The Absolute vs Relative Poverty Conundrum

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The Absolute vs Relative Poverty Conundrum

Malaysians feel a sense of disconnect with official poverty statistics. They feel that their incomes are barely enough to make ends meet and yet, by official count, we have almost no poverty in the country. New ways of capturing poverty are needed and some have even argued that we should ask Malaysians themselves what the poverty line should be[1].

However, poverty is not a homogenous concept. There are no standard answers to questions of 'who are the poor?' and 'how they are poor?'. People recognise that poverty is multidimensional, affirmed by their everyday lived experiences. Hence, having multiple poverty measures to capture different facets of deprivation is broadly agreeable. It is embraced with different degrees of fervour by national governments and international development organizations.

But do these different poverty concepts and dimensions[2] always complement each other? Or are there trade-offs we should be cognizant of? Faced with fiscal constraints, national governments may have to choose the type of poverty to prioritise in poverty reduction programmes and strategies.

The two inter-related concepts of absolute and relative poverty could be central to this trade-off. Absolute poverty, a concept that does not measure income distribution, is premised on a set of minimum standards largely accepted by society as constituting basic needs[3]. The 'minimum' is usually determined through a combination of societal consensus and scientific inputs. It can be measured by the income required to purchase a set of goods and services considered necessary to lead a satisfactory life.

Relative poverty, on the other hand, articulates the minimum standards in terms of the average living standards of society and therefore, captures the distributional component of poverty. It is focused on the conditions of those at the bottom of the income distribution and how they fare when compared with other selected benchmark population in the income distribution.

Fixing absolute poverty i.e. lifting people above the poverty line may not make a dent on relative poverty numbers. This is especially so when absolute poverty rate is low and relative poverty depends on how other parts of the income distribution are moving. Conversely, relative poverty can be improved without significantly lifting people out of absolute poverty – getting those slightly above the poverty line to grow faster than the benchmark population already does the job!

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[1] Ravallion (2019a)

[2] Poverty concepts are used here to refer to the different 'types' of poverty e.g. chronic poverty (based on duration), transient poverty (based on fluctuations), absolute poverty (based on minimum standards), relative poverty (based on benchmark population), multidimensional poverty (based on several dimensions including non-income ones). On the other hand, poverty dimensions refer to the 'spheres' of poverty within a particular concept of poverty i.e. multidimensional poverty, which includes dimensions such as education, health, living standards, etc.

[3] Serageldin, 1989

Malaysia uses the poverty line income (PLI) to measure poverty. The current PLI methodology is revised in 2004/2005, and is used to measure absolute poverty. Prior to that, the PLI is calculated for a model household of five members in 1977, updated annually with the consumer price index (CPI). After the revision, the PLI is calculated for each household, adjusting for household composition, age distribution, gender, and regional differences. The underlying philosophy is still cost of basic needs, calculating the amount of household expenditure needed to fulfil both food and non-food needs, and using income to determine whether households fall above or below the poverty line.

Based on this, absolute poverty is low and hardcore poverty is considered eliminated. Figure 1 shows the incidence of poverty and the number of poor households. The incidence of poverty fell from 37.4% of all households in 1979 to 8.5% in 1999, further falling to 0.4% in 2016. In absolute terms, this translates to a reduction of about 370,097 households, from 394,797 households in 1999 to 24,700 households in absolute poverty in 2016[4]. The sizeable decrease in poverty rate is attributed to rapid economic growth, distribution policies and improvements in public services in the last three decades[5].

