Rethinking the Welfare State

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Abstract

The U.S. spends non trivially on non-medical transfers for its working-age population in a wide range of programs that support low and middle-income households. How valuable are these programs for U.S. households? Are there simpler, welfare-improving ways to transfer resources that are supported by a majority? Quantitatively, what are the macroeconomic effects of such alternatives? We answer these questions in an equilibrium, life-cycle model with single and married households who face idiosyncratic productivity risk, in the presence of costly children and potential skill losses of females associated with non-participation. Our findings show that a potential revenue-neutral elimination of the welfare state generates large welfare losses in the aggregate. Yet, most households support eliminating current transfers since losses are concentrated among a small group. We find that a Universal Basic Income program does not improve upon the current system. If instead per-person transfers are implemented alongside a proportional tax, a Negative Income Tax experiment, there are transfer levels and associated tax rates that improve upon the current system. Providing per-person transfers to all households is quite costly, and reducing tax distortions helps to provide for additional resources to expand redistribution.

Keywords: Taxes and Transfers, Household Labor Supply, Income Risk, Negative Income Tax

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