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Welfare Reform and Opportunity in the Low-Wage Labor Market

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One measure of opportunity in any society is its ability to provide jobs for everyone who wants to work. With the enactment of welfare reform in 1996 this issue has taken on new salience. This brief addresses whether enough jobs are available for all those who are thrust into the labor market by welfare reform, whether former welfare recipients can compete successfully for those jobs, and—if they do find jobs—what their chances are of ever earning enough to become self-sufficient.

We conclude that in today's strong economy many welfare recipients are successfully making the transition from welfare to work. Recent job growth and tougher welfare policies together have pulled and pushed into the job market many of those who would otherwise have remained dependent on government assistance. In the future, however, if the economy slows, the push may become stronger than the pull, and we could see as many as 100,000 to 150,000 additional new workers per year competing for a less rapidly growing number of jobs. Almost regardless of the state of the economy, the most disadvantaged are likely to encounter real difficulties in securing steady employment.

Most of those who are able to find full-time employment should stay above the poverty line with the help of subsidized child care and other government assistance (such as the Earned Income Tax Credit and food stamps). And opportunities do exist for low-wage workers to move up the economic ladder rather quickly. But given their characteristics, many former welfare recipients who find entry-level jobs are unlikely to experience this upward mobility.

The economy can produce a sufficient number of jobs to accommodate welfare recipients entering the labor force . . . but some welfare recipients are likely to encounter difficulties in securing steady employment and many are unlikely to move up the economic ladder.

Are Jobs Available?

With the unemployment rate in mid-1997 at its lowest level in 24 years, it is hard to argue that jobs are not available. The economy has been generating an average of almost two million new jobs a year since 1983, and the proportion of working-age adults in jobs has reached an all-time high. In the process, millions of new entrants—including baby boomers, immigrants, and women returning to work—have been absorbed into the labor force.

The pace of job creation has been particularly strong in the last four years. Between April 1993 and April 1997, the economy generated almost 10 million new jobs, allowing the unemployment rate to fall from 7.1 percent to 4.8 percent even as the number of persons working or looking for work was growing by 6 percent. This job growth has benefited everyone, including the poorest, the least educated, and the least skilled.[1] Welfare reform, in short, could not have come at a better time.

But how many new workers are there likely to be in total because of welfare reform, and can the economy absorb the influx? Our analysis suggests the new law is likely to add over 800,000 new workers between 1997 and 2002—roughly 140,000 per year, on average (see sidebar for details). Compared to the projected growth of the labor force over this same period—which, at 1.4 million a year, is more than 10 times as great—140,000 is a relatively small addition. And if the demand for workers continues to grow as rapidly as it has over the last decade (about 2 million per year), the economy can easily produce a sufficient *number* of jobs to accommodate welfare recipients or other low-skilled workers entering the labor force.[2]

Even if the entry of these new workers is not accompanied by *any* adjustment in total demand for workers (to accommodate the new influx)—so that all of those entering the labor force as a result of welfare reform remain unemployed (or displace other workers into joblessness)—the overall unemployment rate will rise by less than a tenth of a percentage point each year (one-half a percentage point cumulatively over six years).[3] In particular areas of the country, the task of absorbing recipients into the local labor market will be more challenging, however, because the ratio of recipients to jobs is much higher in some communities than others.[4]

If and when the economy enters a recession, of course, the picture will change. The number of jobs will grow more slowly, if at all, and depending on how states react, more people will become jobless and/or the welfare rolls will swell.[5]

Will Welfare Recipients Be Able to Compete for the Available Jobs?

Even if plenty of jobs are available, new entrants with few skills and little exposure to the world of work will not

How many new workers will welfare reform add to the labor force?

Under the new welfare law, states are likely to put increasing pressure on recipients to leave welfare for work for at least three reasons: (1) the difficulties of serving a potentially growing caseload with a fixed-dollar federal block grant; (2) requirements that states place an increasing proportion of eligible recipients in approved work activities (which include taking a job); and (3) a five-year time limit on federally funded assistance for any individual.

Most attention has focused on time limits. However, states can always choose to use federal monies to support short-term recipients, freeing up their own funds to support individuals on the caseloads longer than five years. If most states choose this option, the other two factors—generalized fiscal pressures associated with the block grant and increasingly stringent work requirements—are likely to have even more influence on state efforts to move recipients toward self-sufficiency.

