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Effectiveness of Means-tested Transfers in Western Europe: Evidence from the Luxembourg Income Study

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"If poverty prevails, the welfare state is a failure." (Ringen 1987:41)

1 Introduction

In recent years, the discussion about welfare state reform has often focused on the effectiveness of social security schemes. This debate is torn between calls for more effective poverty alleviation on the one hand and concerns about welfare dependency and the need for stronger targeting of social security benefits on the other. Means-tested benefits have been a major subject in this debate, since they are explicitly directed toward low-income groups. Basically, means-tested benefits are characterised by income and/or asset tests (examples are social assistance or housing benefits in most countries).

In spite of the growing concern regarding the effectiveness of means-tested benefits in alleviating poverty, our knowledge on the impact of means-tested benefits remains inadequate. Although a number of studies have assessed the effects of tax and transfer systems as a whole and have provided accounts of the effectiveness of specific social security schemes or the impact of redistribution on specific groups of the population, evidence on the effectiveness of means-tested benefits is still limited. We know astonishingly little about the effects of means-tested transfers on poverty. How effective are they in reducing poverty rates? To what degree can they fill the gap that income redistribution through taxes and non-means-tested social security benefits leaves? How large is the impact of means-tested transfers in private household budgets, and how does the role of means-tested benefits vary across countries?

The Luxembourg Income Study (LIS) offers detailed micro-data of private household incomes and facilitates the analysis of the impact of means-tested transfers in a comparative perspective. This paper will explore the potential of these data for assessing the effectiveness of means-tested benefits. Three countries have been chosen for this purpose: Germany, Sweden and the United Kingdom. The evaluation of the effectiveness of means-tested benefits in these countries addresses variations in the effectiveness of means-tested benefits across countries. Can we identify specific patterns in the impact of this kind of benefits? How can we relate these patterns to the institutional settings found in these countries?

The structure of the paper is as follows: The first section considers the role of means-tested benefits in industrial welfare states and discusses the question of how the effectiveness of social policies can be evaluated. The methodological framework of this paper is laid out in the second section and is followed by an assessment of the distribution of means-tested benefits on house-

holds and the weight of means-tested benefits in private household budgets in the third section. The fourth section analyses the effectiveness of means-tested transfers in three steps. Compared to the counterfactual of an income distribution without any means-tested transfers, how effectively do means-tested benefits reduce poverty rates? How far are poor households pushed up the income scale by means-tested benefits? To what degree do means-tested benefits achieve to close the poverty gap? The paper concludes with a short discussion of these results.

2 Welfare states and the alleviation of poverty

2.1 The role of means-tested benefits in industrial welfare states

Industrial welfare states have developed elaborate systems of income redistribution to prevent individuals from a loss of earnings. In Western Europe, most welfare states are organised in a multi-tiered fashion, with - typically non-means-tested[1] - social insurance benefits and means-tested benefits.[2] Social insurance benefits are designed to cover a broad variety of contingencies (such as old age, sickness, invalidity, unemployment, etc.) on the basis of the previous payment of social insurance contributions or other requirements. Social insurance benefits alone, however, may not be enough to make ends meet. This may be the case if individuals are ineligible for social insurance benefits, or if these transfers do not fully cover the needs of the household. In these cases, means-tested benefits shall prevent people from poverty. These benefits are based on the notion that a certain standard of adequacy in a society exists below which nobody should be allowed to fall (cf. Veit-Wilson 1998).

The procedure of means-testing seeks to guarantee that benefits are directed to the poorest segments of the population. Basically, this procedure includes the assessment of household income and private assets. Means-tested benefits are granted only if the household's income does not meet a certain minimum standard. There may be varying minimum income standards for different categories of the population, but most countries provide for a minimum income standard set by universal social assistance schemes, as for example income support in the United Kingdom, socialbidrag in Sweden or Sozialhilfe in Germany. Housing benefit schemes help to cover rent and mortgage costs for low-income households. In addition, there are some means-tested benefits for specific categories of the population in most countries, as e.g. student grants, unemployment assistance or school milk for children from low-income families (cf. Eardley et al.

