of Housing and Urban Development, is that "rather than benefitting from the surging economy, low-income renters are left to compete for the dwindling supply of affordable rental housing available on the private market."[8]

The effect of W-2 and its antecedents on housing access continues to generate controversy. The W-2 cash grant does not vary with family size, and many recipients lose benefits as a sanction for failing to comply with program rules. Program opponents assert that these features have increased the numbers of those actually homeless and of those at risk of eviction. Panel 2 of Table 4 looks at housing problems. The question on which the table is based focuses on cash flow problems: "Have you at any time been unable to pay for rent and utilities during the previous 12 months?"

Wisconsin compares well with other states in this respect. Milwaukee, though again experiencing more problems than the rest of the state, is doing better than the national average in the area of housing. We cannot, however, conclude from this that W-2 has had no effect; the NSAF is not well-suited to the study of homelessness, which must be investigated by more direct means.

Health insurance

Guarantee of access to health insurance for all Wisconsin families with children was a major feature of the original

Table 4
Measures of Material Well-Being

State figures in **bold** are significantly different from the national average;
Milwaukee (MKE) figures in **bold** are significantly different from the balance of Wisconsin (BW)

	Comparison States		Wisconsin			
	MI	MN	All	MKE	BW	U.S.
Children in Families Reporting "Food Problems" (%)[a]						
Lower income	51.9	50.1	**46.8**	**55.9**	43.8	53.9
Higher income	13.6	13.3	**12.1**	13.4	11.9	15.4
All	**26.6**	**24.4**	**23.3**	**32.7**	21.3	31.8
Parents Reporting Problems with Housing Costs 1996–1997 (%)[b]						
Lower income	30.3	28.2	25.9	27.0	25.6	28.4
Higher income	9.0	8.0	**7.3**	8.1	7.2	9.1
All	14.9	**13.1**	**12.0**	**14.6**	11.5	16.0
Children in Lower-Income Families with Current Health Insurance Coverage, 1997 (%)						
Privately insured	**47.9**	**46.8**	**58.0**	**40.2**	64.0	39.7
Publicly insured	40.0	40.6	**27.4**	**45.9**	21.2	39.0
Uninsured	**12.2**	**12.6**	**14.6**	13.8	14.9	21.3

Source: National Survey of America's Families.

Note: "Lower income" and "higher income" defined in the text, note 3.

[a]Percentage of all children living in households in which adults report that (1) they or their families worried that food would run out before they got money to buy more, (2) the food they bought did run out, or (3) one or more adults ate less or skipped meals because there wasn't enough money for food.

[b]Percentage of parents reporting "that they were unable to pay their mortgage, rent, or utility bills at any time during the previous 12 months."

W-2 proposal. The plan, which called for universal, income-based copayments, was rejected by the federal government. A less ambitious version, known as BadgerCare, was approved and began operation in July 1999.[9]

Health insurance coverage in Wisconsin is better than in the nation as a whole, though several other states have somewhat higher rates of coverage. Interestingly, insurance coverage in Milwaukee is no lower than in the rest of the state, but the source of the insurance differs; Milwaukee children are much more dependent on Medicaid.

Answers to other questions about health care revealed more differences. Almost 25 percent of adults in low-income families in Milwaukee reported that they had no usual source of care (other than emergency rooms), compared to just over 17 percent for the rest of the state.[10] And whereas 90 percent of Wisconsin families with children, in Milwaukee and elsewhere, were reasonably confident that their family members could get care if they needed it, about 17 percent of Milwaukee adults without children had no such confidence.

This sampling of the indicators of access to health care suggests that Wisconsin's health care system, though quite good, is not exemplary. The problem lies in Milwaukee, and it is not so much a matter of access to insurance as it is of finding ways to link low-income families and adults without children to regular sources of care.

The NSAF messages

There are already some important implications from the data now in hand; more will emerge as work with the first wave continues.

- *Poverty persists*, and is associated with genuine hardship as revealed by food, shelter, and health care problems. When compared to other states, however, Wisconsin's achievements are very good.
- *Employment is central to the Wisconsin lifestyle*. The employment rate of single parents with children has increased dramatically nationwide. But even against this backdrop the state's relative achievement is substantial, and it is hard not to believe that the employment rates observed in the NSAF are, at least in part, the product of policy.
- *The health issue goes beyond insurance.* It is important that attention be devoted both to connecting people to the health insurance system and making sure that those insured have effective access to health services.
- *Policy effects are still uncertain*. The consequences of the variation in reform strategy among the Minnesota-Wisconsin-Michigan neighbor states are not readily detected using the first wave of the NSAF. Care should be taken in asserting the superiority of any particular strategy until more information is gathered. The second NSAF wave, completed this year,

Table 5
Attitudes Toward Welfare Reform in Wisconsin and the United States, 1998

Question	Response	Wisconsin	U.S.
Do you know whether your state has adopted major welfare reform changes in the past two years, or not?	Yes	81%	48%
	No	4	16
	Don't Know	15	35
Compared to two years ago, do you think that the number of people in your state receiving welfare has increased, decreased, or stayed about the same?	Increased	6	18
	Decreased	77	41
	Stayed the Same	12	28
	Don't Know	6	12
Who in your state do you believe is making decisions about welfare reform policies?	The Governor	76	45
	State Legislators	23	31
	(Six Other Responses)[a]	—	—
Sample Size		323	2,221

Source: Questions are selected from Bonney and Co., *The National Devolution Survey Conducted for the W. K. Kellogg Foundation* (Virginia Beach, VA: Bonney and Co., 1999).

[a]Multiple responses were permitted, so other responses are not aggregated. None was selected by more than 6 percent of respondents nationwide.

should provide more information on differences across these and other states, in the direction of change of welfare indicators.

- *In Wisconsin, Milwaukee remains the problem.* On virtually all measures studied, Milwaukee does worse than the rest of the state. Yet the social policy environment in the city has changed far more than proponents or opponents of W-2 anticipated. Although 60,000 children in the county still live in families that report incomes even below the penurious federal poverty standard, the state and its contractors have demonstrated that jobs can be found and the hard-to-employ moved into them. The challenge is to make this work pay off in poverty reduction, the disappearance of hunger, better housing, better health. The challenge, in other words, is to move beyond the caseload as a measure of success.

Ending caseload fixation

In January 1999, the Kellogg Foundation released the results of a nationwide poll of attitudes toward the devolution of governmental responsibility for welfare and health care reform. The knowledge and attitudes reported by adults interviewed in Wisconsin were very different from those reported in the rest of the country (Table 5).

To an extent not evident elsewhere in the United States, Wisconsin citizens are aware of the welfare reform efforts and the caseload contraction. Not surprisingly, four out of five respondents in Wisconsin and the nation reported "favoring" welfare reform. Goals most favored were "eliminating fraud and abuse," "helping people who have been on welfare get jobs that allow them to take care of themselves and their families," "making sure poor children get the help they need," "helping people stay off welfare for good," and "reducing teen pregnancy." Respondents were not asked to judge the consequences of reform—for example, did the new system serve such goals better than the old system? Without such questions, it is impossible to judge progress toward one goal of W-2—improving the public assessment of state and local welfare operations.

The Kellogg survey and similar polls strongly suggest that the public is interested in much more than caseload decline. A change in focus from caseload to consequences is, indeed, overdue. In principle, once welfare has been transformed, the number of people participating is also transformed from a negative into a positive—a measure of the extent of genuine need successfully addressed by the government. No such sea change in public opinion is yet evident in the national political discourse. Like welfare reform itself, ending caseload obsession will require leadership, both in Washington and in Wisconsin. ■

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[1]This article is based upon an extended report with the same title that was published by the Urban Institute in summer, 1999. The complete report is posted on the Urban Institute's ANF web site, <http://www.newfederalism.urban.org/>.

[2]In this respect, Milwaukee County differed. The county was divided into six districts, and responsibility for the W-2 program was determined in each district by competitive bid. Private nonprofit and for-profit agencies manage the W-2 programs in all districts.

[3]To the extent possible the analysis is linked to the information provided in the Urban Institute's publication, *Snapshots of America's Families: A View of the Nation and 13 States from the National Survey of America's Families* (Washington, DC: Urban Institute, 1999). For the indicators included here, several definitions are particularly pertinent. *Nonelderly adults* are persons aged 18–64; *children* are persons aged 0–17. *Poor* refers to a household or family with pretax money income at or below the federal poverty standard; *near-*

poor to a person with income between one and two times the poverty standard. The term *low-income* encompasses both poor and near-poor individuals. *Higher-income* is used to describe a person living in a family with pretax money income more than twice the relevant poverty standard (for a family of four, the boundary between lower and higher income is $32,000).

[4]This does not mean that the number of families receiving assistance was increasing in Milwaukee—only one other county in the nation experienced a higher rate of reduction from 1994 to 1998. This was Duval County (Jacksonville), in Florida. See B. Katz and K. Allen, *The State of Welfare Caseloads in America's Cities: 1999* (Washington, DC: Brookings Institution, 1999), p. 7.

[5]Wisconsin Department of Workforce Development, *Wisconsin Works* (Madison, WI: DWD, 1998), p. 2.

[6]A caveat to be emphasized is that the measure of income employed here is unsophisticated. Virtually all poor families identified in the NSAF would have been eligible for food stamps, and because a very high proportion of adults, especially single parents, are working, they could also benefit from federal and state Earned Income Credits.

[7]The dilemmas involved in a consumption-based measure of poverty are briefly described in P. Saunders, "Toward a Better Poverty Measure," *Focus* 19, no. 2 (Spring 1998): 39–42.

[8]U.S. Department of Housing and Urban Development, *Waiting in Vain: An Update on America's Rental Housing Crisis* (Washington, DC: HUD, 1999), p. ii.

[9]On Wisconsin health policy, see T. Coughlin, J. Wiener, J. Marsteller, and colleagues, *Health Policy for Low-Income People in Wisconsin* (Washington, DC: Urban Institute, 1998).

[10]The proportion of children for whom there was no usual source of care was lower in both instances: 8.8 percent in Milwaukee and 4.4 percent in the rest of the state.

Of interest on the World Wide Web

The latest *LaFollette Policy Report*, Vol. 10, No. 1, Spring/Summer 1999 has two articles of particular relevance to current poverty policy debates.

Gary Burtless, **Political Consequences of an Improved Poverty Measure**

David Vanness and Barbara Wolfe, **Government Mandates and Employer-based Health Insurance: Who Is Still Not Covered?**

The report can be accessed from the LaFollette web site, <http://www.lafollette.wisc.edu/outreach/pubs/> and click on "LaFollette Policy Report."

Luxembourg Income Study Summer 2000 Workshop

The Luxembourg Income Study has made comparable over 75 large microdata sets which contain comprehensive measures of income and economic well-being for over 25 modern, industrialized welfare states. The LIS databank currently includes Australia, Austria, Belgium, Canada, the Czech Republic, Denmark, Finland, France, Germany, Hungary, Ireland, Israel, Italy, Luxembourg, the Netherlands, Norway, Poland, Russia, the Slovak Republic, Spain, Sweden, Switzerland, Taiwan, the United Kingdom, and the United States. It is also negotiating with Japan, Korea, Greece, Portugal, New Zealand, and South Africa.

The LIS Summer Workshop is a one-week pre- and postdoctoral workshop designed to introduce young scholars in the social sciences to comparative research in income distribution and social policy using the LIS database. The 2000 workshop will be held in Differdange, Luxembourg, from July 9 through July 15. The course of study will include a mix of lectures and assistance and direction using the LIS database to explore a research issue chosen by the participant. Workshop faculty will include the entire LIS staff (including Timothy Smeeding, Overall Director, Lee Rainwater, Research Director, and John Coder, Technical Director) and other experienced LIS users.

For more information about the workshop, please contact LIS administrative assistants Caroline de Tombeur, LIS at CEPS/INSTEAD, B.P. 48, L-4501 Differdange, Luxembourg
(e-mail: caroline@lissy.ceps.lu)
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(e-mail: lisaa@maxwell.syr.edu).

For an application form, please check the LIS home page on the World Wide Web at http://lissy.ceps.lu/index.htm. Applications are due by May 1, 2000.

Food pantries and welfare reform: Estimating the effect

Peter Eisinger

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As the various elements of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (PRWORA), or welfare reform, began to take effect, social service providers in the nonprofit sector braced for the expected deluge of people cast out of the federal safety net.[1] By setting time limits on the ability to draw cash assistance, welfare reform mandates a regime of self-reliance for which many people are unprepared. Thus, nonprofit welfare-to-work programs as well as homeless shelters geared up to accommodate those expected to lose their monthly welfare checks. Daycare facilities began planning for new clients, as welfare mothers entered the workforce. Private food pantries and soup kitchens also anticipated a new burden, for PRWORA not only eliminated Aid to Families with Dependent Children (AFDC) but also wrought major changes in the Food Stamp Program.

The changes in food stamps affected many more people than did the transformation of AFDC into a block grant. Not only did the new law tighten eligibility for the food assistance program but it also further diminished the purchasing power of food stamps for all participants (see below). In Michigan, for example, the site of this present study, the average per-person monthly food stamp allotment fell from $69 to $67 a month between 1994 and 1998. In inflation-adjusted dollars, that is an average loss of nearly $9 a month in food purchasing power.[2]

One possible effect of these changes is that many people who formerly relied on their own resources and perhaps food stamps to feed themselves might be driven into the nonprofit or charitable food sector—the system of lay and church-based food pantries and soup kitchens—because they lost their eligibility for food stamps or their food stamp benefit decreased in value.[3] This article offers an estimate of the size of the "welfare reform increment" borne by the charitable food system in the Detroit metropolitan area, with a population (in 1996) of over 4 million.

If welfare reform has expanded the role of the charitable sector in a partnership with government to feed poor people, then it is important for food assistance policy to determine what the added burden on that sector really is and how well prepared its institutions are to meet it. Although the overall capacity of what is often called the emergency feeding network has grown significantly in recent years, few analysts have believed that these providers could assume a significantly larger role than they now play, or could come close to filling the gap between what the federal food assistance programs provide and what is actually needed.[4]

Welfare reform is driving more hungry people to emergency food programs and causing food shortages, City Councilman Gifford Miller (D-Manhattan) reported yesterday.

A random survey by his staff of 31 soup kitchens and food pantries found that 87% experienced a greater demand for emergency food in the past six months. And 55% of the programs said they had to ration food to avoid turning people away.

New York Daily News, May 21, 1999

First, the 1996 welfare law made work a prerequisite for cash assistance. Now the latest bad news: people are shunning food stamps. Since 1996, the food stamp rolls have dropped nearly 30 percent, more than the decrease in official poverty. Many former welfare recipients are deciding to go it on their own.

This move toward self-sufficiency should be cause for celebration. Instead, the food stamp bureaucracy and its supporters in Congress are determined to snuff it out. . . . Predictably, the advocates have trotted out the most powerful appeal to buttress their case for expanding the rolls. Kids are going hungry. . . .

Disturbing claims, if true, but concrete evidence for them is nonexistent. . . .

Food pantries—ideally ones that ask for something in return—are in fact a wiser response to temporary hunger than expanding the rolls, for independence is a better guarantee of eating well than entitlements can ever be.

Heather MacDonald, contributing editor to the Manhattan Institute's *City Journal*, in the *New York Times*, August 12, 1999

Welfare reform and the Food Stamp Program

In ending "welfare as we know it," Congress also modified the Food Stamp Program in a variety of ways designed to save money and reduce dependency. One set of changes reduces the value of the average allotment by freezing indefinitely the standard deduction from income at $134 per month per household and setting the maximum vehicle exemption at $4,650. Since the household food stamp allotment varies inversely with income after deductions, the face value of the average food stamp benefit will diminish, even if household income grows only at the rate of inflation. PRWORA also changed the baseline worth of the maximum food stamp allotment from 103 percent of the annually adjusted cost of the USDA Thrifty Food Plan to 100 percent of the cost.

