

The Poverty Line Revisited

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Poverty has been in the news recently. According to a report released in December 2001 by the Smith Family and the National Centre for Social and Economic Modelling (Natsem), 'in 2000, about one in every eight Australians lived in income poverty — 13 per cent of all Australians' (p. vii). Moreover, 'there was a steady increase in poverty among all Australians during the 1990s' (Harding, Lloyd and Greenwell, 2001:4).

A response was provided by a team from the Centre for Independent Studies (CIS) in January 2002 (Tsumori, Saunders and Hughes, 2002). The CIS authors concluded that the findings of the Smith Family/Natsem report are dubious because they confuse poverty and inequality and 'rest on data that is in some respects unreliable' (p. 1). They argue that 'the debate over the future of welfare requires more reliable data on the extent and causes of deprivation'. Other commentators have subsequently joined in the discussion.

Controversy over poverty lines is nothing new in Australia. The Smith Family/Natsem report uses a modified form of the Henderson poverty line. This poverty line was developed for a Melbourne study in the late 1960s and rose to national prominence in the report of the Commission of Inquiry into Poverty in 1975. This poverty line has been subsequently updated by the Melbourne Institute according to changes in Average Weekly Earnings and (later) Household Disposable Income per capita. The Henderson poverty line was never endorsed by government and, from time to time, criticisms of the Henderson poverty line were mounted from official sources. Eventually, the Minister for Social Security asked the Social Welfare Policy Secretariat to construct a poverty line that would be suitable for use in contemporary Australia.

The Social Welfare Policy Secretariat (SWPS, 1981) subsequently reported that the task was impossible. They concluded (p. 208) that:

there are no entirely satisfactory techniques which would allow us to assess whether the money amounts of pensions and benefits are adequate or not. Further, many factors other than the needs of families in different circumstances influence decisions about the level of pensions and benefits.

I was the principal author of the SWPS report. Despite, or perhaps because of this finding, the Henderson poverty line has continued to be published. Although interest may have diminished in the years following publication of the SWPS report, more recently the poverty line has made a comeback. Despite the

absence of official endorsement, the Henderson poverty line has, for example, been quoted in ABS publications (see, for example, ABS, 1998:125-129).

In asking me to write this article, the editors of *Agenda* have kindly invited me to revisit these issues twenty years later. My purpose in writing this article is to investigate the usefulness of the estimates of the extent of poverty that have recently gained such prominence in the Australian debate and to comment on the work that needs to be done if we are to understand better the extent and nature of disadvantage in Australia today. I will proceed by first reviewing the recent contributions by the Smith Family/Natsem authors and the CIS authors. I will then discuss the issues that are raised by these authors. These include: what is meant by poverty in Australia today; the problems in representing these ideas about poverty by a poverty line; and the usefulness for policy of the estimates by the Smith Family and Natsem of the composition of the low income population. Finally, some conclusions are drawn.

The Smith Family/Natsem Report

This report was commissioned by the Smith Family and prepared by three authors who work at the National Centre for Social and Economic Modelling at the University of Canberra. In her forward, the Director of Natsem refers to 'The Smith Family's report on financial disadvantage and poverty in Australia'. Certain critical judgements (such as the choice of a poverty line based on half average income) are justified, according to the authors, by 'The Smith Family's commitment to work for a more cohesive society'. However, the Chief Executive Officer of the Smith Family refers to the 'annual Smith Family/Natsem report on financial disadvantage'. It seems safest to conclude that both organisations are jointly responsible for the whole report.

The authors of the Smith Family/Natsem report develop their arguments through a number of stages. First, they adopt a relative definition of poverty. This is controversial, and is discussed further below. Secondly, the authors develop a number of alternative poverty lines. Twelve poverty lines are constructed. These differ accordingly to the method of setting the line (half average income, half median income or the 'traditional Henderson' approach), the equivalence scale used to adjust for differences in families' needs, the method of updating the poverty line and whether poverty before or after housing costs is considered. As might be expected, these poverty lines differ greatly. The authors point out (p. 24) that all but one of these poverty lines suggest that poverty rose during the 1990s. However, poverty lines based on half median income show no increase in poverty, or only a small increase, over the 1990s.