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1 There are, however, some minor exceptions to this pattern, as for example the second tier of unemployment insurance in Germany or the means-tested addition to the basic pension in Sweden.

2 Non-European welfare states do not necessarily comply with this assessment. Exceptions are in particular Australia and New Zealand where practically all social transfers are means-tested (cf. Castles 1996).

1996a, 1996b; Guibentif/Bouget 1997). Table 2 below gives an overview on the means-tested benefits considered in this paper.

The interplay of social insurance and means-tested benefits has often been neglected in comparative welfare state analyses. Means-tested benefits are generally regarded as being inferior to social insurance benefits, since they are often perceived as stigmatising (cf. Rainwater 1982). Unlike most social insurance benefits, means-tested transfers are not considered as being „earned" by previous contributions, but rather granted on the basis of individual need. Therefore, a fully-fledged analysis of welfare states should take into account the relationship between non-means-tested and means-tested schemes as one major internal division within welfare states (Lødemel/Schulte 1992). How do they complement each other? How well does social insurance prevent poverty? Which role is then left for means-tested benefits and how effective are they?

Recent discussions on welfare state reforms have raised the question of whether means-tested benefits should be expanded in order to provide more effective transfers in the context of strained public budgets (e.g. OECD 1994; Smolensky et al. 1995). If the welfare state is perceived as being too large, focusing social transfers on the „truly needy" appears to be a viable alternative. Indeed, there is some evidence that the salience of means-tested benefits has grown in many welfare states at the expense of non-means-tested benefits in some countries (cf. van Oorschot/Schell 1991; Sinfield 1994: 139; Ferge 1997). There are, however, concerns that the targeting of social transfers undermines public support for redistribution since the population is more visibly divided into beneficiaries of social transfers on the one hand and those who pay for it on the other (cf. Coleman 1982). This would intensify stigmatisation of recipients as well as make these social transfers more vulnerable to curtailments in the long run (Le Grand/Winter 1987; Skocpol 1991).[3] In addition, critics of means-tested schemes assert that means-tested benefits cannot satisfactorily prevent poverty because of stingy benefit levels and low take-up rates due to stigmatisation (cf. Smolensky et al. 1995; van Oorschot/Schell 1991; van Oorschot 1998). These claims, however, have not yet been extensively tested. Means-tested benefits are explicitly designed to alleviate poverty, but their performance in achieving this goal requires further examination. It would therefore be particularly worthwhile to investigate the effects of means-tested benefits in a cross-national perspective in order to identify different patterns of impact.

The three Western European countries chosen for this analysis, Germany, Sweden and the United Kingdom, have each assigned a different role to means-tested benefits and have organised them in different ways. In the British welfare state, means-tested transfers have a comparatively large weight; they are closely integrated with the flat-rate social insurance and are based on strong entitlements, though with rather low benefits. The relatively generous social insurance benefits in Germany and Sweden leave a significantly smaller role to means-tested benefits,

[3] For a challenge to this argument, cf. Pierson 1994.

though their importance has increased over the past years. In Sweden, means-tested benefits complement the quasi-universal social insurance and extensive social services. Most means-tested benefits are administered by local communities, with a relatively generous benefit level though with tight controls and a high degree of local discretion. The German means-tested benefits supplement social insurance benefits that are primarily based on the previous earnings and contribution record rather than on individual needs. They exhibit both a more balanced relationship between central and local levels, a stronger emphasis on entitlements than in Sweden, and a relatively low level of benefits (cf. Eardley et al. 1996a: 109-139; Eardley et al. 1996b; Guibentif/Bouget 1997; OECD 1998).

Not surprisingly, these three countries have also been mentioned as „prototypes" for a specific cluster of countries in typologies of poverty or social assistance regimes (Leibfried 1992; Lødemel/Schulte 1992). Similar to Esping-Andersen's (1991) influential typology of welfare states, these authors have identified four types of provision of means-tested benefits: a Scandinavian („social democratic" or „institutional") model, an Anglo-Saxon („British") model, a Continental („Bismarck") model and a Southern European („rudimentary") model.[4] A more recent typology of social assistance schemes combines Germany with the United Kingdom in a cluster of „integrated safety nets", yet concedes that Germany could also have been added to a cluster with France and the Benelux countries (Eardley et al. 1996a: 168-170).

