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Southwest Economy

Is Mexico Ready to Roar?

Mexico has become a much more open economy over the past 20 years. And since the 1994 financial crisis, Mexican authorities have shown a commitment to macroeconomic discipline.

Given this progress, many observers are enthusiastic about the country's prospects. Some, in fact, wonder whether Mexico is about to take off and become the world's next economic tiger. The evidence suggests, however, that much work remains to be done before Mexico can catch up to First World nations the way countries such as Singapore and South Korea did in the last few decades.

Until the early 1980s, like most developing nations, Mexico sharply restricted foreign investment and trade in hopes of expanding domestic production capacity. But a severe financial crisis in 1982 prompted a change of tactics. Foreign investment limits were lifted in 1983 in some sectors. In 1985, Mexico announced it would join the General Agreement on Tariffs and Trade and did so the following year. Between 1985 and 1990, the country's maximum tariff fell from 100 percent to 20 percent. Most sectors were opened to foreign investment in 1989, paving the way for a successful wave of privatizations. By 1994, 80 percent of

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Welfare Reform Revisited

In the late 1980s, the number of people receiving welfare benefits in America began to rise. As the trend continued into the 1990s, a bipartisan coalition searched for ways to reform the American welfare system. Convinced that many welfare recipients could work if presented with appropriate incentives, political leaders devised a welfare reform bill that was intended to promote self-sufficiency while retaining a social safety net for those who temporarily have no other options.

The bill was intensely controversial. An influential policy adviser said the bill would inflict "serious injury to American children."[1] A senator who specializes in welfare issues said there was "absolutely no evidence that this radical idea has even the slightest chance of success."[2] And the Center on Budget and Policy Priorities predicted that the most significant effect of welfare reform would be "a large increase in poverty."[3]

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The Politics of Brazil's Financial Troubles

Welfare Reform Revisited

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Over these objections, President Clinton signed the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) into law in August 1996. And in the years following passage of the law, welfare recipiency has declined significantly—without a corresponding increase in the poverty rate. Many observers now cite welfare reform as one of the most successful policy experiments in a generation. In the words of President Clinton, the welfare system has become "a second chance" instead of "a way of life."

Because PRWORA expires on Sept. 30 unless renewed by Congress, it is an opportune time to examine the law's effects and draw lessons for its future. This article looks at the structure of the law, details its results and discusses what is likely to happen later this year when the law is reauthorized.

What Did the Welfare Reform Law Do?

The welfare reform law focused on the Aid to Families with Dependent Children (AFDC) program, which was the cash-grant portion of America's social safety net. (The box "A Brief Description of the U.S. Welfare System" describes the other portions of the safety net.) The law replaced AFDC with a program called Temporary Assistance to Needy Families (TANF) and made four major changes to the welfare system.

The first—and perhaps most significant—change was a requirement that recipients work in exchange for their cash benefits. Previously, recipients were required to make only a minimal effort at finding employment. Under the new system, many of those who received benefits for more than two years lose their cash grant unless they perform a work-related activity for at least 30 hours per week. Private employment is one way to fulfill the requirement, but education or training can generally also be counted as work for purposes of this legislation.

Second, the law imposed a five-year lifetime limit on the amount of time any single family can receive cash benefits. Previously, it was possible to spend a lifetime on the welfare rolls, which led many analysts—and more than a few welfare recipients—to conclude that welfare created a "cycle of poverty" from which welfare families could never escape. Under the new system, all but the most hardship-stricken recipients are permanently barred from cash grants after five years even if the recipient remains outside the workforce. The idea was akin to FDR's vow that the welfare system would provide a temporary "hand up" rather than a permanent "handout."

