Intergenerational material wellbeing: including wealth into the measurement of monetary poverty
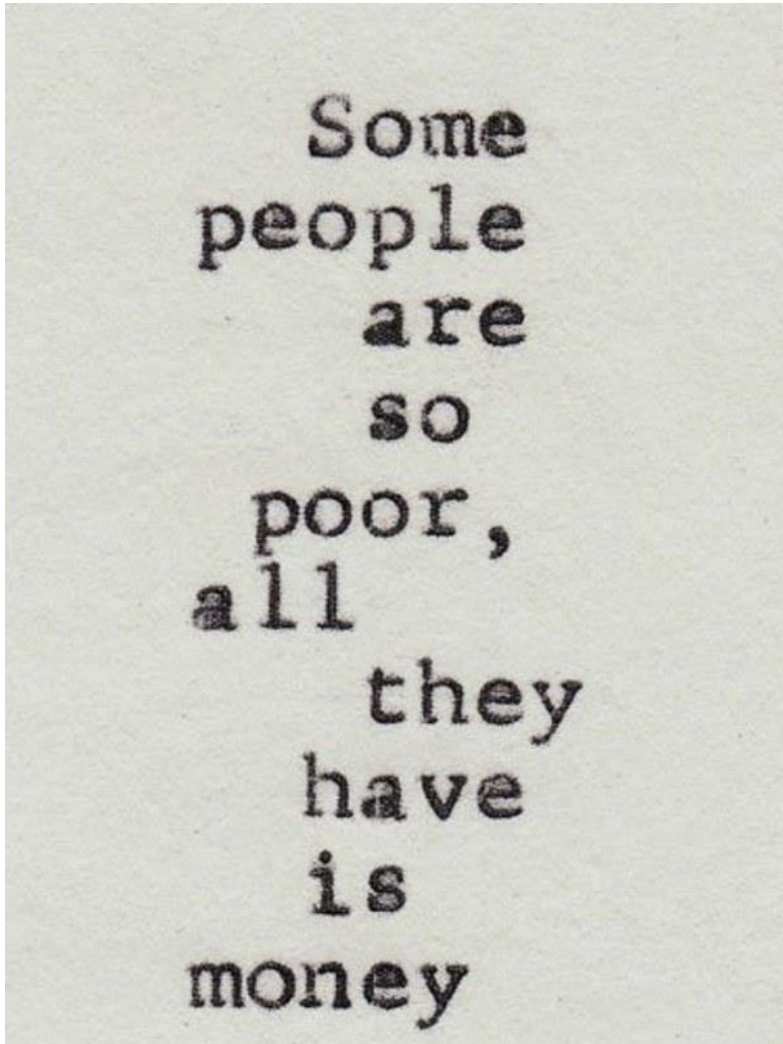
Laura Ravazzini, Christian Suter
Institute of Sociology, University of Neuchâtel
DACH project on the wealth distribution in Swiss and German survey data

Expert Meeting on Measuring Poverty and Inequality

Vienna, 29 - 30 November 2018

What we will see today:

Some
people
are
so
poor,
all
they
have
is
money

In Germany, more than half of the people who should receive social benefits according to income criteria do not claim them (UNECE 2017).

Europe 2020 aims at improving means-tested programmes.

Many income poor are wealth rich.

Asset tests correct for the wrong assignment of welfare benefits, but they are administratively expensive and complex.

Is there a better way? Should we include wealth into the measure of poverty?

