POLICY SERIES

The Definition of Poverty

By David Seymour

SENIOR POLICY ANALYST

About the Author

David Seymour, Senior Policy Analyst, and Director of our Saskatchewan Office, joins the Frontier Centre from New Zealand. He holds degrees in Electrical Engineering and Philosophy from the University of Auckland, where he also taught economics. After working as an engineer in New Zealand he is applying his passion for high performance government to policy issues on the prairies. In his first year working for the Frontier Centre David has carried out extensive media work, presenting policy analysis through local and national television, newspapers, and radio. His policy columns have been published in the Winnipeg Free Press, Regina Leader Post, Saskatoon Star Phoenix, Calgary Herald, Edmonton Journal, Windsor Star, Nova Scotia Herald and the National Post. David has produced policy research papers in the areas of Telecommunications Privatization, Education, Environmental Science, Housing, Anti Poverty Policy and Fiscal Policy. However, his major project with the Frontier Centre is the Local Government Performance Index (LGPI). The second annual LGPI was released in November 2008, at a time when municipal accounting standards in Canada must be improved if the municipal government sector is to reach its potential as an economic growth engine for Canada.

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Executive Summary

This Policy Series paper answers the question: What is poverty and how is it measured? To start, it is necessary to distinguish between relative poverty, where poverty is defined as having less than others in the same community, as distinct from absolute poverty, where poverty is defined as lacking access to some basic bundle of goods. Both measures have their flaws, but it is important to recognize the characteristics of any given measurement in question.

A survey of major Statistics Canada methodologies that are often used as proxies for poverty levels finds that both the Low Income Cut-off (LICO) and Low Income Measure (LIM) are relative measures, replete with the characteristics we would expect of them.

Economist Chris Sarlo's solution is presented as the best attempt to date to navigate between the transience of relative measures and the elusiveness of a universal absolute definition. His model is notable because by focusing on

'the means required for physical survival,' it takes into account the question of adequacy in a constantly updated context.

There are considerable questions raised over the use of income as a proxy for consumption. An extreme example wherein some people registered as being in the bottom decile for income were found to be in the top decile for expenditure brings this question into sharp relief. With additional data from statistics Canada, the case is made that income based poverty measures are highly unreliable.

Finally it is worth pausing for thought at the possibility that poverty is not something measurable but a question of being able to achieve aspirations.

Overall, this paper is not designed to define poverty out of existence or dismiss attempts to understand it. On the contrary, it is an examination of our understanding of poverty that finds serious flaws in the way it is currently measured and concludes that we need to do better.

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Introduction

Concern about poverty is a worldwide phenomenon. While the last two centuries have seen unprecedented and impressive growth in the health and wealth in the Western world after 1800, and after 1950 in other regions such as East Asia, it is disturbing that some people are still left without the basics required to survive. This paper aims to identify what poverty really is, and assess some of the approaches to measuring it that are commonly cited in mainstream debates on poverty.

Concern for poverty is a sign that the people of Canada feel compassion for fellow citizens and want to give everyone a 'fair go.' However, as we will see, much of the attention given to poverty by the media, academics, and advocacy groups is poorly focused.

An Analogy to Poverty Measurement from another Field

In the mainstream media and in some specialist publications, poverty rates are assumed to be a concrete concept. They are reported as something tangible and real that can be measured like, for instance, temperature. A more helpful analogy comes from the field of psychometrics where attempts are made at measuring something more abstract, the concept of general intelligence or 'g.' [1]

G is a hypothetical quantity of the human mind that attempts to predict an individual's ability to think and solve problems. It is not something that can be directly measured, nor does it even exist in a concrete sense

> *Much of the attention given to poverty by the media, academics, and advocacy groups is poorly focused.*

but it is a useful model. Various IQ tests that measure problem-solving abilities are said to be a proxy for g, and the fact that a range of different tests can be found to give similar results for any given individual suggest that these tests go some way towards measuring it.

However, it would be a mistake to assume that any one test is a direct measurement of g, and this is where an analoge to poverty measurement can be drawn.

Just like the various IQ tests act as a proxy for g but none actually measure it directly, the various indexes and statistical measurements of poverty are merely attempts at expressing how many people in a society live in a condition we can define as poverty. But it is just as abstract a construct as general intelligence. Extending the analogy a bit, we could say that the various poverty measurement techniques assessed in this backgrounder are actually attempts at measuring 'p.'

The critical similarity between attempts to measure g and attempts to measure poverty is that both attempts at measurement are only as good a reflection of the measured quantity as the test itself. In the field of psychometrics there have been many good and many bad attempts — for example, those that infamously confused cultural familiarity with the subject of the test with intelligence. As we will see, poverty measures also have varying success depending on the mechanical features of the measurement.