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A Brief Description of the U.S. Welfare System

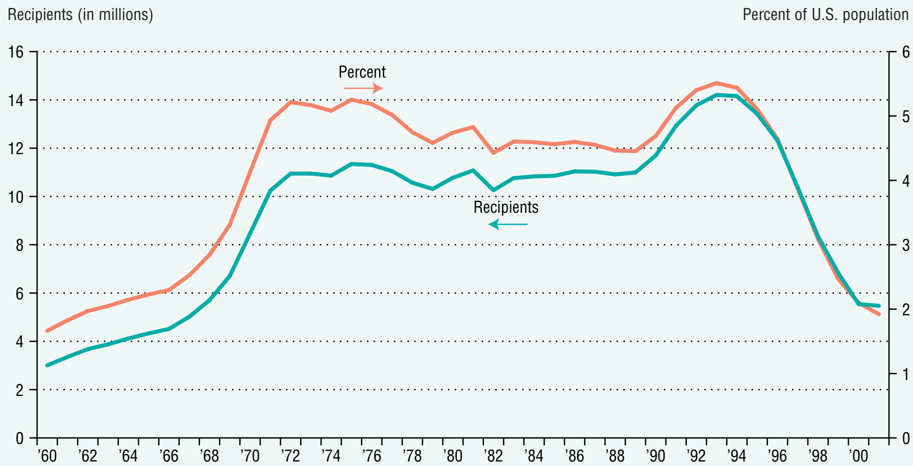
In the United States, many federal programs are available to help the poor, including programs to provide home heating oil, housing subsidies and even infant formula. But for our purposes, the U.S. welfare system consists of three major components: Temporary Assistance to Needy Families (TANF), food stamps and Medicaid. (A fourth program, Supplemental Security Income or SSI, provides significant support to the elderly and disabled but is not considered here.)

The programs differ in three respects: funding source, benefit type and scope of coverage. TANF (formerly known as Aid to Families with Dependent Children) gives cash benefits to poor families with children and is jointly funded by states and the federal government. The Food Stamp Program gives food vouchers to low-income individuals—including TANF recipients but also including many single workers with low-paying or seasonal work—and is funded by the federal government. Finally, Medicaid provides medical care to poor and near-poor individuals and is largely funded by the federal government, with some help from the states.

Many people believe that welfare is one of the largest areas of government spending, but the extent to which this is true depends on the definition of welfare. Cash grants through the TANF program amounted to $18 billion in 2001, slightly less than 1 percent of the federal budget. Food stamps took up an additional $19 billion (1 percent) of the federal budget, and Medicaid consumed $129 billion (7 percent) of the budget. Summed together, these programs are about half as large as the defense budget.

Chart 1

Welfare Rolls Decline Dramatically



SOURCE: The Administration for Children and Families.

Third, the law made it more difficult for noncitizens to receive cash benefits or food stamps. Previously, noncitizens who were legal permanent residents of the United States could access most of the safety net available to citizens, which led some observers to conclude that there was an incentive for impoverished residents of other countries to enter the United States and become welfare recipients. To guard against this possibility, the welfare reform law barred many noncitizens from either cash grants or food stamps, although these restrictions were later relaxed for some of those affected.

Finally, the law removed the cash-grant portion of the welfare system from the list of entitlement programs. Previously, anyone who met certain eligibility criteria had a legally enforceable right to cash benefits, regardless of the fiscal circumstances of states or the federal government, the number of people on the welfare rolls or how hard recipients tried to find alternative means of supporting themselves. Under welfare reform, individuals no longer have an automatic right to cash benefits simply because they are poor or have children.[4]

Did Welfare Reform Reduce the Welfare Rolls?

In the five years following passage of the welfare reform law, the number of individuals receiving cash grants declined by 56.5 percent, a result beyond the predictions of even welfare reform's most ardent advocates. The current welfare participation rate, a 35-year low, returns welfare recipiency to where it stood at the dawn of Lyndon Johnson's Great Society (*Chart 1*).