Figure 1: Incidence of poverty and number of households under PLI, 1979 – 2016
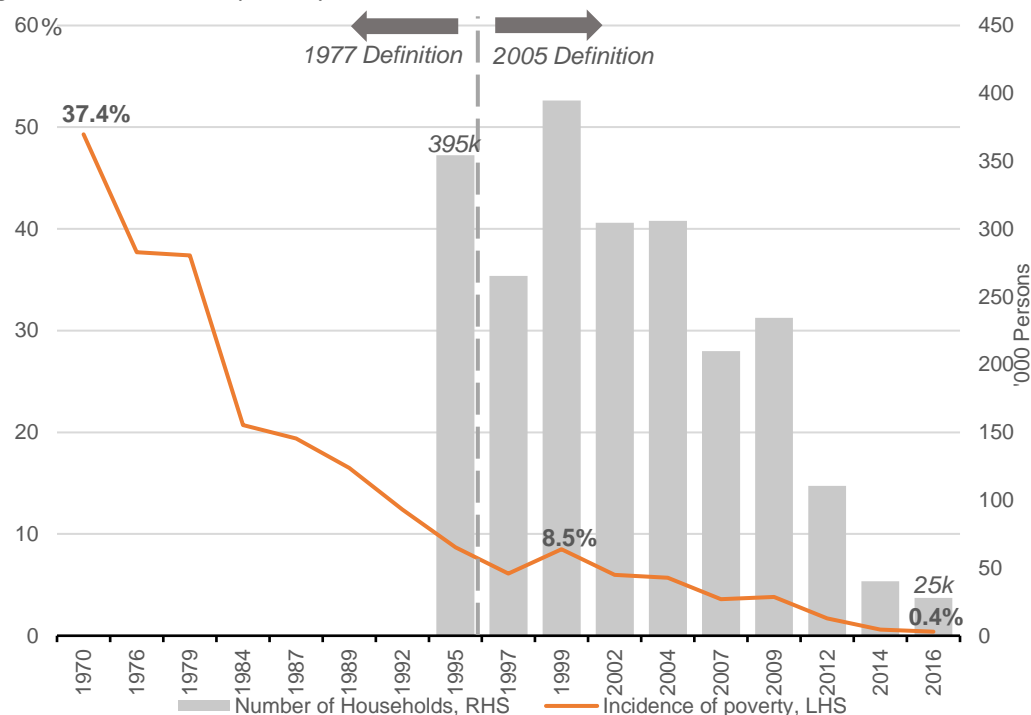
Source: DOSM, EPU, Authors' Calculation

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[4] The number of households for 1995-2012 is estimated using publicly available census data while the number of households for 2014 and 2016 is published in the Household Income and Expenditure Survey reports. The data on the number of households before 1992 is not publicly available, hence it is not reported in this article.
[5] Khazanah Research Institute (2018)

However, despite updating the PLI with the CPI to reflect changing cost of living, Malaysia's poverty line is still lower than expected when compared with countries that have similar mean incomes[6]. This perhaps explains criticisms that the current poverty rate is not reflective of realities on the ground[7]. The assumptions behind how the food and non-food baskets are derived may need to be revisited to better reflect Malaysia's progress made in its average living standards. Furthermore, such low poverty figures cannot be used meaningfully for policy planning purposes to address the continued deprivations experienced and felt by different segments of the Malaysian population.

Instead of revising the PLI methodology, the government has decided to shift its focus from the poor to the bottom income distribution. It started with the bottom 30% in the 8th Malaysia Plan and has shifted to the bottom 40% (B40) since the 9th Malaysia Plan. In the 11th Malaysia Plan, the government has also officially announced the use of the Multidimensional Poverty Index (MPI) to complement the PLI.

More recently, in the Mid-Term Review of the 11th Malaysia Plan, a relative poverty concept[8] was introduced in the form of 'low income households' as a subgroup of the B40, defined as households earning between the PLI and 50% of the national median monthly household income. Median monthly household income is RM5,228 in 2016 and 50% of the median is RM2,614. Based on official statistics, this amounts to 15.5% of overall households and 1.08 million households.

