

Poverty, Capabilities & Australia's (COAG's) New Human Capital Reform Agenda

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OVERVIEW

- Linking 2 topics: (i) Australia's (COAG's) new Human Capital Reform Agenda launched in 2005 & (ii) financial poverty
- POVERTY – improved understanding needed: conceptually it makes no sense to continue to base measures of poverty solely on low income
- How to improve our understanding & measurement? New measure takes account of a household's **consumption & wealth**, as well as its income.
- *Links to the COAG Agenda:* show that the new poverty measure is strongly related to low human capital/low capabilities, as defined in **COAG's Human Capital Reform Agenda**.
- **Progress indicators:** suggest indicators to monitor gains & lags relating to the Reform Agenda & add poverty indicators. The **HILDA & LSAC longitudinal data sets** are well placed to measure annual progress.

COAG's HUMAN CAPITAL REFORM AGENDA 2005-

- “Third Wave” of reform. Wave 1 = opening of economy. Wave 2 = NCP – National Competition Policy. Wave 3 = human capital reform – enhancing capabilities/skills.
- Human capital reform essential to success of a “knowledge-based economy”
- Human capital is very broadly defined by COAG – includes physical & mental health, as well as education & job training.
- The Agenda draws on the ideas of 1998 Nobel Laureate, **Amartya Sen**, whose concept of “**capabilities**” includes health & social capital & can be regarded as a broad definition of human capital.

The COAG Agenda: 3 main areas- health, education & work incentives

- **HEALTH**: reduce proportion of population not working due to illness & disability (sub-text: reduce DSP payments).
- **Reduce prevalence of risk factors** leading to chronic diseases, esp. Type 2 diabetes & obesity.
- **Mental health**: reduce prevalence & duration of **mental health problems** ('epidemic of depression').
- Only about 35-40% of the 15-20% of the population per year in Oz who have mental health problems are getting treatment (ABS, 1997). **Young adults are most at risk but least treated**. Need easier & cheaper access to psychologists. Note – intro of new item numbers for psychos in October 2006. Could be a step of major long term importance.

The COAG Agenda (contd)

- **EDUCATION & TRAINING:** improve early childhood education (influence of Heckman)
- Improve standards of literacy & numeracy (ABS Literacy Survey, 1996, which showed that about 45% of Australians lack Level 3 literacy/numeracy), which is key level required for good employment & earning prospects.
- Increase proportion of adults with Year 12 & post-school qualifications - very high unemployment & nlf among those who did not complete Year 12.
- **Skills For The Future** program announced in October 2006 mainly to fund literacy, numeracy & vocational training for those who did not complete Year 12. \$837 million. Small beer?
- **WORK INCENTIVES:** reduce the disincentives to work which are built into existing tax-transfer provisions.

IMPROVED UNDERSTANDING OF POVERTY

- Now going to appear to change tack by talking about *poverty* (but will then integrate with the COAG Agenda).
- *Conventional low income approach*: in Oz & most Western countries poverty is defined entirely in terms of low income – note the standard 50% (OECD) & 60% (EU) *income poverty lines*.
- *BUT this is conceptually flawed. Poverty IS a low material standard of living - involuntary.* So poverty should be defined & measured as involuntary *low consumption*. Income is only an *indirect measure*. (Note: main ideas in Ringen, 1988. He found that in some countries the income poor & the consumption poor ARE the same people – in other countries NOT SO).
- More exactly, a household can only be said to be poor right now if it has a low income AND low consumption AND (in principle) a low level of wealth (low net worth – assets minus debts). Discuss – for example, high income + low consumption = miser/hoarder. High consumption + low income = ??

