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# Public Spending on Income-Tested Social Welfare Programs for Investment and Consumption Purposes

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*The Clinton administration contends that public spending for investment should be increased, but public spending for consumption should be decreased. This article reports findings from a study that investigated the trend in public spending from 1975 to 1992 for social welfare programs that are targeted to low-income families and individuals. The study found that public spending for social welfare programs for investment purposes declined generally during that period and public spending for consumption purposes increased primarily because of the increase in medical benefits.*

The Clinton administration has established a new priority in public spending: investment in human capital over consumption. That is, the administration is advocating new spending to develop or expand programs that are designed to invest in future generations of Americans, such as Head Start, a new program of national service, and a time-limited training program for welfare mothers. The corollary to this new priority is the administration's willingness to scale down public spending for "consumption" that is represented by many entitlement programs, such as Medicaid, Aid to Families with Dependent Children (AFDC), food stamps, and housing.

Having won a big electoral victory in the 1994 national election, many members of the Republican Party intend to implement "Contract with America." Among the pledges in the contract is the cut back in public spending for welfare programs for both investment and consumption purposes. Thus, the battle between the administration and Republican-dominated Congress revolves around what to do with the programs for human capital investment. Clinton believes that the federal government should

increase its spending on social welfare programs designed to enhance human capital. The Republican Party seems to believe that all social welfare spending should be cut back.

With the foregoing discussion as a backdrop, this article analyzes the patterns of public spending for low-income families and individuals during the past 18 years. Has public spending for investment purposes increased and, if so, what types of programs are responsible for such an increase? If not, why not? Likewise, has public spending for consumption purposes increased and, if so, what types of programs are responsible for such an increase? Is there a relationship between the two types of spending? That is, has public spending for consumption purposes increased to the detriment of public spending for investment purposes? Finally, which type of public spending has changed in tandem with the rise and fall in the poverty rate?

To shed light on these questions, the author investigated the trend in U.S. public spending for income-tested social welfare programs. As of 1992, some 80 publicly provided social welfare programs were targeted to low-income families and individuals (for a list of these programs, see Appendix 1). According to the categories set by the Congressional Research Service (1993), an organ of the Library of Congress, 17 programs were related to educational benefits, 8 were related to social services, 7 were related to jobs and training aid, 9 were related to medical benefits, 11 were related to cash aid, 11 were related to food benefits, 15 were related to housing benefits, and 2 were related to energy aid. Broadly conceived, these programs constitute "welfare programs" in the United States.

#### Source of Data and Methodology

The data used for the analysis presented here were provided by the Congressional Research Service (1993). I categorized publicly provided social welfare programs with income testing into two groups: those for investment purposes and those for consumption purposes. Programs for investment purposes provide educational benefits, jobs and training aid, and social services. Programs for consumption purposes provide medical benefits, cash aid, housing benefits, and energy aid. Expenditures for some

types of medical care, such as prenatal care and medical care for children, may be considered an investment, whereas others, such as intensive care for the terminally ill and medical care for the elderly, may be thought of as consumption. However, in this article, all public spending for medical benefits for low-income people is considered consumption, in line with the Clinton administration's view and its willingness to trim public expenditures for Medicare and Medicaid (Birnbaum & Harwood, 1993).

In this article, the term *spending* means public spending and includes both federal and state-local spending, and all expenditures are expressed as a percentage of the gross domestic product (GDP). Measuring the expenditures for income-tested social welfare programs as a share of the GDP is appropriate because the GDP encompasses population growth, as well as economic growth, and this method of measuring expenditures automatically takes care of the fluctuation in prices. As was mentioned, all programs analyzed in this article have income testing and thus target their benefits to low-income families and individuals.

To investigate the relationship between public spending for investment purposes and for consumption purposes on the one hand and the poverty rate on the other hand, Pearson Product-Moment correlation coefficients were obtained. Similarly, to investigate whether public expenditures for investment purposes and for consumption purposes are related, a Parson Product-Moment correlation coefficient was obtained.

### Public Spending for Income-Tested Programs in the Aggregate

#### *All Programs*

The total outlay for income-tested social welfare programs increased 106 percent from \$140.7 billion in 1975 to \$289.9 billion in 1992—in 1992 dollars (Congressional Research Service, 1993).

