

The Dynamic Effects of Time Limits in Welfare Reform

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During the late 1990s, an overhaul of the welfare system with time limits as a novel key component led to an unprecedented flow of single mothers from welfare to work. My dissertation is a single treatise on the short and long term effects of time limits on a variety of economic outcomes of single mothers.

Model I construct a finite-horizon dynamic optimization model of labor supply and multiple program participation, where time limits are summarizable as option values to welfare participation. The option value lowers the welfare reservation wage and increases the direct utility cost of welfare participation. The key to analyzing time limits is to identify the option values from exogenous variations in time limit policies and welfare eligibility horizons among individuals.

Estimation I estimate the model by simulation using monthly panel data from the SIPP for the years 1996 to 1999. The actual program formulas of TANF (welfare), Food Stamp, EITC and Federal taxes are used, thus permitting detailed counterfactual constructions of income. Welfare dependence is formalized by the welfare participation cost, which is determined by observable characteristics as well as an estimated random effects structure.

Results In both the short and the long runs, time limits reduce TANF and Food Stamp participation significantly, and increase labor supply and earnings slightly. There are no effects on the income of single mothers of all income levels.

The nonmonetary well-being from programs is computed from equivalent variation. It is defined as the deadweight loss plus the welfare participation cost. Initially, it is positive because some mothers yield direct utility from welfare participation. However, it diminishes quickly in the long run when they become ineligible for welfare due to hitting the limits.

There are large variations in welfare dependence. A considerable part comes from the unobserved permanent component. It is the most important factor in determining who are time-limit leavers, defined as those who eventually hit the limits.

Time-limit leavers work little and heavily participate in programs prior to hitting the limits. They do not react much to time limits until they hit, when their behavior change abruptly. In general, time limits have heavy disproportionate effects on highly welfare-dependent individuals.

Policy Implications If welfare-dependent individuals have severe barriers to work or other difficulties, time limits may have detrimental effects on them. Time limits should be implemented carefully with comprehensive support programs for the disadvantaged population. Although income is not affected, special attention should be directed to the deprivation of peripheral services valued by welfare recipients upon hitting the limits.