A second set of changes affected the eligibility rules. Until PRWORA, eligibility extended to anyone with a net monthly income at or below the federal poverty line.[5] A few categories of people were barred from the program—students and the institutionalized, for example. The 1996 welfare reform added to this ineligible list by barring most classes of legal immigrants. Twenty states promptly sought to shield legal immigrants by funding food stamps from state monies, but Michigan was not among them. Although Congress restored the eligibility of about 250,000 legal immigrants in the summer of 1998, the law still prevents perhaps 650,000 who were in the program from returning.

In addition, able-bodied adults between the ages of 18 and 50 who had no dependents were limited to 3 months of food stamps within any 36-month period if they were not working or engaged in job training. Estimates indicate that this rule change reduced the rolls by about 1 million people. States could seek an exemption for a percentage of these adults in areas of high unemployment, but Michigan, alone among the larger states, declined to do so.[6] Michigan implemented these new federal eligibility changes between December 1996 and August 1997.

The effects of the welfare changes: Preliminary evidence

Many local political leaders and social service providers around the country are sure that the welfare reform increment in the charitable food system is substantial. Among 34 cities surveyed by the U.S. Conference of Mayors in 1997, three-quarters said that demand for charitable food assistance by legal immigrants had risen by an average of 11 percent in the first half of 1997. Even more cities (81 percent) said that demand for emergency food from all quarters had increased, by 17 percent on average. Most respondents said either that welfare reform was primarily to blame (41 percent) or was equal to other factors in explaining the increase (39 percent).[7]

Officials in metropolitan Detroit maintain that demand for food assistance in the postreform period rose between 1997 and 1998 (by 40 percent in Macomb County and by 59 percent in Oakland County), but no one has attempted to estimate the magnitude of the welfare reform increment.[8] Nor does the state of Michigan track what is happening to people coming off the welfare rolls. Partial data collected by the Hunger Action Coalition from member food providers in the tricounty metropolitan area also indicate that overall demand at pantries grew by 23 percent between January and December 1997, while demand at soup kitchens grew by 26 percent.[9] Demand has risen steadily at these street-level feeding institutions every year in the decade, both before and after the passage of PRWORA, so there is no way of knowing how much of these increases can be attributed to the changes in food stamp benefits and eligibility effected by welfare reform.

The Detroit-area survey

The directors

In order to explore more systematically the question of the welfare reform increment, we surveyed directors of emergency food providers (EFPs) and clients in the tricounty region in the winter and early spring of 1999.[10] The world of street-level food providers is both tenuous and turbulent, and lists of providers are out of date as soon as they are printed, but we interviewed 92 directors, from among 157 providers. The programs range widely in size, with the food pantries serving fewer than a dozen up to approximately 7,000 people a month (the median is 138) and the soup kitchens from 35 to 2,500 (the median is 835). In all, the organizations whose directors we interviewed provide about half the free food in the metropolitan area. The other half of charitable food in the Detroit area is provided by three large institutions that do not fall under the Hunger Action Coalition: the Salvation Army at several different sites, a large Capuchin soup kitchen that operates at two huge feeding sites, and Focus Hope, a combination job training, child care, adult education, and food pantry center.[11]

Directors were asked to provide figures on the number of clients served by their programs in the months of December 1997 and 1998 (Table 1). The cumulative client burden rose in this period, but the number of people served actually decreased for 8 providers and remained stable for another 21. Thus, 63 programs experienced increases.[12]

All directors who said that their client burden had changed were then asked to explain why. All 8 directors

Table 1
Total Number of Emergency Food Clients Served by Sample Programs, Detroit Tricounty Area, 1997 and 1998

	Dec. 1997	Dec. 1998	% Change
Food Pantries	36,458	52,959	+45.2%
Soup Kitchens	12,338	17,833	+44.5%
Total	48,795	70,792	

Source: Tricounty survey of emergency food providers, 1999.

Note: The number of clients tends to rise in the winter holiday months. December totals are higher than the number of clients served in the average month. Figures supplied by directors on average monthly visits in 1998 total about 54,000. N = 92.

who experienced *declining* client loads (their programs served between 40 and 1,000 clients per month) mentioned the improved economy and labor market tightening as explanations for the improvement in people's circumstances. Among the 63 directors facing *growing* burdens, 41 cited the cuts in food stamp benefits or "welfare reform," particularly the change in eligibility rules for single adults, as among the major factors driving increasing numbers of people into the emergency food programs. None mentioned the limits on legal immigrants. About one-third of the directors cited a major factor other than welfare reform, including job layoffs, unemployment, low-paid work, the unusually harsh winter, and the increased cost of living.

In sum, most but not all food pantry and soup kitchen directors had to deal with increased client loads in the two years after welfare reform implementation, and two-thirds of those dealing with a growing burden believed that welfare reform effects on food stamps were critical factors in explaining their situation.

The clients

Very few people spontaneously report that they have had to visit a food pantry or soup kitchen because they have been purged from the food stamp rolls or had their benefits reduced by the 1996 welfare reform. But we can nevertheless estimate the size of the welfare reform increment by sifting a sample of food pantry and soup kitchen clients through a series of questions that establish the likelihood that the person is present because of hardship induced by welfare reform.

We interviewed food pantry and soup kitchen users in the tricounty Detroit area at the facilities, at about the same time that we surveyed the directors, from February through May 1999. Eight large pantries and kitchens contributed the bulk of the respondents and 6 smaller ones the remainder. Interviews, conducted generally during the last week of the month when even under the best of circumstances food stamps and welfare checks begin to give out, took only 5 minutes, and respondents were paid $5 for participating. We interviewed 229 clients from different households. There were virtually no refusals.

How representative is this sample of food assistance clients? There are few baseline data sources against which to compare it, and none from the Detroit area. One source of comparison is the huge Second Harvest national survey of food assistance clients, conducted in 1997 according to selection and randomness rules similar to those that governed the Detroit area survey. Although the Detroit sample is drawn from a metropolitan population that is heavily African American and the Second Harvest survey is national in scope, drawing from many rural white areas as well as inner cities, there are enough similarities on other dimensions to suggest that the Detroit sample is a reasonable representation of the population of charitable food assistance clients (see Table 2). Perhaps the most important similarity is that virtually identical proportions are not enrolled in the Food Stamp Program.

Estimating the welfare reform increment

There are two factors related to welfare reform that might drive clients to use food pantries and soup kitchens. One is that they lost their eligibility for food stamps after

Table 2
Comparing the Detroit Area Sample with the Second Harvest National Sample

	Detroit	Second Harvest
African-American	70.9%	35.3%
< High school education	37.0	40.0
High school/GED	41.3	36.2
In school or job-training program	6.5	3.8
Employed[a]	16.2	20.7
> 65 years[b]	12.2	16.0
Female	56.5	62.4
Enrolled in Food Stamp Program	43.7	41.4

Source: Tricounty survey of emergency food providers, 1999; Second Harvest, *Hunger, 1997: The Faces and Facts* (Chicago: Second Harvest, 1998).

Note: The Detroit sample underrepresents Hispanic clients. Interviewers were unable to gain access to the two main Hispanic food pantries.

[a]The Detroit unemployment rate (7.0% in 1998) was high compared to the national average (4.5%).

[b]The African-American population tends to be younger than the white population.

Table 3
Why Certain Emergency Food Clients Are Not Receiving Food Stamps

	% Saying the Statement Applies
I applied but was turned down	19.4% (25)
I was receiving food stamps but lost my eligibility	26.4% (34)
I haven't applied because I know I'm not eligible	24.8% (32)
I haven't applied because it's too much trouble	23.3% (30)
I don't know how to apply for food stamps	3.1% (4)
I haven't applied for some other reason	22.5% (22)
N	129

Source: Tricounty survey of emergency food providers, 1999.

Note: Respondents could answer "yes" to more than one statement.

passage of PRWORA. People in such a situation may have been purged from the food stamp rolls, exhausted their limited eligibility, applied but been turned down, or, knowing that they were ineligible, may not even have attempted to enroll. Recall that over half the clients (129, 56.3 percent) in the Detroit sample were not enrolled in the Food Stamp Program.

Another group of clients (100, 43.7 percent) does receive food stamps, but they may have been driven to supplement their stamps at EFPs because their benefits have been cut as a result of welfare reform. We examine each group separately.

Clients without food stamps

When a respondent said that she or he was not currently receiving food stamps, the interviewer probed further (e.g., "Why were you turned down?"). Of the 129 clients not receiving food stamps, 69 answered yes to one or more of the first three statements in Table 3: their application had been turned down, they had lost eligibility, and/or they believed that they were not eligible.

In order to determine whether the status of these 69 clients was the result of PRWORA, interviewers asked for a fuller explanation of benefit denial or ineligibility. Most said that their income was too high (the income bar has long been in existence and is not a product of the welfare reform of 1996). Only 19 cited reasons directly related to the welfare reform changes in food stamp eligibility effected by the 1996 law. All of these reasons had to do, in one way or another, with the requirement that adults without dependent children could only draw food stamp benefits for 3 months out of every 36 unless they were working or enrolled in a job training program. None said that they were legal immigrants. Thus, respondents explained to interviewers that they were not getting food stamps because: "single men are not eligible," "Engler [the governor of Michigan] passed a law saying you can only get food stamps three months over three years," "government cut off single people," "I have no kids, only grandchildren," "they cut off stamps unless you go to the Work First program," and so on.

Can we conclude that these 19 people constitute the welfare reform increment among those clients not receiving food stamps? Most of them likely do, but not all. Two of the 19 had been regular visitors to the food pantry or kitchen at which they were being interviewed for more than two years, that is, since *before* welfare reform changes in food stamp eligibility were implemented in Michigan. The remaining 17, however, had been visiting the food pantry for less than two years, and some were there for the first time. Did welfare reform changes transform these people into clients of the charitable food sector?

In all likelihood, some already had a history of sporadic reliance on charitable food programs. The Detroit survey did not ask respondents about the first time they *ever* used an emergency food facility in the metropolitan area, but the Second Harvest survey did, and the answers suggest that slightly over one-third of pantry and soup kitchen clients had first used such a facility more than two years before. Let us assume, then, that the same proportion, about one-third, of the 17 Detroit clients who had first visited the program within the last two years had probably used some other emergency food provider before the present one.[13] If we follow a conservative set of decision rules, we do not count this one-third as part of the welfare reform increment.[14] They are long-term or habitual, if sporadic, clients. Thus, we are left with 11 or 12 clients, roughly 9 percent of the 129 clients not receiving food stamps, who are most likely to have used a charitable food program for the first time within the last two years because the welfare reform law ended their eligibility for food stamps. They represent one portion of the welfare reform increment.

Food stamp recipients

In the Detroit area sample exactly 100 of the emergency food system users were receiving food stamps at the time they were interviewed. These respondents were asked whether their food stamp allotment had decreased ("less than I used to get") or stayed the same ("I get about the same . . . as I did a couple of years ago"). Fifty-nine said that their benefits had decreased. Yet feeling the pinch of an inadequate food stamp allotment is not necessarily proof that a person has suddenly been driven to the emergency food system.

Indeed, 9 of these 59 food stamp recipients had been patrons of the food pantry or kitchen at which they were interviewed for more than two years, that is, prior to the implementation of welfare reform changes in the food stamp system. Welfare reform made their situation more difficult, but it did not drive them into the emergency food system.

Of the remaining 50, we may apply the same discount as we did to those emergency food clients not receiving food stamps: about one-third of them probably first used a charitable food program more than two years ago. Thus, it is likely that only two-thirds, or about 34 of the 50 clients, entered the emergency food system for the very first time after the imposition of the PRWORA food stamp reductions. This is not dispositive proof that welfare reform alone drove them into the charitable pantries, but it is not unreasonable to argue that the cuts in food stamp benefits were probably a critical stimulus.

The welfare reform increment in the Detroit area

The number of respondents in this analysis is small, and the sampling techniques in the turbulent world of the emergency food sector may not produce perfectly random samples. Thus, the conclusions must be considered in this tentative light. Nevertheless, the data provide the first basis on which to estimate the welfare reform increment in a large urban setting. In all, we have estimated that 45 (11 + 34) clients just recently came into the emergency food system; they constitute 19.7 percent of the total sample of Detroit-area pantry and soup kitchen visitors. *That is to say, the welfare reform increment appears to amount to approximately one-fifth of the client population.*[15] Although there is no census of the total number of monthly visitors to Detroit tricounty charitable food programs, we can estimate the number at around 185,000 in the average month.[16] One-fifth of this population is about 36,445 people.

If the welfare reform increment amounts to approximately one-fifth of the emergency food provider clientele, it should be made clear that the real burden on the charitable food sector is actually a multiple of this figure. The food acquired at the pantry must often feed a household. Each client was asked in the survey to specify the number of children and other adults living in the household. The answer is, on average, an additional two people, children or adults. This suggests that the total additional burden on the emergency food sector in the Detroit area generated by welfare reform area is roughly three times 36,445 or about 100,000 people.

What is finally important about the calculations in this article is that the new burden on the charitable food sector is not the product of some large economic downturn, industrial upheaval, or natural disaster. It is instead the consequence of a policy decision to reduce both access to public food assistance and its value. One ostensible purpose of this reform was to end the debilitating dependency that comes with long-term reliance on public welfare but, for many, dependency on public aid may have been replaced by dependency on private aid.

Furthermore, the more capable provider of food assistance, government, has been replaced by the less capable provider, the charitable food sector. In 1998, over half of 30 cities surveyed by the U.S. Conference of Mayors reported that EFPs were not able to provide enough food to meet demand, 60 percent said that EFPs had had to reduce the quantity of food provided and/or the number of times a person could visit, and 23 percent said that the charitable food programs were unable routinely to provide nutritionally balanced food.[17]

In Detroit, about one-fifth of the directors in the survey reported that food donations decreased in the year prior to the interview, and another 30 percent reported that donations were steady, even in a period of rising demand. At least since the recession of the early 1980s, nonprofit charitable organizations have played an increasingly important role as partners with government in providing food assistance to the needy. But that partnership has been predicated on the assumption that the relationship between the public and the nonprofit sector is one of mutual cooperation and support in pursuit of a common goal.[18] Welfare reform has meant, however, that the government partner is doing less and providing little, if any, compensatory support for its nonprofit partner. In the process the federal government has sloughed off part of its burden on a partner that is currently having difficulty bearing the additional load. ■

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[1]J. Poppendieck, *Sweet Charity?* (New York, NY: Viking, 1998), p. 284.

[2]If the $69 figure had kept up with the annual rate of inflation, which averaged about 2.4 percent per year from 1994 to 1998, the typical food stamp benefit in Michigan would have been worth $75.92 in 1998. These figures are closely aligned with national averages.

[3]For an analysis of the public and private food security network and the role of the federal government, see P. Eisinger, *Toward an End to Hunger in America* (Washington, DC: Brookings Institution, 1998).

[4]Of the approximately 94,000 emergency food providers under the Second Harvest umbrella, the largest charitable food association in the country, over 37 percent were established in the seven years after 1991. An additional 23 percent were begun between 1986 and 1990 (Second Harvest, 1998). But capacity remains an issue. One estimate is that donations to the nation’s food banks would have to increase by more than ten times their current rate of growth by 2002 to meet the additional expected demands. J. Cook and J. Brown, “Analysis of the Capacity of the Second Harvest Network to Cover the Federal Food Stamp Shortfall from 1997 to 2002,” Report, Center on Hunger, Poverty and Nutrition Policy, Tufts University, July 1997.