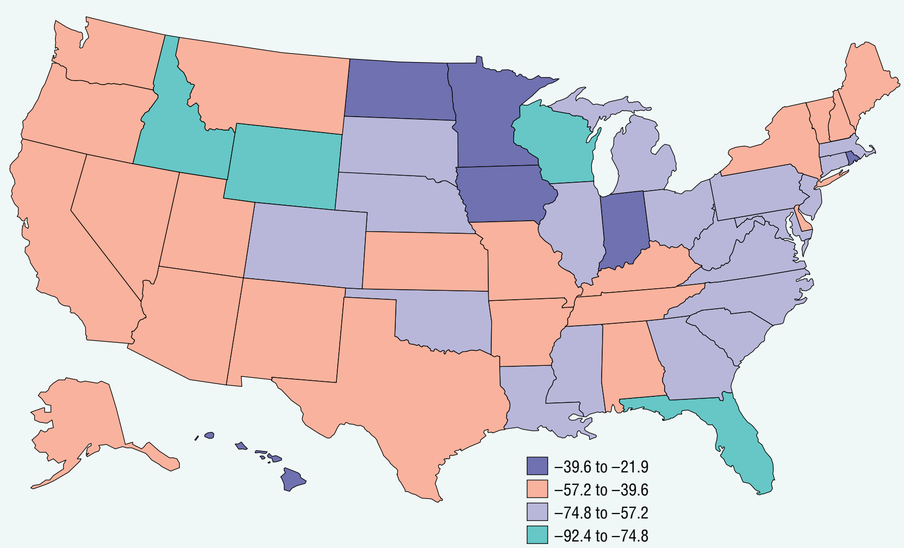
During the post-welfare-reform period, recipiency declined in all 50 states (*Chart 2*). The largest reduction (92 percent) occurred in Wyoming, which now has fewer than 1,000 recipients. Several large states also experienced significant success in cutting their welfare rolls, such as the 78 percent decline in Florida and the 72 percent decline in Illinois. The smallest reductions occurred in Indiana and Rhode Island, whose welfare rolls declined by 22 percent and 29 percent, respectively. Texas welfare rolls declined by 49 percent.

It may seem natural to credit the 1990s economic boom rather than welfare reform for this decline. But while the strong economy surely played a role, there are two reasons to think welfare reform was also important. First, the number of welfare recipients did not fall in other postwar economic expansions. Second, the number of people participating in other welfare programs did not fall by as much as cash-grant recipiency fell in the 1990s; food stamp recipiency fell by only half that amount, and Medicaid recipiency actually rose during the 1990s (*Chart 3*). This evidence suggests welfare reform was a significant contributor to the declines, a finding confirmed by a recent Council of Economic Advisers report.[5]

By itself, however, the reduction in welfare recipiency does not make welfare reform a successful policy experiment. Opponents of reform had made serious charges about how welfare reform "punishes the poor." If welfare reform slashed the amount states could spend on each recipient, if those who

Chart 2

Decline in AFDC/TANF Recipients, Fiscal Years 1996–2001

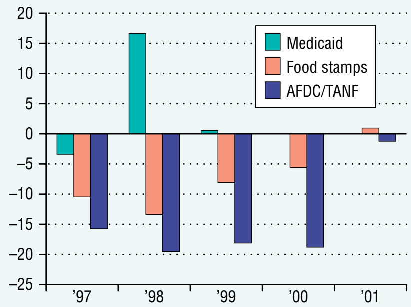


SOURCE: The Administration for Children and Families.

Chart 3

AFDC/TANF Shows Biggest Drop

Percent change in recipiency (year-over-year)

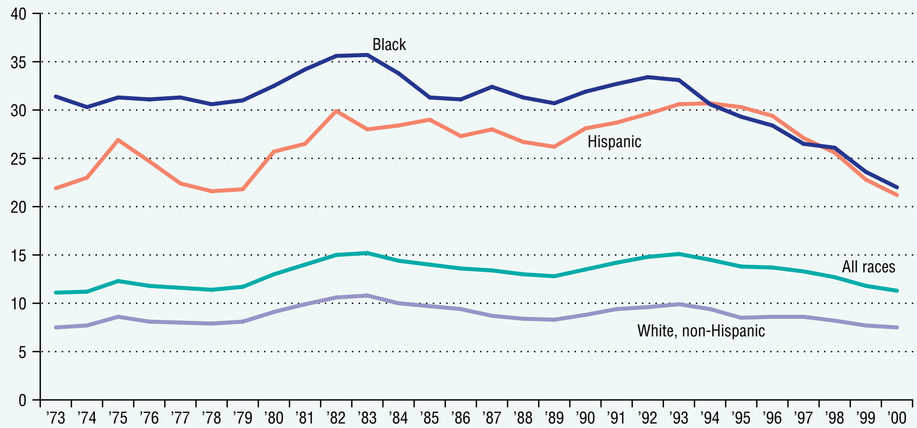


SOURCES: The Administration for Children and Families; Centers for Medicare and Medicaid Services; USDA.

