Debt, Asset Accumulation, and Livelihoods in the Welfare Population

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Introduction

While sociologists have long considered financial well-being in terms of labor market outcomes, economic security rests on more than earnings. A family s ability to maintain a certain level of consumption depends on its total resource base, including a constellation of financial and non-financial resources. Thus, household wealth is central to family economic well-being and a critical determinant of life chances (Spilerman, 2000; Henretta and Campbell, 1978; Henretta, 1984). However, in sociology, wealth is an understudied outcome, and when it has been studied, the focus has been on net worth as an indicator of stratification or status attainment (Keister and Moller, 2000; Spilerman, 2000). Less attention has been given to components of net worth, particularly personal assets such as homeownership and debt, and their role in maintaining family consumption levels. This paper examines one factor that contributes to household net worth-- debt and attempts to determine the role debt plays in welfare recipients household resource management.

In contemporary society, people use credit to shield their savings, to smooth out demands on income, and to deal with financial crisis (Parker, 1988). For the welfare population, low earnings expectation limits the credit options available. This not only makes household finances more difficult to manage, but also constrains personal asset growth because savings cannot be diverted to long-term investments as it must be available to meet consumption needs. Despite the key role credit plays in most U.S. households today and despite recent attention to asset growth as a poverty alleviation strategy, little research exists that examines indebtedness in low-income households, particularly welfare-dependent households. Does debt allow low-income households to accumulate assets? Overall, for this population, is debt a sign of financial ineptness, crisis-

ridden lives, or a shrewd strategy? In this paper, I contribute to the literature on savings in low-income households by looking at the relative contribution of income, reliance on public assistance, and personal pre-disposition towards personal debt in a sample of welfare households from three Louisiana labor market areas.

 Discussion of Results

In the research literature, investigations of the economic life cycle model provide inconsistent results with respect to the effects of income fluctuations on total net worth. This variation in the relationship of income uncertainty to wealth may occur because the basic life cycle model does not allow people of the same age or at opposite ends of the permanent income distribution to have different rates of wealth accumulation. However, differences in opportunity affect savings and borrowing at each age and may accumulate over time. Children of the poor, for example, may be raised in neighborhoods with worse schools and fewer jobs. Also, the poor face risks that the non-poor do not, e.g. lack of readily accessible health insurance. In this section I present results assessing the application of the economic life cycle model to the welfare population. I also examine the effect of incorporating measures for use of public assistance and health risks. In addition, I assess whether the economic life cycle model may be enhanced by attitudinal measures and controls for livelihood strategies such as coresidence and kin support.

[TABLES 1 & 2 AB OUT HERE]

Testing the Economic Life Cycle Model

Before assessing the fit of different models to the accumulation of debt among this 1998-

99 sample of welfare recipients from selected Louisiana labor market areas, I review the debt pattern among sample members (Table 1). About 70 percent of the sample reports no debt. The level of debt among respondents with debt ranges from below $1,000 to $40,000. On average, indebted respondents owe around $3986 (median $2000). This suggests that respondents have consumer debt, possibly from credit cards or the purchase of a vehicle. Less than 5 percent of the sample reports buying a home between interviews. Yet the distribution of indebtedness among these persons is similar to the distribution across the entire sample, with 70 percent reporting no debt and debt ranging between $1,000 and $20,000. Here, the reader should note that in Louisiana the cost of a house is well below the national average and over one half of all houses are exempt from property taxes which are invoked once the value exceeds a $75,000 threshold.

Even without including variables designed to capture economic behavior specific to the poor, the economic life cycle model fits as expected theoretically (Table 2, Model 1). Although the direction of some associations are not as expected, the variables that are significant are the main explanatory variables from the economic life cycle theory. Higher education, a proxy for permanent income, is not significantly associated with the latent measure of "potential debt captured in tobit models. Stable income staying employed is significantly associated with greater potential debt than not being employed. Theoretically, net of consumption, stable employment or transitions to employment should not increase borrowing. Net of permanent income as captured by the lagged dependent variable and education, employment exits (signaling loss of income) should be positively associated with debt. However, results show that exits are not significantly associated with debt.