Financial poverty = low income and low consumption and low wealth

- But can this understanding/definition of poverty be implemented in practice?
- Problem: unusual to find measures of household income, expenditure/consumption & wealth all in the same survey – but HILDA is currently doing this (Wave 6 - 2006).
- HILDA = large scale Aussie panel study (2001-) conducted by MI for FACSIA. Annual interviews with 15,000 folk aged 15+ in 7,000 HHs. (Data available for research purposes).
- Main practical difficulty in implementing improved poverty measurement = measuring HH expenditures in a standard survey format. HILDA tries!
- Pilot results (mid-2005): HILDA appears to have accurately measured about 60% of total HH expenditure on goods & services. These items correlate about 0.80 with total expenditure (using the ABS Household Expenditure Survey 2003-04 as a benchmark). Improvements needed – but we are in sight of being able to estimate total HH expenditure & hence consumption poverty.

Poverty: Prelim HILDA Results For 2005 - Comparing Measures

N.B. My prelim results only – neither FACSIA nor HILDA team implicated!

- Income poverty – EU's 60% of median line: shows about **20% poor** in 2005. (About 12% if 50% poverty line is used).
- Consumption poverty – 60% line: shows about **15% poor** (evidence of 'consumption smoothing' – as perm. income theory predicts).
- Income poor + consumption poor = **7%**
- Income poor + consumption poor + net worth (assets minus debts) less than \$200,000 = **6.5%**

**** Plainly, if the logic behind these revised poverty measures is accepted, it also has to be accepted that existing income measures are in serious error. (Note Irish measure of 'consistent poverty').**

Who is income poor but not consumption poor - & vice-versa?*

- **Income poor, but not consumption poor?**
people who own their homes outright (inc. many older people); young well educated people; single people esp. young women.
- **Consumption poor, but not income poor?**
Renters who have lowish incomes & pay a high proportion of income in rent.

* *What this implies is that the distributions of income & consumption are fairly different.*

Evidence - do the new measures improve understanding of poverty?

- Poverty measures based on consumption as well as income - or on consumption, income & wealth combined - correlate about 50% more strongly with measures of human capital/capabilities than measures based solely on income. Confirms **validity** of new measures.
- Correlations are considerably higher with measures of education and with physical & mental health (& also with self-assessed prosperity/poverty).

COAG's Agenda: Framework for Assessing Progress – Add Poverty Reduction?

- COAG has itself set out a framework for **assessing progress** relating to its Agenda.
- The concept of **progress indicators** is quite valuable – aim is to make progress, *not* pretend to abolish low capabilities or abolish financial poverty. Accept that total success is unachievable.
- **Life cycle**: the COAG framework is based on the idea that different targets/progress indicators are appropriate for different stages of the life cycle (e.g. literacy & numeracy targets for kids of different ages; vocational & advanced education targets for the adult population).
- **Quantitative targets & timelines** In the diagram (about to show) I have taken the liberty of adding quantitative targets & timelines, as well as poverty reduction targets to the basic framework set out by COAG.

Possible Progress Indicators: 2010

HUMAN CAPITAL / CAPABILITIES

Age 17/18:

- 80% Level 3 literacy & numeracy
- 80% complete Year 12
- Depression reduction target?

Age 25:

- 70% Level 3 literacy & numeracy
- 60% voc. or adv. education
- BMI reduction target?

Prime Age Adults:

- 65% Level 3 literacy & numeracy
- BMI reduction target?
- Type 2 diabetes reduction target?

Retirement Age:

- Physical and mental health improvement targets

FINANCIAL POVERTY

Kids:

- reduce child poverty to 2%
(Use EU 60% pov line)

Prime Age Adults:

- reduce poverty to 5%

Retirement Age:

- reduce poverty to 5%
- 50% self-funding (or partly so) in retirement = wealth target

COAG's AGENDA: MONITORING PROGRESS via panel surveys

- HILDA is moving towards providing a **set of HH accounts** with annual data on wealth, income & consumption, as well as human capital/capabilities.
- HILDA, in combination with ABS cross-sectional surveys & with LSAC (the panel survey of Aussie kids), can do the job of monitoring progress relating to the COAG Agenda.

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