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All government policy ultimately uses sovereign power to sacrifice one opportunity for the gain of another...

The Importance of Focus

Poor focus leads to solving the wrong problem, and solving the wrong problem in public policy inevitably leads to making the wrong sacrifices. All government policy ultimately uses sovereign power to sacrifice one opportunity for the gain of another that may have a greater democratic mandate. An example from another policy area is the freeze on Saskatchewan university fees which artificially depresses university revenues and draws funding away from other government activities, but has the politically popular benefit of reducing nominal prices for students.

In the case of fighting poverty, many choose to focus on income levels as an indicator of poverty. The conflation of equality and poverty is seen in the tendency of some to define as many as one in five Canadians as being in 'poverty.' However, it is likely that this figure dilutes our focus on those who are in the most acute need of better anti-poverty policy. As we will see, these methods of poverty estimation are wrought with inaccuracies and lead to increased political demand for a bigger welfare state and a greater volume of income redistribution, moves that target inequality but not necessarily poverty.

Given that poverty should not be defined as all those earning below a certain income, we will look at opportunities for improvement as a real measure of poverty.

Some different definitions of poverty

Focused poverty concern means having a clear understanding of what we mean by the term. Unfortunately the history of the poverty debate in Canada has been plagued by disagreement over what the poverty problem really is. The key questions have been whether poverty is an absolute or a relative concept, and whether it should be measured by the income, expenditure, or consumption of those alleged to be in on poverty. A more abstract third question is whether poverty should be objectively or subjectively measured.

The Old Chestnut: Relative and Absolute Poverty

As a relative (and income based) concept, poverty has been defined to include anyone earning less than the median or some other marker in the income distribution. It should be clear that this is much less a measure of poverty as a measure of equality. Even if the entire society became ten-fold richer tomorrow, this definition would still identify the same number of people in poverty. One manifestation of this effect is that Statistics Canada's relative measure, Low Income Cut-off (LICO) finds more people below the low income cut-off line using after-tax measures than it does using before-tax measures. The reason is not that taxes are redistributed to lower income earners but rather they are redistributed from higher income earners. In other words they compress income differences by reducing the incomes of higher income earners and more people are thus "poor" if the LICO measurement is used as the gauge. As Statistics Canada explains regarding the LICO:

> The number of people falling below the cut-offs has been consistently lower

on an after-tax basis than on a before-tax basis. This result may appear inconsistent at first glance, since incomes after tax cannot be any higher than they are before tax, considering that all transfers, including refundable tax credits, are included in the definition of "before-tax" total income. However, with a relative measure of low income such as the LICO, this result is to be expected with any income tax system which, by and large, taxes those with more income at a higher rate than those with less.[2]

This is an example of how relative measures define poverty. It is actually possible to reduce poverty under this measure by making people poorer. Even if the lowest income earners are living comfortable lives, this definition still defines them into 'poverty.' The only way to eliminate poverty under this definition would be to have exactly the same income for every single person. Needless to say historical attempts at reaching this goal have resulted in greater poverty, among other serious problems.

If measuring poverty as a purely relative concept is unhelpful; the alternative appears to be measuring 'absolute' poverty.

Absolute poverty is the measurement of people's means of survival against some 'bottom line.' That is, regardless of what most people in the community possess, poverty is defined as lacking access to certain means. The immediate problem in defining poverty as an absolute concept is the decision as to what those certain means should be. If we consider changes in wealth through time and across the globe, there is no enduring standard. Poverty in Canada in 2009 is non-existent compared to what might be considered poverty in sub-Saharan Africa, or compared to Canada itself during the Great Depression. Of course, if absolute poverty measures change as economies and expectations grow, then we are back to a relative measure.[3]

> **Even if the entire society became ten-fold richer tomorrow,** *this definition would still identify the same number of people in poverty.*

The Role of Statistics Canada

As the primary compiler of statistics on almost everything in Canada that can be counted, many look to Statistics Canada ("StatCan") for guidance in the poverty debate. Most of the statistics cited in this debate come from StatCan's LICO, Low Income Measure (LIM) and the longitudinal (following the same individuals for several years) Survey of Labour and Income Dynamics (SLID).

Because StatCan's job is primarily to count things rather than answer political questions, they have refused to give a definition of poverty. Nor do they claim that their measurements actually reflect poverty, much to the frustration of some poverty researchers and advocates.

