RESEARCH BRIEF • AUGUST 2023

The (Lack of) Anticipatory Effects of the Social Safety Net on Human Capital Investment

Based on BFI Working Paper No. 2023-107, "The (Lack of) Anticipatory Effects of the Social Safety Net on Human Capital Investment," by Manasi Deshpande, University of Chicago; and Rebecca Dizon-Ross, University of Chicago

Most parents whose children receive Supplemental Security Income (SSI) benefits overestimate the likelihood that their child will receive SSI benefits in adulthood; further, reducing parents' expectations that children will receive benefits in adulthood does not increase investments in children's human capital.

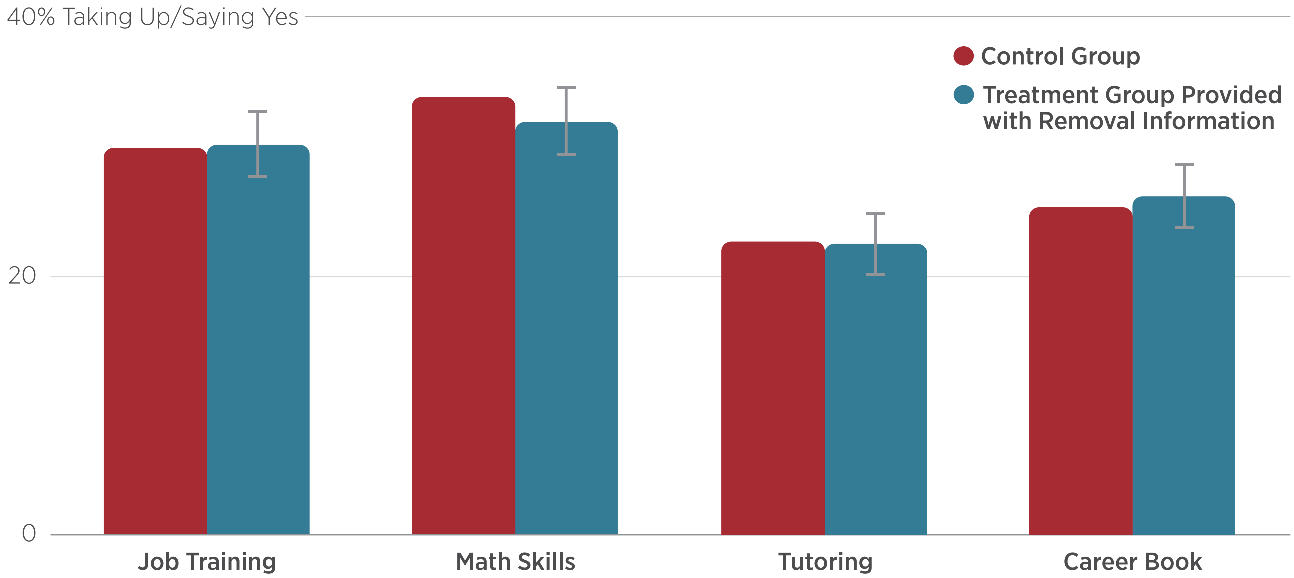
Research has shown that social safety net programs improve children's short- and long-term outcomes by providing financial resources to families in need. However, what if parents anticipate that their children will retain government benefits into adulthood? Will those parents decrease their investment in their children's education and other development opportunities?

A simple economic model suggests some answers to these questions, revealing that the anticipation of benefits in adulthood decreases human capital investment on two counts: (a) income effects—parents invest less in human capital because they do not expect their child to "need" money from working in the future; and (b) substitution effects—parents invest less in human capital because, due to the phase-out rules for transfer programs, a child's adult benefits will be reduced if they work as an adult.

Several theoretical models capture these discouragement effects, including those modeling the effects of a universal basic income, while empirical work has revealed that human capital investments are responsive to many types of dynamic or anticipatory considerations, including life expectancy and adult earnings returns. Further, while direct evidence on dynamic discouragement effects of the social safety net is limited, experts on child development think this effect is large. However, is there more to the story? Might there be reasons that the anticipation of future benefits might not decrease human capital investment? Parents, for example, may be constrained to invest less than they would like by limited money, time, or bandwidth, so changing expectations alone would not increase investments without accompanying changes to these constraints. Also, parents may make decisions about human capital investment based on non-financial objectives.