Hence, we would expect to find different patterns of poverty alleviation through means-tested benefits in each of the countries considered. In the United Kingdom, means-tested benefits are expected to alleviate poverty to a minimal extent, leaving possibly a large share of people in moderate poverty. For Sweden, we would predict that the breadth and generosity of social insurance leave a relatively small gap to fill for means-tested benefits, and this gap is expected to be almost fully closed due to the high level of means-tested benefits. The earnings-related social insurance benefits in Germany should leave a large gap for means-tested benefits. Since benefit levels are not very generous, we would expect that means-tested benefits are not able to alleviate poverty in an effective way. The following sections discuss the question of how the effectiveness of means-tested benefits can be measured and how the impact of this kind of benefits can be compared across countries and over time.

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4 The most substantial deviation from Esping-Andersen's work in fact concerns the countries of the „Latin Rim", most of which were not taken into account in Esping-Andersen's work (Spain, Portugal, Greece). France and Italy have been classified as „conservative" by Esping-Andersen (1990). Both Leibfried (1992) and Lødemel/Schulte (1992) include the „Latin Rim" of Southern Europe as a fourth model with a rudimentarily implemented work and welfare rights. For a critique of the classification of the Scandinavian countries, cf. Bradshaw/Terum (1997).

2.2 Assessing the effectiveness of social policies

The effectiveness of tax and transfer systems as a whole has been assessed in a number of studies, most of which used Beckerman's (1979) influential methodological approach. This method is based on a comparison of poverty measures before and after redistribution. While Beckerman had to rely on a sub-optimal database[5], more recent studies could use the micro-data of the Luxembourg Income Study (LIS) for extended analyses. These data allowed Mitchell (1991) to scrutinise the effectiveness of redistribution though taxes and transfers for the population as a whole and for specific groups such as families with children or the elderly. Similar analyses have been made by Förster (1994) and McFate et al. (1995) for the non-elderly population, by Hauser (1987) for single parent families and by Shaver (1998) for the elderly.

This broad approach side-steps a major problem in comparative research: Countries have organised their social transfers differently, and therefore the same goals are approached by various means. For example, redistribution may be achieved by direct transfers to clients, as well as, in principle, through the tax system.[6] Deleeck et al. (1992) have attempted to isolate the effects of specific social security schemes for seven European countries and regions.

Means-tested benefits have not yet comprised the main focus of this research so far. One could argue, however, that their effectiveness has been indirectly tested in the analyses of total redistribution, since means-tested benefits provide for the basic layer of social security. Therefore, the existence and extent of poverty point to an ineffective alleviation of poverty through means-tested transfers. This is certainly true, but there are specific patterns of poverty alleviation through means-tested transfers that cannot be identified with the rather crude instruments used in this kind of analysis. Given that means-testing transfers are explicitly designed to alleviate poverty, a closer look at this type of benefit promises useful insights into the logic behind them.

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[5] The lack of available data at that time forced Beckerman to use average expenditure per recipient as a proxy for the actual social security benefits received by households. This measure is problematic, as benefits may not be distributed equally among the recipient population. The unequal distribution tends to overestimate the poverty-alleviating effects of social security transfers especially if benefits are income-related. Low take-up rates may also overstate the effectiveness of benefits (cf. Beckerman 1979: 16-17). Another critique refers to the negligence of the tax system. Most more recent studies do not confine themselves to the analysis of social security transfers, but include the tax system into their analysis. They argue that the effectiveness of the welfare state can only be judged if one allows for the fact that countries organise the redistribution of incomes in different ways. Focusing on either component alone (social security schemes or the tax system), the redistributional impact of the other would be underestimated. In addition, social security transfers are taxable in some countries. Confining the analysis only to transfers would neglect the impact of tax claw-back of benefits.