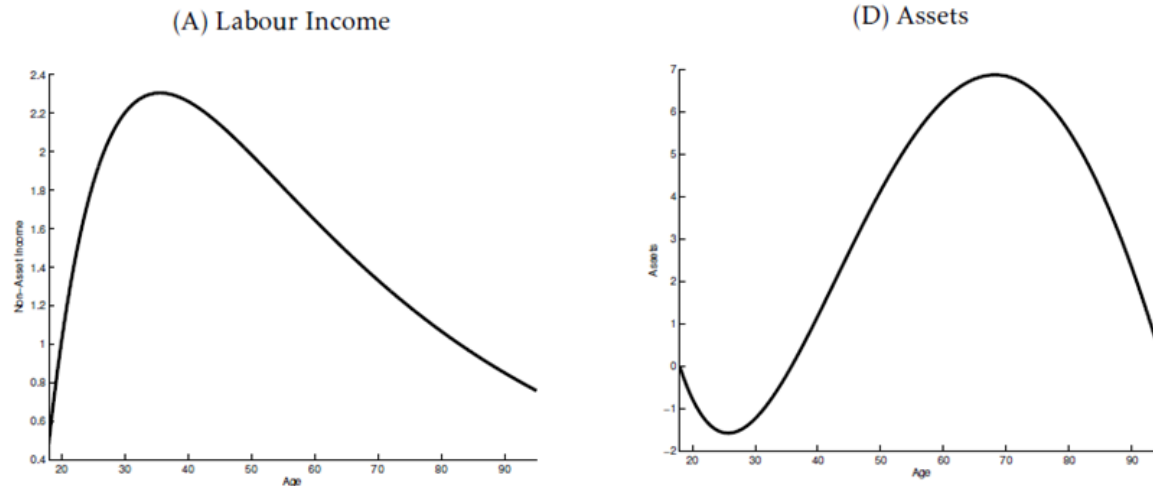# Some have already tried and found that

Poverty estimates including wealth are much lower than the traditional income-based measures,

and

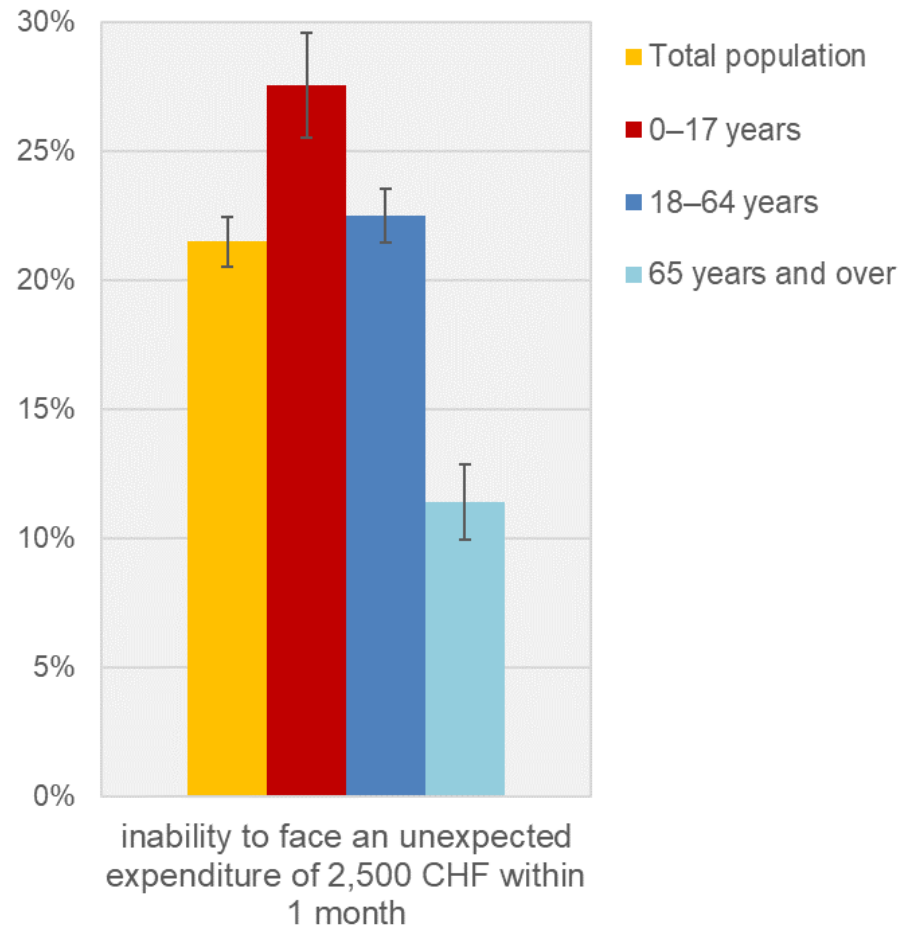poverty rates of the **elderly** are much more affected than those of the non-elderly.