Our own calculations using 60% median show a slightly higher number as we use a higher percentage and include also those below the PLI. The selection of the cut-off point is subjective – the OECD set it as income per adult equivalent between 40-60% below median[9]. We use the upper bound number of 60% within the OECD range. Figure 2 shows the incidence of relative poverty and number of households earning less than 60% median monthly household income from 1995 to 2016. The percentage has decreased from 26.2% in 1995 to 22.2% in 2016, but the number of households has increased from 1.08 million households to 1.54 million households[10]. This is an update of our analysis in the State of Household 2018 report.

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[6] Ravallion (2019b)
[7] Free Malaysia Today (2018), The Star (2018)
[8] The term relative poverty is not officially used but it is similar to how relative poverty is calculated internationally.
[9] OECD (2008)
[10] If we use 50% median, relative poverty decreased from 19.6% in 1995 (0.8 million households) to 15.8% in 2016 (1.1 million households).

Figure 2: Incidence of poverty and number of households earning less than 60% median household income, 1995 – 2016
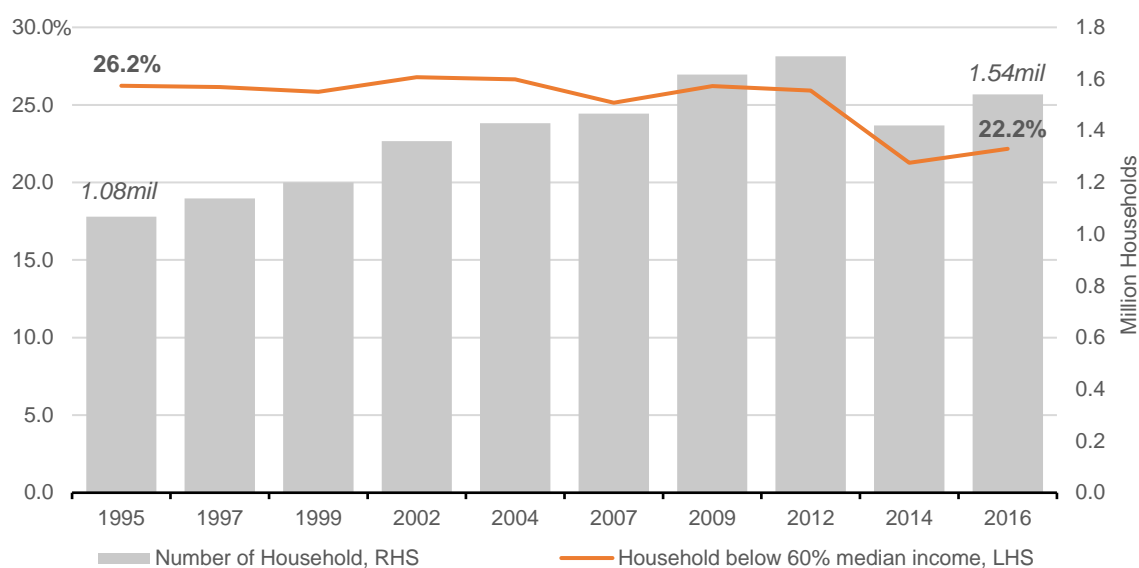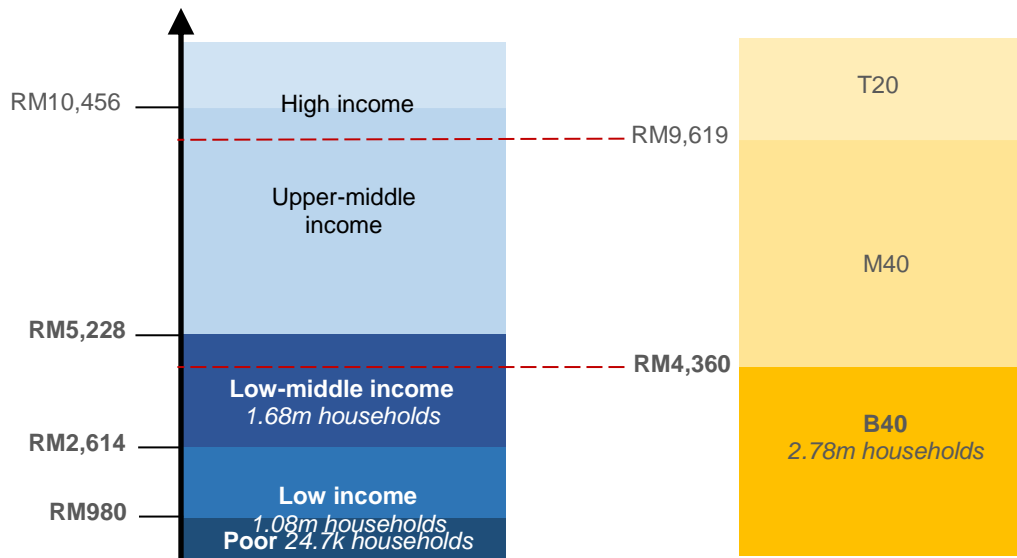
While the shift towards relative poverty is perhaps necessary given the low rates of absolute poverty, the official conceptualisation of the B40 (see Figure 3) that are composed of absolute and relative poverty is problematic. This is because it treats relative poverty as absolute poverty in terms of extending social assistance and implementing welfare programmes although absolute and relative poverty actually measure different types of poverty and require different strategies to address them. At the same time, because it treats absolute and relative poverty as mutually exclusive groups, lifting the 24,700 households identified as 'poor'[11] would only add on to the number of households defined as 'low income' – hence, the increase in the number of relatively poor households. Conversely, and somewhat absurdly, relative poverty will decrease if low-income households fall below the PLI *ceteris paribus*!