Figure 1 plots the percentages of the GDP spent for the programs for investment purposes and those for consumption purposes, as well as for all programs. The poverty rates for the years 1975 through 1992 were also plotted. As Figure 1 shows, the total outlay for the income-tested social welfare programs was 3.40 percent of the GDP in 1975 and increased to 4.01 percent in 1981. But in 1982, it started to decline, reaching the low point of

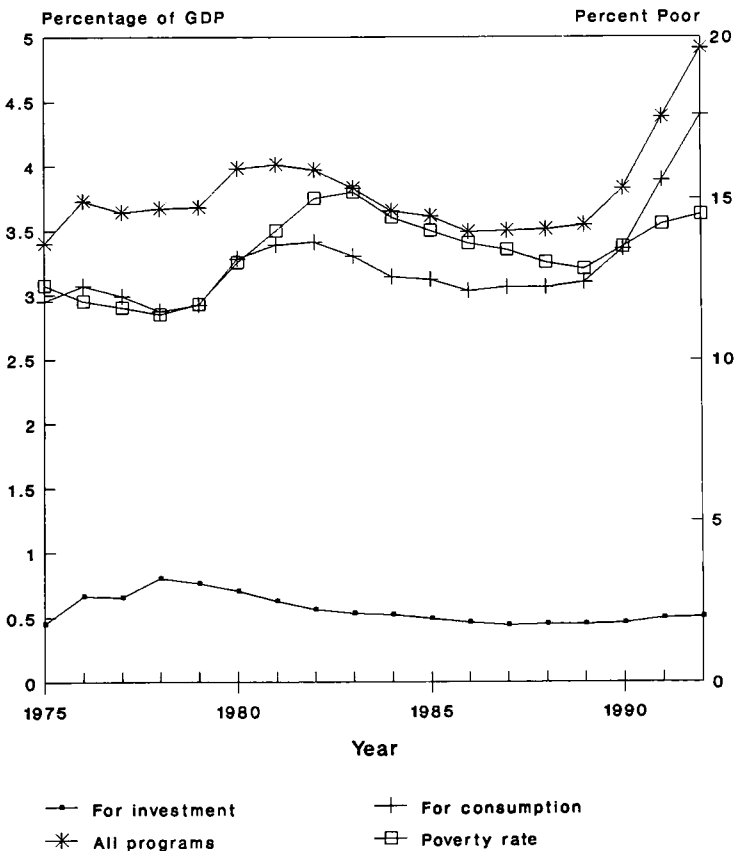
3.50 percent in 1987. Since then, it increased steadily to reach the highest point of 4.91 percent in 1992. All told, the expenditures for all programs increased from 3.40 percent of the GDP in 1975 to 4.91 percent in 1992—or a 44.4 percent increase.

*Programs for Investment Purposes*

The outlay for the programs for investment purposes increased steadily until 1978, when the expenditures abruptly

Figure 1

*Expenditures for Income-Tested Programs for Investment and Consumption*



dropped. Since 1978, the outlay for these programs consistently declined until 1987, when it resumed climbing. Thus, in 1992 it was 0.51 percent of the GDP, compared with 0.45 percent in 1975.

More important, perhaps, is that the outlay for the programs for investment purposes was never high in any year. Public spending has been well below 1 percent of the GDP for all programs in the areas of education, jobs-training, and social services for low-income families and individuals.

The expenditures for these programs were correlated inversely with the poverty rate; the Pearson Product-Moment correlation between the two variables was  $-0.523$  ( $p < 0.05$ ). This means that when the poverty rate was high, the level of expenditures tended to be low.

#### *Programs for Consumption Purposes*

Figure 1 shows that the outlay for the programs for consumption purposes fluctuated between the low of 2.87 percent of the GDP in 1978 and the high of 4.40 percent in 1992. It is interesting that during the Reagan-Bush era (1981–92), the average percentage of the GDP spent for these programs was higher (3.36 percent) than the average during the Carter era (1977–80), which was 3.02 percent.

The outlay for the programs for consumption purposes tended to follow the trend in poverty rates; the Pearson Product-Moment correlation between the two variables were 0.598 ( $p < 0.01$ ). This means that when the poverty rate was high, the level of expenditures also tended to be high.

The increase in medical benefits accounts for the statistically significant relationship between the outlay for consumption purposes and the poverty rate. The Pearson Product-Moment correlation between the public spending for medical benefits and the poverty rate was positive and significant (0.535;  $p < 0.05$ ), but the correlation between the poverty rate and public spending for consumption purposes, excluding medical benefits, was not significant.