[5]In addition, most adult applicants had to register for work and to maintain eligibility had to be engaged in a job search or training or take a suitable job offered in order to qualify.

[6]See, e.g., J. Cook, “The Food Stamp Program and Low-Income Legal Immigrants,” *Nutrition Review* 56 (July 1998): 218–21; J. Richardson, *Food Stamp Reform: The Continuing Debate*, Congressional Research Service, Washington, DC, June 20, 1997.

[7]United States Conference of Mayors, *Implementing Welfare Reform in America's Cities*, Washington, DC, 1997.

[8]See W. Wendland, "Food Banks Say the Need Is Growing," *Detroit Free Press* Jan. 15, 1999.

[9]Hunger Action Coalition (HAC) is a United Way agency that provides money, training, and coordination to the approximately 160 food pantries and soup kitchens in Macomb, Oakland, and Wayne counties (Detroit is in Wayne County). Data reported in an interview with HAC officials, Nida Donar and Sandra Henry, July 9, 1998. HAC collects data from only a fraction of the food providers under its umbrella and there appear to be data points missing.

[10]Respondents were told that they were "being asked to participate in a research study to see how families in the Detroit metropolitan area manage to feed themselves." The impact of welfare reform was not mentioned.

[11]Prior to the larger survey, directors of the Capuchins' soup kitchen and two of the Salvation Army programs were interviewed as a pretest of the director instrument. They were not included in the sample because part of the survey sought specifically to explore the nature of the Hunger Action Coalition external help network, of which several of these larger institutions are a part. Nevertheless, their answers are entirely consistent with the patterns found among the 92 food providers.

[12]Forty-one directors said that welfare reform explained the increase and 22 attributed it to other factors.

[13]Food pantry and soup kitchen clients tend to be loyal consumers, rarely using more than one facility concurrently. Beth Daponte and her colleagues found that only 3.4 percent of her Pittsburgh sample of food pantry users used more than one pantry at the same time. B. Daponte, B. Osborne, G. Lewis, S. Sanders, and L. Taylor, "Food Pantry Use Among Low-Income Households in Allegheny County, Pennsylvania," *Journal of Nutrition Education* 30 (January/February 1998): 50–57. The Second Harvest survey found that 86 percent of pantry clients and 66 percent of soup kitchen clients visit only one facility (Second Harvest, *Hunger, 1997: The Faces and Facts* [Chicago: Second Harvest, 1998], Ch. 4, pp. 14–15).

[14]It is, of course, possible that some of these people may have stopped using emergency food at some point prior to the passage of PRWORA, worked or managed independently in some other way for a period, but lost the ability to support themselves entirely and had to return to a pantry or kitchen because they were suddenly ineligible for food stamps.

[15]To the extent that the survey turned up no respondents who claimed to be legal immigrants, this figure may slightly understate the welfare reform increment in the Detroit area.

[16]The 92 emergency food programs in the sample serve about 54,000 different people in the average month and represent 58.5 percent of the 157 programs under the HAC umbrella. The HAC programs provide about half the free food in the metropolitan area, according to HAC officials. This means that the share of free food in the Detroit region that is provided by the 92 programs in the sample is 29.2 percent (.585 x .50). If the proportion of people served roughly equals the proportion of food distributed (there is no evidence that it does not) then the 54,000 people served each month by the 92 programs represent 29.2 percent of the total client population in the Detroit tricounty area, or 185,000 in an average month.

[17]U.S. Conference of Mayors, *A Status Report on Hunger and Homelessness in American Cities*, Washington, DC, 1998.

[18]S. Smith and M. Lipsky, *Nonprofits for Hire* (Cambridge, MA: Harvard University Press, 1993).

Implementation Evaluation Methods: A Conference

On October 14-15, 1999, over 50 members of the academic, policy, and practitioner communities involved in evaluation research met in Washington, DC, to establish a methodological framework for planning and carrying out implementation evaluations, to develop a common terminology and language concerning these methods, and to advance general standards and strategies for answering key questions regarding implementation of welfare reform. The conference was motivated by the enormous changes taking place as welfare policy is delegated to the states and experimental evaluations are no longer required and sometimes not even feasible.

The conference was cosponsored by IRP and the Research Forum on Children, Families, and the New Federalism at the National Center for Children in Poverty (Columbia University). The sponsors gratefully acknowledge the support of the Office of the Assistant Secretary for Planning and Evaluation, U.S. Department of Health and Human Services, the Charles Stewart Mott Foundation, and the Joyce Foundation.

Papers presented and discussed at the conference (these will be published in a conference volume) include:

Overview: Process and Implementation Evaluations: Emerging Roles in a Devolved Social Policy World (Thomas Corbett, IRP and Mary Clare Lennon, Research Forum on Children, Families, and the New Federalism)

1. **Theoretical and Substantive Dimensions in Process and Implementation Studies of Welfare** (Pamela A. Holcomb and Demetra Smith Nightingale, Urban Institute)

2. **The Public Management Perspective** (Joel Rabb, Ohio Department of Human Services, and Don Winstead, Florida Department of Children and Families)

3. **Implementation Analysis: From Intention to Intervention** (Thomas Corbett and Thomas Kaplan, IRP)

4. **Street-Level Research: Policy at the Front Lines** (Evelyn Z. Brodkin, University of Chicago)

5. **Field Network Studies** (Irene Lurie, SUNY at Albany)

6. **What's Behind the Impacts: Doing Implementation Research in the Context of Program Impact Studies** (Kay E. Sherwood and Fred Doolittle, Manpower Demonstration Research Corporation)

7. **Performance Analysis** (Lawrence Mead, New York University)

8. **Approaches to Data Collection** (Leanne Charlesworth and Catherine Born, University of Maryland - Baltimore)

9. **The Use of Administrative Data for Implementation Research** (Robert M. Goerge, Chapin Hall Center for Children)

10. **What Client-Based Ethnographic Research Can Add to Welfare Reform Research** (Kathryn Edin, University of Pennsylvania)

IRP Minority Scholars, 2000

In Spring 2000, four scholars will spend one to two weeks in Madison as part of the IRP Minority Scholars Program, now in its third year. Scholars will present seminars on their current research and consult with IRP faculty mentors and other UW faculty during their stay. The scholars are:

Richard Brooks, Assistant Professor of Policy Analysis and Management, Cornell University. Prof. Brooks's research interests involve the effects of legal rules on economic organization. He is exploring the relationship between socioeconomic status and African-American perceptions of fairness in the American legal system, and is also examining the role of churches in providing housing, developing real estate, and reducing crime in poor neighborhoods. In 1998 Prof. Brooks received a Ph.D. in Economics from the University of California, Berkeley, and a J.D. from the University of Chicago.

Mignon R. Moore, Ford Foundation Postdoctoral Fellow, Program on Poverty and Social Welfare Policy, School of Social Work, University of Michigan, Ann Arbor. Dr. Moore's research interests include urban poverty, especially the diversity in experiences and outcomes among adolescents in high-poverty urban communities. She is also studying stepfamily households among African Americans. Dr. Moore received a Ph.D. in Sociology from the University of Chicago in 1998 and will join the faculty of Columbia University as an Assistant Professor in January 2000.

Mary Pattillo-McCoy, Assistant Professor of Sociology and African-American Studies, Northwestern University. Prof. Pattillo-McCoy's research interests focus on socioeconomic instability and fragility among the black middle class and their myriad connections to the urban poor. She is also examining issues of social isolation and neighborhood/concentration effects. She has completed a book, *Black Picket Fences: Privilege and Peril among the Black Middle Class*, that is being published in 1999 by the University of Chicago Press. Prof. Pattillo-McCoy received a Ph.D. in Sociology from the University of Chicago in 1997.

Sonia Perez, Deputy Vice President, Office of Research, Advocacy, and Legislation, National Council of La Raza, San Juan, Puerto Rico. Ms. Perez's research interests include the social and economic status of the U.S. Hispanic population, in particular the factors that influence educational outcomes for young Hispanics. For the past two years she has worked on a book on employment policy issues for Hispanic workers; she is currently participating in a study of San Juan residents in federally funded housing programs that is part of a large comparative study including five cities on the U.S. mainland. Ms. Perez received an M.A. in Public Administration from the Kennedy School, Harvard University, in 1990.

The effects of early childhood interventions in young adulthood: Continuing the Chicago Longitudinal Study

Since 1986, the Chicago Longitudinal Study has been evaluating the progress of children enrolled in an early childhood intervention program, the Child-Parent Centers (CPCs) that began in poor Chicago neighborhoods in 1967.[1] A new three-year grant from the U.S. Department of Education will now make it possible to follow participants into young adulthood.

The central goal of this new study is to determine if participation in the CPC program is associated with greater educational attainment and employment, better social behavior, and a better quality of life up to age 23—that is, 13 to18 years after the children were enrolled in the program. Using a quasiexperimental cohort design with over 1,200 minority youth, the study will assess the very long term effects of the program using a combination of survey and administrative data. A benefit-cost analysis of the program will also be conducted. Co-principal investigators for the project are Arthur J. Reynolds, Associate Professor of Social Work at the University of Wisconsin and an IRP affiliate, and Judy A. Temple, Associate Professor of Economics at Northern Illinois University and an IRP associate.

Longitudinal studies beginning in early childhood are rare, especially for children from underrepresented populations in central cities. Thus the Chicago Longitudinal Study offers a unique opportunity to add to our knowledge about the benefits and costs associated with a large-scale public program of preventive intervention in early childhood. The outcomes to be investigated in this study are key indicators of economic, educational, and social success in adulthood. Failure to complete high school or at least some postsecondary training, for example, has high costs to society and to youth and is likely to carry even higher costs, given the increasing importance of educational attainment.

For further information, please contact Arthur Reynolds (608-263-1847; e-mail: ajreynol@facstaff.wisc.edu; web site: www.waisman.wisc.edu/cls/)

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[1]See A. Reynolds, and B. Wolfe, "School Achievement, Early Intervention, and Special Education: New Evidence from the Chicago Longitudinal Study," *Focus* 19, no. 1 (Summer/Fall 1997): 18–21.

The employment, earnings, and income of less-skilled workers over the business cycle

Hilary Hoynes

Hilary Hoynes is Assistant Professor of Economics at the University of California, Berkeley, and an IRP affiliate.

One of the most substantial risks facing workers is the possibility of losing a job.[1] The loss of earnings and employment is likely to be more serious for less-skilled workers, who may have greater difficulty than skilled workers in replacing lost income with savings and the earnings of other family workers. Government transfer programs have helped to reduce the variability of family income as employment fluctuates over the business cycle. But recent state and federal policy changes in welfare programs raise questions about the role of this safety net in future recessions. Employment among welfare recipients has certainly increased, and with this greater labor market attachment comes the potential for greater family income, but also greater risk in recessions. Income may become more irregular when families no longer have recourse to the relatively certain source that cash welfare programs once provided.

How severely are fluctuations in the business cycle likely to affect less-skilled workers? And will some groups be more affected than others? In the research summarized in this article, I examine the relative impact of changes in the economic conditions of local labor markets on the employment, earnings, and income of individuals in groups defined by sex, race, and education level. My goal is to examine how changes in labor market outcomes vary within different metropolitan areas and over particular time periods—for example, from the peak to the trough of a recession. The combination of detailed outcome measures and comparisons across demographic groups allows me to present a more complete picture of how families are affected by cycles than has hitherto appeared in the literature.

The relative responses of demographic groups to the business cycle and the different individual and family outcomes shed light on particular problems that may exist for less-skilled workers, for women versus men, and for whites versus nonwhites. Further, the examination of different outcome measures can be used to more precisely demarcate the effects of particular government transfer programs designed to insure against fluctuations in income. Policies such as unemployment insurance and job training, for example, are geared toward individuals; their effects will show up in *individual* earnings or income. Other policies such as Temporary Assistance for Needy Families (TANF) and the Earned Income Tax Credit are geared toward families; their effects will show up in *family* earnings or income.

Data

The data I use are from the Current Population Survey (CPS): the Outgoing Rotation Group (ORG) data for 1979–92, and the March Annual Demographic Files (ADF) for 1975–97. The ORG sample is about three times as large as the ADF—a particular advantage in presenting results by metropolitan areas—but the ADF provides broader information on family employment, earnings, and income over the past year.[2] Combining the two sources gives us a comprehensive picture of the effects of business cycles on workers and families over three decades.

In the analysis, race is defined as white or nonwhite, and nonwhite includes African Americans and Hispanics. Skill groups are defined by education: less than 12 years, 12 years, 13–15 years, and 16 or more years. But over the three decades encompassed by this study, education levels have been steadily rising, and the percentage of the population with less than a high school education has shrunk and has become relatively more disadvantaged.[3] In some of the analyses I use two groups only, comparing those with a high school education or less to those with more than a high school education, to minimize the problem of making comparisons over time for a group whose composition is changing.

For local labor market areas, I use the standard Metropolitan Statistical Areas (MSAs) in the two data sets, combined to form Consolidated MSAs (for example, New York, Los Angeles, and Chicago) that provide a closer approximation to metropolitan labor markets. In 1975, the sample accounts for virtually all of the metropolitan population, but in 1990 it accounts for only about 60 percent of it.[4]

Trends in labor market outcomes among skill groups

Trends in employment are captured by two measures: the ratio of those employed at all in the past year to the total population in that particular education (skill) group, and

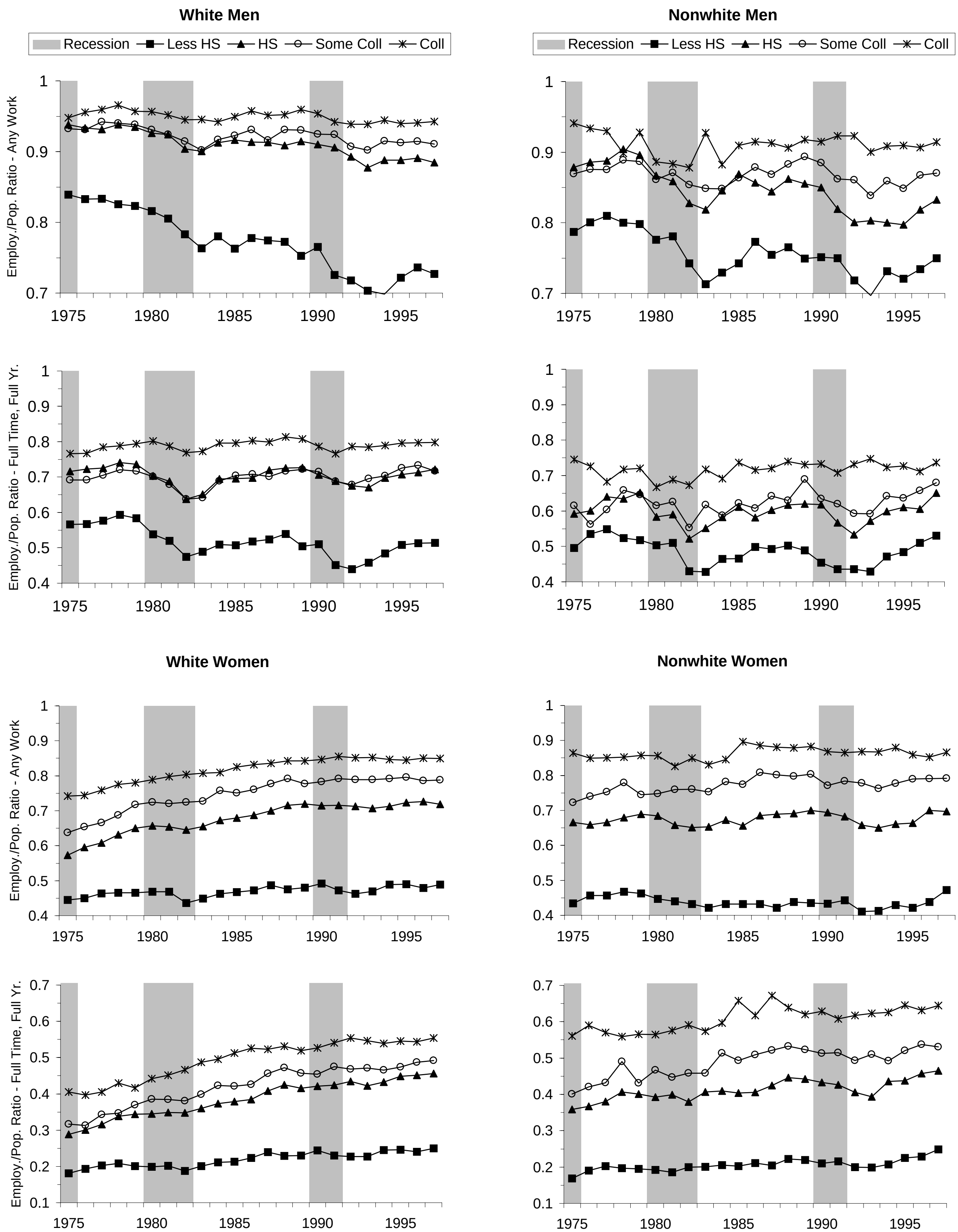

Figure 1. Employment-population ratios for men and women, by race and education, 1975–97.