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[11] As reported in the Mid-Term Review of the 11th Malaysia Plan, EPU (2018)

Figure 3: Demarcation of Malaysian households, 2016

This brings us to three concluding points. First, the B40 is composed of subgroups that are poor in both absolute and relative terms. Although introducing relative poverty in the form of low income households effectively increases the welfare threshold from between RM960-RM1,180[12] to RM2,614, it confuses relative poverty with absolute poverty in terms of extending social assistance and welfare programmes. Moreover, treating these two as mutually exclusive subgroups set them off into an inevitable and bizarre trade-off. Instead, we need to revise the PLI methodology introduced in 2004/2005 to reflect Malaysia's improvement in living standards. In short, we need an upgraded absolute poverty line for Malaysia and a consensus on what constitutes this new 'minimum'.

Second, relative poverty is still relevant but should be introduced alongside, not as a way to prop up, absolute poverty threshold. In fact, relative poverty defined as a percentage cut-off point below the median has advantage over the use of B40[13]. The clearest advantage is the number of households below the relative poverty line can vary depending on the effectiveness of policies whereas for B40, there will always be 40% of the population in the bottom income distribution. Worse, if the B40 is confused for absolute poverty, we will have 40% of the population perpetually qualified for social assistance!

Third, we need different strategies for absolute and relative poverty, as well as social spending that corresponds with different types of poverty. Absolute poverty forms the basis for welfare and social assistance to deliver basic needs while relative poverty provides the ground for the promotion of socio-economic participation for those left behind from the processes and outcomes

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[12] RM960 in Peninsular Malaysia, RM1,020 in Sarawak, and RM1,180 in Sabah/Labuan.
[13] B40 was introduced in the 9th Malaysia Plan as a relative poverty concept.

of economic growth. If the fiscal space is broad enough, we should be addressing both absolute and relative poverty with equal vigour and urgency. However, with social spending on a declining trend, we need to deliberate and debate on how to prioritise and allocate limited fiscal resources between absolute and relative poverty.

In balancing between absolute and relative poverty, we may want to ask Malaysians what they think. But before asking, we may want to get our concepts clear and our questions right. Therefore, the first step in reconnecting official statistics with lived realities is perhaps to get out of this absolute vs relative poverty conundrum.

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