(Kuypers & Marx 2018 on Belgium and Germany)

(A) Labour Income

(D) Assets

This is linked to the concept of horizontal redistribution, which is redistribution from one social group to another.

The importance of this measure in Switzerland

- Most people **inherit** their wealth when they are 55 or older (Stutz, Bauer & Schmugge 2007)

- Even though 22.5%of 65+ were at risk of poverty according to an income based measure in 2016, only 11,4% could not face an **unexpected expenditure** of 2,500 CHF (OFS 2018)

- Some cantons are already computing these measures with tax register data, but there is no legitimacy and the methods are always different (Wanner & Gabadinho 2008; LUSTAT 2013).

Legend:
- Total population
- 0–17 years
- 18–64 years
- 65 years and over

inability to face an unexpected expenditure of 2,500 CHF within 1 month

unine

Before aggregating income and wealth, we should decide:

The wealth components

- **Housing wealth** is the most important wealth component held by the middle class.

- The main residence can be seen a fourth pillar for retirement as it reduces housing expenditures freeing resources for other types of consumption

But

- Younger households will appear mortgage-indebted, whereas older households will appear very wealthy because they have already repaid their mortgages.

- The main residence is often difficult to liquidate in the short term and does not assure financial stability for current expenditures other than housing costs.

Possible solution: liquid financial assets that are easily monetized and gains from home ownership

The equivalence scales

- There are no internationally accepted standards, wealth can be seen as extra income or not

- Some applications have used wealth per capita (Balestra & Tonkin 2018)

- The most used scale for income is the modified OECD with 1 to the household head, 0.5 to each additional adult and 0.3 to each child under 14 years old

- Alternatively, some have used the square root of the household size √

(Brandolini et al. 2010, Azpitarte 2012, Kuypers & Marx 2018), or other adjustments based on the household size (e.g. CSIAS for income including or excluding housing costs)

- Normative scales to account for vulnerability (Menon, Perali & Sierminska 2017) extra weights to single parents (0.40), the unemployed (0.40), retirees (0.20) and people with at least 50% of invalidity (0.50).

- Wealth-based equivalence scales (CSIAS for wealth with no equivalence scale for adults and limited equivalence scales for children).
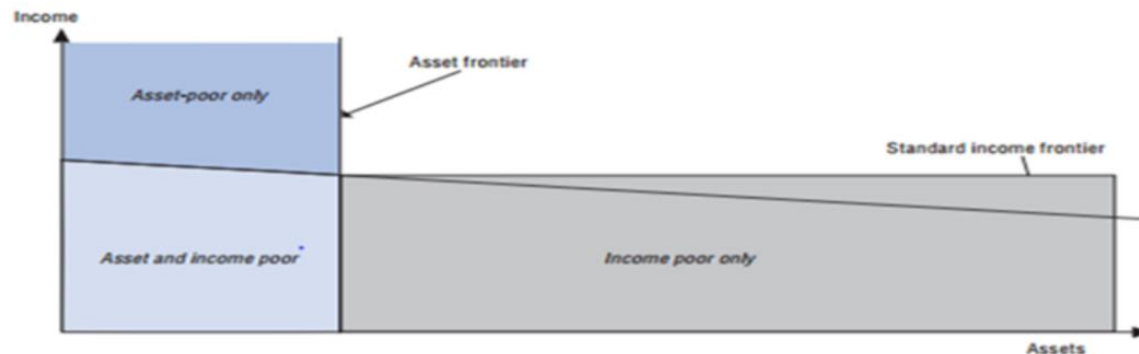
The approach

- Unidimensional poverty index through the annualisation of wealth

Annualized income poverty: AY = Y + $AY = Y + \left[\frac{r}{1-(1+r)^{-le}}\right] NW < Z$

Interesting but there are some negative aspects:

- younger households typically have lower net worth and longer life expectancies, which translates into much lower annuities and higher poverty rates.

- the saving potential of younger adults and their fertility decisions are not taken into account by this measure.