The third step taken by the Smith Family/Natsem authors is to discuss in some detail the methodological choices involved in developing a poverty line. The problems and choices made by the authors are set out carefully. Indeed, it could be argued that the Smith Family/Natsem report includes a criticism of itself that anticipates many of the points that are made by the CIS authors. Having discussed the problems in setting poverty lines the Smith Family/Natsem authors

conclude that ‘it is probably safer to discuss “financial disadvantage” rather than “poverty”’ (p. 27). Sometimes these authors refer to ‘income poverty’. This suggests that there are other aspects of poverty that do not depend on income and cannot be represented by the poverty line.

The fourth step taken by the Natsem/Smith Family authors is to choose a preferred poverty line. This line is set for a standard family of two adults and two children at half average disposable income (that is, income after income tax has been paid). The incomes of other families are made comparable with those of standard families through adjustment for differences in need by the Henderson equivalence scale. This fourth step is controversial. As the CIS authors correctly note, most researchers these days use relative poverty lines that are based on median rather than average income. Median incomes are less affected than average incomes by changes in very high or very low incomes that are not representative of the incomes earned by most people. Average incomes grew more rapidly over the 1990s than median incomes because high incomes grew rapidly during the decade.

The Smith Family/Natsem authors do not provide an extensive justification for their choice of poverty line. They argue (p. 2) that a poverty line defined in terms of average income is transparent and easy to update through time. There is, they argue, no clear consensus about whether it is preferable to take a proportion of median or average income as the poverty line (p. 26). Moreover, use of the half average income line ‘denotes acceptance of the proposition that the living standards of the poor should be measured against the living standards of all the population, including the affluent’. Use of a poverty line based on half average income ‘better captures relative deprivation in times of rising income inequality’ and therefore reflects ‘the Smith Family’s commitment to work for a more cohesive society’ (p. 27).

These arguments are not convincing. Although it may be of interest to compare the living standards of the poor with those of the affluent, this is not the same thing as defining poverty partly in terms of the living standards of the affluent. If poverty is not being able to afford to purchase the goods and services that most people enjoy, it is the living standards of ordinary people that is relevant. Most people cannot afford to buy the luxuries that the affluent enjoy. Nor is it necessarily true that a society where income is equally distributed will be cohesive. A country may be able to achieve a fairly equal distribution of income through regulation of the labour market and provision of generous welfare payments for people who are unable to find employment at the regulated wages. (Some European countries are like this.) Such a country is likely to be sharply divided between those who are working and those who are receiving benefits. Those who are not able to find work at the regulated wage are likely to resent their exclusion from work; those who are working may well resent the amount they have to pay in tax to support people who may not be much worse off than they are. By contrast, a less egalitarian society with higher levels of employment may well be more cohesive.

Having chosen a poverty line, the fifth step undertaken by the Smith Family/Natsem authors is extensive analysis of the characteristics of groups with incomes less than the poverty line and how this has changed through time. This analysis is of considerable interest even for those who do not accept the Smith Family/Natsem poverty line; it provides information on the lowest 10 to 15 per cent of the population by income. I discuss this analysis later in this article.

Finally, the Smith Family/Natsem authors emphasise the headline conclusions about poverty and its growth that were outlined at the start of this article. They note (p. 24) that:

given the strong link between unemployment and poverty it is of concern that our society did not manage to reduce poverty during a period of strong economic growth. As we enter more uncertain economic times, the need to protect those at the bottom may become greater.

The CIS Report

A team of authors from the Centre for Independent Studies has provided a commentary on the Smith Family/Natsem report. They conclude (p. 2) that the Smith Family/Natsem report

has been professionally researched and painstakingly compiled and it has received a lot of attention in the media. Its conclusions are, however, misleading.