Was there a relationship between the expenditures for investment purposes and the expenditures for consumption purposes? The answer is no. The Pearson Product-Moment correlation was not significant.

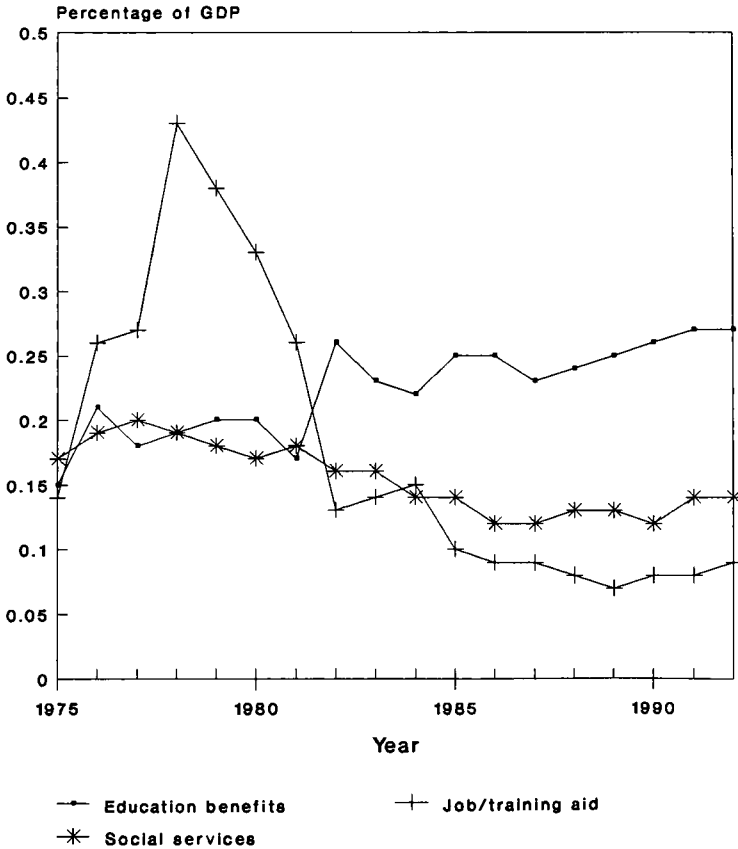
Public Spending for Specific Sectors of Income-Tested Programs

*Programs for Investment Purposes*

The trend in expenditures for investment purposes masks the extremely volatile nature of expenditures for specific sectors of programs for such purposes.

Figure 2

*Expenditures for Income-Tested Programs for Investment*



*Job and Training Aid.* The most volatile expenditures are for the sector of jobs and training aid. The outlay for such purposes hit the high of 0.43 percent of the GDP in 1978, but then steadily and drastically decreased. Thus, in 1992, only 0.09 percent of the GDP was spent for programs for jobs and training. This volatility reflects, in part, the shift in federal policy on jobs and training. The enactment of the Comprehensive Employment and Training Act (CETA, P.L. 93-203) in 1973 greatly increased federal funding to retrain and place long-term unemployed, inefficiently employed, or disadvantaged people in largely public-sector service jobs. But CETA quickly became unpopular and hence the budget for it was cut. The Reagan administration replaced CETA with the Job Training Partnership Act of 1982 (JTPA, P.L. 97-300), which included Training for Disadvantaged Adults and Youth, the JOB CORPS, and the Summer Youth Employment Program. With JTPA, the strategy changed from training structurally and cyclically unemployed people for public-sector service jobs to training them for private-sector jobs (DiNitto, 1991). But the scope of these programs was scaled down year after year during the Reagan and Bush administrations (U.S. House of Representatives, 1992, p. 1692). Also, the decade of 1975–1985 saw a steady decline in public spending for the Work Incentive Program (WIN) from \$750 million in 1975 to \$400 million in 1985, in 1992 dollars (U.S. Office of Management and Budget, 1992). The implementation of the Jobs Opportunities and Basic Skills (JOBS) Training program, which replaced WIN, provided under the 1988 Family Support Act, no doubt will increase public spending for jobs and training in the future. However, it will take some years for the JOBS program to make a difference. Although Congress appropriated federal matching funds of \$600 million for 1989, \$800 million for 1990, and \$1 billion for 1991, 1992, and 1993 for this program, many states failed to take full advantage of these funds because they could not raise enough money for their own 10-percent matching funds, required under the law (Burke, 1993). As a result, in 1993, for example, only \$646.6 million of the \$1 billion available federal matching funds were used (U.S. House of Representatives, 1994 pp. 342 and 349).