The authors focus on the Supplemental Security Income (SSI) program, the largest cash welfare program in the United States that, in 2022, spent $51 billion on cash payments to 1 million children and 5.5 million adults with disabilities and low incomes. Most children receiving SSI qualify for the maximum annual benefit of around $10,000 per year, which is about

Figure 1 · Providing Parents with Information on Child's Likelihood of Removal from SSI Does Not Increase Human Capital Investment



Note: This figure shows the percent of respondents taking up each resource and 95% confidence intervals. The sample limits to those who a) underestimate the removal probability by at least 30pp at baseline, and b) are not in the Information-Perverse group. "Job training" indicates completing an intake form for vocational rehabilitation services (in applicable states) or requesting information on how to sign up for those services. "Math/computer" indicates signing up for the math/computer skills platform in the Resource Center. "Tutoring" indicates choosing the $300 in tutoring, versus $50 in cash in the lottery or no response. "Career book" indicates choosing a $35 survey payment plus career book (worth $16), versus a $40 survey payment or no response. Sample sizes: Control group N = 2282; Information group N = 2307.

half of household income for the median family. The majority of children who receive SSI qualify on the basis of mental and behavioral conditions. Many of these children have poor life outcomes in adulthood, so understanding human capital investment in this population is critical.

Before describing the authors' methodology and results, it is useful to note that when children who receive SSI turn 18, they are reevaluated for SSI as adults, and nearly 40% of SSI children, including 70% of those with mental and behavioral conditions, are removed from benefits at age 18. This stands in contrast to parents' beliefs: from the authors' baseline survey data, more than half of the parents in the sample believe there is no chance their child will stop receiving SSI benefits in the coming years, despite a median removal probability of 70%.

To study the effects of dynamic discouragement, the authors conducted a randomized controlled trial (RCT) with about 6,000 parents with children (aged 14–17 years) who received SSI. Parents randomly received information on their child's predicted likelihood of removal from SSI at age 18. The information was delivered to the treatment group via video, and the message was direct. For example, parents of children with a 70% removal probability (the median) were told that their child "will most likely not receive SSI benefits as an adult … and they will need to find other sources of income to support themselves."

Parents got the message:

- Treated parents updated their perceived likelihood of removal for their child by 20 percentage points (pp) relative to the control group.
- They expressed 10pp greater demand than the control group for a hypothetical insurance product to insure them against the loss of SSI benefits.
- And treated parents were 9pp more likely to make plans to work more themselves in the future if already employed.

However, these effects did not translate into more human capital investments for children:

- Treated parents did not accept offers of tutoring and job training at a higher rate than control parents.
- These effects hold for parents who underestimated the likelihood of removal and those that thought there was no chance of removal.
- To stress the point, the authors find a zero effect for all observable subgroups, including parents who believe in a high return to human capital, parents who strongly believe that offered resources would help their child succeed in school, and parents who feel they have the capacity to plan for the future.

What explains these results? Why do parents, who clearly update their beliefs on whether their children will receive benefits post-18, choose not to act on those beliefs and not to invest more in their children's human capital development? The strongest evidence suggests that parents have alternative plans to recover the lost income. Among parents who are already working, information leads to an increase in the parents' plans to work in the future and in actual parent employment and earnings in the year after the authors' experiment. Parents are also motivated by non-financial objectives, which can help explain reduced responsiveness, especially if parents are also nearing the limit of the investments that they can make subject to time and resource constraints. Among other effects, the authors also find evidence that the wealth effect—the reduction in permanent income due to the SSI loss—negatively impacts college-going plans as parents may believe they can no longer afford college without SSI.

Bottom Line: Reducing parents' expectations that children will receive benefits in adulthood does not increase investments in children's human capital. For policymakers hoping to improve the life outcomes of children who receive SSI, this novel finding is disappointing news. As recent research reveals, removing children at age 18 from SSI has adverse effects on children and society, including large increases in criminal activity (see BFI Research Brief, "Does Welfare Prevent Crime? The Criminal Justice Outcomes of Youth Removed from SSI," based on Deshpande and Mueller-Smith, 2022). This new work suggests that dynamic discouragement stemming from lack of information about SSI removal alone is not the cause of these adverse effects, and hence that providing information about removal is unlikely to counter the adverse effects. Improving the adult outcomes of children who receive SSI benefits will thus require other policies, potentially in conjunction with information. However, for the safety net more generally, the authors' findings may be good news: the existence of a social safety net for adults does not appear to discourage human capital investment in childhood.

READ THE WORKING PAPER

NO. 2023-107 · JULY 2023

The (Lack of) Anticipatory Effects of the Social Safety Net on Human Capital Investment

bfi.uchicago.edu/working-paper/2023-107

ABOUT OUR SCHOLARS

Manasi Deshpande
Associate Professor, Kenneth C. Griffin Department of Economics
economics.uchicago.edu/directory/manasi-deshpande

Rebecca Dizon-Ross
Associate Professor and Charles E. Merrill Faculty Scholar, Chicago Booth
chicagobooth.edu/faculty/directory/d/rebecca-dizon-ross

CHICAGO BOOTH
The University of Chicago Booth School of Business