The CIS authors reach this view for three main reasons. First, in the opinion of the CIS authors the Smith Family and Natsem have confused poverty and inequality by adopting a relative view of poverty. By contrast, most people think of poverty in absolute terms as a shortage of food, accommodation and clothing. The CIS authors (p. 1) argue that:

sustained economic growth coupled with government welfare provision means that absolute poverty is extremely rare in Australia today. Indeed, as the Smith Family report itself notes, Australia's poorest families became better off in absolute terms during the 1990s — their real (inflation-adjusted) incomes rose by an average of \$38 per week over this period.

Second, the CIS authors (p. 3) are of the view that, by adopting a poverty line based on average rather than median income, the Smith Family and Natsem have made an unusual choice that exaggerates the seriousness of poverty in Australia.

Had the more usual median income been used as the basis for these calculations, the result would have been (a) a much lower estimate of the size of the poverty problem (8.7 per cent as compared with 13 per cent),

and (b) a conclusion that poverty did not worsen over the Howard years. This would have given us a different (and much less dramatic) picture of the scale and nature of 'relative poverty' in Australia.

Third, the CIS authors argue that the Australian Bureau of Statistics (ABS) data on which the Smith Family and Natsem rely are not sufficiently reliable for conclusions to be drawn from them about the extent of poverty. The problems include the under-reporting of incomes especially by welfare beneficiaries and the self-employed, the exclusion of certain important sources of income (such as income in kind and government benefits provided below cost) and the decision by the Smith Family/Natsem authors to base their estimates on weekly income. Some families that had an unusually low income in the survey week may not have been counted as poor had data been collected for a longer period such as a year. There are, moreover, many problems involved in choosing an equivalence scale to take account of the differing needs of households of different size and composition. Thus (p. 10):

the income data that get analysed in studies such as this one are constructions of the researchers themselves. It is quite possible to shift estimates of poverty up or down simply by tweaking the assumptions you make about the equivalent running costs of different types of household.

Finally, the CIS authors argue that expenditure data provide a better basis for assessing standards of living than income data.

Despite their scepticism, the CIS authors (p. 11) conclude by arguing that:

the development of reliable poverty estimates is an essential precondition for any reasoned debate about the direction that social policy in Australia should take over the years to come.

They think that this can be done by developing 'an absolute poverty line adjusted for different kinds of households and location' based on calculating the costs of necessities. They acknowledge that this is a difficult exercise.

I think that it is useful to comment on a number of aspects of this debate:

- What is meant by poverty and how well the concept of poverty is represented by absolute or relative poverty lines;
- The methodological problems in constructing poverty lines;
- The continuing attractiveness of poverty lines, despite all the problems;
- The conclusions of the Smith Family/Natsem report on the composition of the low income population and the implications of these findings, if any, for government policy;

- What can most usefully be done to further advance an understanding of poverty and deprivation in Australia.

Comments follow on each of these points.

The Concept of Poverty

Poverty is usually taken to mean the absence of the essentials of life, such as food, shelter and clothing. It is a disgraceful state: poor people lack, in Adam Smith's words the ability to appear in public without shame. Frequently it is argued that it is the responsibility of government to ensure that people can avoid the disgraceful state of poverty.

I think it is reasonable to argue that the essentials of life include more than just certain goods and services. This focus on commodities ignores, at a time when despair and hopelessness seem to be so common, less tangible aspects of living decently. Children do not always have a safe and stable environment in which they can develop easily the skills required for success in adult life, for example, because of widespread substance abuse within their communities. Adults do not always live in an environment in which it makes sense for them to believe that they can improve their circumstances through their own efforts, for example, because of widespread welfare dependency. The absence of hope only too often leads to self-destructive behaviour, violence and suicide. Noel Pearson and others have recently reminded us that these are serious problems in some remote aboriginal communities (Pearson, 2001). Although these communities face particular difficulties, these problems are not confined to them.

The CIS authors argue that absolute poverty (in the sense of having insufficient income to maintain a minimum standard of life) is extremely rare in Australia today. This statement is correct as far as it goes. However, because of the behavioural problems noted above, not everyone in Australia has everything they need to live a decent life. These non-material aspects need to be considered, it seems to me, in a full account of absolute poverty in Australia.