In another set of models, I incorporate variables specific to analyses of the poor use of

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public assistance and indicators of health risk (Table 2, Models 1 and 2). Public assistance may take the form of income assistance such as TANF or in-kind assistance such as Food Stamps which makes up most of the other public assistance that 77 percent of all respondents received. Including public assistance variables improves the model significantly $(-2((-332.51)-(-326.44))=13.4$ with df 3). Health risk variables added to the model (depression index, respondents having a health problem, respondents children having a health problem) theoretically affect consumption needs, but under a precautionary savings scenario would not significantly affect debt accumulation because the exposure to risk theoretically increases savings. Although having children with a health problem is highly significant in this model specification, the effect is essentially due to only a few respondents who have no debt and have children with health problems. Because of the problems with the sample for the precautionary savings model; and with no significant finding with the addition of values or livelihood variables to the public assistance specification of the life cycle model (Table 3), I use the public assistance model from Table 2 to decompose the marginal effects of significant variables. Before proceeding with this decomposition, I briefly discuss why values and livelihood variables have no significant effects.

[TABLE 3 ABOUT HERE]

Effect of Values

Model 1 in Table 3 incorporates welfare background and attitude towards social mobility. The addition of these variables does not enhance the explanation of amount owed. Lee,

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Singelmann and Yom-Tov (2004) also find no relationship between attitudes and employment nor between welfare family background and employment. That neither attitudes nor parents use of welfare help to explain levels of debt may be due to values predicting welfare status and education levels (supported by findings in Lee et al. 2004) . I assess this possibility by excluding these variables. Without the presence of these variables (estimates available from the author), values still do not help to predict debt levels. The other possibility is that these particular attitudes do not affect the level of debt or are inconsequential given that recipients have very limited access to credit. If recipients cannot borrow money regardless of values, then values have no predictive power.

Effect of Livelihood Strategies

Because they have limited income and limited access to credit, many welfare recipients have no choice but to reduce consumption or to reduce the cost of consumption. Among the strategies adopted by economically disadvantaged households, particularly African American households, are cohabitation and coresidence (Lichter and Brown 2004). Another strategy is reliance on family for services that other households can afford to pay for, e.g. childcare. Inclusion of livelihood variables does not improve the explanatory power of the economic life cycle model. Again, it is possible that these households are so financially strapped that they must engage in these strategies regardless of the amount they borrow. The percent of the sample pursuing these strategies is substantial   46 % receive assistance from family while 20% receive help from an absentee parent and 20% reside with another adult earner (Table 1).

[TABLE 4 ABOUT HERE]

Decomposition of Tobit Results

Decomposition of tobit coefficients into marginal effects on amount owed among debtors and on the probability of going into debt among non-debtors allows us to make more meaningful interpretation of the estimates. Roncek (1992) indicates that a fixed proportion of the estimated tobit coefficient represents a marginal effect on the uncensored observations (e.g. on those with debt). In this case, the effect of a one unit increase of the covariate on the amount by which debt increases in approximately 25% of the coefficient estimate. Decomposition results are presented in Table 4. For continuous variables (lagged debt, days between interviews), marginal effect are evaluated at the mean. For dichotomous variables the effect is evaluated for the shift from 0 to 1.

Owing more money initially, having acquired a home between interviews, remaining employed between interviews, and having a spouse present in the home, all increase debt accumulation from one year to the next. For every one percent difference in amount owed last year, one is likely to observe a .31% difference in the amount owed in the current year. Those who acquired a home between interviews owed, on average, 129% (1.29 x 100) more than those who did not. Similarly those who stayed employed for a year had 141% higher debt levels than those who did not. Having a spouse is associated with just over 100% more owed than not having a spouse. If one considers that credit availability rises with the ability to guarantee a steady income stream, then these findings are not surprising.

Staying off welfare between interviews and more time passed between interviews are associated with a decline in the amount owed. Those off TANF for about 1 year owe just over 90% less than those still on TANF. For everyday that has lapsed between interviews, respondents with debt owe 1% less. Time between interviews is one control for survey design effects.

According to economic theory because cash assistance helps maintain income at anticipated levels, TANF participation should increase savings and decrease borrowing. TANF exit should create a deficit of income with which to meet consumption needs. Because borrowing is one way to make up for this deficit, TANF exit or being off TANF, net of employment transitions and changes in consumption needs, should result in more not less borrowing.

With respect to effects on the probability of going into debt (becoming uncensored), the direction of the marginal effects is similar to observed effects on debt among debtors. Having owed money in the last interview increases the chances of being observed in debt in the current interview. Similarly, acquiring a new home increases the odds of being in debt in the current wave by 25% (exp[.22]=1.25). Remaining employed between waves increases the odds of being in debt by 28%, receiving public assistance by 15%, and having a spouse present by 20%. Factors associated with a lower probability of becoming indebted are staying off welfare (-15%) and having more time elapsed between interviews (-0.2% per day). These results remain consistent with the notion, that factors that increase access to credit among the recently poor are associated with increased levels of debt.