- the correlations between life expectancy and the level of wealth held by individuals or the dependency between the level of their (financial) education and the interest rates used to annualize wealth are difficult to include in the model.

- wealth should be entirely consumed during the life course.

- Separate income poor, asset poor and jointly poor households

With two different thresholds: *Income poverty*: $Y < Z$
Asset poverty: $NW < \delta Z$

The threshold

We choose a relative approach

for income: **60% of the median equivalent disposable annual household income**

and

for wealth: it could be a **survival time** of 3, 6, or 12 months out of poverty (1/4, ½, 1 of the income poverty line)

3 months   6 months   12 months

We use a relative approach for international comparability with 6 months of survival time.

Official statistics might prefer an absolute threshold and use the relative only for comparability reasons. A 3 months survival time is also often used.

We test

- *Different wealth components*

- *Different equivalence scales*

We compare a measure with no scales

with measures that consider **higher economies of scales for children** like the income poverty line (with the modified OECD scale),

or economies of scales among all household members **independently of children** (with the squared root of the household size or the CSIAS scale for income),

or no economies of scale but **different needs across household members** (with the household size),

or **different needs plus a vulnerability factor for the retirees** as suggested by Menon et al. (2017) (with the household size and a 0.2 factor for retirees).

or **different needs plus a vulnerability factor for families** as suggested by the **CSIAS for wealth** (with the number of adults and a 0.25 factor for families and 0.5 factor for single parents)