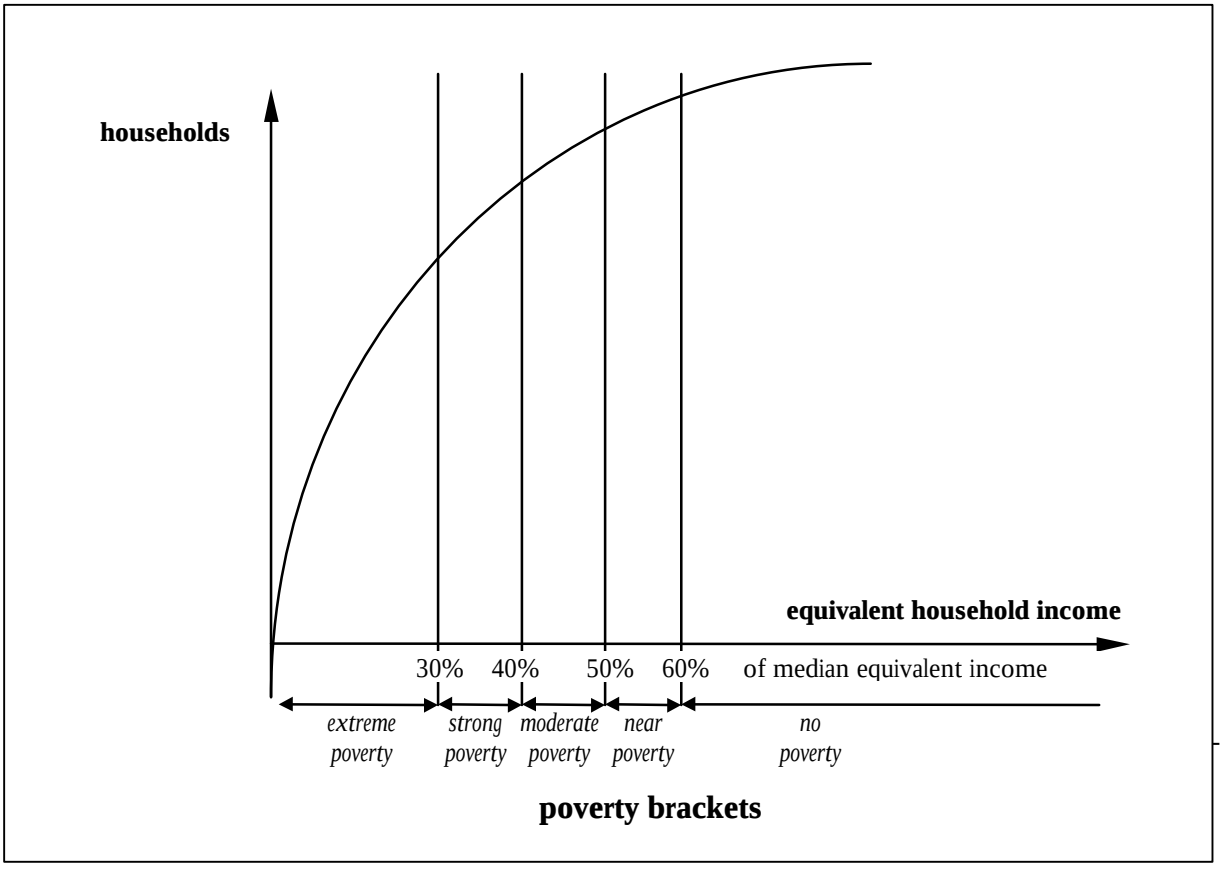
[6] Obviously, some tax allowances tend to favour some groups of the population that are typically *not* the most needy, but this does not mean that the tax system as such is not qualified to achieve the same goals as direct transfers.

3 Methodology

The micro-data of the Luxembourg Income Study provide very useful basis for the evaluation of the effectiveness of means-tested benefits in a comparative perspective[7]. However, the LIS data operate with some definitions that impose certain restrictions on the subsequent interpretation of the data. This section presents the methodology used in this paper and discusses some methodological problems.

