

## CYCLICAL POVERTY IN MATURED WELFARE STATES

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### Summary

The term “short-term” or “cyclical poverty” is not widely used, while most of the statistics on poverty fulfilling a role in the political debate, either in the developing or the so-called developed world, deal with snapshots of poverty. Information on cyclical poverty presupposes the availability of panel data that make possible a longitudinal view on poverty. Using panel data for the Netherlands, Germany, the United Kingdom, the United States and Canada, the chapter draws attention to the incidence and distribution of transient (single-year), cyclical and persistent poverty in affluent societies. Since panel data are used for quite distinct policy regimes, the chapter provides some interesting and dynamic evidence on the performances of these different policy regimes in preventing short and long-term poverty. The chapter also examines the events which trigger the occurrence of these poverty profiles over time. The challenges for future policies are briefly sketched and the different responses of social policy to these challenges, in view of the broader debate about anti-poverty policies, are discussed. The chapter places the discussion on policy in the framework of more fundamental debates about the changing roles of the state, the citizen and community.

The chapter ends with a plea for a new model of the welfare state, called the “enabling society” or the “social investment society”. The role of the state in such a model is to draw heavily on investments in the “competence” and “social capital” (social networks, voluntary organizations) of its constituent citizens. A government supporting the “social capital” building process of their citizens might therefore be better equipped to deal with concerns of social exclusion and to promote social integration in order to bring a sustainable, fair and just society within its horizon.

## 1. Introduction

The term “short-term” or “cyclical poverty” is not widely used, while most of the statistics on poverty fulfilling a role in the political debate, either in the developing or the so-called developed world, deal with snapshots of poverty. Information on cyclical poverty presupposes the availability of panel data (repeated survey with the same person) that make possible a longitudinal picture of the changes in poverty statuses of individuals and households over time [see *Global Dimensions of Poverty and particularly Poverty Dynamics*]. However, panel data are not readily available yet, especially in developing countries, a fact which must be attributed to lack of resources since these panel studies are rather expensive and technically very complicated to handle. The first section of this paper deals, therefore, first with clarification of the definitions of poverty and social exclusion within such a dynamic perspective and how they relate to the standard snapshot approach. In a subsequent section the notion of “cyclical poverty” is compared with the range of familiar notions of longitudinal poverty as they exist in the literature -- such as recurrent, occasional, single-year, incidental and persistent poverty. Through the use of panel data for a number of European countries as well as the United States and Canada in this section, more insight is given into the incidence and distribution of cyclical poverty in affluent societies. Since panel data are used for the US, Canada, the UK, Germany and the Netherlands, it is possible to compare the outcomes for clearly distinct types of welfare state regimes [see *Poverty Perspectives and Public Actions Programs*]. Then, the focus shifts to the events triggering the occurrence of various poverty profiles over time. The interest focuses on the sort of mechanisms and causes that might explain the huge income mobility and the occurrence of large flows of people entering and escaping income poverty. In the next section of the paper, the role of social policy and welfare state regimes is briefly discussed. The paper ends with a concluding section on the future of welfare state policies in dealing with longitudinal poverty [see *Poverty in the Developed Countries of the World*].

## 2. Definition and Measurement of Poverty and Social Exclusion

In the literature on poverty a distinction can be made between definitions of income poverty and of relative deprivation [see *Concepts of Poverty*]. Reference is often made to the distinction made by Stein Ringen between direct (income definitions) and indirect (consumption or deprivation related) definitions of poverty. Related distinctions were made by Sen on the direct and income method and by Atkinson on the minimum level of resources and the broader notion of the minimum standard of living. The income method is mono-dimensional, focusing solely on income, whereas the deprivation method is multi-dimensional, covering a broad set of indicators for the measurement of people’s actual living conditions or living standards. The multidimensional approach has some support in the academic debate at the international level, at least in the developed countries, and also the World Bank in their World Development Reports has shown increased interest in the multidimensional approach.