- *2 approaches*

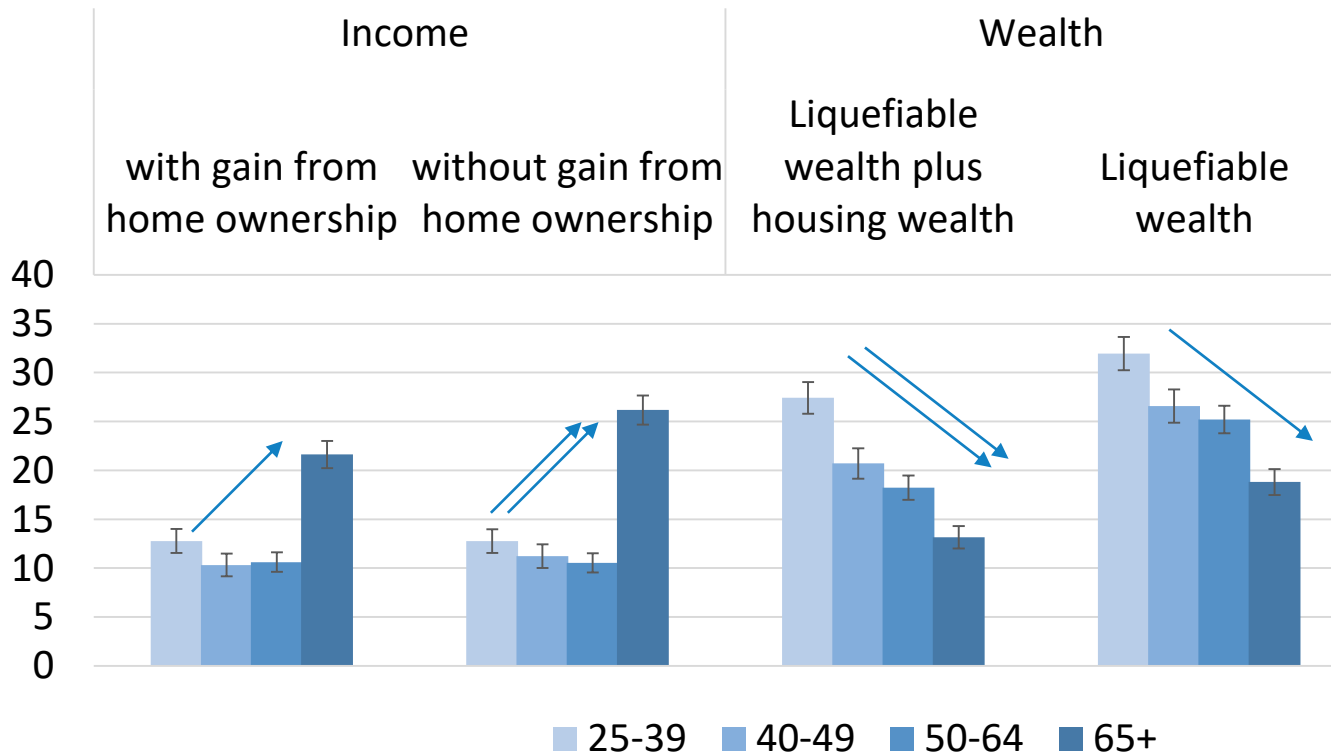- *Different age groups*

Results

Poverty rates by EITHER income OR wealth
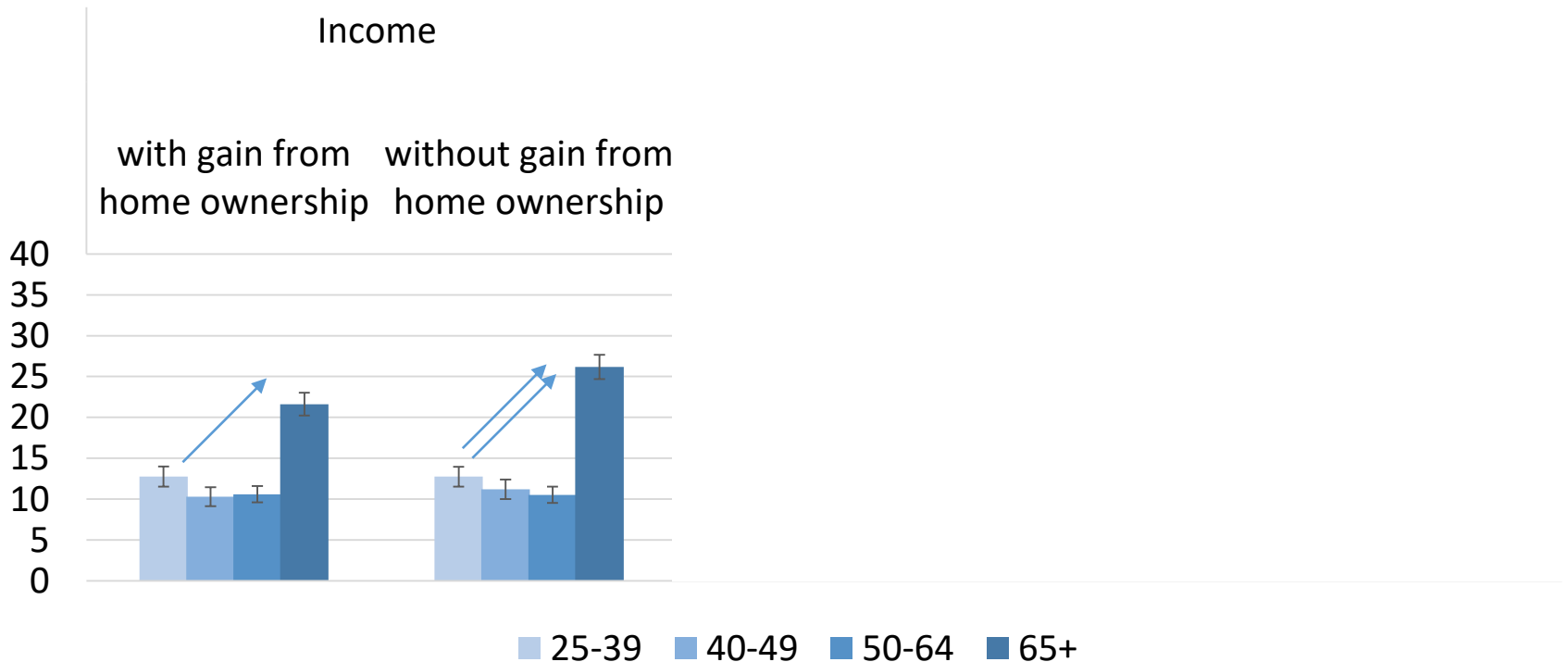
The elderly are the group that suffers the most from income poverty.