Poverty can be measured in a number of ways, but this report uses a relative definition of poverty. Similar to many other comparative studies, this paper primarily defines a poverty line at 50% of the median disposable household income adjusted for household size.[8] Furthermore, three additional poverty lines, set at 30%, 40%, and 60% of the equivalent median household income are applied for two reasons. First, they allow for the assessment of different intensities of poverty, and secondly, they can be used to illustrate the degree to which the poor are pushed up the income scale by means-tested benefits. For this purpose, households are classified into „poverty brackets" according to their incomes. The poverty brackets are defined as incomes lower than 30% of the median equivalent household income („extreme poverty"), between 30% and 40% („strong poverty"), between 40% and 50% („moderate poverty"), between 50% and 60% („near poverty") and over 60% („no poverty"). Figure 1 shows the lower part of an income distribution and illustrates the use of different poverty lines and poverty brackets as defined in this paper.

Figure 1: Poverty lines and poverty brackets



The calculation of poverty rates is very sensitive to the adjustment for different household sizes, especially if specific socio-demographic groups of the population are singled out (cf. Buhmann et al. 1988; OECD 1995: 18-21; Burkhauser et al. 1996). The equivalence scale used in this paper attaches the weight of 1 to the head of household, .7 for other adults and .5 for children living in the household. In order to enhance representativity of the sample, this paper uses household weights as provided by LIS.

The evaluation of the impact of means-tested transfers in this study follows Beckerman's (1979) influential approach („Beckerman ratios"), as in the studies discussed above. Incomes before and after means-tested transfers are compared in terms of incidence and intensity of poverty. The relative poverty lines calculated from disposable income are applied to both income before and after means-tested transfers. Therefore, the poverty lines applied to incomes *before* means-tested transfers are not relative poverty lines in a strict sense, but are equal to the relative poverty lines for incomes *after* means-tested transfers in absolute terms.

Income after transfers, as used in this paper, equals the disposable income as defined by the Luxembourg Income Study, adjusted for family size.[9] The definition of the income before transfers is less obvious. Under the assumption that means-tested benefits are not taxed, the income before means-tested benefits is calculated by subtracting all means-tested benefits (cash and near cash) from the disposable income.[10] This definition comes near to the actual calculation of means-tested benefits in most countries, considering net income after taxes in order to evaluate claimants' needs. Table 1 below displays the poverty lines used in this study in national currency units.

The paper uses the most recent data available for each of the three countries, that is 1994 for West Germany[11], 1992 for Sweden and 1991 for the United Kingdom.

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[9] Households with negative and zero disposable incomes have been excluded from the study since missing values are re-coded as zero by LIS.

[10] In terms of LIS-variables, household income before means-tested benefits is calculated as follows: DPI - MEANSI.

[11] The Eastern part of Germany has been excluded from this analysis for methodological reasons.

Table 1: Definition of poverty lines (based on disposable income)

Poverty lines (% of median)	**West Germany 1994**	**Sweden 1992**	**United Kingdom 1991**
median	24.070,59	111.451,00	5.878,77
60%	14.442,35	66.870,60	3.527,26
50%	12.035,30	55.725,50	2.939,39
40%	9.628,24	44.580,40	2.351,51
30%	7.221,18	33.435,30	1.763,63

Source: Own calculations from LIS. The median and the poverty lines for each country are reported in national currency units and refer to yearly income. Y = disposable household income adjusted for household size.

In many income surveys, there is a problem of underreporting, especially regarding benefits for the lower income strata; this is likely to be the case with the LIS data as well. First, some relevant groups of the population, e.g. the institutionalised population, are excluded from the sampling frame altogether. In addition, households with low incomes generally tend to have low response rates.[12] Second, not all income is reported properly, especially for the lower and higher ends of the income strata as the evidence compiled by Atkinson, Rainwater and Smeeding shows (OECD 1995: 142-154); therefore, the results of this study should be interpreted with due respect to the limits of the survey data. The extent of this bias appears to vary across countries, however. For the German data, there were concerns that means-tested benefits were subject to underreporting.[13] These concerns finally lead to the decision to use a synthetic estimate of the amount of social assistance for the 1994 wave.[14] In the United Kingdom, the underreporting of transfers seems to be less problematic (Atkinson/Micklewright 1983: 43-48). For the Swedish data, we would expect a markedly smaller bias, as the data are based on tax files rather than on survey data. Tax files are assumed to provide more reliable data than surveys (OECD 1995: 25-30).