The work provision mandates that 25 percent of eligible recipients in one-adult families participate in approved work activities in 1997. The required percentage increases by 5 percentage points each year, reaching 50 percent by 2002. Participation requirements among two-parent families are significantly higher—75 percent in 1997, increasing to 90 percent in 1999 and thereafter. The financial penalties for failing to meet these requirements are significant and the political costs may be even greater.

Meeting such stringent work requirements would be very difficult for most states if it were not for a provision of the law that counts any decline in a state's welfare caseload since fiscal year 1995 toward the participation requirement. Although states are not allowed to change eligibility rules to meet their targets, they can make other changes—such as instituting tougher work requirements for individual recipients, imposing sanctions for noncompliance with these or other requirements, imposing shorter time limits, or taking other measures that will ensure that fewer people apply for, or remain on, welfare.

Because welfare caseloads have already declined by 800,000 households since 1995, most states are expected to meet their work participation targets for 1997—at least for single-parent families, who make up 90 percent of the nonexempt caseload. The challenge for future years will be to either reduce caseloads or increase enrollments in work activities by about 5 percentage points more each year. Either way, most of those so affected will represent net additions to the labor force and will count toward meeting the targets.[a]

Assuming that (1) the average fiscal year 1997 monthly caseload falls to 4.0 million and then increases slowly in later years, and (2) all states just meet the participation requirements for both types of families, our calculations indicate that net additions to the labor force will average 139,000 additional workers per year, or a total of 832,000 workers over the six years from 1997 to 2002. The impact on the labor market is likely to be highest in the first year (due in good part to the stringent participation requirement for two-adult families). If some states do better than their targets and hardly any do worse, the net annual increases would exceed 139,000. Conversely, if a number of states fail to meet the targets—which is most likely to happen for the two-parent family requirements—the number would be lower. More detailed calculations are available from the authors (by sending an e-mail to dmcmurre@ui.urban.org).

a. Because a large proportion of welfare recipients are already working but not reporting it to the authorities, some of the additions to the workforce will be "statistical" rather than "real." Kathryn Edin and Laura Lein (*Making Ends Meet*, New York: Russell Sage Foundation, 1997, p. 181) estimate that up to 40 percent of welfare recipients work without reporting it (although not all of these individuals are working sufficient hours to count as "working" under the new welfare law).

necessarily be able to compete successfully with other workers for these jobs. The likelihood is that some will find jobs whereas others will not.

One piece of evidence suggesting that many recipients are employable is the sharp drop in caseloads between January 1994 and January 1997. Almost one million recipients disappeared from the rolls. We don't know for sure how many actually found jobs—some may have already had jobs that they had not reported to the welfare system, some may have turned to other sources of income, some may simply have become poorer[6]—but the strong implication is that a greater reliance on work was at least part of the story for these individuals.

To be sure, much of this decline in welfare receipt can be attributed to the expansion of the economy and only confirms what has long been known. Strong labor markets create opportunities for everyone, including the least skilled. However, new welfare rules at the state level (which include more work requirements, tougher sanctions for not complying with these requirements, and time limits for welfare recipients) have also contributed to the drop.[7] These rule changes have discouraged people from coming onto the rolls as well as encouraged those already on to leave.

So, the experience of the past few years suggests that—when pulled by a strong economy and pushed by new welfare rules—at least some of the unskilled can find work.

The bad news is that those who remain on welfare are going to be an increasingly disadvantaged group, made up disproportionately of those least likely to succeed in the job market. Once the more job-ready recipients have found work, states will have to dig deeper into the caseload, where they will find a higher proportion of persons who are sick, addicted to alcohol and drugs, or functionally illiterate.[8] Pressure to push these hard-to-employ individuals into jobs—which is already substantial because of the new law—will become even greater as they begin to exceed the five-year federal time limit on welfare receipt.[9] States will then need to choose between supporting such individuals with their own funds or pushing them into a job market where they are more likely to sink than swim.

These very disadvantaged recipients may be unable to find a job—any job. Employment opportunities for unskilled workers in some areas are limited, and even where such opportunities exist, employers are not willing to hire those who do not meet certain minimum standards. For example, some inner-city residents report difficulties in obtaining even entry-level, minimum-wage jobs in the fast food industry, while inner-city employers simultaneously complain that they cannot find qualified applicants even for jobs that require relatively few skills.[10] Tight labor markets may cause employers to relax their hiring standards, but cannot entirely solve this problem.