Their poverty rate increases if we exclude gains from home ownership because of their high home wealth.
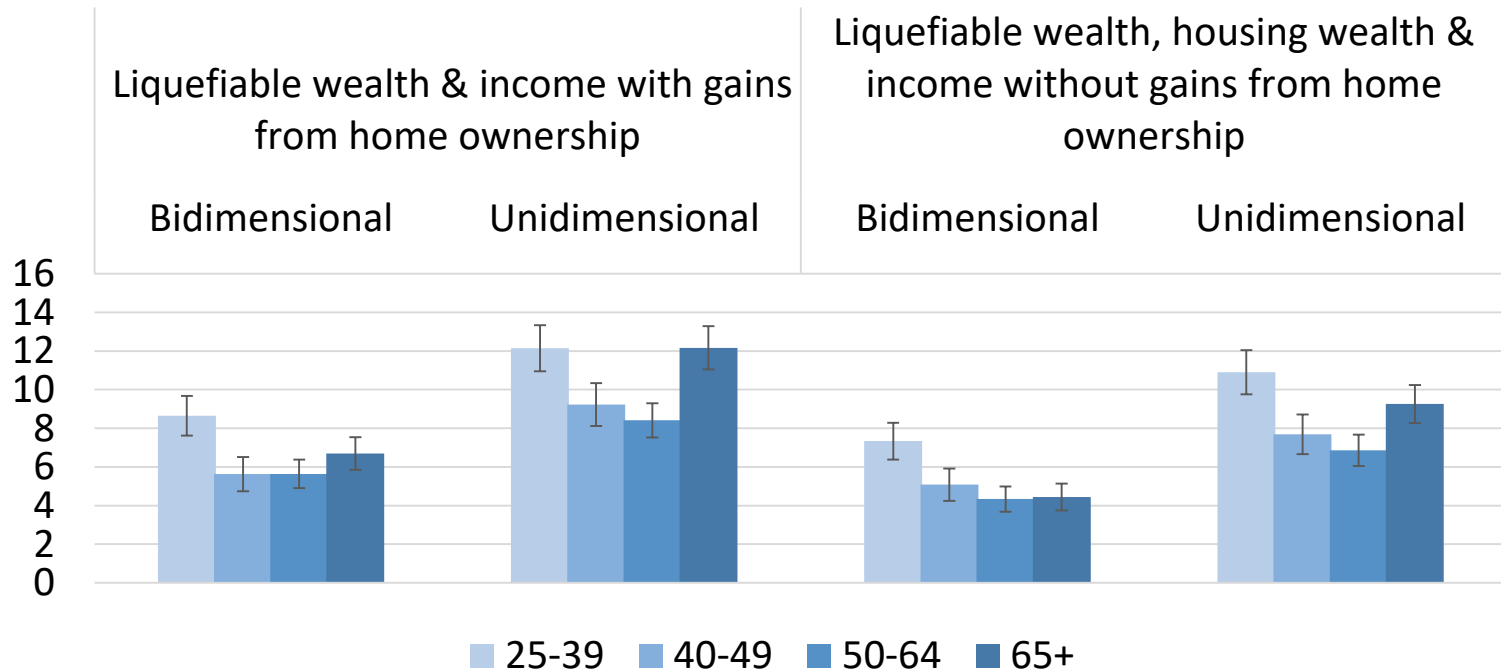
Poverty rates by EITHER income OR wealth

The young become the group that suffers the most from wealth poverty.

The difference between the young and the elderly is aggravated by housing wealth.