Source: U.S. Bureau of the Census, Current Population Survey, March Annual Demographic Files. Gray bars indicate recession years.

the ratio of those employed full time, full year to the same population. Figure 1 shows these findings for men and women. As expected, employment is higher among those with higher education levels. Among men with less than a high school education, the proportion working declines significantly; by the mid 1990s, fully 30 percent are not working at all over the year—in part, no doubt, because the composition of this group is changing.

Equally striking are the cyclical trends in these ratios. Employment rates, especially full-time rates, for lower-skilled and nonwhite men vary significantly over this 30-year period, with especially high rates of unemployment in the worst recession years 1982 and 1992. The pattern for annual hours worked is in general similar, although the relative variability of the different skill groups is less dramatic.

For women, the steady secular increase in employment (see Figure 1) is the dominant pattern, making it difficult to draw any inferences about variation over the business cycle. Particularly notable are the results for highly skilled white women, whose employment shows less cyclical fluctuation than all other groups, including highly skilled white men. This may be due to differences in the industries and occupations in which men and women work, but it may also be that women act as "added workers," who enter the labor force during recessions to make up for the lost earnings of a principal earner—a point I take up later.

Employment and earnings both grow more slowly for lower-skilled women than for those with higher skill levels. Most severely affected are low-skilled nonwhite women, whose employment rates fluctuate five times as much as those of highly skilled white men.

Family income, and to a lesser extent family earnings, show less variability across demographic groups than do individual earnings (earnings are not shown in Figure 1).

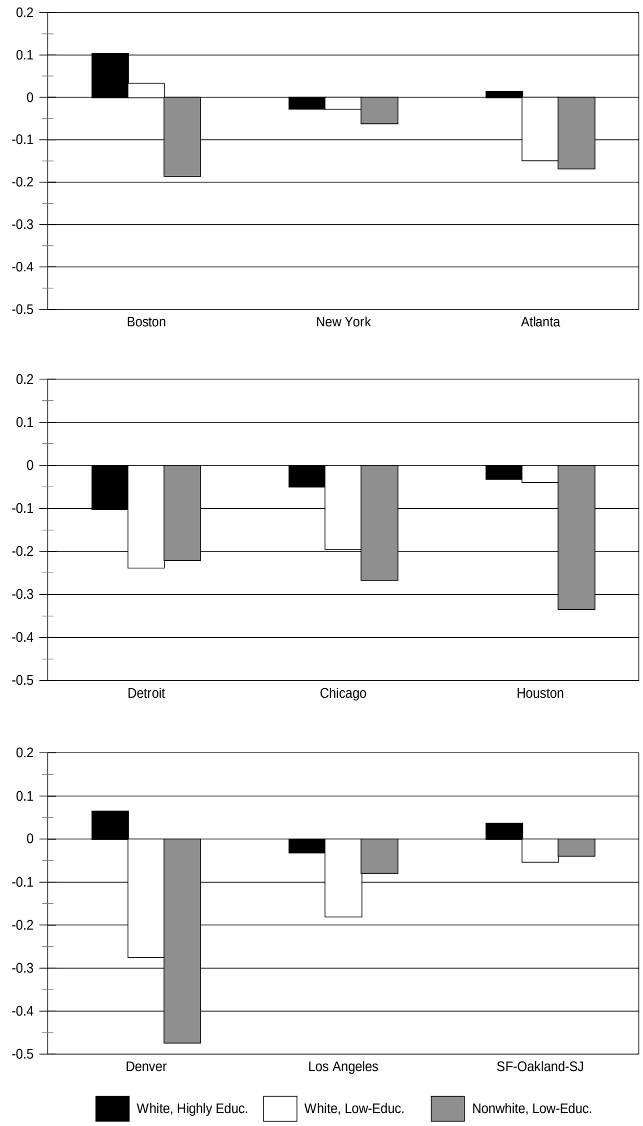

Figure 2. Change in the full-time, year-round employment-to-population ratio for men in selected metropolitan areas, 1979–83 (log values; reference group = highly educated white males).

Source: U.S. Bureau of the Census, Current Population Survey, Outgoing Rotation Group data.

Effects of the recession of 1981–82 on the employment rates of male workers

The business cycle of 1979–82 includes the most severe recession in the period covered by the CPS data. The variables in the analysis include employment rates, hours worked, earnings, average hourly wage, and family measures such as the earnings of the family head and the spouse, transfer income, and other family income. For this analysis I use, as noted, only two education groups, an approach that is likely to mute rather than emphasize the effects of business cycles on different groups.

The shock of this business cycle, from its peak in 1979 to its trough in 1982, more severely affected lower-skilled males than higher-skilled males in different MSAs (see Figure 2). Nonwhite, low-skilled males were the most severely affected, whether we are considering any employment or full-time employment.[5] The recession had particularly marked effects on full-time, year-round work.

The data also suggest how differently metropolitan areas respond to business cycles, in part because industries are not uniformly distributed. The 1981–82 recession, for example, hit the industrial Midwest hardest of all. Detroit, Pittsburgh, and Cleveland saw employment reductions on the order of 10–15 percent, but in San Francisco, New York, and Boston employment was reduced only 1–3 percent. In the 1992 recession, in contrast, these east and west coast cities were harder hit than the industrial Midwest.

Table 1
The Relative Effects of Business Cycles on Labor Market Outcomes, Using Individual Measures

Skill Group	Full-Time, Full-Year Employment/Population Ratio	Annual Hours	Annual Earnings	Hourly Wage
Higher-Skilled (education > 12 years)				
White men	1	1	1	1
Nonwhite men	2.26**	2.28*	1.55*	0.95
White women	0.02**	0.09**	0.34**	0.36**
Nonwhite women	0.96	1.14	0.78	0.27**
Lower-Skilled (education < 12 years)				
White men	1.38	1.32	1.04	0.72
Nonwhite men	2.82**	3.28**	1.90**	0.74
White women	0.58**	1.22	0.88	0.66
Nonwhite women	2.04**	3.88**	2.36**	1.42

Source: Current Population Survey, Annual Demographic File (ADF), 1975–96.

Note: In each column, the estimates for other groups are presented as the responsiveness of the group to MSA shocks, relative to the responsiveness of white, higher-skilled males, whose estimates are normalized to 1. Each column presents estimates of an equation in which the dependent variable is the change in the log or level of the particular labor market outcome evaluated at the mean for the cell defined by MSA, year, and skill group. For details of sample selection and variable construction, see the conference paper cited in note 1 of this article. N = 2,160.

*significant at the 1% level; **significant at the 5% level.

Estimated effects of business cycles on lower-skilled workers, 1975–97

Annual ADF data enable me to examine measures for the family—the key economic unit—in addition to individual measures, and also to examine changes in the intensity of employment.[6] Using higher-skilled white men as a point of reference, I estimate the relative effects of a downturn or expansion in a given MSA on employment, on annual hours and earnings, and on wages of different groups of workers (see Table 1). For all groups, the estimated changes in annual earnings were greater than changes in annual hours or employment rates—not surprising, since earnings capture changes in both employment and the number of hours worked.

Once again, the responsiveness to a change in the local economy is shown to be higher among those who have lower education levels, and who are nonwhite. The effect of a downturn on the annual hours worked by lower-skilled minority men and women is over three times as great as the effect on higher-skilled white men. More highly educated white women are less affected even than highly educated white men. But the cyclical fluctuations in the wages of more highly skilled white men appear to be larger than those found for nonwhites, women, and less-skilled workers (from Table 1, column 4). There are a couple of possible reasons for this difference. First, it may reflect greater rigidities in wages for low-skilled workers. For example, if equilibrium wages rates are driven down in recessions, to the extent that the minimum wage creates a wage floor for low-skilled workers, the reduction in earnings for low-wage workers will be smaller, relative to highly skilled workers, than their reduction in employment. Alternatively, it may reflect changes in the composition of workers over the business cycle and the differential effects of these changes on skill groups.[7]

The same analyses using measures of family rather than individual outcomes produce very similar results to those in Table 1—those who have lower education or who are nonwhite are more affected by cycles than the highly skilled white groups (Table 2). Among the most disadvantaged groups, there is little evidence of labor substitution among family members in downturns; family earnings fluctuate more than the earnings of the head of the household. (For the more highly skilled, family earnings fluctuate *less*.) Comparing total family earnings with total family income (columns 5 and 6), we see how transfers (e.g., welfare, unemployment assistance) have mitigated the effects of business cycles among the most disadvantaged. The family *earnings* of less-educated nonwhite women fluctuate three times as much as those of more highly educated white males, but their family *income* fluctuates only 2.5 times as much—a 15-percent reduction in variability with the business cycle.

The most striking results are those for the earnings of spouses, which are more variable for poorly educated workers. This is partly because fewer people in the low-skilled groups are married, but may also reflect differences in the propensity for women in the different skill groups to be "added workers" in the family. Simply put, an added worker is someone who seeks work when the earnings or employment of other family members are reduced; this worker may also exit the labor market when the primary worker regains employment or earnings. This is a form of family insurance against economic shocks. My results suggest that families with more highly

Table 2
The Relative Effects of Business Cycles on Labor Market Outcomes, Using Family Measures

Skill Group	Own Earnings[a]	Head's Earnings[a]	Spouse's Earnings[a]	Other Family Income[b]	Total Family Earnings	Total Family Income
Higher-Skilled (education > 12 years)						
White men	1	1	1	1	1	1
Nonwhite men	1.35	1.34	3.28*	0.59	1.63*	1.44
White women	0.34**	0.91	0.43	1.23	0.88	0.93
Nonwhite women	0.84	1.03	3.42**	1.44	1.64*	1.54
Lower-Skilled (education < 12 years)						
White men	0.94	0.98	1.70	0.57	1.14	1.01
Nonwhite men	1.50**	1.44*	4.64**	1.36	2.15**	1.83**
White women	0.83	0.93	2.26	0.87	1.21	1.12
Nonwhite women	2.18**	2.00**	7.24**	1.50	3.07**	2.46**

Source: Current Population Survey, Annual Demographic File (ADF), 1975–96.

Note: In each column, the estimates for other groups are presented as the responsiveness of the group to MSA shocks, relative to the responsiveness of white, higher-skilled males, whose estimates are normalized to 1. Each column presents estimates of an equation in which the dependent variable is the change in the log or level of the particular labor market outcome evaluated at the mean for the cell defined by MSA, year, and skill group. For details of sample selection and variable construction, see the conference paper cited in note 1 of this article.

N = 2,160; *significant at the 1% level; **significant at the 5% level.

[a]This sample includes heads, spouses, etc. "Own earnings" are the earnings of the individual that appears in this sample. "Head's earnings" are the earnings of the head of the individual's family, who may be the same person, but may not. "Spouse's earnings"are the earnings of the spouse if there is one in the family; it is 0 otherwise.

[b]Transfers, capital income, and earnings of other family members (other than the head and spouse.)

skilled workers are more likely to engage in this practice than families with lower-skilled workers.

Why are the responses to the business cycles different?

There are several possible reasons that particular groups might respond differently to business cycles.[8] Some groups may simply be less tied to the labor market, and may rely on transfer income or the earnings of other family members. Some demographic groups may be less willing than others to move in response to regional and sectoral shifts in employment and wages. The more mobile the group, the lower the expected effect upon it of a downturn in a regional labor market. Demographic groups also tend to be employed in different sectors and occupations that may have greater or lesser risks of layoff. Those working in construction and manufacturing, younger workers, and those in nonunion employment experience greater employment fluctuations, whereas managerial jobs, civil service jobs, or jobs in the finance, insurance, and real estate (FIRE) sector, among others, are more stable.

I examined the characteristics of workers in the CPS sample and found that, indeed, highly educated white women, who show the lowest responsiveness to business cycles, are least likely to be in construction and manufacturing and most likely to be in retail trade, FIRE, and public-sector jobs. Nonwhite, lower-skilled men, in contrast, are the most represented in construction, manufacturing, and laboring jobs, and have the lowest union participation rates. The results are mixed for nonwhite lower-skilled women, the group most responsive to business cycles. On the one hand, they have the lowest rates of attachment to the labor market and the highest welfare reliance, which would seem to make them less responsive to business fluctuations. On the other hand, those that do work are more likely to be in manufacturing and laborer positions.

In addition to these group differences, there are also substantial differences between the two major business cycles covered by these data. The 1982 and the 1992 recessions differed a great deal in the industries and occupations that were most heavily affected, as well as in the geographic distribution of unemployment. In the early 1990s, displacement rates among more highly educated workers increased relative to those with lower education levels.[9] The ADF data show that the relative sensitivity to recession of lower-skilled workers, especially male workers, declined after 1988 (see Table 3). The effects of the 1992 recession on the low-skilled group were much closer to the effects on the highly skilled group, for both white and nonwhite workers.

The reasons for the changed responsiveness of low-skilled groups to the business cycle are unclear. It may be that the less-skilled groups had somewhat low employ-

Table 3
The Changes in the Relative Effects of Business Cycles on Labor Market Outcomes Across Skill Groups, Before and After 1988

Skill Group	Own Earnings	Total Family Earnings	Total Family Income
Higher-Skilled (education > 12 years)			
White men	0	0	0
Nonwhite men	-0.96	-1.12**	-1.05**
White women	-0.69**	-0.06	-0.08
Nonwhite women	-1.28**	-0.80	-0.88*
Lower-Skilled (education < 12 years)			
White men	-0.30	-0.24	-0.19
Nonwhite men	-0.81	-1.22**	-1.08**
White women	-0.49	-0.21	-0.09
Nonwhite women	-0.58	-0.44	-0.42

Source: Current Population Survey, Annual Demographic File (ADF), 1975–96.

Note: In each column, the estimates for other groups are presented as the *change* in the responsiveness of the group to MSA shocks, relative to the responsiveness of white, higher-skilled males, whose changes are normalized to 0. Each column presents estimates of an equation in which the dependent variable is the change in the log or level of the particular labor market outcome, evaluated at the mean for the cell defined by MSA, year, and skill group. For details of sample selection and variable construction, see the conference paper cited in note 1 of this article.

N = 2,160; *significant at the 1% level; **significant at the 5% level.

ment rates going into the 1992 recession. Or differences in the industries affected by the two recessions may be reflected in these findings. The causes deserve examination, particularly in view of the emphasis on labor market engagement in the new state and federal welfare-to-work policies.