Overall, then, welfare reform is likely to have mixed effects. Many welfare recipients appear to be finding work in today's strong economy, but others will almost certainly encounter serious difficulties. The cumulative effect will depend in large part on the state of the economy and on the success of efforts to train and place low-skilled workers in available jobs. Such efforts have had only modest success in the past, but at the margin they can make a difference.[11]

Welfare recipients are not the only ones who will be affected by welfare reform. Other low-skilled workers will face greater competition for available jobs and may suffer increased joblessness as well. In addition, the increased competition for jobs is almost certain to depress earnings at the low end of the scale.

Table 1
Earnings of Current or Former AFDC Female Recipients, Various Studies and Years

Study	Data Source	Sample	Actual Wage Rate/Earnings (1996 Dollars)[a]	"Potential" Earnings If Working Full-Time, Year-Round (1996 Dollars)
Burtless (1995)	National Longitudinal Survey of Youth	Received AFDC sometime between 1979–81 and had earnings	\$7.00/hour in 1979 \$7.77/hour in 1990 \$4,538/year in 1980 \$11,575/year in 1990	\$14,000 in 1979 \$15,540 in 1990
Harris (1996)	Panel Study of Income Dynamics	Exited welfare sometime between 1983–88, estimated earnings	\$8.00/hr at exit \$7.78/hr after 12 mo. \$7.74/hr after 24 mo. \$8.04/hr after 36 mo.	\$16,000 at exit \$15,560 at 12 mo. \$15,480 at 24 mo. \$16,080 at 36 mo.
Meyer and Cancian (1996)	National Longitudinal Survey of Youth	Received AFDC between 1979–87 and had earnings	\$6,087 1st year after exit \$9,900 5th year after exit	N/A

Source: Urban Institute 1997, based on references cited in full in end notes 12 and 13.
a. Real earnings for female workers at the 20th percentile of the earnings distribution (which are roughly comparable to the earnings of former welfare recipients, based on analysis of AFDC recipients and workers at 25th percentile in Burtless 1995, p. 80) declined at an annual rate of 0.3 percent between 1989 and 1995 (Lawrence Mishel, Jared Bernstein, and John Schmitt, *The State of Working America 1996–97*, Washington, D.C.: Economic Policy Institute, 1997). We adjusted earnings for this annual rate of decline, and then adjusted them for inflation.

How Much Will the Jobs Pay?

Studies that have examined the earnings of those who were, at one time, on welfare provide some insight into the likely earnings prospects of current welfare recipients. They suggest that former welfare recipients earn \$7.00 to \$8.00 per hour (in 1996 dollars) during their first year after exiting welfare and receive, on average, very low annual wage increases. (Table 1 summarizes the study results.[12] Even though the numbers have been adjusted to account for the recent decline in real earnings for low-wage workers, they may still overstate the earnings prospects of current welfare recipients. This is because those who went to work in the past did so voluntarily and were probably more job-ready than many current recipients.)

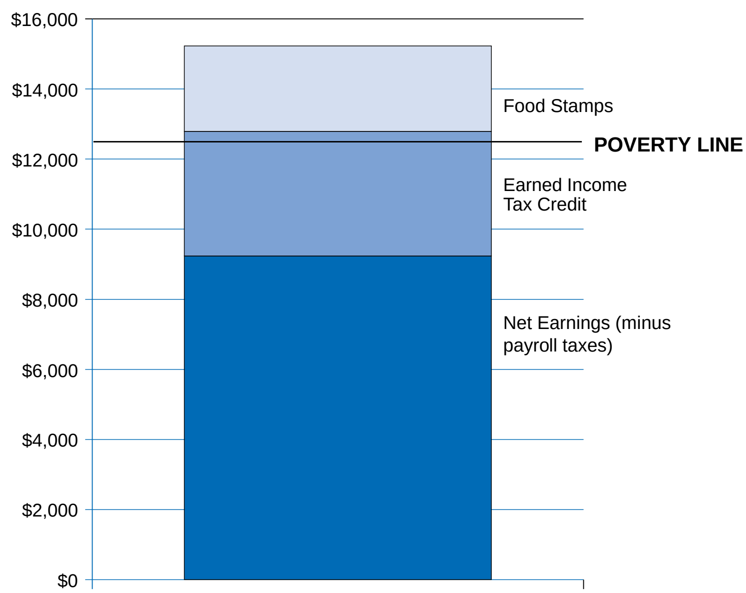
If former recipients were to work full-time, year-round at these wage rates, their earnings would be between $14,000 and $16,000, which is higher than the 1996 poverty line of $12,600 for a mother with two children. *Actual* annual earnings for such workers, however, are significantly lower than the poverty line, due to the low number of hours worked by such mothers. Their actual earnings are typically between $9,000 and $12,000 (or between 70 and 95 percent of the poverty line).[13]