Some recent writers have attempted to develop an understanding of poverty that is more profound than mere absence of commodities. For example, Amartya Sen has encouraged us to think about a person's well being in terms of his or her 'capability set' — the opportunities potentially open to the person as well as the one actually chosen (see for example, Sen, 1999:75). Poverty may then be thought of as capability deprivation. The capability deprivation approach is readily able to encompass non-material aspects of poverty. Although low income is a source of capability deprivation, so too may be lack of access to education and health services and unemployment rates that 'make a mockery of people's ability to help themselves' (Sen 1999:98). Moreover, the relationship between income and capability deprivation is variable, depending on the circumstances of communities and families within those communities. For example, a higher income is needed to sustain a decent standard of living in a richer community than in a poorer one because what is considered decent varies with the standard of

living of the community. This provides some support for the idea of relative poverty.

However, the association between poverty and the poverty line breaks down if this more sophisticated understanding of poverty is adopted. The circumstances of families vary greatly. As the early poverty researchers noted, families vary greatly in their ability to manage on a limited income. Some families are able to grow their own food or receive other types of income in-kind. Some families own houses or other assets that reduce the amount they would otherwise have to spend, for example, on rent.

A family in which someone cooks, cleans and attends to household repairs will enjoy a higher standard of living than a household in which no-one does these things. Travers and Richardson (1993:201-202) writing about a study of material well being in Australia that they had undertaken note that:

in particular, we found that inequality in money income and inequality in other components of full income (for example, home-ownership) tend to offset each other. The use of full income does not produce a more egalitarian picture of Australia than does current income, but it does show that there is little compounding of disadvantage when the broader aspects of material well being are considered. Those who are weak in one resource (income) are often strong in another (housing or non-employed time).

Moreover, disadvantage in material well being tended only to a limited degree to spill over into other aspects of life such as social activities, happiness, health and a general sense of optimism. According to Travers and Richardson (p. 206):

it requires a great deal of information about a person's assets, family relationships, receipts in kind and income before his or her material well being can be identified with any accuracy.

All this calls into question whether what we mean by poverty can be adequately represented by any poverty line.

Problems in Constructing Poverty Lines

In my view the issues outlined above are sufficiently important to make it unlikely that a poverty line can be developed that successfully separates those people who are able to live decently from those who are not able to do so. However, this is not the view of either the CIS authors or of the Smith Family/Natsem authors.

The CIS authors argue that it is possible to develop an absolute poverty line for Australia (p. 11). This involves first developing a list of goods and services for different types of families that are essential in Australia today and then calculating an amount of income that is sufficient to purchase these essentials. The poverty

lines that were developed by the early poverty researchers in late nineteenth and early twentieth century England emphasised what was required for 'mere physical efficiency'.

I think it is unlikely that anyone would advocate so austere a poverty line in Australia today. Instead a researcher would have to consider questions such as whether not eating meat or not having a telephone, car, television, holiday or an occasional night out, constitutes poverty. The difficulties are considerable. Not everyone wants to eat meat, view television or drive a car. Thus it is hard to know (in the absence of a good deal of information about a family and the community they live in) whether the absence of these things indicates voluntary choice by a household or deprivation. The early poverty researchers (such as Booth and Rowntree in England) were able to draw on a great deal of detailed knowledge about the communities they were studying in developing the first poverty lines and making estimates of the number of people in those communities with incomes below these lines. By contrast, who from the relative (and remote) comfort of a research institution or government department would be so presumptuous as to specify the minimum requirements of a decent life in contemporary Australia?

The CIS authors draw attention to a low cost budget standard constructed by researchers at the Social Policy Research Centre (SPRC). As noted in a SPRC discussion paper (Saunders, 1998:6), this low cost budget standard

represents a standard of living which may require frugal and careful management of resources but would still allow social and economic participation consistent with community standards and enable the individual to fulfil community expectations in the workplace, at home and in the community.

The SPRC researchers emphasise that the low cost budget standard is not a poverty line; it is closer to 70 to 75 per cent of median living standards than to 50 per cent.