Conclusion

The results presented here show conclusively that the labor market outcomes of less-skilled workers, especially nonwhites, vary more widely over business cycles than do those of more highly skilled workers. The less-skilled are more affected by changes in local economic conditions. Low-skilled women, again especially nonwhite women, are significantly more sensitive to business downturns than highly skilled women; they are more likely to have reductions in employment and earnings during a recession, though also more likely to have gains during a recovery.

Examining individuals in isolation, however, gives an incomplete picture of the effect of cycles on well-being. The results also show that government transfers and the earnings of other family members decrease the differences between skill groups and mitigate the effects of business cycles on family income. Welfare reform is generating an inflow of less-skilled workers into the labor market. The effects of a business downturn or recession on families could be very adverse if these relatively new entrants have exhausted their TANF time limits yet have incomplete coverage in the unemployment insurance program. ■

[1]This article summarizes “The Employment, Earnings, and Income of Less-Skilled Workers over the Business Cycle,” a revised (April 1999) version of a paper presented at the conference on Labor Markets and Less Skilled Workers of the Joint Center for Poverty Research, Washington, DC, November 1998. The material is used here by permission of the Joint Center. The revised version appears as IRP DP 1199-99.

[2]For the ORG, I used indicators for employment last week, full-time employment last week, and earnings last week, where full-time employment includes those working at least 35 hours a week. For the ADF (the March CPS), I considered many different individual and family annual outcome measures. Persons 22–62 years old are included. Full-time, full-year employment is defined as working 35 hours a week for 50 or more weeks in the past year. Excluding the self-employed, those working without pay, and those with income but zero hours of work, the final sample included about 220,000 observations per year in the ORG and 70,000 observations in the ADF.

[3]For example, among white men, the percentage with less than a high school education has declined from 25 to less than 10 percent, and among nonwhite men, it has dropped from 50 to 30 percent.

[4]The incomplete coverage in the later part of the period comes from the need to create metropolitan areas that are consistent geographic units over the entire time period. So metropolitan areas that were added in the middle of the period, for example, are not included in the sample. Considerable effort was made to insure that the MSAs were comparable units over time. With each decennial census, the Bureau of Labor Statistics redefines MSAs. This usually amounts to adding a new MSA or splitting up an existing MSA in growing areas, but could in principle lead to eliminating MSAs in declining areas. In this analysis, split-off MSAs were combined, making the series comparable over time. However, some MSAs can also be redefined by adding additional areas to an existing MSA. I cannot address these changes. Fortunately, changes in MSA definitions occur only once per decade, following the decennial census. The results are not sensitive to dropping the “seam years.”

[5]This approach is best applied to groups that are not experiencing significant trends over time. As noted earlier, the time trend of increasing employment for women is sufficiently large to mask cyclical effects. Hence these results are presented for men only.

[6]Estimates using weekly ORG data appear in the conference article cited in note 1.

[7]This point has been discussed in the empirical literature on cyclical behavior of real wages; for example, see G. Solon, R. Barsky, and J. Parker, “Measuring the Cyclicity of Real Wages: How Important Is Composition Bias?” *Quarterly Journal of Economics* 109, no. 1 (1994): 1–26.

[8]Previous research studies on these issues are briefly reviewed in the conference article cited in note 1.

[9]On this, see H. Farber, “The Changing Face of Job Loss in the United States, 1981–1995,” unpublished paper, Princeton University, 1997.

When financial incentives encourage work: The Canadian Self-Sufficiency Project

Charles Michalopoulos, Philip K. Robins, David E. Card, and Gordon Berlin

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Modern industrialized nations have taken very different routes in creating social safety nets for their citizens. But in virtually all these countries, the contradictory pressures generated by economic restructuring, high unemployment, and large government deficits in the 1980s and early 1990s have reopened debate over the structure of social protection and the extent of the state's role. Paradigmatic welfare states such as Denmark are reconsidering the financial and behavioral consequences of their policies.[1] At the other pole, the United States and the United Kingdom have embarked upon radical reform, curtailing welfare entitlements and devolving policy and program responsibilities to lower levels of government.

The Canadian system of social support has not been exempt from these pressures and has made many efforts to accommodate them. This article examines one of the most innovative and ambitious experimental programs, the Self-Sufficiency Project (SSP). Launched in 1992, SSP set itself the challenging task of trying to deal simultaneously with the problems of poverty and dependence. It has lasted almost 10 years and has involved over 9,000 single parents in two provinces. The project is being evaluated using a complex, random-assignment evaluation design by the Social Research and Demonstration Corporation (SRDC), a nonprofit research organization, in conjunction with its U.S. partner, the Manpower Demonstration Research Corporation. SRDC's reports on the first years of the project document increases in full-time employment and earnings and reductions in poverty that are among the largest ever seen in a social experiment designed to encourage welfare recipients to work.

The structure of social welfare in Canada

The Canadian social welfare system, which was created mostly after World War II, has always been more decentralized than the U.S. system.[2] The federal government took the lead in structuring and extending the system, but it administers very few programs directly. Each of Canada's ten provinces and two territories designs, administers, and delivers its own social assistance programs to those whose incomes are judged insufficient by standards set by the provincial government. Because the provinces have been responsible for most of the social spending, they have historically had considerable scope for innovation.[3] The federal government contributes toward the cost of "approved" expenditures incurred by the provinces and municipalities.

The consequence is a system that is less comprehensive than those of many European countries but more extensive than that of the United States. Thirty years ago, Canada spent about 15 percent of GDP on social programs. In the 1980s, however, as Canadian governments sought to restrain the consequences of rising income inequality through the social welfare system, social expenditures rose sharply, averaging roughly 22–24 percent of GDP over the decade.

The results of this Canadian policy were mixed. As in the United States, social assistance was quite successful in reducing poverty rates for the aged, but much less so for other groups. Child poverty rates stayed stubbornly high, most especially in single-parent families, and they continued to grow even as the recession of the early 1990s ended. In 1996, 21.1 percent of children under the age of 18 lived in families whose total income before taxes fell below the federal government's Low-Income Cut-off (Canada's equivalent of the poverty line).[4] Income Assistance (IA), the basic cash benefit program operated by the provinces and available to all low-income people, whether employable or not, was so structured that a single mother with two children would be worse off working at the minimum wage than staying on welfare. Unemployment persisted, and the Unemployment Insurance system was heavily criticized as an income maintenance system with negative incentive effects, no significant capacity to foster retraining or job search, and little or no integration with social assistance.

In the last few years, major reforms have altered the landscape of social policy in Canada. In 1996, two of the most important federal social welfare programs were abolished: the Canada Assistance Plan, which paid the federal share of provincial expenses for IA and social services, and the Established Programs Financing, a block grant for health and postsecondary education. They were replaced by a single block fund, the Canada

Main features of the SSP

Full-time work requirement. Supplement payments were made only to eligible single parents who left Income Assistance (IA) and worked full time—at least 30 hours a week over a four-week span. The full-time requirement was intended to ensure that (1) supplement recipients were preparing for real self-sufficiency; (2) most supplement recipients would need to increase their work effort to qualify; (3) earnings combined with the supplement payment would represent a large increase in income for most people.

Generous financial incentive. The supplement was calculated as half the difference between a participant's earnings from employment and an "earnings benchmark" for each province, set at a level to make full-time work pay better than IA. During the first year, the benchmark was $37,000 in British Columbia and $30,000 in New Brunswick (all dollar values are Canadian dollars [$1= 84 cents U.S. in 1992]). Thus a participant in British Columbia who worked 35 hours a week at $7 an hour would earn $12,740 a year and collect an earnings supplement of $12,130, for a total gross income of $24,870. Unearned income such as child support or the earnings of other family members did not count against the supplement. The supplement was reduced by only 50¢ for every dollar of increased earnings, and was fully phased out only at the earnings benchmark levels.

Restricted eligibility. Single parents make up a substantial proportion of the IA caseload and face considerable barriers to employment (particularly if they have young children). Long-term recipients (those with at least a year of welfare receipt) account for a disproportionate share of welfare costs and are thus a critical group to target.

Time limits. IA recipients selected to participate in the program group had one year from the date of selection to take up the offer; thereafter they became ineligible for the supplement. The supplement was offered to recipients for a maximum of three years, to eliminate the possibility of long-term dependence.

A voluntary alternative to welfare. No program group member was required to accept the earnings supplement. People could not receive IA at the same time as the earnings supplement, but at any point they could opt out of the experiment and return to welfare. As long as they were still within their three-year eligibility period, they could also reactivate the supplement by going back to work full time. The program allowed two episodes of less-than-full-time work in each of the three years but penalized further episodes by withholding the supplement payment for the month in question.

Health and Social Transfer, which provides a federal contribution estimated to be about 15 percent lower than in the past. Unemployment Insurance has also been restructured, in particular to emphasize rapid return to work, and has been renamed Employment Insurance. Faced with cutbacks in federal support, provinces have made a variety of changes to welfare programs, reducing benefit levels, tightening eligibility, and imposing work requirements.

The Self-Sufficiency Project

Facing mounting expenditures, persistent pockets of poverty, and increasing concern that the income support system discouraged people from working, Human Resources Development Canada (HRDC; formerly Employment and Immigration Canada) in 1990 began discussions that resulted in the SSP. The premises of SSP were, basically, that a temporary earnings supplement would provide sufficient inducement for a small but significant proportion of IA recipients to enter employment. Over time, work experience and on-the-job training would lead to wage increases that would enable them to become self-sufficient on their earned income. The SSP offered a substantial wage supplement to eligible single parents who left IA and worked full time. Acceptance of the supplement was voluntary, and it could only be taken for a maximum of three years. (The key features of the SSP offer are described in the box above.)

It was clearly necessary to test such a program before implementing it on a large scale. A wage supplement would be very costly, and in a time of tight budgets it could be justified only if it had significant effects. Moreover, many people leave welfare for work on their own. Would a financial-incentive program encourage people to stay longer on social assistance? Would it increase or decrease overall work effort? The proposed program was so different from previously evaluated programs that very little about its effects could be reliably predicted.

For these reasons, HRDC chose to test the efficacy of the program under real-world operating conditions in two provinces, British Columbia and New Brunswick. In both provinces, unemployment was at historically high levels, though labor market conditions improved slightly over this period. Table 1 outlines some relevant demographic features of the provinces.

The structure of the SSP evaluation

The evaluation by SRDC had three parts:

1. *The recipient study*: Between 1992 and 1995, about 6,000 single-parent IA recipients who had already been

Table 1
Selected Characteristics of the Populations of British Columbia and New Brunswick

Characteristic	British Columbia		New Brunswick		
	Vancouver	Province	Saint John	Province	Canada
No. of residents 15 years of age and older, 1992 (000)	1,362	2,698	103	584	21,986
Employed (%)	63.2	60.0	57.7	51.8	58.4
Unemployment rate, 1992 (%)	9.3	10.5	11.5	12.8	11.3
Avg. wage for all hourly employees, 1992	—	$15.05	—	$11.88	$13.75
Minimum wage, 1992	—	$5.50	—	$5.00	n/a
Families below Low-Income Cut-off, 1992 (%)	—	13.4	—	11.7	13.3
Rural residence, 1991 (%)	3.8	19.6	9.0	52.3	23.4
Immigrant population, 1991 (%)	30.1	22.3	4.3	3.3	16.1
All IA cases, March 1993	80,889	193,825	7,729	42,123	1,616,200
Single-parent cases as % of all IA cases	22.8	24.8	34.6	30.8	26.4
Basic monthly IA grant to single parent with 2 children, 1992	$1,131	$1,131	$747	$747	n/a

Source: W. Lin, P. Robins, D. Card, K. Harknett, and S. Lui-Gurr, *When Financial Incentives Encourage Work: Complete 18-Month Findings from the Self-Sufficiency Project*, SRDC, September 1998, Table 1.1.

Note: Dollar amounts are in Canadian dollars ($1 = 84¢ U.S. in 1992). For the Low-Income Cut-off, see article, note 4. Dashes indicate the information is not available, n/a = not applicable.

on welfare for at least a year were randomly assigned to a program group that was offered the earnings supplement, and a control group that received no such offer. SSP provided information and referrals to existing employment and training services, but did not itself provide such services.[5]

2. *The SSP Plus study*: The aim of this part of the experiment was to learn whether adding job-search assistance and job counseling services to the supplement would improve the ability of long-term recipients to find and keep full-time employment. Between November 1994 and March 1995, about 900 long-term recipients in New Brunswick were randomly assigned to three research groups, the original program and control groups plus a third group that received both the supplement offer and the offer of job-search and counseling services. (Results of this part of the evaluation are briefly noted in the box on p. 41.)

3. *The applicant study*: This part of the study looked at two issues in particular: (a) possible negative effects, and (b) long-term consequences.

(a) From the outset, the SSP evaluation was designed to learn whether the program would have unintended effects. Would knowledge of the earnings supplement induce some single parents to change their behavior—either to apply for welfare in the first place or to remain on welfare longer than they had intended in order to fulfill the one-year eligibility requirement?

(b) When a program such as SSP is fully deployed, all new applicants for welfare will have access to information about their potential future eligibility, and the population will come to include individuals with shorter welfare histories, more likely to become self-supporting. The applicant study sample more closely resembled such a population than did the recipient study sample. A second main purpose of the applicant study was, therefore, to estimate what the very long term costs and benefits of a mature earnings supplement program might be.[6]

Between February 1994 and February 1995, over 3,000 single parents in British Columbia who began a new spell on IA were randomly assigned to either a program or a control group; these constituted the sample for the applicant study.

The recipient study

Participation

In general, sample members could be considered a highly disadvantaged group. Most were female, with relatively low levels of education; over 50 percent had not completed high school. Two-fifths were raised by a single parent, and a quarter had grown up in families receiving some form of welfare; 40 percent had themselves been receiving welfare continuously for over three years. About 50 percent of the sample had a child under the age of 5 living in the household. Although almost all had worked at some point, less than 20 percent were working even part time when they were assigned to the program.[7]

For program group members in the recipient study, the decision to leave welfare and accept the earnings supplement posed risks and unknowns as well as the potential reward of greater income. What if one did not find work? One woman (who did not take up the offer) commented, "If you've been looking for the past ten years to find something anyway, and now you've got nine months to suddenly—you know? After ten years you're going to find something in nine months? It just didn't mean that much to me."

Table 2
The Effects of SSP for Long-Term Recipients of Income Assistance (IA), in the 5th Quarter after Random Assignment

Outcome	Program Group	Control Group	Difference (effect)
Full-time employment rate	29.3%	14.0%	15.2**
Part-time employment rate	11.7	13.9	-2.2*
Overall employment rate	41.0	28.0	13.0**
Receiving IA	70.2	83.2	-13.0**

Source: W. Lin, P. Robins, D. Card, K. Harknett, S. Lui-Gurr, *When Financial Incentives Encourage Work: Complete 18-Month Findings from the Self-Sufficiency Project*, SRDC, September 1998, Table ES1.

Note: "Full-time employment" is defined as working 30 hours or more in at least one week during the month; "part-time employment" is defined as having some employment but no full-time employment during the month. Estimates for quarter 5 calculated by averaging the estimates for months 13–15. Percentages have been rounded.
* = significant at the 5% level; ** = significant at the 1% level.