*Social Services.* The declining outlay (from 0.17 percent of the GDP in 1975 to 0.14 percent in 1992) for social services stemmed



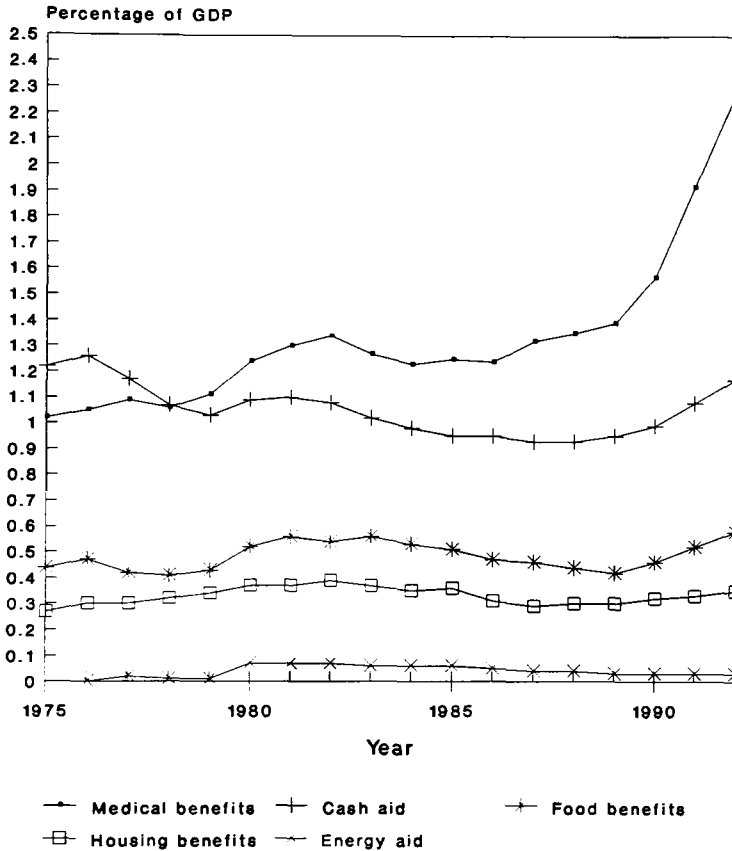
from the founding structure established for the Social Service Block Grant (Title XX) and the Community Services Block Grant—two dominant programs in the area of social services. The Social Service Block Grant had a funding cap of \$2.7 billion for 1984–88 and of \$2.8 billion for 1989 and subsequent years. Thus, the total outlay was not adjusted for inflation or economic growth, and, therefore, the spending for the Social Service Block Grant not only eroded in value, but lagged far behind the growth in the economy. The same declining trend can be observed in the funds for the Community Services Block Grant. Congress appropriated a declining amount of federal funds each year, in real terms. For example, the appropriation for 1990 was \$396.8 million, or 20 percent lower than that for 1982 (Spar, 1990). Hence, both types of grants eroded in real value over time.

*Educational Benefits.* As Figure 2 shows, the only bright spot is seen in public spending for programs for educational benefits, which rose from 0.15 percent of the GDP in 1975 to the record 0.27 percent in 1992. The Head Start program continued to be popular, with annual enrollments and expenditures increasing year after year (U.S. House of Representatives, 1992, p. 1696). Other educational benefits programs, such as Stafford Loans (formerly called Guaranteed Student Loans), Pell Grants, the College Work-Study Program, Supplemental Educational Opportunity Grants, and Vocational Education Opportunities, were popular in Congress throughout the 1980s.