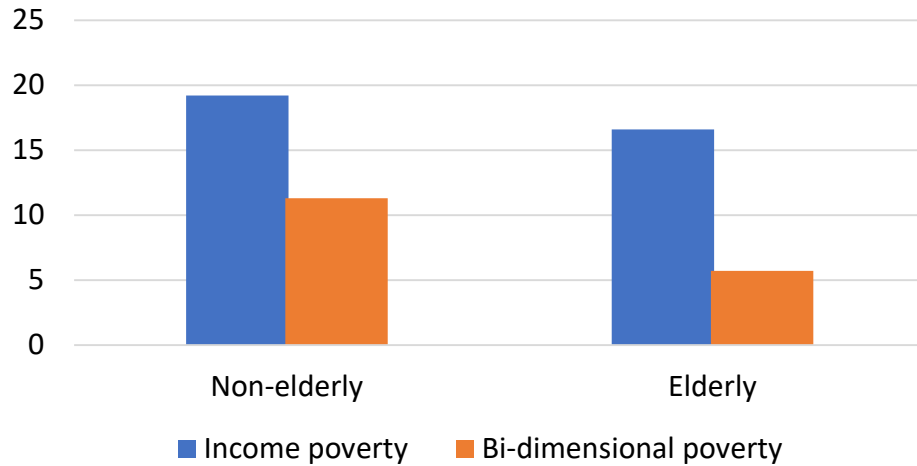# Poverty rates by BOTH income AND wealth

The bi-dimensional approach provides lower estimates than the unidimensional approach, which remains more income based.
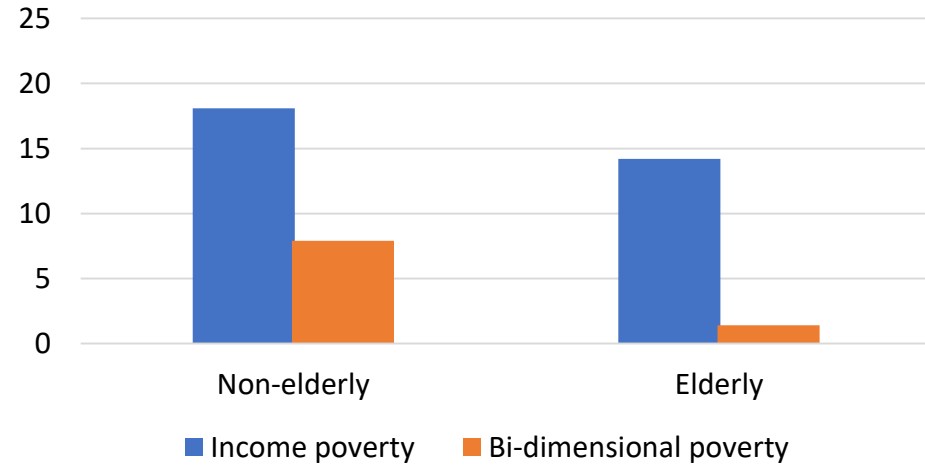
The young are the most vulnerable population according the bidimensional approach. The elderly are more penalised with housing wealth.
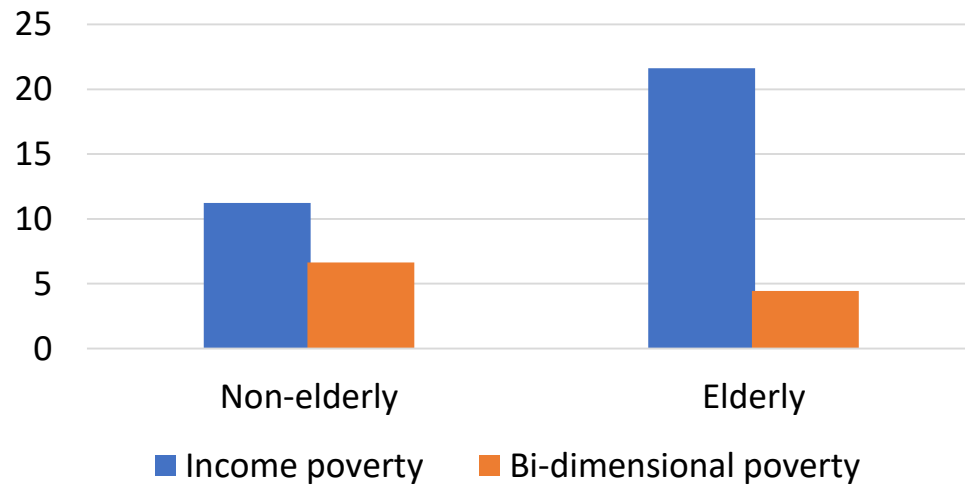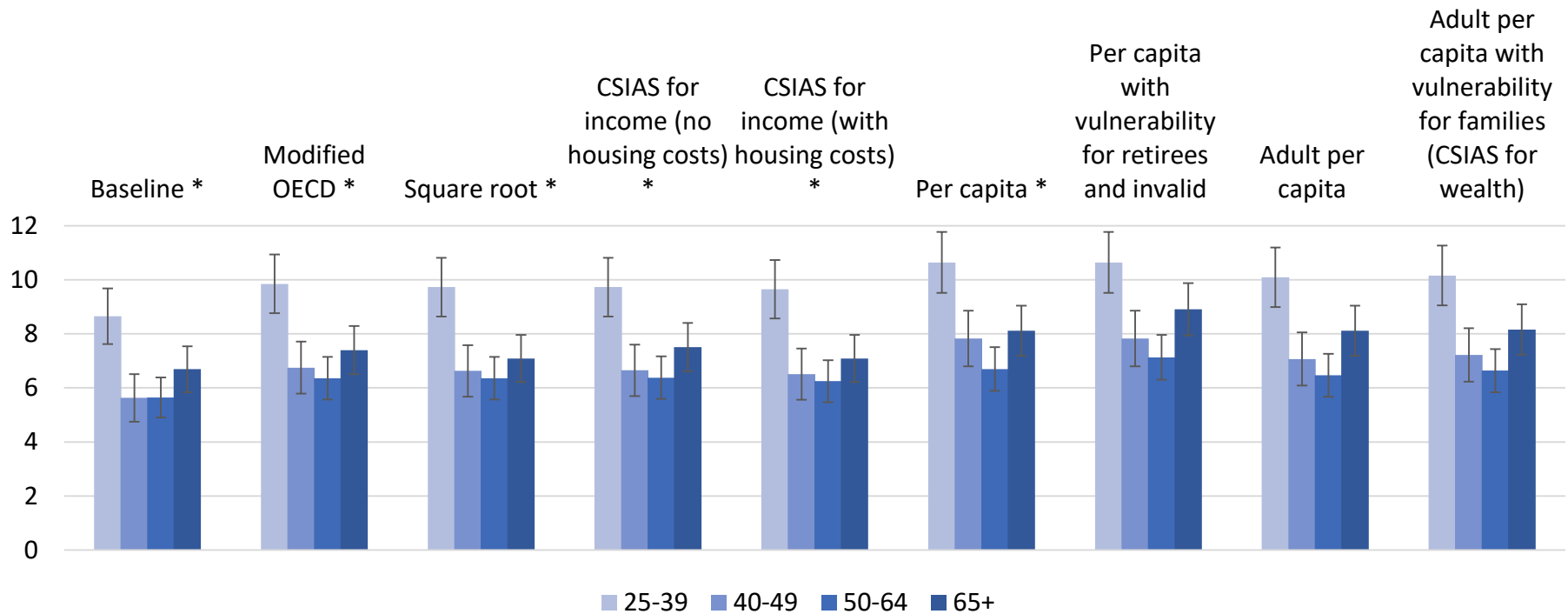
Comparison with other countries

Effect of the equivalence scales

Almost identical effect of the modified OECD, the square root and the CSIAS for income with and without housing costs.

Adding a vulnerability factor to the per capita measure makes the difference between the young and the elderly insignificant. The same effect also for an adult per capita equivalisation. The vulnerability for families added by the CSIAS for wealth does not really change the picture.

Conclusions

- Although the elderly are the most vulnerable group according to a measure of income poverty

- young adults are the most vulnerable group according to both a bi-dimensional and a unidimensional measure that includes income and wealth

- Most of the elderly have sufficient liquefiable resources to survive six months without falling into poverty

- Including home wealth (and gains from home ownership) in the measure of poverty would create a higher vulnerability for the elderly that would not be captured by the poverty rate.

- The inclusion of equivalence scales increases the risk of poverty for all age groups.

- The choice of the equivalence scale changes the significance of the difference between the young and the elderly.

Thank you for your attention!

unine