Table 3
SSP's Effects on Monthly Earnings, Net Transfer Payments, and Income, Quarters 5 and 6 ($ Canadian per month)

Outcome	Program Group	Control Group	Difference (effect)
1. Earnings	$347	$222	$124**
2. SSP supplement payments	196	0	196**
3. IA payments	621	723	-103**
4. Projected income taxes	53	14	39**
5. Net transfer payments (rows 2 + 3 - 4)	764	709	55**
6. After-tax income from earnings, SSP, and IA (rows 1 + 2 + 3 - 4)	1,111	932	179**

Source: W. Lin, P. Robins, D. Card, K. Harknett, and S. Lui-Gurr, *When Financial Incentives Encourage Work: Complete 18-Month Findings from the Self-Sufficiency Project*, SRDC, September 1998, Table ES3.

Note: Income taxes were projected from federal and provincial tax schedules and data on income and SSP payments (which are taxable income also). Dollar amounts have been rounded. ** = significant at the 1% level.

Many fears and uncertainties surfaced in focus group discussions, revolving about women's feelings of their own inadequacies in the job market: "I don't have education or skills where I'm able to get a nice job. You know, I'm just like, [a] minimum-wage type, and I feel guilty, but I don't want to do that." Some worried that after three years of receiving subsidies, "a pipe dream . . . liv[ing] high on the hog," they would almost certainly run into a brick wall: "if you have grade 7 education, there's no way you're bettering yourself in your job. So three years down the road . . . you're going to go back to welfare, and say, 'I can't make it'."[8]

In all, nearly two-thirds of the program group, 65 percent, did not take up the offer. When these women were asked the main reason why, far and away the most common answer was "unable to find a job" (32.2 percent). Including those who didn't think they could get a job (3 percent) or were unable to find a job that would give them enough hours to qualify (8 percent), 43 percent cited difficulties in finding work as the main reason. "Personal/family responsibilities" (15.4 percent) and "health problems/disability" (13.5 percent) ranked next in importance. Despite the large numbers with very young children, only 4 percent said that they couldn't find adequate child care and 2 percent that they didn't want to use it.

Although 35 percent of the program group qualified for the supplement during their one-year eligibility period, at any one time only about 25 percent were actually receiving payments. About 70 percent of the supplement takers forfeited payments because they lost a job or did not work enough hours, and less than 5 percent because they earned too much money.

Employment and welfare receipt among program group members

SSP significantly increased full-time employment and reduced IA receipt among recipients in the program group. The effects were highest in the fifth quarter after random assignment (see Table 2), and then declined slightly, both because some did not remain employed full time and because full-time employment continued to rise, though more slowly, among the control group.

Supplement receipt was quite widely distributed across the rather diverse groups that participated in the program, but the effects for some subgroups were larger than for others. Those who were already employed or looking for work at the time of random assignment, those with a high school diploma, those with shorter histories of IA receipt, and those who did not report health problems or disabilities were employed at much higher rates. This is a pattern familiar from U.S. studies.[9]

Most of the program group members who went to work had relatively low earnings, concentrated at wages between the minimum wage and $1 or $2 above the minimum. Clearly, the earnings supplement made work financially attractive to the program group, but whether the employment effects persist after the supplement ends will depend on whether wages or hours go up enough for program group members so that work is financially attractive even without the supplement, or whether changes in attitudes strengthen their work inclinations.

Effects on earnings, net transfer payments, and income

Among this group of long-term welfare recipients, SSP reduced government spending on IA payments, but the savings were more than offset by the cost of the supplement payments. Interim measures show that after 18 months, net transfer payments to individuals in the program group were $55 higher per month than payments to those in the control group (Table 3). Nevertheless, some 15 months into the program, every dollar of those addi-

Adding job services to the SSP: How much do they help?

Although the SSP financial incentive was a generous one, two-thirds of the eligible single parents who were long-term IA recipients did not take up the offer. Some preferred to stay home with their children or attend school. But others were unable to find full-time work or did not even look. This raises an important question: if these people had also been offered job-search and related services, would more of them have found full-time jobs and taken advantage of the earnings supplement? Some who did find full-time jobs lost them, raising a second question: if employment assistance increased job taking, would these new employees be able to hold onto their jobs?

To look for answers, SSP Plus added a variety of job-related services to the original offer: an employment plan, a résumé service, job clubs and other workshops, job coaching, and job leads. But in the first 18 months after program group members were first offered the supplement, the incremental effect of the SSP Plus services, though positive, was modest, primarily because the services provided by SSP Plus seem to have created only temporary full-time employment.

Program members did make use of most of the services. Almost all completed an employment plan, more than two-thirds used the résumé service and received job coaching, and job leads were provided to over three-fifths of the group. Over 50 percent of the SSP Plus program group took advantage of the supplement offer, compared with 35 percent of the regular program group—a significant difference. But 15 months after taking up the offer, SSP Plus program group members had a full-time employment rate of 33 percent, versus 30.6 percent for the regular group. At the same time, 60.7 percent of the SSP Plus program group was receiving Income Assistance, versus 64.6 percent of the regular group. Neither difference was statistically significant.

Adding services to the financial incentive appears to have succeeded in "digging deeper" into the welfare caseload by getting a greater number of people to overcome employment barriers, such as fear of the labor market. Most of the additional people who found jobs as a consequence of the services had difficulty holding these jobs, however, and the postemployment services provided by SSP Plus staff were apparently not enough to help them overcome this problem.

G. Quets, P. Robins, E. Pan, C. Michalopoulos, and D. Card, *Does SSP Plus Increase Employment? The Effect of Adding Services to the Self-Sufficiency Project's Financial Incentives*, SRDC, May 1999.

tional net transfer payments was generating more than $2 of increased earnings and $3 of increased income for program group members. SSP thus stands in sharp contrast to most income support programs, in which a dollar spent on transfer payments typically results in less than a dollar of extra income for poor families, many of whom cut back on work, reducing earnings.

From the narrow perspective of government expenditures, the long-term benefits and costs of SSP are currently unknown. If supplement takers continue working, so that reductions in IA payments or increases in tax revenue persist after the supplement expires, then the program will produce savings that offset at least some of the extra costs incurred during the supplement period. Over and above this prospect, however, the applicant study has now produced striking evidence, reported later in this article, that the program may pay for itself even while it is in force.

From the broad perspective of family well-being, the results of SSP appear unambiguous. By about the fifth quarter after acceptance, SSP had reduced the fraction of families with incomes below the low-income threshold from 90 to 78 percent—a significant antipoverty effect. Program group members spent about 20 percent of the additional income generated by SSP on three basic necessities—food, housing, and children's clothing. They made less use of food banks than control group members. And they also were significantly more likely to have savings accounts—important for long-range well-being and a family's ability to cope with small crises.

The applicant study

The single parents who were selected into the SSP applicant study in British Columbia were considered likely to be less disadvantaged, more job-ready, and possibly more likely to respond to SSP's incentives than the long-term IA recipients participating in the recipient study. Like those recipients, they were overwhelmingly women from relatively disadvantaged families with a high rate of welfare receipt, and were equally likely to have very young children living in the household. But only 41 percent had less than a high school education, versus 54 percent in the British Columbia recipient sample, and 20 percent had some postsecondary education. Only 24 percent had never married, compared to 44 percent of longer-term recipients. These applicants also had a higher rate of home ownership (11 percent versus 4 percent of longer-term recipients).[10] They had a lower incidence of physical and emotional problems, more extensive work histories, and shorter welfare histories.

Did SSP have unintended negative consequences?

A common fear of public officials is that welfare policies will have effects directly counter to those they were expected to achieve. The one-year waiting period for the

Table 4
The Effects of SSP in the New Applicant Study
(mean monthly outcomes in the 6 months before the 30-month interview)

Outcome	Program Group	Control Group	Difference (effect)
Employment and Earnings			
Employed full time (%)	40.7	28.5	12.2**
Avg. hours of work	75	56	19**
Avg. earnings	$836	$613	223**
Cash Transfers			
Receiving IA (%)	38.9	49.7	-10.9**
Receiving SSP (%)	18.7	0	18.7**
Ever received SSP (%)	26.2	0	26.2**
Receiving IA or SSP (%)	56.3	49.7	6.5**
Avg. net transfer payments[a]	$571	$600	-29
Total Income			
Projected taxes[b]	$193	$115	78**
Avg. individual income net of taxes[c]	$1,529	$1,355	174**
Avg. family income, pretax[d]	$1,972	$1,686	286**
Below the Low-Income Cut-off (%)	57.2	68.5	-11.3**

Source: C. Michalopoulos, P. Robins, and D. Card, *When Financial Work Incentives Pay for Themselves: Early Findings from the Self-Sufficiency Project's Applicant Study*, SRDC, May 1999, Table ES-1.

Note: Dollar values are in Canadian dollars.

[a]Average monthly public expenditures on SSP, IA payments, and other transfers (Child Benefit, tax credits, unemployment benefit, net of projected taxes).

[b]Includes projected Employment Insurance and Canada Pension Plan premiums and projected income taxes.

[c]Includes earnings, IA and SSP payments, unearned income, and tax credits.

[d]The sum of the sample member's income plus the labor earnings of any other family members.

earnings supplement made it unlikely that single parents would go on IA merely to qualify. But it seemed quite possible that people might remain on IA longer in order to become eligible for the SSP earnings supplement, and such effects could overwhelm SSP's positive results for long-term welfare recipients.[11]

At the time they applied, about a third of new applicants for welfare expected to be on welfare for less than 6 months; over 50 percent "had no idea." The relatively high economic and psychic costs of being on welfare for those who were highly motivated and job-ready suggested that the supplement offer might not influence their behavior very much. The rather larger fraction facing serious obstacles to self-sufficiency, including low education or physical, emotional, and family difficulties—a group considered likely to stay on welfare for more than a year—also seemed unlikely to respond to the supplement offer; the recipient study provided good evidence that this was so. But there remained a middle group of single parents who might be willing to stay on welfare for a few extra months to gain the future benefit of an earnings supplement.

In fact, very few IA recipients prolonged their stay in order to qualify for SSP.[12] About 60 percent of the program group and 56 percent of the control group were still on IA after a year. There was no sharp change in the rate at which the program group left welfare as they approached the one-year eligibility mark, when the cost of delaying their departure from welfare in order to qualify for the supplement would diminish. Nor were there any serious labor market effects: both the control group and the program group showed steadily increasing employment in the months following random assignment.

In discussions with program group members, SRDC found that the supplement offer played a minor role, if any, in the decision to leave or stay on IA, even among those who knew most about it. In general, those who left welfare before they became eligible for the offer had their minds fixed on leaving and were simply not open to a longer stay on welfare, whatever the incentive. The picture that emerges is of people who have a strong work ethic, who are thinking of the future, and who, with older children, are better placed to pursue that future.

The group that stayed on IA long enough to become eligible for the offer was more likely to have sought assistance because of a failed relationship, with the attendant family and personal turmoil, rather than a job loss. Only a few in this group said that the supplement offer was important in their decision to stay—most cited difficulty in finding a "suitable" job, the need for further education or training, dealing with personal issues such as depression, recovery from marital breakdown or an abusive relationship, and child care concerns.

The small size of the entry effects in SSP is notable because the financial incentives offered are so substantial. Compared with other kinds of welfare innovations that involve job search requirements or workfare, SSP had few deterrents, and it was both generous and voluntary. The results suggest that entry effects associated with similar kinds of waiting periods and job requirements may also be limited.

The longer-term benefits and costs of SSP

The proportion of applicants receiving the supplement steadily increased, reaching a plateau of about 26 percent of the entire program group (44 percent of the eligible group).[13] (In the recipient study at same point in time, 35.2 percent of the entire program group had taken up the offer.)

By the 30-month follow-up period, SSP's supplement offer had resulted in significant changes in full-time employment, earnings, income, and poverty among the new IA applicants. Earnings rose by more than one-third, hours of work by 19 per month. About one-third of the impact on employment resulted in jobs that paid more than $10 per hour, substantially above the minimum hourly wage of $7. Most remarkably, at the end of the period, the cost of supplement payments was more than offset by reduced IA payments and increased tax revenues. Altogether, SSP considerably increased the average income of program members, reduced the percentage living below the poverty level, and did so with no increase in government transfer costs, which, indeed, dropped by nearly $30 per month (see Table 4).

These impacts are even more impressive considering that only 60 percent of the program group was eligible for the supplement. If we look only at the effects per eligible program member, SSP increased employment by about 20 percentage points, earnings by about $375 a month, and family income by about $481 a month. It thus increased the proportion of families above Canada's Low-Income Cut-off by 19 percentage points, still with no increase in net transfer payments.

Policy implications

The effectiveness of the SSP adds to the growing evidence that financial incentives with a work requirement can encourage welfare recipients—even long-term ones—to work, increase their income, and reduce their dependence on welfare. Some critics of financial incentives have worried that they would be expensive because they primarily reward people who would have worked without the incentive. SSP sought to keep costs low by offering the incentive only to those least likely to work, by requiring people to work full time, and by setting a one-year eligibility period. Targeting, however, raises a second concern: that such programs might be inexpensive mainly because nobody uses them.

The interim results from SSP's applicant study should allay such concerns. Those most likely to work left welfare quickly and never became eligible for the supplement. Those who remained were more likely to have graduated from high school and to have worked recently than the longer-term recipients, and were less likely to have emotional or physical barriers to work. SSP appears to have motivated this group of employable people who, without the supplement, might have remained on welfare.

There are, however, reasons for caution. Reports published so far apply only to the first two-and-a-half years of the study, before any sample members had exhausted their three years of supplement payments. The ultimate effects on individual behavior and the long-run cost-effectiveness of the program are presently unknown. Further studies will explore both issues. ■

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[1]See the article in this *Focus* by Lisbeth Pedersen, "The welfare state and the labor market in Denmark."

[2]This brief summary draws upon the discussions by A. Berry and K. Banting in *Social Policy in a Global Society: Parallels and Lessons from the Canada–Latin America Experience*, ed. D. Morales-Gómez and M. Torres A. (Ottawa: International Development Resource Centre, 1995).

[3]For instance, the Canadian national health system originated in the province of Saskatchewan during the administration of T. C. Douglas, premier of the province from 1944 to 1961.

[4]By comparison, in the United States in 1996, 20.5 percent of children under 18 lived in families with incomes below the U.S. poverty line, $12,980 for a family of three (U.S. Census, *Poverty in the United States 1996*, Report P60-198, Washington, DC, September 1997).

The Canadian Low-Income Cut-offs are estimated as the income level at which a family spends 20 percentage points more than the average on food, shelter, and clothing, and vary by community size. In 1996, the cut-off for a family of three, living in an urban area with a population of more than 500,000, was $26,633 (U.S. $19,442).

[5]The main interim report for the recipient study is W. Lin, P. Robins, D. Card, K. Harknett, and S. Lui-Gurr, *When Financial Incentives Encourage Work: Complete 18-Month Findings from the Self-Sufficiency Project*, SRDC, September 1998.

[6]Two reports from the applicant study are G. Berlin, W. Bancroft, D. Card, W. Lin, and P. Robins, *Do Work Incentives Have Unintended Consequences? Measuring "Entry Effects" in the Self-Sufficiency Project*, SRDC report, March 1998, and C. Michalopoulos, P. Robins, and D. Card, *When Financial Work Incentives Pay for Themselves: Early Findings from the Self-Sufficiency Project's Applicant Study*, SRDC, May 1999.

[7]Lin and others, *When Financial Incentives Encourage Work*, Table B-2.

[8]Lin and others, *When Financial Incentives Encourage Work*, p. 34.

[9]See, for example, M. Cancian, R. Haveman, T. Kaplan, D. Meyer, and B. Wolfe, "Work, Earnings, and Well-Being after Welfare: What Do We Know?" *Focus* 20, no. 2 (Spring 1999): 22–25.

[10]Berlin and others, *Do Work Incentives Have Unintended Consequences?*, Table 1.

[11]Berlin and others, *Do Work Incentives Have Unintended Consequences?*

[12]Through surveys, SRDC had determined that at least one-half and perhaps as many as three-quarters of the program group had relatively precise knowledge of the key features of the SSP.

