



# Economic Downturns, Endogenous Government Policy and Welfare Caseloads\*

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## Abstract

Governments can soften the impact of the business cycle on welfare spending. Depending on the political costs and the extent of unemployment, they might choose between a decrease in the proportion of accepted applications, a decrease in the level of benefits, or some combination of the two. This paper is motivated by this concern, weaving together the intensive literature on the determinants of welfare caseloads and the fundamentals of public choice theory applied to the design of welfare programs. The paper is based on data from the minimum income program of Catalonia's government (PIRMI). We use autoregressive distributed lag models to find that the generosity of the program is clearly predictive of the receipt of benefits even in contexts of high and growing unemployment rates. We also find a fairly strong correlation between unemployment growth and the proportion of rejected applications and a trade-off between the level of benefits and rejections.

*Keywords:* Welfare caseloads, Poverty, Endogenous policy, ADL models.

*JEL Classification:* I30, I38, C22

## 1. Introduction

The magnitude of the welfare caseload has been a subject of increasing concern to voters and policy-makers. When it comes to public policy discussions of welfare programs, there is no doubt that the growing number of recipients and the consequent increase in spending are major topics. Interest in the analysis of the determining factors of the changes in the number of welfare recipients has heightened recently, fed by concerns about the increasing costs

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