Chart 5

Poverty Rates Decline for All Races

Percent below poverty level



SOURCE: U.S. Census Bureau.

left the welfare rolls were continually rebuffed in their job searches or if the poverty rate surged to new heights, the sharp welfare-roll reductions might be viewed as exacting a high social cost. On the other hand, if these outcomes did not occur, welfare reform might instead be viewed as one of the most successful policy changes of the 1990s.

On the spending side, per-capita outlays doubled between 1996 and 2001 (*Chart 4*) as recipiency plunged.[6] On the employment side, the General Accounting Office found that a majority of former welfare recipients have entered the labor force and continue to work today.[7] And the poverty rate for all races fell from 13.7 percent in 1996 to 11.3 percent in 2000 (the last year for which data are available) (*Chart 5*). Of special significance is the fact that the largest decline in the poverty rate during this period occurred among blacks, who form a disproportionately large share of the welfare rolls and were expected to have the most difficult time adapting to welfare reform. Taken together, the data suggest welfare reform proceeded in exactly the way President Clinton predicted when he signed the law: It encouraged many families to work without throwing many families into poverty.

Is There Anything Left to Reform?

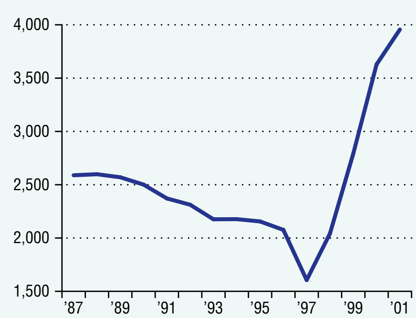
Since the welfare rolls have already fallen by more than half over the past five years, it is inevitable that further reductions due to welfare reform will eventually slow. It appears this may be happening now: Cash-grant recipiency remained constant in the fourth quarter of 2001, and anecdotal evidence suggests it may have risen slightly in the first half of 2002. Absent further welfare reform, and especially at a time of economic weakness, the heady days of hundreds of thousands of new workers entering the labor force may be over.

At first glance, the legal changes wrought by the welfare reform law appear so sweeping that it is difficult to imagine what could be left to reform. Indeed, there is little doubt that the 1996 welfare reform law represents the most substantial reworking of America's social safety net since the 1960s. Welfare recipients must work. Welfare recipients must exit the rolls after five years. Many noncitizens cannot receive welfare benefits. No one is legally entitled to cash from the welfare system. However, a closer look at the provisions of the welfare reform law reveals broad exceptions to each of these stipulations, making the law less sweeping than it appears.

Chart 4

Spending Per Recipient Soars

Real dollars



SOURCE: The Administration for Children and Families.

Recipients do face a five-year lifetime limit on welfare recipiency—but each state may exempt up to one-fifth of its welfare recipients from the ban if the state decrees those recipients to be hardship cases. Recipients no longer have an entitlement to cash assistance—but they continue to have an automatic right to food stamps and Medicaid, which form the majority of benefits for the typical recipient. And many legal residents are disqualified from receiving benefits—but not if they become U.S. citizens.

The work-requirement rule has the broadest set of exceptions. First, recipients are able to spend two years on the welfare rolls before they must work. Second, states may exempt up to half their welfare recipients from the rule. Third, states may calculate the maximum number of exemptions using either their current caseloads or their 1995 caseloads, which in practice allows some states to exempt almost every welfare recipient from the rule. Fourth, states may shift some of their welfare funds into a social services block grant, which can be given to recipients who do not meet work requirements. Finally, since states may define work to include many forms of education and training, even those recipients covered by the work-requirement rule need not work at anything resembling a private sector job to receive their cash grant.

Giving states discretion over these issues is not a problem in itself. Indeed, one of the greatest features of American democracy is that states act as laboratories of democracy, and many states have developed innovative ways to reach the targets set by the welfare reform law. However, since the amount of federal funding each state receives is partially determined by the extent to which it meets the welfare reform law's targets, states have a strong incentive to give numerous exemptions from the law's work requirements rather than encouraging recipients to work.