The SPRC discussion paper (Saunders, 1998:15) noted the difficulty of reducing this budget standard to the poverty level:

(To) reduce the low cost standard for a couple with two children to one half of the corresponding modest but adequate standard would involve reducing it from \$602.10 (a week) to \$408.70, or by \$193.40. For this family type, a budget of \$408.70 would not allow them to meet their housing, energy, food and clothing needs at the low cost standard There would thus be no money left over for health, transport, leisure and personal care needs — all of which facilitate social participation — nor would there be any money for household goods and services, a category which includes expenditure on many basic household goods as well as education and child care costs.

All participants in this debate accept that researchers have a good deal of discretion in developing *relative* poverty lines. Although the choices made by the Smith Family/Natsem authors are reasonable, other equally reasonable choices could have been made that would have resulted in very different answers. The main issues here include the following:

- ABS income surveys are the main source of data for the Smith Family/Natsem study. The institutional and homeless populations, which are perhaps particularly likely to be disadvantaged, are excluded from the survey population. The income survey also suffers from sampling error. The Smith Family/Natsem authors think that the 1997 survey is so unreliable (it shows a lower level of poverty than the preceding and subsequent surveys) that they have excluded it from the analysis (p. 51). However, this is a somewhat arbitrary approach to the problem.
- Some sources of income are under-reported in the surveys (for example, income from self employment). Moreover, income as reported in the surveys grew less rapidly than the broader measures of income that are presented in the National Accounts.
- The percentage of the population that is estimated to be in poverty depends on whether weekly or annual income is measured, and on whether the household or the nuclear family is chosen as the unit of analysis. The Smith Family/Natsem authors have chosen procedures that lead to larger estimates of the extent of poverty than some alternative procedures. Because weekly income is more variable than annual income, poverty appears to be greater if weekly income is used. Because nuclear families (or abbreviations of them such as adult children) may share resources within a household, poverty appears to be greater if the family rather than the household is used as the unit of analysis.
- Some decisions made by the Smith Family/Natsem authors or the ABS about particular families can be questioned. For example, the income of families with negative incomes were reset to zero. Income tax was imputed by the ABS on the basis of income and family structure rather than being reported directly.
- As noted earlier, the basis for setting a relative poverty line is entirely arbitrary. Opinions differ as to whether median income, average income or some other basis (for example, a minimum wage) should be used to construct a poverty line. Choosing 50 per cent of (say) median income as the poverty line is arbitrary. Moreover, the percentage of the population that appears to be in poverty is very different if a poverty line is set at 40 or 60 per cent of median incomes, not 50 per cent. However, there is no clear basis for making these choices.
- Relative poverty lines incorporate equivalence scales which show how much more or less income a non-standard family needs to achieve the same standard of living as a standard family.

Developing equivalence scales is a difficult task both in principle and in practice. The equivalence scales that are used by the Smith Family/Natsem authors have been chosen because they appear to be reasonable but they have no clear empirical basis. By contrast, equivalence scales that do have some empirical basis (either based on household expenditure survey data or surveys that request people to make subjective assessments about their own living standards) typically show too small an addition for additional household members to be intuitively appealing — see Buhmann et al. (1988) for further discussion of this issue. However, particularly in a country such as Australia where average household size is fairly large, estimates of the extent of poverty depend greatly on the choice of the equivalence scale.

The Continuing Popularity of Relative Poverty Lines

The points made above are not new and, indeed, are accepted both by the Smith Family/Natsem authors and by the CIS authors. Why, then, do researchers continue to make so much use of relative poverty lines? I think two points are worth making here.

First, relative poverty lines are easy to develop. Governments collect a good deal of information on incomes that is made available to researchers. There is no need to develop a detailed understanding of the circumstances of local communities, as the early poverty researchers were required to do. Moreover, there is no need to make explicit (and difficult) judgements about which goods and services are required for a decent life.