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[12] The problem of underrepresentation of the lower income strata is supposed to be partly solved by the use of sample weights for households provided with the LIS datasets for Germany and Sweden. The samples for the United Kingdom are supposed to be self-weighting, but there seem to be some problems associated with this procedure, as the documentation of these data by LIS indicates.

[13] There is some evidence that low-income households are slightly underrepresented in the German Socio-Economic Panel (SOEP) (cf. Lipsmeier 1993). Earlier estimations on the basis of a comparison of the micro-data of the SOEP and aggregated data of the national accounts (*Volkswirtschaftliche Gesamtrechnung,* VGR) have shown for the first SOEP wave that only half of transfer payments were reported in the survey, and this rate is even lower for unemployment assistance (44%) and social assistance (38%), but considerably higher for housing benefit (84%) (Berntsen 1989: 21, cf. Kasella/Hochmuth 1989). However, we should distinguish two sources of error for this gap since transfer payments may be understated in the SOEP data for two reasons: firstly, low-income households who typically receive this kind of transfers are less likely to take part in the survey than households with higher incomes (but not for very high incomes), and secondly, households who do take part in the survey may not indicate the exact amount of transfer payments received. While the first type of error only has a small impact on the calculations made in this paper, the second type of error must be considered as much more relevant for our purposes. Unfortunately, the salience of these two sources of errors is not known, so we are not able to exactly estimate the degree of underreporting of means-tested benefits in the German SOEP.

[14] Means-tested benefits were estimated on the basis of the legal entitlements, but only for households who have reported the receipt of social assistance payments. For a more detailed description of the simulation procedure, cf. Krause et al. 1996, Krause 1997.

There is, however, another problem in the Swedish data that further limits the comparability across countries. The household definition used in these data considers all young adults from the age of 18 still living with their parents as independent households, although they might still live with their parents and be economically dependent from them. Consequently, the poverty rates tend to be higher than if a household definition more similar to that of other countries had been applied.[15] The exclusion of this group from the sample would, however, understate poverty for two reasons: first, poverty rates of these young people would certainly be understated since we do not know how many students are not supported by their parents and are actually living in poverty. Second, poverty of their parent households would also be understated since these students would have to be added to their parents'household and thus reduce the equivalent household income of this household. Hence, any interpretation of the results of this study should take into account that the comparability of the Swedish data is limited due to differing household definitions.[16]

Means-tested benefits can include both cash and near-cash benefits. The means-tested benefits included in this study follows the definition of means-tested benefits in the Luxembourg Income Study. For all countries examined here, general social assistance benefits and housing benefits are included, as well as some categorical benefits for some countries (see Table 2).[17]

[15] Earlier estimations have indicated that in 1979, one sixth of the poor in Sweden were students aged 18-24, and they accounted for 0,8 percentage points of the poverty rate (5,0% instead of 4,2%) (Smeeding/Schmaus 1990: 6-7).

[16] In order to interpret the Swedish data, one should also take into account the institutional rules of entitlement in Sweden. In some counties, young adults are entitled to social assistance (*socialbidrag*) independently of their parents'income even if they are living with them. The benefit tends to be lower to account for lower rents and other household costs. Students are generally not entitled to social assistance (with some exceptions during the term holidays), since they are eligible for means-tested scholarship grants and additional scholarship loans. However, students may receive social assistance under certain circumstances. (Thanks to Kenneth Nelson (Stockholm) for this information).

[17] The data used for Germany and the United Kingdom would allow a further disaggregation of means-tested benefits, but not the Swedish data (1992). More recent data for Sweden (1995) were not yet available at the time of writing.