> Media, researchers and policy-makers interested in measures of low income are typically concerned with the extent to which individuals in the population are living in poverty. Unfortunately, defining poverty is far from straightforward. The underlying difficulty is that poverty is a question of social consensus, defined for a given point in time and in the context of a given country. Decisions on what defines poverty are subjective and ultimately arbitrary.[4]

Nevertheless their figures are used by many as a proxy for poverty measurement so it is worthwhile understanding how these work.

> *...to live a physically sustainable life in the* contemporary Canadian context, comes much closer...

The Low Income Cut Off (LICO)

The low income cut-off measure (LICO) is a relative measure. It calculates the percentage of income the average family spends on clothing, food and shelter then defines any family spending twenty percentage points more than that average percentage as being below the cut-off. To allow for differences in family sizes, and different costs of living in different locations, the figure is adjusted to reflect Canada's demographic makeup by setting different cut-off levels for different families and locations, then projecting the nationwide number of people below the cut off. Clearly, twenty percentage points is an arbitrary figure that does not necessarily relate to the well being of anybody in a concrete way. This is the characteristic of a relative measure.

However it might be said that even if the measure is arbitrary it still shows yearly variations. To an extent this is correct; if the number below the cut-off income changes from year to year we can predict that there has been a change in the real poverty rate. This claim also brings out another feature of relative poverty measures — that the threshold must be changed to reflect increasing wealth in society.

Each year the income level for the cut-off is recalculated of a base year according to changes in the consumer price index. However this base year is also periodically 'rebased' to reflect that the average disposable income has risen and the

average proportion spent on food clothing and shelter also falls. When the average falls, the income point that is twenty percentage points below the average also falls. So far the LICO point has been rebased in 1959, 1969, 1978, 1986, and 1992.[5] Each time the bar has been raised, meaning a lower proportion of income is required to be spent on food, shelter and clothing before a person is defined into poverty. For example, in the 1969 base year the Low Income Cut-off level for a family of four living in a city of 100,000 to 499,999 people was $5,355. In 1978 it was $11,500; in 1986, $18,382; and in 1992 $21,628. In other words, the income of those below the line has dramatically improved, but they are still considered below the same line.[6]

LICO is a classic relative poverty measure. It uses an arbitrary income gap to define low income, and 'low income' becomes higher as Canada becomes wealthier on average.

The Low Income Measure (LIM)

The Low Income Measure (LIM) is also an arbitrary and relative measure which defines low income as being 50% below the median family income. Like LICO, these 'family' incomes are adjusted for family size where low income for larger families and families with older members is adjusted to be higher than that for smaller families with younger members.

The main justification for the LIM is that its simplicity makes it comparable to other countries' income distribution measures, as well as the OECD standard measure.

Unlike LICO, which attempts to measure income against some basic basket of goods, LIM is purely focused on income distribution. It has no focus on the actual

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standard of living of anybody in Canada, only their income relative to the median. For this reason, LIM should be regarded as either a purely relative measure of poverty, or simply a measure of income distribution.

Sarlo's Solution

One attempt at finding a middle path between futile relative measures and elusive absolute measures of poverty is that of economist Chris Sarlo. Sarlo argues that poverty should be defined as not having the means to live a physically sustainable life.[7] Sarlo's rationale is that his focus on basic needs — the things required to live a physically sustainable life in the contemporary Canadian context, comes much closer to identifying compassionate Canadians' view of a poverty-free life. It is worth noting that for the year 1988, Sarlo's measure found that only a quarter as many Canadians live in poverty as Statistics Canada's Low Income Cut Off methodology (a relative measure) claimed that same year.[8] The significance of this measure is not that it deflates recorded poverty levels, but that it shows the difference between measuring poverty as people having the means to survive versus a birds-eye-view of national income distribution.

The Problems with Measuring Poverty by Income

All of the measures reviewed so far rely on measuring income as a proxy for standards of living and well being.

If we take the position that Sarlo's poverty measure comes much closer to focusing on the kind of poverty, not inequality, that most Canadians would like to see eradicated, it still has one major weakness. Like the Statistics Canada measures, Sarlo's poverty definition is based on reported income.

> **With the advent of longitudinal surveying, the difference between persistent low-income and short-term low-income comes into focus.**

As Sarlo explains: "Although income may understate the actual standard of living … data availability constrains us to use income as our measuring stick."[9] Sarlo is aware that unreported income, drawing on savings, and in-kind benefits can undermine income as a measure of poverty,[10] but nevertheless his poverty measure is the best possible with the data available.