The earnings of low-wage workers are often supplemented by other government programs, notably the Earned Income Tax Credit (EITC) and food stamps. For example, a mother with two children who earned $10,000 per year in 1996 (slightly less than a full-time, year-round worker would earn after the new minimum wage of $5.15 per hour is fully implemented) would also qualify for $3,556 from the EITC and about $2,400 in food stamps. Payroll taxes would reduce earnings by $765. All told, such a worker would have a total income of just over $15,000—before child care and other expenses and after the deduction of the payroll tax (chart 1).[14]

Thus, former welfare recipients who are able to find full-time, year-round employment are not likely to be poor. However, child care expenses or the need to reduce hours of work in order to provide such care oneself complicate the picture. On the assumption that former recipients pay the average $3,000 per year in child care expenses incurred by single mothers who work,[15] the incomes they would have available to spend on other needs would fall below the poverty line. For mothers able to get subsidized care, incomes would be commensurately higher.

Chart 1

Income, Including Earnings, Taxes, and Government Transfers, for Mother of Two Earning $10,000 per Year and Not Receiving Welfare Benefits, 1996



Source: Committee on Ways and Means, *1996 Green Book.*
Note: Food stamp amount will change minimally due to the 1996 legislation.

How Difficult Will It Be to Move up the Job Ladder?

The long-term prospects of those on welfare will depend on their ability to move up the economic ladder. Many workers in low-wage jobs do indeed move up into steady and better-paying employment, often do so relatively rapidly, and usually remain in a good job thereafter.[16] This suggests that significant opportunities to move up continue to exist in the low-wage labor market as a whole, although there are signs that this upward mobility is declining.[17]

Many former welfare recipients, however, are likely to encounter difficulties in taking advantage of these opportunities.[18] Although many workers in low-wage jobs do move up the economic ladder, another large segment of low-wage workers remains in such jobs for extended periods with little or no increase in pay. The characteristics of these workers resemble those of many former welfare recipients, as they are disproportionately less educated, female, and minority.

Thus, opportunities to move up continue to exist for some workers in the low-wage labor market, but they may be becoming more narrowly available. And many former welfare recipients who do succeed in obtaining low-wage work may have particular difficulty moving up the job ladder.

Notes

1. Between 1993 and 1995 (the most recent available data), household income growth was greatest for the lowest fifth of the income distribution. Council of Economic Advisors, *Economic Report of the President 1997.*

2. There have been only three years since 1980 when employment didn't increase by at least one million new jobs per year.

3. The potential impact on the unemployment rate from welfare recipients entering the labor market was calculated by applying the following official projections: (1) the Office of Management and Budget (OMB) projects that the unemployment rate, if there had been no welfare reform, would have been 5.5 percent in 2002 (OMB, *Analytical Perspectives: Budget of the United States Government,* 1997), and (2) the Bureau of Labor Statistics projects that the labor force growth rate, if there had been no welfare reform, would have been 1.1 percent annually through 2005 (Howard N. Fullerton, "The 2005 Labor Force: Growing, but Slowly," *Monthly Labor Review,* November 1995:29–44).

4. The ratio of welfare cases to the number of jobs differs substantially from one community to another. For example, in the middle of 1996, the ratio was about 1 percent in Indianapolis, 4 percent in the District of Columbia, and 9 percent in New York City.

5. Former welfare recipients who have gained sufficient previous job experience will be eligible for unemployment insurance.

6. A recent study by Mathematica Policy Research ("Iowa's Limited Benefit Plan," 1997) found that, among workers in Iowa who had been cut off the welfare rolls, most individuals found some way—either through informal means of support such as family or friends, or through legal or illegal work—to make ends meet. About half reported incomes higher than or equal to their welfare benefits, while the other half experienced a decrease.