[13]Michalopoulos and others, *When Financial Work Incentives Pay for Themselves*.

The welfare state and the labor market in Denmark

Lisbeth Pedersen

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Together with Norway, Finland, and Sweden, Denmark belongs to the Scandinavian Welfare Model.[1] This model is often characterized as "universalistic," because the income transfer system and social services offer widespread coverage and a relatively generous level of cash benefits intended to keep everyone out of poverty.

Denmark is the oldest of the universalistic welfare states. The Danish system was established in the 1890s, about the time that the welfare state began to develop in Germany. But the Danish system is unlike that in Germany, where benefit levels are closely connected to employment status and the social security system is financed by mandatory contributions from employers and employees.[2]

In recent years, the crisis of the welfare state has been a major subject of debate in many European countries. In Denmark as elsewhere, more than two decades of high unemployment combined with generous income support programs have created serious problems. In this article I review recent trends in the Danish labor market and examine aspects of the income transfer system and social services that directly influence employment.

Recent trends in the Danish labor market

Labor supply

From 1970 to 1997 the Danish labor force increased by about 20 percent, mainly because of a substantial increase in the number of housewives entering the labor force.[3] The female participation rate in Denmark began to rise in the early 1960s and the tendency accelerated during the 1970s. The increase was parallel and closely related to a dramatic growth in public sector employment that involved the creation of a large number of jobs attractive to women (for example, public provision of care and teaching). In effect, the public sector assumed a significant part of the care that women had performed as unpaid home work and transformed it into public service goods. This development both released women from many of their former duties at home and facilitated their entrance into the labor market. It also created a large public-sector workforce, which in 1997 constituted nearly 35 percent of the labor force (see Table 1).

The labor force participation rate is now 83 percent among all Danish men and 75 percent among all Danish women (see Figure 1). The participation rate for young and middle-aged women is close to the male level, and more women are moving into full-time rather than part-time employment. Every second woman in the labor force is employed in the public sector.

The increasing labor force participation rate of women, especially younger women, has not compensated for the general trend toward early retirement. Because of high unemployment over the last 20 years and the emergence of new early retirement programs, the average retirement age has dropped to about 61, even though the formal retirement age is 67.[4] At the same time, young people are entering the labor market later, because schooling now lasts longer. The result has been a very high rate of employment for both sexes between ages 25 and 45 and a very high burden on the working population for support of those not employed.

Unemployment, rising and persisting

At the same time that more women began entering the labor market, unemployment became a serious issue. In 1973, the oil crisis spurred a dramatic increase in unemployment in Denmark, as in the rest of the European Union (EU). In the preceding decade, the Danish government had pursued an expansionary policy and, as already noted, the public sector had expanded considerably. That led to a massive balance of payments deficit and, when prices of oil and other raw materials rose, the Danish economy encountered substantial problems. Between 1974 and 1983, the unemployment rate increased from 2 percent to 10 percent.

Unlike the economies of other EU nations, the Danish economy began to recover after 1983. But from about 1986 on, unemployment increased again and worsened (see Figure 2). The persistently high unemployment rate

Table 1
The Danish Labor Force, 1997

Total Population	5,251,027
In the labor force	2,863,330
Working	2,669,658
By Industry	
Agriculture, fishing, and quarrying	4.5%
Manufacture, construction, utilities	24.4
Private services, business services	35.7
Public and personal services	34.9
Activity not stated	0.5

Source: Danmarks Statistik (Statistics Denmark).

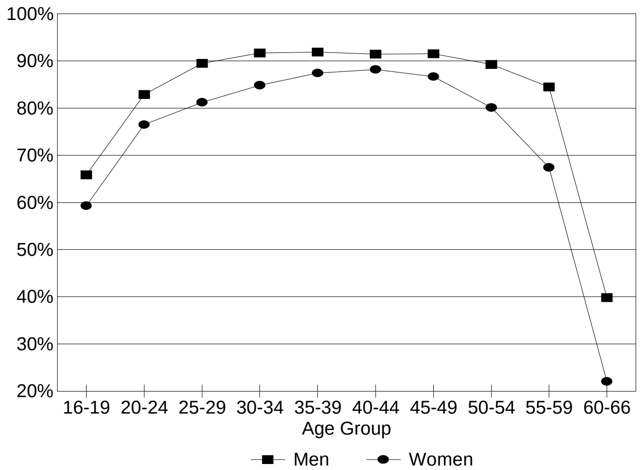

Figure 1. Labor force participation rate in Denmark, by age and gender, 1997.

Note: The rate represents the number of persons in the labor market / number of persons in the age group.)

Source: Danmarks Statistik (Statistics Denmark).

shifted the composition of the unemployed toward a higher proportion of long-term unemployed, and the labor market showed a tendency to polarize between unskilled and skilled workers. After 1993–94, however, registered unemployment dropped dramatically, and the Danish rate is now far below the average European unemployment rate. This is due to positive economic developments, a more flexible labor market, and an increase in the number of individuals who have entered labor market programs or taken early retirement.

The Danish income transfer and social insurance systems have played a significant role in the labor market problems of the 1980s and 1990s. In the first place, the high rate of taxation imposes a heavy burden on real disposable income, especially among those with low incomes. Tax policies and relatively generous benefit schemes put pressure on the lower part of the wage distribution, because the net gain from being employed rather than not working is negligible, especially for unskilled workers. The very compressed wage structure has led to a reduction in the number of jobs for low-productivity workers. Moreover, firms have become accustomed to a more careful screening of the labor force; only highly productive workers are employed and the rest are expected to be taken care of by public transfers. Second, although the growth in the labor force from 1970 to 1992 increased employment, the number of individuals in the labor force who were dependent on public income support grew more rapidly. In 1992, the equivalent of 909,000 full-time-employees, or around 25 percent of the population aged 15 to 66, were either unemployed, on one of the public leave schemes, receiving social welfare payments, or on some form of early retirement benefit (see Figure 3).

The declining unemployment rate after 1994 has made little difference. From 1995 to 1997 the number of

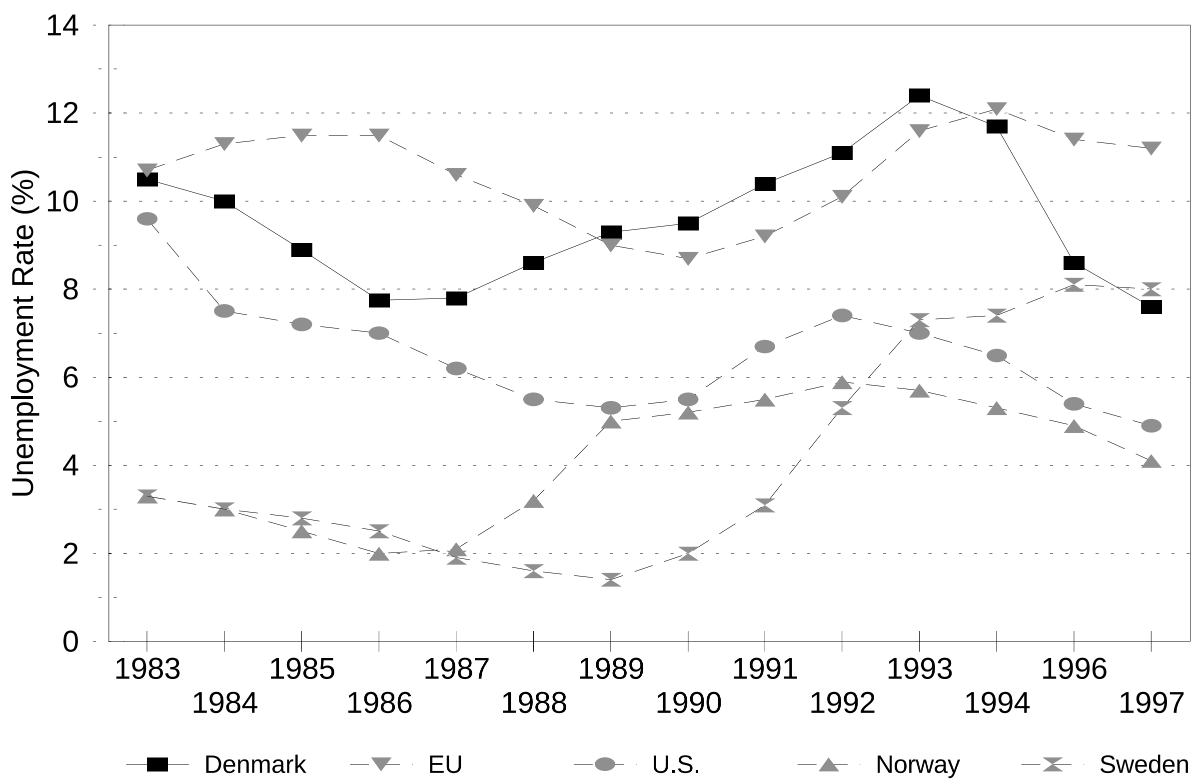

Figure 2. The unemployment rate in Denmark, compared to other Scandinavian countries, the European Union, and the United States.

Source: OECD, *Economic Outlook*, various years.

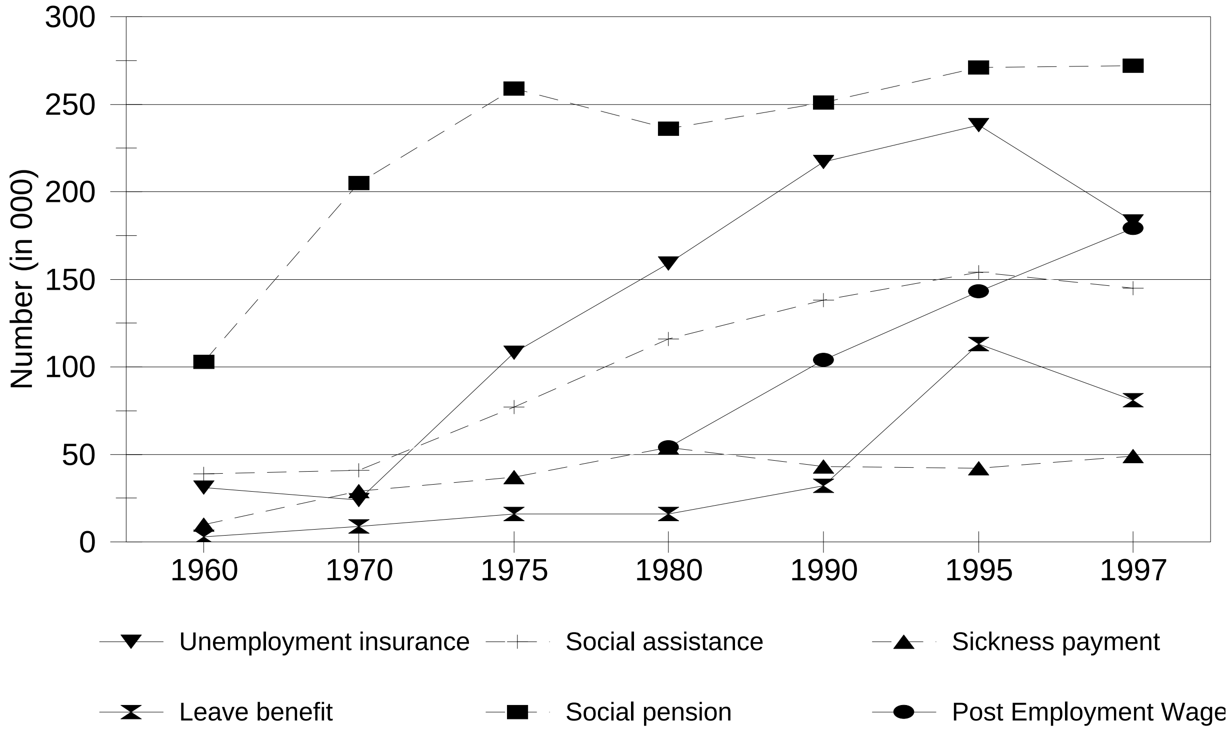

Figure 3. Number of people aged 15–66 on different types of transfer income in Denmark (measured in full-time equivalent workers). Social assistance includes people in rehabilitation, leave benefit includes maternity leave, parental leave, educational leave, and sabbatical leave. Post Employment Wage includes, for 1995 and 1997, those on the Temporary Benefit Scheme (see text).

Source: Denmark, Ministry of Finance, 1997.

people receiving various kinds of social welfare payments dropped only a little or even rose, as Figure 3 shows. We must, therefore, look closely at the characteristics of these programs and how they have contributed to current labor market trends.

The Danish welfare state

The public sector dominates the Danish economy, accounting in 1997 for 57 percent of GDP, compared to just over 30 percent of GDP in the United States. Total public expenditures other than transfers amount to about 25 percent of GDP, and income transfers add another 30 percent. About 43 percent of public expenditures are devoted to social security and welfare services, about 13 percent to education, and 9 percent to health care. (The remaining one-third is mostly for general administration, defense, and industrial development.)

The financing of the public sector in Denmark is heavily based on the value-added tax (VAT) and on duties and direct taxes. This is quite different from other Scandinavian countries and countries such as France, Germany, and Belgium, where social security contributions play a more dominant role. About one-third of direct taxes are levied by the central government and one-sixth by the counties and municipalities. Only a small part of unemployment and work-related disability insurance is financed by contributions from workers and employers.

Public sector responsibilities are unevenly divided among the central government and the two main units of local government—the counties and the municipalities. Measured by expenditures, the central government has responsibility for a little less than 40 percent of public sector activities, local governments a little more than 50 percent; social security funds pay out the remainder. However, the central government finances two-thirds of all activities, local government less than one-third, and the social security funds finance only about 2.6 percent, though social security disburses over 7 percent of all social welfare funds. The central government is responsible for defense, justice, and higher education, whereas primary and secondary education, social services, and health services are the province of local government. Welfare programs are in general under the administration of the local government, but they are federal in the sense that eligibility criteria and benefit levels are determined by the central government and so are identical in all municipalities.

Public sector activity, then, strongly influences the labor market through the collection of taxes, payment of transfer income, and supply of public services. But the Danish labor market is also highly regulated by agreements between the various participants. Wages, working hours, and working conditions are settled through collective bargaining (there is, for example, no legal minimum wage in Denmark).[5] Since one-third of all employees work in the public sector, agreements on working conditions in this sector often have a strong influence on the rest of the labor market.

Transfer income and social services for those in the labor market

This section briefly describes those parts of the social security system that are most important for people in the labor market and some of the most significant efforts to reduce unemployment.[6]

Most benefit payments for those in the labor market in Denmark are individual, in the sense that they are paid independently of marital status and family responsibilities. Moreover, benefit levels depend only to some extent on current income level. The transfer system in general does not give priority to special groups, such as lone mothers and people with low income. In practice, however, a major part of total transfer income is allocated to low-income groups and thereby contributes to equalization of incomes.

Eligibility for some benefits, such as unemployment insurance and sickness and leave benefits, requires that the person has been employed or has at least been officially in the labor force for a brief period (usually 26 weeks). Benefits for industrial injuries are paid to all wage earners; social pensions and old age pensions to Danish citizens and to noncitizens who have been in Denmark for a certain period of time. Most benefits are taxed.

Unemployment. Setting aside those not working because of sickness and disability, there are two main forms of support for working-age individuals who lack employment: an insurance-based *unemployment benefit* and means-tested *social assistance*.