Table 2: Components of cash and near-cash means-tested benefits as defined in LIS

	Germany 1994	**Sweden 1992**	**United Kingdom 1991**
universal social assistance schemes	• general social assistance (*Sozialhilfe: Hilfe zum Lebensunterhalt*) • social assistance in special circumstances (*Sozialhilfe: Hilfe in besonderen Lebenslagen*)	• social assistance (*socialbidrag)*	• income support
categorical schemes	• unemployment assistance (*Arbeitslosenhilfe*) • education maintenance benefits (*Ausbildungsförderung; BAföG*)	• means-tested scholarships (means-test based on student's income not on parents' means)	• family credit • school milk/welfare milk (imputed values)
housing benefits	• housing benefits (*Wohngeld*)	• general housing allowances • housing allowances for pensioners (*kommunalt bostadstillägg, KBT*) • supplementary housing benefit for pensioners (*särskilt kommunalt bostadstillägg, SKBT*)	• housing benefits • community charge benefit • rent rebate

Source: Based on LIS institutional database.

Table 2 illustrates that the programmes included broadly cover the same clientele groups in all three countries. The inclusion of unemployment assistance for Germany appears to be an alien element in this group at first glance since these benefits are based on a contribution record. Its inclusion in this study may, however, be justified on two grounds. These benefits are means-tested, and they fulfil similar functions for the income maintenance of the unemployed in the same way social assistance does in the other countries.[18]

The effects of means-tested transfers can be analysed in a number of ways on the basis of Beckerman's method. However, before discussing the empirical results of these analyses, it is necessary to investigate the role of means-tested benefits in private household budgets.

4 The role of means-tested benefits in private households' budgets

4.1 Distribution of means-tested benefits onto the poor population

Means-tested benefits are not distributed evenly among the poor population, in fact, a substantial number of households do not receive any benefits in spite of low income. Table 3 shows the

[18] The British unemployment benefits (now replaced by the jobseeker's allowance) do not include any second tier, claimants who have exhausted their unemployment benefits after one year have to turn to social assistance. In Sweden, there is a flat-rate unemployment assistance (*konstant arbetsmarknadstöd*, KAS), but this benefit expires after six months (12 or even 18 month for older workers). The German unemployment assistance is unlimited in principle, but does not fully replace social assistance since benefits are limited to a ceiling set at certain fraction of former earnings (57% of net earnings if living with children, 53% if no children) (Ministerie van Sociale Zaken en Werkgelegenheid 1995; BMA 1997: 73-83).

proportion of households who have received any type of means-tested transfers, according to their poverty status before the receipt of these benefits.

Table 3: Distribution of means-tested benefits on households (percentage of households receiving means-tested benefits in each poverty bracket)

poverty bracket		Germany 1994	Sweden 1992	United Kingdom 1991
extreme poverty	*Y < 30%*	66	55	87
strong poverty	*30% £ Y < 40%*	34	49	76
moderate poverty	*40% £ Y < 50%*	28	69	76
near poverty	*50% £ Y < 60%*	24	64	57
no poverty	*Y ³ 60%*	4	16	11

Source: Own calculations from LIS. Y = disposable household income adjusted for household size.
Example: Among all households living in extreme poverty before means-tested transfers in Germany 1994, 66% received some kind of means-tested transfers.

There is strong variation in the distribution of means-tested benefits on the poor population. The United Kingdom has very high recipient rates, especially for households living in extreme poverty, but also for the strong and moderate poverty brackets. The recipient rates tend to be significantly lower in Sweden and Germany where an astonishingly small proportion of the extremely or strongly poor report to have received some sort of means-tested benefits. Sweden displays a remarkable pattern of a lower probability to receive some means-tested benefits in extreme and strong poverty, and higher rates for households in the moderate or near poverty bracket. In Germany, two thirds of the households in the extreme poverty bracket indicated that they received some kind of means-tested benefits, but only a third in the strong poverty bracket and even less in the moderate poverty bracket. Households belonging to the near poverty or no poverty brackets were most likely to receive means-tested benefits in Sweden, and least likely in Germany.