7. The Council of Economic Advisors (CEA) finds that almost one-third of the decline is related to these state rule changes. CEA, "Explaining the Decline in Welfare Receipt, 1993-1996," May 1997.

8. Krista Olson and LaDonna Pavetti, *Personal and Family Challenges to the Successful Transition from Welfare to Work,* Urban Institute, 1996.

9. Up to 20 percent of the caseload may be exempted from the five-year federal time limit, at state option.

10. Katherine Newman and Chauncy Lennon, "Finding Work in the Inner City: How Hard Is It Now? How Hard Will It Be for AFDC Recipients?" Russell Sage Foundation Working Paper No. 76 (1995); and Harry Holzer, *What Employers Want,* New York: Russell Sage Foundation (1996).

11. Robert LaLonde, "The Promise of Public Sector-Sponsored Training Programs," *Journal of Economic Perspectives* 9:149-168 (1995); Larry L. Orr et al., *Does Training Work for the Disadvantaged Worker?* Urban Institute (1995); Dan Bloom, *After AFDC: Welfare-to-Work Choices and Challenges for States*, Manpower Demonstration Research Corporation (1997); and Demetra Smith Nightingale, "Work-Related Resources and Services: Implications for TANF," *New Federalism: Issues and Options for States*, Series A, No. A-7, Urban Institute (April 1997).

12. These data are for individuals who had earnings. They are drawn from Gary Burtless ("Employment Prospects of Welfare Recipients," in Demetra Smith Nightingale and Robert Haveman, eds., *The Work Alternative: Welfare Reform and the Realities of the Job Market*, Washington, D.C.: Urban Institute Press, 1995), who studied 10 years of wage rates and earnings for women who had received AFDC sometime between 1979; and from Kathleen Mullan Harris ("Life after Welfare: Women, Work, and Repeat Dependency," *American Sociological Review* 61:407-426, 1996), who studied 3 years of wage rates for women who exited welfare sometime between 1983 and 1988.

13. Earnings estimates are based on data from Burtless (1995); Daniel R. Meyer and Maria Cancian ("Life after Welfare: The Economic Well-Being of Women and Children Following an Exit from AFDC," University of Wisconsin Institute for Research on Poverty, Discussion Paper No. 1101-96, 1996); and Mathematica Policy Research (1997), which finds weekly earnings of $170 (or $8,840 if year-round) for individuals in Iowa who were recently cut off of benefits. All data are for workers with earnings, and are reported in 1996 dollars after adjusting for declines in real earnings for low-wage workers over this period. See table 1 for more details.

14. Committee on Ways and Means, *1996 Green Book* (U.S. Government Printing Office, 1996, p. 399). The food stamps estimate does not take into account changes in the food stamps law, which will have only minimal effects on the level of benefits for this worker in 1997.

In addition, many welfare families will be able to draw on housing assistance and/or child support payments. The *Green Book* reports that, in 1994, about 30 percent of AFDC households received housing benefits averaging about $2,650 per month. Further, although only about 5 percent reported receiving child support while on AFDC, improved incentives to obtain child support, more efficient procedures to establish paternity, and tougher enforcement tools are likely to increase the role of child support as an income source for employed former welfare recipients.

15. Calculated in 1996 dollars, using average expenditures for single mothers and assuming 40 hours of child care per week. Sandra Hofferth, April Brayfield, Sharon Deich, and Pamela Holcomb, *National Child Care Survey, 1990*, Urban Institute (1991), p. 136.

16. See Ralph Smith and Bruce Vavrichek, "The Wage Mobility of Minimum Wage Workers," *Industrial and Labor Relations Review* 46:82-88 (1992); Congressional Budget Office (CBO), "In Pursuit of Higher Wages and Employment-Based Health Insurance," CBO Memorandum (1993); and LaDonna Pavetti and Gregory Acs, "Moving Up, Moving Out, or Going Nowhere? A Study of the Employment Patterns of Young Mothers and the Implications for Welfare Reform," Urban Institute (1996 draft).

17. For example, earnings are rising more slowly for low-wage workers as they gain experience. See Rebecca Blank, "Outlook for the U.S. Labor Market and Prospects for Low-Wage Entry Jobs," in Nightingale and Haveman (1995).

18. See Burtless (1995).

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