#### *Programs for Consumption Purposes*

*Medical Benefits.* What is so striking about the trend in public spending for income-tested social welfare programs for consumption purposes is the rapid upward movement in the expenditures for medical benefits—from 1.02 percent of the GDP in 1975 to 2.27 percent in 1992. This trend strongly reflects the increasing expenditures for Medicaid—the major program in this sector of social welfare programs. There are three major reasons for the growth in Medicaid. First, the unit price for medical care has increased faster than the Consumer Price Index (U.S. Bureau of the Census, 1994, p. 488). Second, new groups of persons who are not directly linked to the cash assistance programs have become

Figure 3

*Expenditures for Income-Tested Programs for Consumption*

eligible for Medicaid. The Omnibus Budget Reconciliation Act of 1986 (P.L. 99-509) allowed states to cover pregnant women and young children and/or aged and disabled persons who meet state-established income standards as high as 100 percent of the poverty threshold. The Omnibus Budget Reconciliation Act of 1987 (P.L. 100-203) further expanded states' options by allowing the coverage of pregnant women and children up to age 1

with incomes of less than 185 percent of the poverty thresholds. Moreover, the Omnibus Budget Reconciliation Act of 1987 required states to cover pregnant women and children up to age 6 with incomes under 133 percent of the poverty thresholds. Third, Medicaid is increasingly being used to pay for medical care for the elderly, especially for their long-term care. Medicaid expenditures for the elderly accounted for 32 percent of the total Medicaid expenditures in 1992 (U.S. House of Representatives, 1994, p. 806).

*Cash Aid.* Public spending for cash aid has been on the persistent decline since 1976—dropping from 1.26 percent of the GDP in 1976 to 0.93 percent in 1988. After 1988, it increased steadily to reach 1.17 percent of the GDP in 1992. The pattern of AFDC payments partly explains the decline in the expenditures during the 1970s and 1980s. That is, all states, except California, have failed to upgrade their AFDC payments to adjust for the rise in the cost of living. For example, a study by the Congressional Research Service (Solomon, 1992) found that in constant 1992 dollars, the median state's maximum payment for a family of four declined from \$796 in 1970 to \$435 in 1992, a reduction of 45.4 percent. The states' failure to upgrade AFDC payment levels according to the increase in cost of living has resulted in a smaller pool of eligible families (Ellwood & Summers, 1986). The Omnibus Budget Reconciliation Act of 1981, which virtually made working poor families ineligible for AFDC and pushed working AFDC families off the assistance rolls, further shrank the pool of AFDC-eligible families (Bowden & Levy, 1982). All this resulted in a decline in the percentage of poor children on AFDC from 71.6 percent in 1975 to 57.9 percent in 1989. Since 1989, the percentage of poor children on AFDC steadily increased, so that it reached 63.1 percent in 1992 (U.S. House of Representatives, 1994, p. 399). This recent surge in the percentage of poor children on AFDC reflected a sudden increase in AFDC families between 1989 and 1992, adding 950,000 families to the AFDC caseload (or a 27 percent increase) during the same period (Gabe, 1992). All told, the AFDC expenditures declined from 0.51 percent of the GDP in 1975 to 0.37 percent of the GDP in 1992.

The expenditures for Supplemental Security Income (SSI), another major cash aid program, have been stable. The expenditures were 0.37 percent of the GDP in 1975, 0.3 percent in 1990, and

back to 0.37 percent in 1992 (Social Security Administration, 1994, p. 286; U.S. Bureau of the Census, 1994, p. 446).

The slow growth in SSI expenditures was caused by two factors. First, although the number of SSI recipients suddenly grew between 1990 and 1992, it had been relatively stable before 1990—4.8 million in 1990 compared with 4.3 million in 1975—although the composition of SSI recipients changed greatly, with the number of disabled persons increasing and with the number of elderly persons decreasing (Social Security Administration, 1994, p. 285). Second, although the federal SSI payments kept up with inflation, state SSI supplemental payments did not, except in Minnesota and Alaska (U.S. House of Representatives, 1992, p. 790). As a result, the combined federal-state SSI payments eroded in value over time.

The earned income tax credit (EITC) has become an important part of public aid programs. The data for the present study included the refunded portion of the EITC. In 1975, this portion constituted 0.05 percent of the GDP. The proportion stayed stable from 1975 through 1985. But, between 1985 and 1990, it increased from 0.04 percent to 0.09 percent of the GDP. By 1992, it reached 0.16 percent of the GDP, or about a half of the proportion of the GDP spent for AFDC (U.S. House of Representatives, 1994, p. 704).

Largely because of what happened in AFDC, SSI, and the EITC between 1975 and 1992, the share of the GDP devoted to financing cash aid persistently declined from 1.22 percent of the GDP in 1975 to 0.93 percent of the GDP in 1988, and increased thereafter, reaching 1.17 percent of the GDP by 1992 (see Figure 3).

