RESEARCH BRIEF

Public Policy Institute *of* California

DECEMBER 2003 ISSUE #79

How Do Subsidies Affect California's Child Care Market?

The average poor household with a young child spends 34 percent of its income on child care. Because affordable care often makes the difference between welfare and work for these families, public spending on child care support rose dramatically in the 1990s in conjunction with welfare reform. Between 1992 and 2001, expenditures on child care subsidies in California rose from $125 million to $1.5 billion, or some $375 for every child in California under age 5 (see the figure). Despite this dramatic increase, about 200,000 children in California are still on the waiting list for child care subsidies, and many families are eligible for assistance but unaware that they qualify for it.

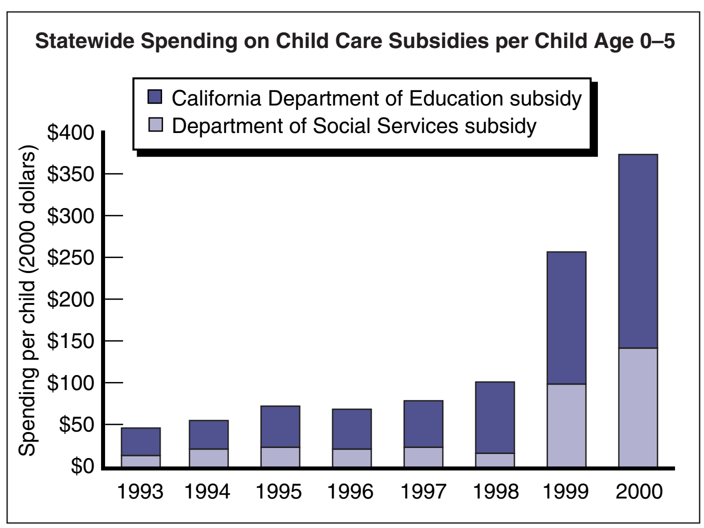
Under CalWORKs (California's welfare program) and Alternative Payment (AP) programs, the state offers low-income families child care vouchers and pays for them with general fund revenues and federal block grants such as Temporary Aid for Needy Families (TANF) and the Child Care Development Fund. Recipients may use the vouchers to purchase care from providers whose prices fall below a reimbursement rate ceiling. California's vouchers are among the most generous in the country. The state has one of the highest income-eligibility thresholds, a very low co-payment requirement, and the highest reimbursement rate ceiling in the nation.

Because voucher recipients purchase child care in the open market, the number of families served under AP depends in part on market prices. Yet little is known about these prices, what determines them, or how recent policy changes have affected the child care market. In *Child Care Price Dynamics in California,* Grecia Marrufo, Margaret O'Brien-Strain, and Helen Oliver address these questions by drawing on market surveys and a broad range of county-level data sources. Their report documents double-digit increases in real prices during the 1990s, significant price variation by region, and earnings for child care workers that just kept pace with average earnings. The authors also conclude that state subsidies, which accounted for roughly 20 percent of gross receipts in the child care market in the 1990s, put significant upward pressure on child care prices.

Significant Market Changes During the 1990s

The authors found that between 1991 and 2000, average prices for child care rose 14 percent in real terms, with the sharpest increases occurring in licensed family day care after 1996. Between 1998 and 2000 alone, child care prices rose 10 percent in the typical California county. By 2000, the average weekly rate for preschool center care was $121, although that rate was as high as $149 in the San Francisco Bay Area and well below $100 in 25 mostly rural counties. For infants and toddlers, the average rate statewide for weekly center care was $177.

The authors also note that price increases might have been larger were it not for the substantial growth in the supply of child care. In 2000, there were sufficient licensed slots for 23 percent of all children under age 5—a 20 percent improvement over 1996. However, those shares varied dra-



Child care subsidies rose dramatically between 1993 and 2000, largely as a result of welfare reform measures.

matically across counties, ranging from 15 percent in San Diego County to 56 percent of children in Siskiyou County.

As child care capacity grew, so did the need for teachers. The increased demand for teachers boosted earnings in the child care industry by 19 percent over the course of the decade. That increase outstripped child care prices by five percentage points but did not exceed earnings increases in other industries. By 2000, child care earnings relative to average earnings across all industries stood at 42 percent—the same as in 1991.

Using standard statistical procedures, the authors isolated the effects of key factors—including the robust economy, key demographic trends, child care wages, welfare caseload declines, and subsidy increases—on child care prices. On the demand side, the rapid decline in welfare caseloads before 1997 increased prices for family day care by 4.4 percent, and the comparable figure for center-based care was slightly more than 2 percent. Caseload declines had no measurable effect on prices between 1998 and 2000, but higher incomes during this period accounted for 5 percent of the price increases in center-based care.

The authors' rough calculations indicate that the voucher program represented as much as one-fifth of the gross receipts in the private child care market. With this sort of market presence, the voucher program exerted significant effects on prices. The authors estimate that total child care subsidies, which increased 289 percent between 1998 and 2000 in the typical county, led to 8.1 percent price hikes for center-based care and 4.5 percent increases for family day care.

Policy Implications

Because their study does not track changes in child care quality over time, the authors draw no conclusions about whether child care consumers in 2000 were better or worse off than they were in 1991. Nevertheless, their findings suggest that the rapid expansion of child care subsidies drove up prices for all families, including poor families not currently receiving assistance.

The most recent state budget cut spending on vouchers by an estimated $155 million, removing $57 million in funding set-aside for former CalWORKs recipients, trimming $16 million by excluding subsidies for 13-year-olds, and cutting $82 million by lowering reimbursement rate ceilings. The authors note that these cuts may reduce pressure on child care prices but that in the current economic climate, these subsidies may now be supporting a child care market otherwise facing declining enrollments rather than adding pressure to an already overheated market.

The authors also point to the ongoing need to consider the effects of child care policies on the larger child care market. One recent welfare reauthorization bill passed by the House of Representatives increases child care funding 7 percent, but this increase, if enacted, is probably too modest to affect child care prices significantly. A more significant policy proposal concerns universal preschool. With a price tag of $5 billion or more, this plan would be three to four times the size of the voucher program. The effects of universal preschool, however, would depend heavily on the details of the program's implementation. Many factors could influence price and quality outcomes for California preschools, even for those children not targeted for the service. These factors include eligibility rules, hours of care, credentialing and other standards, and whether or not the program is based in schools or private facilities. Although concerns over unintended market effects need not be a roadblock to policy changes, the authors conclude that they should be part of the policy calculations.

This research brief summarizes a report by Grecia Marrufo, Margaret O'Brien-Strain, and Helen Oliver, Child Care Price Dynamics in California *(2003, 104 pp., $12.00, ISBN 1-58213-080-9). The report may be ordered by phone at (800) 232-5343 [U.S. mainland] or (415) 291-4400 [Canada, Hawaii, overseas]. A copy of the full text is also available on the Internet (www.ppic.org). The Public Policy Institute of California is a private, nonprofit organization dedicated to independent, objective, nonpartisan research on economic, social, and political issues affecting California.*

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