British poverty researcher David Green also criticizes income as a measure of poverty.[11] Most income-based poverty measures take a new sample each year and report the proportion earning below some cut off level. What this method fails to register is that the people below the cut-off line in one year may not be the same people in the following year. For this reason, Green prefers expenditure as a measure, citing that household expenditure and income are consistently different. In an extreme (but actual) example, three per cent of those in England's bottom income decile were also in the top expenditure decile. Single-year income measurements show us little more than the income a household or individual declared in that year. Statistics Canada's more recent measures based on the Survey of Labour and Income Dynamics have made similar revelations. With the advent of longitudinal surveying (the StatCan Survey of Labour and Income Dynamics), the difference between persistent low-income and short-term low-income comes into focus. From 1993 to 1998, 24% of the Canadian population was deemed low-income at some point, but only 2.9% were in this category for all six years.[12] Or, as another commentator puts it: "Poverty is a

> *...it is peoples' perspective of their own well being versus their expectation that matters.*

revolving door for about 60% of those who are poor in any given year."[13]

Not only do income measurements miss what is actually spent, they often miss other means people have for providing the necessaries of life. Expenditure measures may or may not access to capital assets that are useful, particularly housing.

Subjectivity

Another perspective on poverty holds the concept as subjective. Rather than any given distribution of income or proportion of people below any absolute living standard, the perspective holds, it is peoples' perspective of their own well being versus their expectation that matters. One striking example holds that the twenty years preceding the French Revolution featured dramatic rises in material living standards for almost all French people. However, those increases did not keep pace with expectations, expectations which then contributed to the revolution.[14] This is not to say that we should abandon all attempts at measuring poverty in an objective way, let alone that reducing expectations is a valid strategy for reducing poverty. Rather, it is important to remember that peoples' aspirations and belief in the future can be just as important in framing poverty as external, objective measures of their predicament. The Frontier Centre will revisit this theme throughout the Anti-Poverty Project.

Conclusion

The object of this paper has not been to prove poverty non existent, or argue that we should be unconcerned by poverty. Poverty *does* exist and Canadian compassion should continue to be harnessed in providing support for anti-poverty measures. However it should also be clear that many of the attempts to define and measure poverty to date are inadequate. Relative poverty measures are little more than an opportunity for ideologically-driven advocates of income equality to abuse the concept for their own ends and to set the cut-off line as high as they dare. Attempts at setting absolute poverty measures, particularly that of Christopher Sarlo, have given a definition of poverty much closer to most Canadian's common sense perception of poverty. However even these measurements can fail to capture true living standards because income is not necessarily related to actual consumption. The object of this paper has been to raise the importance of focus, making sure that we are solving the right problem. In short, we need to do more than focus exclusively on income statistics.

SOURCES

1. While some authors, most notably Hernstein and Murray (1994), have drawn parallels between welfare and psychometrics in the past, the point of this comparison is merely to illustrate the concept of measured results versus actual situations.

2. Statistics Canada (2007) *Low Income Cut-offs for 2006 and Low Income Measures for 2005.* Available online: http://www.statcan.ca/english/research/75F0002MIE/75F0002MIE2007004.pdf p10.

3. See Luciani, P. (2001) *Economic Myths; Making Sense of Canadian Policy Issues: Third Edition.* Addison Wesley, Toronto pp. 220-225 for a review of relative and absolute poverty and the conclusion that absolute poverty ultimately collapses into a kind of relative measure.

4. *Op cit.* p. 6.

5. *Ibid.* p. 9.

6. *Ibid.* p. 33-35.

7. See Sarlo, C. (1996) *Poverty in Canada: Second Edition.* The Fraser Institute, Vancouver. See chapter 4 for an overview of Sarlo's basic needs alternative to relative income based poverty measures.

8. *Ibid;* p. 3.

9. *Ibid;* p. 47.

10. *Ibid;* p. 18-34.

11. Green, D. *Benefit Dependency: How Welfare Undermines Independence*. (1998) Civitas, London, pp24-31

12. Picot, G. and Myles, J. (2005) *Income inequality and Low Income in Canada: An International Perspective.* Statistics Canada. p. 22 Available online: http://www.statcan.ca/english/research/11F0019MIE/11F0019MIE2005240.pdf

13. Ismael, S. (2006) *Child poverty and the Canadian Welfare State.* University of Alberta Press, Edmonton p. 55.

14. Kazemipur, A. and Halli, S. (2000) *The New Poverty in Canada*. Thompson Educational Publishing, Toronto. pp. 35-36.

Further Reading:

WHICH BEST HELPS THE POOR?
Minimum Wages, Tax Credits or Tax Exemptions? FC Policy Series No. 37, January 2008

A CONVERSATION WITH DAVID BEITO
Author of *From Mutual Aid to the Welfare State: Fraternal Societies and Social Services, 1890-1967,* July 2000

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