The Work Incentive Effect of Social Assistance

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The recent economic crisis in many countries has produced an increase in the demand for last-resort social benefits together with increased pressures to control spending. As a result, the performance of social assistance schemes of these countries is constantly under the spotlight. SA programmes, and especially minimum income schemes, should achieve two objectives (Blundell, 2006). First, they should avoid extreme hardship for families unable to do so through other income sources. Recent evidence shows that the tax benefit systems in place in many countries were successful in cushioning the short term effect of the crisis on household incomes (Jenkins et al, 2012). Second, social assistance schemes should prevent dependence for their beneficiaries, and rather promote attainment of self-sufficiency.

This paper analyses the work incentives of means-tested social assistance.A recent literature took advantage of discontinuities in policy rules to assess the impact of social assistance on labour supply. Lemieux & Milligan (2008) used the difference in the social assistance benefits received by childless individuals aged under/over 30 in the Canadian province of Quebec, from 1967 to 1989, to assess the effects of SA benefits on labour market outcomes. Applying a regression dicontinuity design to this age-discontinuity, they found that increased welfare benefits at age 30 reduce the employment probability by 3 to 5% for less-educated men and by 1% for the whole men population. Bargain & Doorley (2011) use a similar strategy to analyse the effect of the French minimum guaranteed income on youth labour supply in France. Using Census data, they find a drop of 7 to 10% in the employment rates for unskilled men at 25, the age of eligibility, while no effect is found on the whole men population.

Luxembourg is one of the few European country excluding young adults from its minimum income scheme. When introduced in 1986, only individuals aged at least 30 were eligible for the Revenu Minimum Garanti. In 1999, the age condition was lowered to 25. In this paper, we use this age discontinuity to assess the work incentives of the RMG in Luxembourg in a regression discontinuity design. In the context of a regression discontinuity, the probability of being on treatment is a discontinuous function of one or more variables and the outcome variable is continuous at cut-off points (Imbens & Lemieux, 2008). Administrative rules provide quasi-experimental designs of this type. In our case, following previous literature, the application of RD to the sharp age cut-off will allow to assess whether individuals aged above/below 25 have different employment rates. To the condition that we are able to discard alternative explanations, potential differences may be attributed to the RMG. The paper will be based on Luxembourg Labour Force Survey and Census data (and if available on Luxembourg administrative data).