From an economic point of view, poverty is perceived either as a state of low consumption or, more subjectively, of low welfare. Economists, therefore, first of all have adopted either the standard “budget-line approach” or one modified into a money

income/transferred expenditure poverty line (as the US poverty line). The first one is based on assessing a minimum basket of goods or nutritional standards which are needed to attain a minimum standard of living. The budget-line was originally perceived as an absolute poverty line because it was based on a basket of goods required to maintain a minimum standard of living. The expenditure line is a budget line that is transferred into a money equivalent. In the US budget-line approach it is the money equivalent of the basic food package, multiplied by three, that is required for people to meet the minimum nutritional standards..

However, in the course of time with the increasing affluence of American society, the level of the line has been adjusted to changes in opinions as to what the minimum package should be. The level of the American poverty line is therefore not a hungry or starvation line anymore but a relative poverty line that reflects the rising and high living standards within the American society. In the approach adopted in a number of EUROSTAT (Statistical Bureau of the European Union) reports on the issue, the expenditure line was set at 50% of the median equivalent level of expenditures assessed on the basis of a representative survey. Hence, the expenditure line is also a relative poverty line that has little to do with the sort of absolute poverty lines that are used in the debate about poverty at the global level.

The World Bank in their reports on poverty use the one and two dollar a day level as the low and upper poverty line. These sorts of poverty lines might correctly be called hunger or starvation lines; if such a line were used to measure poverty in an affluent society nobody would be found actually to live in poverty. But in 1998 one in four to five people in developing countries (24%) had to live on less than \$1 a day and thus earn incomes even below this austere poverty line. The World Bank in its recent Human Development Report also applied a relative country-specific poverty line based on the 1993 average consumption level in each country. This expenditure line has been calculated as the money equivalent of one-third of the average consumption level in each country, at 1993 purchasing power parity. This expenditure line is shown in some cases to be equal to \$1.6 a day which is 60% higher than the \$1 line and therefore reveals much higher base lines for the poverty rates in many countries, particularly those with higher average consumption. For the whole set of developing countries the proportional poor went up from 24%, according to the austere absolute line, to 32% according to the relative poverty line in 1998.

The poverty lines used in affluent societies are shown to share their relative nature. That holds *a fortiori* for the so-called subjective poverty lines, which are based on subjective evaluations of people of their income. Subjective approaches are based on questions in representative surveys about what level of household income people would consider as sufficient to maintain a minimum standard of living or, in other words, how much money the respondent thinks the household needs just to make ends meet. People with incomes at the threshold level are then considered to be the experts best qualified to make a judgment about the income they consider just sufficient or that they need just to make ends meet. Equivalence scales are derived from the answers of the respondents themselves and do not need to be imposed by the researcher or the politician. Subjective poverty lines are valuable in providing information about whether objectively- or politically-defined, social minimum standards in society are sufficient to meet the

perceived minimum income needs of the population.