A second reason is the effectiveness of claims about the number of people in poverty in arguing for increases in government benefits. Under the Howard government, unemployment benefits have increased less rapidly than other social security payments (see the Smith Family/Natsem report, p. 23). It is not unreasonable to argue that unemployment benefits should be increased (although the effect of any increases on work incentives should also be considered). However, the argument that benefits should be increased to reduce the number of people in poverty has greater rhetorical force than arguments about the weight that should be given in making policy decisions to each of the competing, but desirable, objectives of improving the adequacy of benefits and minimising work disincentives.

The Low Income Population

The Smith Family/Natsem report includes an interesting discussion of changes in the composition of the low income population during the 1990s. The authors refer to this group as being in poverty or income poverty. However, even people who do not accept the Smith Family/Natsem poverty line may find the analysis of some interest because it describes the characteristics of families who receive the lowest incomes. Because the Smith Family/Natsem authors use a poverty line that increases in line with average income, the percentage of families with incomes

below the line grew over the 1990s. Although this is unlikely to have been a major factor, it does need to be considered when reading the results of the analysis.

The main findings of the Smith Family/Natsem authors regarding the *composition* of the low income population include the following:

- Sole parents and single people are more likely than average to be members of the low income population; couples with or without children are less likely than average to be members of the low income population.
- Persons whose principal source of income is government benefits are more likely than average to be members of the low income population; persons whose main source of income is wages or salary are less likely than average to be members of the low income population.
- Families in which there are no earners or one part-time earner are more likely than average to be members of the low income population; families in which there is at least one full-time earner are less likely than average to be members of the low-income population.
- Persons without post-school qualifications are more likely than average to be members of the low income population; persons with such qualifications are less likely than average to be members of the low income population.

The main findings regarding *changes* in the composition of the low income group include the following:

- Sole parents were less likely to be members of the low income group at the end of the 1990s than at the beginning of the decade. Single people were more likely to be members of the low income group at the end of the decade than at its beginning.
- The percentage of children who are in the low income group fell during the early part of the 1990s but then increased.
- The percentage of aged who are in the low income group grew during the 1990s (but remained below the average for the population as a whole).
- Persons receiving government benefits and part-time earners made up a larger proportion of the low income population at the end of the 1990s than at the beginning of the decade.

Based on these findings, the best advice you could give to someone to prevent them from becoming a member of the low income population is to receive an education, work in a full time job and to marry and to remain married. In the preface to the Smith Family/Natsem report, two Smith Family authors rightly emphasise the importance of education but do not discuss the importance of marriage or full time work.

During the 1990s spending on income support by Australian governments increased from 7.3 per cent of GDP in 1989/90 to 9.8 per cent of GDP in 1999/2000 (ABS, 1996; ABS 2001a). The percentage of the population receiving

income support (and especially the percentage of the population of working age) also increased over the period (see ABS, 2001b:166-169) although economic and demographic conditions were generally favourable. Despite this increase in spending the percentage of the population with incomes below the Smith Family/Natsem poverty line was either stable or increasing.

There is much evidence to suggest that the number of people receiving income support payments depends, among other things, on the level and generosity of those benefits. It is worrying therefore, that the structure of incentives provided by Australia's social security programs encourages sole parenthood over the two-parent family and encourages the receipt of benefits (or a combination of benefits and part time work) over full-time work. Although income support programs are important in avoiding hardship, it is also evident that, at the very least, they are not easy answers to the problems that they seek to address. Moreover, there is a voluntary aspect to poverty if people respond to the incentives provided by the social security system. In terms of the language of the capabilities approach, the opportunities (or capability set) available to those currently below the poverty line may extend above it (although not always by very far). This also needs to be considered when thinking about poverty in Australia.

Concluding Thoughts

The argument of this article has been that poverty lines are far too simple and arbitrary to represent clearly the disadvantage that undoubtedly exists in Australia today. We need to consider more than just income and understand more about the problems that particular communities experience. The ease of construction and rhetorical effectiveness of relative poverty lines will ensure that they will continue to be used. I hope, however, that the arguments made in studies such as this one will encourage the development of a better understanding of what is meant by poverty and disadvantage and further studies that consider more than a short-term measure of income in assessing the standard of living of families and households.

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