*Food Benefits.* Whereas cash aid failed to be responsive to the financial needs of low-income families, food stamps tended to make up for the shortfall, before 1980, as Figure 3 shows. When the expenditures for cash aid were declining rapidly from 1976 to 1979, those for food benefits programs, dominated by the Food Stamp program, were steady. This situation occurred because the Food Stamp program—a 100-percent federally funded program—increased its benefit level according to cost-of-living increases, whereas cash aid programs, such as AFDC, did not. On the other hand, the proportion of poor people receiving food stamps decreased from 65.6 percent in 1981 (a record high) to

59.6 percent in 1990, and increased to 64.0 percent in 1992 (U.S. House of Representatives, 1994, p. 777). The steady decline in the reciprocity rate during the 1980s was, in part, attributable to the stricter eligibility requirements instituted by the Reagan Administration under the Omnibus Budget Reconciliation Act of 1981 (Bowden & Levy, 1982). Thus, the trend in spending for food benefits followed closely the trend in spending for cash aid during the Reagan-Bush era.

*Housing Benefits.* The expenditures for housing benefits ranged from 0.27 percent to 0.39 percent of the GDP during those years under investigation. Public spending for this purpose steadily declined from 1982, when it peaked at 0.39 percent of the GDP, to 0.29 percent of the GDP in 1987, and rose to 0.35 percent of the GDP in 1992. The persistent decline in housing expenditures during the 1980s occurred in the face of the increasing number of homeless people during that decade. A study by The Urban Institute (1988) estimated that there were 560,000 to 680,000 homeless persons in 1988.

*Energy Aid.* Public spending for energy aid originated in 1976. It increased greatly in 1980, but declined steadily afterward, so it was only 0.03 percent of the GDP in 1992, compared with 0.07 percent in 1980. Thus, energy aid programs played an increasingly minor role in assisting low-income families as the years passed.

### Discussion and Conclusions

Has public spending for programs to invest in low-income families and individuals declined? The answer is yes, except during the past few years. What is even more serious is that the trend in expenditures for investment purposes have been highly volatile and uncertain. For example, the programs for jobs and training have been under an onslaught of budget cuts for many years. The expenditures for social services have been de facto neglected because of the spending cap in the Social Service Block Grant and the Community Service Block Grant. Even the expenditures for educational benefits—though on an upward trend—have been unpredictable. In short, the data presented in this article indicate the absence of a systematic and comprehensive national strategy for human capital development. If the United States has a serious commitment to developing human capital among the

low-income population, one would expect that public spending for investment purposes would grow at a faster rate than that of the economy and that the expenditures for programs for such purposes would be *steadily* rising. The reality has been far from such a desirable trend.

Has public spending for consumption increased to the detriment of the public spending for investment? The answer is no, as was indicated earlier by the insignificant correlation coefficient between the two variables. Public spending for programs for all types of consumption rose from 1975 to 1992, but this increase was largely due to the growth in programs for medical benefits. When medical benefits are excluded from the analysis, public spending for consumption purposes actually decreased from 1.93 percent of the GDP in 1975 to 1.70 percent in 1989, only to climb back to 1.97 in 1991 and to 2.13 percent in 1992 (see Figure 3). Mostly notably, the expenditures for cash aid programs, of which the public tends to be especially critical, declined considerably during the 1980s, only to climb back to the level of 1981 in 1992. One can conclude that except for medical benefits, the United States has not increased the scope of provisions of daily necessities for low-income families and individuals, commensurate with the growth in the economy.

All told, the level of public spending for all 80 income-tested social welfare programs for both investment and consumption purposes should be considered modest, indeed. In 1992 the United States spent only 4.91 percent of the GDP for all income-tested social welfare programs (see Figure 1). In contrast, it spent 4.87 percent of the GDP in that year for the social security program (OASDI) alone (U.S. House of Representatives, 1993, p. 85).

As the United States faces the challenge of global competition in the coming decades, the policymakers in Washington should take a hard look at the nation's haphazard commitment to public spending for programs to enhance human capital among low-income families and individuals. To face the future challenge, they need to create a more coherent and comprehensive policy for the development of human capital and a national strategy to accomplish the objective. Furthermore, they ought to recognize that the United States certainly has not overspent for programs to help low-income families and individuals consume the daily necessities of life.

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