#### *A broader view*

However, any reflection on the social position of the poor in modern affluent societies needs a much broader basis than the simple focus on income or consumption, which leaves aside the socio-psychological and societal or non-monetary aspects of poverty. According to this view the societal and non-monetary aspects of poverty might be held responsible for what a Dutch researcher eloquently called the “Devil’s Circle of Poverty”. Particular groups of people in society were apparently unable to escape poverty quickly after having entered it. Persistent and recurrent poverty seem to be of increasing concern within the poverty debate in affluent, developed societies. The understanding of these new phenomena of poverty in the developed world calls for a wider perspective on poverty that is reflected in the notions of relative deprivation and *social exclusion* [see *Concepts of Poverty*]. The concept of social exclusion is also dominant within the European social policy debate, particularly when it achieved a legal basis in the social protocol of the 1992 Maastricht Treaty and in the new article 137 of the Amsterdam Treaty in 1997. The use of these new concepts reflects the need for a more comprehensive poverty concept that is associated with the notion of lack of participation in the common life-style of society, including attachment to various institutional, social, cultural and political ties within that society. It refers to a limited access for particular vulnerable groups in society to the most common societal resources available to the “modal” citizen. In this interpretation the concept of poverty bears close resemblance to the notion of exclusion from *full citizenship*, defined in terms of access to a satisfactory income, good health, decent housing, a satisfactory social network, sufficient education and access to paid work. The non-monetary approach fits therefore into a more general framework of “relative deprivation”. It involves both Townsend’s “lifestyle” and Mack and Lansley’s “consumption deprivation index” approach. These deprivation poverty approaches are generally based on a more or less extended and inclusive list of deprivation-related dichotomous items (having good health or not, etc.) posed to a representative sample of the population. Deprivation is defined as “enforced lack of items” on a deprivation scale. Only when a person for financial reasons does not possess an item which (s)he considers a necessity is (s)he considered deprived of that item. People are considered deprivation-poor whenever their resources are below a certain empirically-assessed, cut-off point on the distribution of deprivation scores (lacking x or more items).

The World Bank uses the term “vulnerability” to illustrate the multi-dimensional nature of poverty. The World Bank distinguishes several dimensions underlying this concept: the number of physical assets, human capital (education), diversification of income sources, links to networks (household’s social capital), participation in the formal safety net and access to credit markets for consumption smoothing. According to the definition of the World Bank, vulnerability is the risk that a household or individual will experience an episode of income- or health-poverty over time. Hence, *vulnerability* is a dynamic concept. This brings us to the *time dimension* of poverty which is crucial for a good understanding of the phenomenon in modern societies.

The time dimension brings an essential distinction to the fore between static and

dynamic approaches to poverty. A static approach pertains to actual states or situations (stocks) of poverty whereas a dynamic approach points to changes in poverty statuses over time, and processes causing people to move into or out of poverty. In Table 1 the matrix combining the twin concepts “direct-indirect” and “static-dynamic” is depicted. The definition of *impoverishment* (cell 1.1) pertains to life-course processes (life events) because of which people enter income poverty (cell 1.2), whereas the definition of *social exclusion* (cell 2.1) points to exclusion processes eventually leading to a state of so-called relative deprivation (cell 2.2). In the meaning of processes, both definitions of impoverishment and social exclusion refer to chains of life events causing people’s income and living conditions to deteriorate gradually over time because of which, eventually, a state of income poverty or relative deprivation might be attained. Both processes of impoverishment and social exclusion might be triggered by *internal* or *external economic shocks*, causing people’s employment, social security or welfare statuses to change abruptly in the course of time. Internal shocks are related to endogenous idiosyncratic life events that are associated with individual life biographies (marriage, divorce, separation, death), whereas external shocks are associated with commonly-shared and exogenous life events, occurring independently of individual life course decisions, like a (civil) war or a natural catastrophe.

	<b>Processes (flows)</b>	<b>States (stocks)</b>
Income (indirect) definition	1.1 <i>Impoverishment</i> →	1.2 <i>Income poverty (insecurity of subsistence)</i>
Consumption, deprivation (direct) definition	2.1 <i>Social exclusion</i> →	2.2 <i>Relative deprivation (social disadvantage, vulnerability)</i>

