

Cash Is Better Than Food Stamps in Helping Poor

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Newt Gingrich has been castigated for referring to President Barack Obama as the “best food-stamp president in American history.” I, too, dislike the former House speaker’s inflammatory phrasing.

Yet I am also troubled by the more than \$100 billion designated for “food and nutrition” in the president’s 2013 budget. The current dominance of in-kind transfer programs, such as food stamps, Medicaid and housing support, relative to cash-based welfare programs, such as the Earned Income Tax Credit and Temporary Aid to Needy Families, is based on politics rather than economics. A consolidated cash-based program could more efficiently deliver assistance and more effectively encourage employment.

Redistribution has costs -- direct ones that are paid by taxpayers and indirect ones, by discouraging earnings and savings -- but it also has benefits, particularly by creating a society with less painful poverty.

The amount of redistribution that you think is appropriate depends on your attitudes toward inequality and paying for equality. I’m not a preacher, a philosopher or a politician, and I won’t try to convince you that the U.S. should do more or less for its poorer citizens. I am interested in a better-designed welfare system.

Path to Prosperity

We should ask for two things from any redistribution system. It should do as much as possible for society, especially the poor. It should do as little as possible to encourage permanent poverty. And, whenever possible, it should help poor Americans find a path toward self-sustaining prosperity.

The conventional economic logic is that cash transfers are more effective at helping the poor than in-kind gifts, such as food stamps and housing vouchers. I am grateful for the freedom I enjoy when spending my earnings; surely, aid recipients also like autonomy.

They can choose the spending that best fits their needs if they are given unrestricted income. In “Free to Choose,” this logic led Milton and Rose Friedman to argue for “replacing the ragbag of specific programs with a single comprehensive program of income supplements in cash.”

Yet over the past 40 years, in-kind programs have grown steadily more important than cash transfers. In 1968, the last year of Lyndon Johnson’s presidency, the federal government spent \$1.61 billion (\$10.5 billion in 2012 dollars) on Aid to Families with Dependent Children (the predecessor of Temporary Aid to Needy Families); it spent \$1.81 billion (\$11.8 billion in 2012 dollars) on Medicaid and \$505 million (\$3.3 billion in 2012 dollars) for food and nutrition assistance. There was no Earned Income Tax Credit or housing vouchers, so the ratio of in-kind aid to cash transfer was 3 to 2. The 2013 budget contains \$293 billion for Medicaid, \$112 billion for food and nutrition service (food stamps) and \$28 billion for tenant- and project-based rental assistance, which includes housing vouchers. That is a total of \$433 billion of in-kind transfers from these three primary programs.

By contrast, the budget includes only \$17 billion for the Administration for Children and Families (which administers Temporary Aid to Needy Families). The Earned Income Tax Credit paid out \$59.5 billion in 2010, and Obama’s proposal would eventually increase its generosity by about \$1.5 billion a year. Considering just these programs, the ratio of in-kind assistance to cash aid is now to 5.6 to 1. In 1968, the in-kind share of assistance was 60 percent; now it is 85 percent.

In-Kind Transfers

There are other programs that could be included in the mix, but they don’t change the basic picture of increasing reliance on in-kind transfers. If we added unemployment insurance as a cash transfer, we’d find that the in-kind share was 37 percent in 1968 and 74 percent in 2013. The current in-kind share would be higher if we excluded the legislative proposal for more generous benefits. Including other programs, such as the Federal Housing Administration, would increase the apparent share of spending going to in-kind transfers. Including the increased expenditures on disability insurance would do the most to limit the rising share spent on in-kind transfers, but that program isn’t means-tested and isn’t designed to fight poverty per se.

Given the economic case for providing cash, is there a good argument justifying the rise of in-kind benefits? Recent advances in behavioral economics illustrate the imperfections of human decision-making, which might seem to create a rationale for some government paternalism, such as efforts to control the spending habits of aid recipients. For example, a recent Florida bill proposes restricting the use of food stamps to purchase candy and soda. But understanding the limits of human rationality doesn't lead naturally to an increased faith in public-sector control. After all, governments are made of people and are subject to psychological quirks. I've argued that governments, which have only limited incentives to get things right, may make far more mistakes than ordinary consumers. Given the prevalence of obesity among poorer Americans, it's hard to see the sense in pushing the poor to spend more on food, except that this spending satisfies agricultural advocates.

A somewhat better rationale for in-kind transfers is that we are trying to get parents to spend more on services that will help their children. Both food stamps and housing vouchers can be seen as tools for pushing intra-household redistribution from poor parents to their children. Yet the Moving-to-Opportunity experiment, which used random trials to evaluate housing vouchers, found that such assistance made parents happier but did little to improve long-run outcomes for children. The childhood obesity problem should also make us wonder whether food stamps are really good for kids.

Aid Abuses

Perhaps the best explanation for the rise in in-kind transfers is that taxpayers care about how aid recipients use their money. Economists can argue for the value of freedom until they are blue in the face, but there will always be a scandal when public aid, such as the debit cards issued after Hurricane Katrina, is spent at strip clubs.

Vilification of welfare recipients makes it particularly hard to make the case for entrusting them with unrestricted cash, even if that is the most effective means of administering aid. But the added cost of relying on in-kind transfers is that, unlike our cash-based programs, these efforts are rarely well- designed to limit the adverse incentives that come from anti-poverty programs. Any assistance program that channels aid to people who earn less creates an incentive to work less hard. Any aid that is asset-tested destroys the incentive to accumulate capital.

Well-designed programs, such as the Earned Income Tax Credit, do as much as possible to limit these negative incentives and even create some positive effects. That credit initially increases with earnings, creating an incentive to go to work; benefits taper off slowly, which limits the tendency to work too little. The design is smart, and the program seems to have encouraged employment substantially. The 1996 welfare reform that produced Temporary Aid to Needy Families was also aimed at creating better incentives for employment.

By contrast, food stamps and Medicaid (USBOMDCA) are more like old- style welfare systems that create strong incentives to earn less. To get food stamps, you typically need to have less than \$2,000 in assets, so recipients are pushed to save nothing.

Although food stamps typically require recipients to be employed, every extra dollar of “net income” reduces the benefit by 30 cents. Housing vouchers require recipients to earn less than 50 percent of median income in their area, and the voucher amount also decreases by 30 cents as income increases by a dollar. A family that gets both food stamps and a housing voucher loses more than 50 percent of each extra dollar earned in the form of reduced benefits. Medicaid (USBOMDCA) benefits, likewise, disappear with significant income or assets.

Perverse Incentives

The proliferation of in-kind programs leads aid recipients to spend on things that they value less and creates perverse incentives to earn less and save little. The problem with food stamps isn't that we are giving too much to the poor.

I'd prefer a more robust welfare state, especially when it comes to caring for disadvantaged children. Unfortunately, we are giving money in fragmented, poorly coordinated programs that do little to target aid efficiently or induce better economic outcomes.

There is a natural solution: Combine our disparate aid efforts into a single program that delivers cash assistance and minimizes perverse incentives. We may still want some in-kind assistance, particularly for health care, and that could be handled by issuing vouchers. But for most aid, the Friedman solution of cash still seems right. By combining our aid programs and primarily giving cash, we can have a more efficient welfare system that provides more freedom and better incentives for aid recipients.