The Danish unemployment benefit system is characterized by a long duration of benefit, a high replacement ratio for low-wage workers' earnings, relatively liberal eligibility rules, and a high degree of state financing. Unemployed persons who have a sufficient previous employment record and have joined an unemployment insurance fund are able to draw unemployment benefits related to the amount of their prior earnings but unaffected by other sources of current income. Around 75 percent of the workforce joins unemployment insurance, even though it is not mandatory. To be eligible for unemployment benefits, it is necessary to have worked 52 weeks in the previous three years, to be currently available for work, and to be searching for a job. The unemployment benefit is 90 percent of prior earnings, with a payment ceiling of approximately $1,700 per month (12,000 DKr). The average replacement ratio for manual workers is currently about 65 percent.[7]

A major labor market reform was implemented in 1994. The maximum duration of benefit, previously about nine years, has gradually been reduced, and in 1999 is four years. After one year, the recipient is placed either in an educational program or in publicly supported job training. The reform did not reduce benefit levels.

A person who loses a job but is not entitled to unemployment insurance benefits will usually receive social assistance. This is a flat-rate benefit, which, for a household head, is 60–80 percent of the maximum unemployment insurance benefit, depending on whether the person is a provider for children. Social assistance is means-tested, taking into account the individual's own income and the income of a spouse. Availability for work and active job search are required as a condition of eligibility. The benefit consists of a base amount, a fixed amount per child, and a housing payment. In addition, some nonrecurring expenditures can be covered.

Evaluation of this active labor market policy has shown that job training is much more effective in private firms than in public organizations. After one year, about 50 percent of the individuals receiving job training in private firms are still in the firm, whereas only 33 percent remain in public organizations. However, few find permanent jobs in the firms where they were trained, and only longer-term education seems to be effective. The active labor market policy also seems to have been successful in determining the unemployed individual's job readiness for the labor market, especially among the youngest participants.

Danish analysts have shown that low-skilled individuals, women, and the youngest and the oldest in the labor market are at an especially high risk of unemployment. During the 1980s and the early 1990s the risk of unemployment increased among the oldest workers and diminished among the youngest, probably as a result of the institutional changes in the labor market and the fact that the probability of finding employment during the 1993–94 economic recovery differed for the two age groups. Even though the low-skilled always are at greater risk of unemployment than the higher-skilled, it seems that the risk increases during a recovery, when the most productive workers are the first to find work. In contrast, unemployment is more equally distributed during an economic depression.[8]

Sickness, disability, and injuries. All wage earners are eligible for sickness payments. Salaried employees and public servants receive full wages during periods of sickness. Others can receive sickness payments for up to a year from the municipality in which they live, but an increasing number of workers have gained the right to additional payments that bring their benefit up to the full wage level through agreements with their employers. The municipal benefit is 100 percent of the employee's wage, with a maximum of around $1,700 per month.

Those who lose their ability to work, in whole or in part, receive a *social pension*. The amount of this benefit ranges from about $1,100 to $1,800 for a single person, depending on the degree of disability. The number of persons receiving social pensions has increased since 1970, although not dramatically. However, the number of recipients younger than 55 years has increased about 40 percent since 1980, most likely because of the decline in employment opportunities for low-skilled workers and an increasingly more demanding labor market.

As a supplement to sickness payments or social pensions, all wage earners are eligible for benefits if they have suffered an *industrial injury*. The benefit depends on the degree to which the injured person has lost his/her ability to work and on age and education. It is the only true earnings-related benefit in the Danish system.

Medical care is generally provided by the county or municipality and is paid for through taxes. Only the costs of certain special procedures are paid in part by the patient.

Children. Parents are entitled to *maternity leave.* The length of leave has been changed several times over the last few years. At the time of writing it is 4 weeks in the private sector (8 weeks in the public sector) before the child is born and 24 weeks after the birth. Fathers may take 2 weeks with the mother when the child is born and 2 weeks at the end of the 24-week period. The father rather than the mother may take the last 10 of the 24 weeks after the birth, but very few parents choose this option. All public sector workers receive full payment during maternity leave. Private sector workers are entitled to 90 percent of wages, with a maximum of $1,700. However, large groups of private sector workers have been able to secure full wages through agreements between the unions and the employers' federations.

Since 1994, maternity leave has been supplemented by a *parental leave scheme,* open to all parents who have a child under 9 years old. For a minimum of three months and a maximum of twelve months, the parent can receive 60 percent of the maximum unemployment benefit while on leave. Measured in full-time employment, about 30,000 individuals, or a little more than 1 percent of the labor force, were on parental leave in 1997. The number has decreased since the leave scheme began, because benefit levels have been reduced.

A 1996 study showed that 90 percent of those on parental leave were women. The preponderance of employed people who take parental leave are in public sector jobs—nurses, teachers, etc.—that are dominated by female employees.[9] Somewhat fewer that half of those on parental leave in 1996 were unemployed. This group has a clear tendency to take longer leaves—an average of 10 months in 1994–95, compared to an average of 7.5 months for the employed—perhaps reducing even further their opportunities for entering the labor market.

In recent years wage differentials between women and men in the Danish labor market have increased—a development that is quite contrary to the trend in other countries of the European Union and the United States.[10] The reason may lie in the introduction of these parental leave schemes.

Most *formal day care* for children is provided through subsidized public services, and availability is high compared to other countries. The subsidy covers 70 percent or more of the full cost of care. Families with very low incomes can obtain child care free of charge. Nearly 50 percent of children below the age of 2 and 80 percent of those aged 3 to 6 are in public day care. In 1998 10,500 children under the age of 6 (or around 2 percent of all children under 6) were on waiting lists for a day care opening.

Studies from Denmark show that the presence of young children in the household has no significant effect on the mother's labor supply—a finding contrary to labor supply studies from other countries.[11] The main explanation for this fact is clearly related to the very large increase in affordable, publicly provided child care.

Retirement. Retirement pensions come through different channels. The Old Age Pension is available to all citizens from the age of 67, but the actual average retirement age, as noted earlier, is now about 61, mostly because of the introduction of the Post Employment Wage in 1979. From 2004 on, the official retirement age will be 65.

Employed and unemployed persons are eligible for the Post Employment Wage from the age of 60, if they have been members of an unemployment insurance fund for a certain period of time. The benefit is equivalent to 91 percent of the unemployment benefit. Individuals receiving the Post Employment Wage do not have to be available for work. Since its introduction, increasing numbers of people aged 60–66 have joined this scheme.

The original purpose of the Post Employment Wage was to reduce the size of the older labor force and thereby create new jobs for younger unemployed people—that is, the scheme was considered more as part of labor market policy than as part of social policy. As more people over 60 retired earlier, unemployment did indeed go down. But the success of the policy with respect to its primary goal has been very moderate. It has been estimated that only about 20 percent of the jobs which were freed because of the Post Employment Wage were filled by unemployed people, whereas the rest of the jobs have most probably been lost.[12]

From 1992 to 1996, the Post Employment Wage was supplemented by the Temporary Benefit Scheme, which allowed long-term unemployed over the age of 55 (over

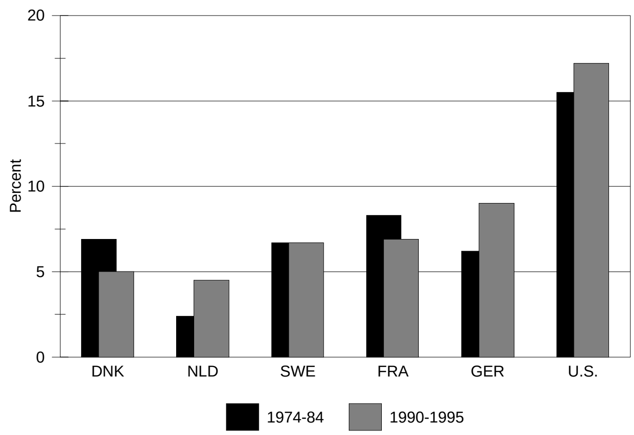

Figure 4. Percentage of the population with disposable incomes below 50 percent of median income in Denmark, the Netherlands, Sweden, France, Germany, and the United States.

Source: OECD, *Economic Outlook,* 1997 and Denmark, Ministry of Finance, *Strukturovervågning-international benchmarking af Danmark,* 1999.

the age of 50 after 1993) to enter an early retirement scheme. Access to the scheme was halted in 1996.

In addition to the public pension schemes, just over 50 percent of wage earners have private pensions. Only 10 percent of elderly women and virtually no men leave the labor market before the age of 67 without any income from a public or private pension scheme.

Pros and cons of the Danish welfare state

Many of the relatively generous Danish welfare schemes were designed in the late 1960s and early 1970s when unemployment was low. As unemployment increased during the 1970s and 1980s, these transfer schemes created significant pressure on the welfare state because they became very expensive to finance. But they also generated new expectations about what the welfare state should provide, and it is politically very difficult to abolish a scheme once it has been implemented.

The financial difficulties of the welfare state have to some extent been alleviated by the fact that in most families both spouses are in the labor force; nevertheless, financing these programs imposes a heavy burden on the employed population. The large expenditures on public transfers and public services lead to high tax pressures that are believed to have negative incentive effects on labor supply and to increase off-the-books work and do-it-yourself activities. The total tax bite in Denmark is larger than in the United States, Germany, France, and Sweden—it is a little more than 50 percent in Denmark and a little less than 30 percent in the United States. In particular, the marginal tax rate for high-wage manufacturing workers is higher in Denmark than in other countries. The connection between taxes and labor supply is not straightforward and has therefore been difficult to assess using Danish data.[13] Yet it seems obvious that the relationship between the low-skilled workers' wage levels, unemployment benefits, and tax pressures must have some influence on labor supply. An analysis from 1993–94 shows that the difference between disposable income (net of work expenses) when one is full-time employed and disposable income when one is full-time *unemployed* was less than about U.S. $70 per month for about 20 percent of those employed.[14]

It seems, furthermore, that those with a marginal attachment to the labor market become trapped in the welfare system. Even after the economic recovery of 1994 and the consequent decrease in unemployment, it has proved almost impossible to move a significant group of the long-term unemployed back to work. The reason is in part to be found in the incentive problems mentioned earlier, but also in the fact that work qualifications deteriorate the longer people are out of the labor market. Data from 1996 show that on average only about one-third of the very long term unemployed (that is, those unemployed more than 70 percent of the time over three years) managed to leave that category during a four-year period.[15] Nevertheless, when people on social pensions were surveyed about their attitude toward work, 40 percent said that they would have preferred to have a job.[16]

In general, however, the Danish welfare state seems to have great public support, although attitudes are inconsistent.[17] This may be due to the fact that it has very efficiently alleviated poverty (Figure 4); poverty rates are among the lowest in the European Union and quite insensitive to changes in the business cycle.[18] In addition to a more equal income distribution, the welfare state has also created a congenial environment for higher social mobility and has reduced gender inequality.

The Danish welfare state cannot be said to be in liquidation, but a solution to the heavy financial pressures it imposes is necessary. One solution is to encourage citizens to save for their own retirement, and this was implemented in the reform of the Post Employment Wage at the beginning of 1999.[19] Another lies in improving employment, both by expanding work among the young and the elderly, and reducing the high and resistant rate of unemployment among those who have been jobless for far too long during their adult lives. ■

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[1]This article has benefitted from comments by Dr. Hans Hansen of the Danish National Institute of Social Research.

[2]Differences among the European welfare states are described in N. Ploug and J. Kvist, eds., *Social Security in Europe: Development or Dismantlement?* Kluwer SOVAC Series on Social Security, vol. 3 (The Hague: Kluwer Law International, 1995).

[3]The Danish labor market is more fully described in L. Pedersen, P. Pedersen, and N. Smith, “The Working and Non-working Population in the Welfare State,” in *Work Incentives in the Danish Welfare State: New Empirical Evidence*, ed. G. Viby Mogensen (Aarhus: Aarhus University Press, 1995).

[4]L. Pedersen and N. Smith, “The Retirement Decision,” in *Work Incentives in the Danish Welfare State,* ed. Mogensen.

[5]There are of course exceptions. For instance, the minimum amount of vacation time is determined by law.

[6]For a description of the Danish income transfer system, see Ploug and Kvist, *Social Security in Europe*.

[7]For most insured unemployed there is also a minimum of 82 percent of the maximum benefit.

[8]J. Soendergaard and L. Pedersen, “Arbejdsmarkedet og de ressourcesvage” (The Labor Market and People with Few Resources),Working Paper, Danish National Institute of Social Research, 1998.

[9]Results of the evaluation are reported in D. Andersen, A. Appeldorn, and H. Weise, “Orlov – evaluering af orlovsordningerne” (Leave – Evaluation of the Leave Schemes), Working Paper 96:11, Danish National Institute of Social Research, 1996.

[10]N. Gupta, R. Oaxaca, and N. Smith, “Wage Dispersion, Public Sector Wages and the Stagnating Danish Wage Gap,” Working Paper 98-17, Center for Labour Market and Social Research, Aarhus, 1998. But gender equality in wages is still very high in Denmark. In 1970, women’s average wages in manufacturing were 74 percent of male wages in Denmark, compared to 58 percent in the United Kingdom. In 1990 and 1995, women’s wages were 85 percent of men’s in Denmark, a slight drop from the 1980 ratio of 86 percent (the peak year seems to be 1975 for manual workers and 1980 for white collar workers). In the U.K., women’s manufacturing wages had risen to 71 percent of men’s by 1993–95 (United Nations, Statistics Division, Statistics and Indicators on the World’s Women, Table 5.5, Women’s Average Wages in Manufacturing as a Percentage of Men’s, 1970, 1980, 1990, and 1993/95, UN World Wide Web site <http://www.un.org/Depts/unsd/gender/>).

[11]S. Dex and N. Smith, “The Labour Force Behavior of Married Women in Denmark and Britain: A Comparative Study,” Working Paper 94-8, Center for Labour Market and Social Research, Aarhus, 1990; L. Pedersen, H. Weise, S. Jacobs, and M. White, “Lone Mothers’ Poverty and Employment,” unpublished working paper, Danish National Institute of Social Research, 1999.

[12]Danish Social Commission, *De aeldre* (The Elderly) (Copenhagen, 1993).

[13]L. Pedersen, “Progressiv indkomstbeskatning og arbejdsløshed” (Progressive Income Tax and Unemployment), in *Er der veje til fuld beskæftigelse?* (Roads to Full Employment), ed. L. Pedersen, Working Paper 97:13, Danish National Institute of Social Research, 1997.

[14]P. Pedersen and N. Smith, “Taxed and Non-taxed Labour Supply: Wages, Taxes and Costs of Work,” in *Work Incentives in the Danish Welfare State*, ed. Mogensen.

[15]O. Ingerslev and L. Pedersen, “Marginalisering 1990–1994" (The Marginally Attached 1990–1994), Working Paper 96:19, Danish National Institute of Social Research, 1996.

[16]S. Juul, “Ynger førtidspensionister” (Young People on Social Pension), Working Paper 92:17, Danish National Institute of Social Research, 1992.

[17]A 1995 survey showed that three out of four thought that the welfare state was an achievement that should at any price be preserved. But just as many thought that the income transfer system was too costly. J. Soendergaard, “Borgerne om velfaerdssamfundet” (The Citizen about the Welfare Society), *Saernummer af Socialforskning*, August 1996.

[18]P. Pedersen and N. Smith, “ Low Income in Denmark, 1980–1995,” Working Paper 98-19, Center for Labour Market and Social Research, Aarhus, 1998.

[19]In brief, the reform involved (1) institution of a uniform benefit (91 per cent of the unemployment benefit) through the whole period of the Post Employment Wage, (2) an extended requirement for unemployment benefit membership, (3) a monthly financial contribution in order to take up the option for early retirement and a premium if the option is not taken up, (4) a means-tested capital pension for those under age 62 (a capital pension is a particular type of private pension that benefits from a low tax rate; the amount of the Post Employment Wage depends on the size of the pension), and (5) a premium for delaying the option until age 62.

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