Table 1: Static and Dynamic Definitions of Poverty and Social Exclusion

Internal shocks co-determined by individual life-course decisions might be emerging also because of the typical features of the social system, and particularly its institutional set-up. Institutions are set-up to offer opportunities but at the same time impose constraints (e.g., minimum wage regulations, implicit tax rates, entitlement conditions, benefit levels, and guards against malfunctioning, corruption or inefficiencies etc.) on people’s behavior. The resulting institutional set-up offers an amalgam of concrete social rights and duties which, however, for some particular vulnerable groups in society, such as the single widowed, the long-term disabled and some ethnic groups, appears insufficient to protect them against problems of exclusion and poverty. Moreover, stigmatization, discouragement effects and “moral hazard” seem to reinforce these problems. People dependent on welfare are sometimes stigmatized by employers, for example, and therefore are not offered the job opportunities needed to escape from welfare. Discouragement effects occur whenever the “unemployed worker”, because of lack of success in past application experiences, is discouraged from searching for a paid job and therefore stays unemployed longer. Moral hazard behavior is at stake when people consume more of the social benefits than is strictly needed because of the

existence of generous social benefits. But also just because of being unlucky or subject to discriminatory practices [see *Case Poverty*], situations of income poverty and relative deprivation tend to be sustained, causing welfare dependency and eventually contribute to processes of impoverishment and social exclusion [see *Understanding the Meaning of Poverty*].

In the conventional approach there is little consideration for the longitudinal aspect of poverty. In modern dynamic societies what really matters for people is how their poverty statuses evolve over time: whether they are able to deal with temporary income shocks and to avoid cyclical and persistent poverty. The question addressed in this chapter is how stable or unstable income positions are over time and whether poverty is a persistent or a cyclical phenomenon. The interest focuses, therefore, on longitudinal patterns of poverty and deprivation, and on the factors which determine the processes of *impoverishment* and *exclusion* from average living standards. The longitudinal approach adds the time dimension to the static poverty concept, which makes it fundamentally different. As the British researcher Walker in the early 1990s argued, it is not just another dimension: “It is the medium within which poverty occurs and shapes the experience of being poor”.

The aim of this chapter is therefore to bring to the fore the question of what sort of hypothesis might be raised about the changing features of poverty in modern societies. A related issue is how policies should deal with changing patterns of poverty over time. If indeed short-term poverty tends to be of more concern in western societies in the modern era, how should policies deal with that issue and should they deal differently with cyclical poverty compared to single year or incidental and persistent poverty?

### **3. Cyclical and Persistent Poverty: Poverty Profiles**

Given the time dimension of poverty one should take into account that once individuals have entered poverty they do not necessarily have to stay in poverty for extended periods. People may be able to move into and out of poverty rapidly and, hence, experience multiple instances of short-term or temporary poverty. This phenomenon of *recurrent poverty* will in the sequence be called *cyclical* poverty. In developing countries cyclical poverty would mean that people lack the resources occasionally to secure their basic needs, due to natural disasters or inefficient agricultural production. In developed countries short-term poverty might arise from the fluctuations in the business cycle, causing people to become unemployed, retired or partially disabled, or from adverse economic shocks they may be exposed to. Modern, rapidly evolving societies have, according to the German sociologist, Ulrich Beck, evolved into “risk societies” where large numbers of people are increasingly exposed to a wide range of social risks. Poverty has become, therefore, a new social feature because it is now much more widespread among the population (“democratization of poverty”). Poverty statuses might therefore change quickly due to adverse economic shocks caused by changes in global economic conditions, changes in labor markets, changes in social welfare arrangements, changes in domestic policies and changes in individual life-biographies.

Time should therefore also be part of the definition of poverty itself, because the subjective experiences of short-term and long-term poverty, the welfare assigned to the

standard of living in each case, and the strategies to cope with poverty and exclusion at the individual level are quite distinct. In the short run people may be able to make ends meet by drawing on their savings and reducing their expenditure, but in the longer run these strategies are often insufficient to cope with the income shortfall. In the longer run persistent poverty might be at stake.