Some states, such as Wisconsin, have adopted innovative programs to encourage work. Others, such as Massachusetts—where only 9 percent of welfare recipients worked in 2001—have not. Statistical evidence indicates that welfare recipiency declined most sharply in states that strictly enforced the law's work requirements, which suggests that stricter limits on the use of exemptions would further reduce welfare recipiency. The question policymakers must now answer is whether states that do not wish to strictly enforce the law's provisions should be required (or encouraged) to do so.

What Happens Now?

Congress faces three possibilities for welfare reform. First, the welfare reform law could be strengthened to further reduce welfare recipiency, as discussed above. Second, the welfare reform experiment could be ended entirely and the system could return to the pre-1997 world in which needy families automatically receive benefits without federally imposed time limits or work requirements. Third, welfare reform could be retained as it currently stands, cementing the gains of the past five years without attempting to further reduce welfare recipiency.

In February 2002, President Bush released a welfare reform proposal that largely maintains the provisions of the 1996 law. Work requirements and time limits would remain, as would the restrictions on noncitizen recipiency and the non-entitlement status of cash welfare grants. Food stamps and medical care would remain entitlements, and funding would be maintained at current levels. States would retain much of the flexibility they currently possess.

However, the Bush plan would alter the 1996 law in at least two important ways. The first and most controversial is a proposal to implement stricter work requirements. States could exempt only 30 percent of their current caseloads (rather than 50 percent of their 1995 caseloads) from the work requirement. Also, the minimum hours a recipient must work would rise from 30 to 40, with 24 of those hours spent in a private sector or public sector job, and states would have less flexibility to define work. These changes would almost certainly reduce the welfare rolls still further, though with a weaker economy and a much smaller pool of welfare recipients, any further reductions would almost certainly not be as large as those achieved under the 1996 law.

The other main change from current law in the Bush plan is an effort to address the controversial issue of marriage. The welfare system currently provides a fiscal incentive to remain single because recipients can lose their benefits if they marry. To be sure, individuals base their matrimonial decisions on many factors other than the welfare system, so any marriage-related measures in the welfare reform law would be unlikely to have a very large effect on marriage rates. Still, while it seems clear that government should not compel anyone to marry, many observers believe it is appropriate for government to offset any unintentional bias the welfare system creates against marriage. As a first step, the Bush plan would allocate $300 million for as-yet-unspecified pilot programs to encourage marriage among welfare recipients.

At the time of this writing, the House has essentially approved the Bush proposal, while a Senate committee has approved something very close to the 1996 welfare reform law. The final version will likely fall somewhere in between, though a one-year extension of the 1996 law may be necessary while negotiators work out the details. Congress' action suggests that the broad policy prescription for the welfare system has been determined—the dramatic changes wrought by the 1996 law will continue in the years to come. What remains to be seen is how much further the 2002 law will go in reforming the welfare system—and reducing the welfare rolls.

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Notes

I would like to thank Anna Berman, Pia Orrenius and Alan Viard for their comments and assistance with this paper. Any remaining errors are my own.

1 Peter Edelman (1997), "The Worst Thing Bill Clinton Has Done," *Atlantic Monthly*, March, pp. 43–58.

2 Sen. Daniel Patrick Moynihan, quoted in "Senate Approves Welfare Overhaul," *USA Today*, Oct. 15, 1996, www.usatoday.com/elect/ep/epd/epdc053.htm.

3 "The New Welfare Law," Center on Budget and Policy Priorities, August 1996, www.cbpp.org/WECNF813.HTM.

4 The funding mechanism also moved from a per-recipient grant toward a flat $16.5 billion per year, divided among states on the basis of how much they received under AFDC. However, supplementary grants and other provisions can add to this amount, so funding levels actually vary somewhat from one year to the next. For example, TANF expenditures rose from $13.8 billion in 1998 to $18.3 billion in 2001 even though the statutory allocation in both years was $16.5 billion.

5 The study, "The Effects of Welfare Policy and the Economic Expansion on Welfare Caseloads: An Update," suggests the welfare-reform law and the strong economy each substantially reduced welfare rolls in the late 1990s.

6 These figures include job training and other expenditures on behalf of welfare recipients, as well as cash.

7 While former recipients with limited skills and work experience typically begin in low-wage jobs, their labor market prospects can be expected to improve over time.