Research on the topic of poverty shows that, from a dynamic perspective, poverty has two *images*, which occur simultaneously. On the one hand, there is a great deal of mobility and turnover in the stock of people living in poverty. A part of the poor population remains in poverty only for short periods but might return quickly after having left it (cyclical poverty). On the other hand, a substantial proportion of poor people are exposed to the risk of staying in poverty for long periods without having much chances to escape (persistent poor). The goal of alleviating poverty, as modern welfare states pursue it, matters a great deal more in the longer than in the short term. Instant poverty can be unpleasant but is not life threatening and in some circumstances hardly matters at all. Many of us have been temporarily poor as students, or experienced short periods of poverty between jobs, being forced to run down savings, borrow and belt-tighten. Medium and long-term poverty, on the other hand, and frequent movements into and out of poverty, cause serious distress and often detaches people from their normal social networks, leisure pursuits and “mainstream” lifestyle. It might discourage people from applying for jobs and from entering the labor market because of its negative effect on the incentive to work. It therefore might, in the longer term, create welfare dependency and exclusion from social networks and normal life-styles [see *Poverty and Life Support Systems*]. Policies should be designed in such a way that they promote economic mobility and prevent welfare dependency and social exclusion. By comparison of almost prototypical welfare states over the short and medium term, one may address the question of how well different welfare state regimes perform in terms of combating longitudinal poverty. These policy achievements are assessed on the basis of panel data for a number of European countries and for Canada and the United States. But the focus should move away from the snapshots of poverty in society to the distribution of poverty across the population in a time perspective. Particularly, its recurrent cyclical nature and therewith the *prevalence of poverty* in society over time should be subject to the concern of academic researchers, policy makers and politicians even in modern societies [see *Poverty Research*].

The distribution of poverty over time depends on the level of income mobility, the duration of poverty spells and the extent of recurrent or cyclical poverty. The length of the spell is measured by the well-known spell-approach as proposed by the American researchers Bane and Ellwood in the early 1980s. This method is derived from life-table and survival analyses in biological research. It gives information about the exit or escape rate out of poverty proportional to the number of years of residence in poverty. Whereas these exit rates give information on the income mobility, the survival probabilities (the reverse of the exit rates) render insight into the stability of income positions over time. The extent of *recurrent or cyclical* poverty can be measured by looking at the frequency of poverty hits during the observation period. Eventually, the volatility or stability of poverty can be measured in several ways, among which is the earlier explained life-table or spell-approach that gives information about the conditional probability of persistent poverty. If persistent poverty is defined as being in

poverty for three consecutive years than the spell approach provides estimates of the average probability of being poor for three years or longer. A simpler method is to look at the *number of years in poverty* and to calculate the proportion of people who are in poverty for a chosen number of years without taking into consideration that some spells are uncompleted. The estimated percentages of persistent poverty are therefore somewhat biased upwards in this measure since no correction is made for left and right censoring, meaning that no adjustment is made for the number of uncompleted spells at the start or at the end of the observation period. Therefore poverty appears slightly longer than if such a correction had been made.

### *Poverty profiles*

But, apart from viewing the dimensions separately, it is also feasible to combine these three dimensions into one measure that may capture information on the various and divergent poverty patterns over time. This measure might be called the “*poverty profile*” and it provides information simultaneously about the size of transient, cyclical and persistent poverty. This measure summarizes the information in the data on the various types of poverty profiles:

- The persistent non-poor (never poor in the observation period);
- The transient poor (once poor in the observation period);
- The recurrent or cyclical poor (more than once poor but never longer than  $x-1$  years);
- The persistent poor (poor for a consecutive period of  $x$  years).

The value for  $x$  (the number of years) in the definition of persistent poverty has to be chosen by the researcher or the politician and depends on the length of the observation period and the distribution of poverty risks over time in society. The value for  $x$  of 3 years for presenting information on persistency of poverty (being poor for at least three consecutive years) is rather arbitrary. For the few countries for which longer running panel-data are available, it is found that the likelihood of residing in poverty for longer than 3 years is extremely low (the average duration is about 1.5 to 2.5 years in developed countries). It can also be shown that the likelihood of escaping poverty diminishes rapidly after having resided in poverty for two or more years.

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