As this section has demonstrated, means-tested benefits are not distributed equally onto the poor population. Although the minimum income levels embodied in the schemes considered here may be different, means-tested benefits are designed to at least prevent people from falling into the lowest poverty brackets. Three possible explanations may account for these astonishingly low recipient rates: First, some households may not have been eligible for any means-tested benefit, yet all of the countries considered provide at least some universal social assistance benefit that covers the majority of the population. A statutory exclusion from means-tested benefits only affects minor parts of the population in the countries considered, mainly concerning recent immigrants.[19] In addition, people working more than 16 h per week are not entitled to receive the British income support, though they may receive family credit. Their earned income should

[19] Households without permanent residence in the United Kingdom (cf. Adler 1997) and asylum seekers in Sweden since 1988 (cf. Westerhäll 1997; Salonen 1993) and in Germany since 1993 (cf. Fasselt 1997) are excluded from the general social assistance schemes, but they may receive some benefits at a lower rate. However, only a very small proportion of these people is included in the LIS database at all (cf. OECD 1995: 124-128).

however prevent most of them from falling into the very lowest poverty brackets. Second, some households may not have claimed all benefits they are entitled to. Low take-up is indeed a problem that might be reflected in the low recipient rates reported here, but unfortunately, we cannot tell this from the third problem: the underreporting of means-tested income. Some households may not have reported all means-tested income, possibly because of the associated stigma. Therefore, we have to assume that at least some part of the non-recipients found in these data either do not claim all benefits they are entitled to, or do not report all benefits they have received.

Because the magnitude of these problems cannot be measured, non-recipient households will be neglected for the further course of this paper. Hence, the following sections focus exclusively on the effectiveness of means-tested transfers actually paid. Consequently, the analysis considers only households who have reported their receipt of any means-tested transfers. To be sure, problems of exclusion, low take up rates and underreporting cannot be fully avoided for this group of households. However, it is assumed that salience of underreporting is significantly smaller for households who actually have reported their receipt of some kind of means-tested benefits, rather than for households who have not reported the receipt of any means-tested benefits.

4.2 Composition of household income

Frequently, means-tested benefits are not the only source of household income, as poor households may draw their resources from earnings, other social security benefits, private transfers, and also to a limited extent private assets. Families often live from an income package comprised of different income types, in which means-tested benefits typically are not the only income source (cf. Rainwater et al. 1986).

Focusing on households who reported to have received some kind of means-tested benefits, what is the relative weight of means-tested benefits in their total household income? Which share of total household income do means-tested transfers contribute? Table 4 shows the relative weight of means-tested benefits in households ’budgets and indicates large variations across poverty brackets and countries. The upper part of Table 4 shows the share of means-tested benefits for households according to their poverty status before means-tested transfers, and the lower part for their poverty status after having received means-tested benefits.

Table 4: Average share of means-tested benefits in total household income (only households with some means-tested benefits)

poverty bracket		Germany 1994	Sweden 1992	United Kingdom 1991
Poverty status before means-tested benefits				
extreme poverty	*Y < 30%*	66	64	84
strong poverty	*30% £ Y < 40%*	31	31	33
moderate poverty	*40% £ Y < 50%*	25	23	24
near poverty	*50% £ Y < 60%*	9	15	16
no poverty	*Y ³ 60%*	10	8	8
Poverty status after means-tested benefits				
extreme poverty	*Y < 30%*	62	48	61
strong poverty	*30% £ Y < 40%*	49	38	83
moderate poverty	*40% £ Y < 50%*	48	29	48
near poverty	*50% £ Y < 60%*	34	27	39
no poverty	*Y ³ 60%*	20	19	26

Source: Own calculations from LIS. Y = disposable household income adjusted for household size.
Example: For Sweden 1992, means-tested benefits covered 64% of household income for households living in extreme poverty before means-tested benefits. Households being still extremely poor after having received some kind of means-tested benefit received 48% of their total income from this source.

For households living in extreme poverty before means-tested transfers, most household income stems from means-tested benefits in the three countries, even more than four fifths the United Kingdom and some two thirds in Sweden and Germany. In the other poverty brackets, the budget share of means-tested income varies surprisingly little across countries and decreases with the intensity of poverty.

Moving on to poverty rates after transfers, we find a more distinct pattern. British and German households still living in poverty after having received means-tested transfers derive most of their household income from these benefits, especially in the extreme and strong poverty bracket, but obviously not enough to lift them over the poverty line. Poor Swedish households receive less than half of their total household income from means-tested transfers. The average weight of means-tested benefits in the household budgets falls far behind the British and the German cases. Apparently, poor Swedish households were able to draw on additional resources to a larger degree than their British or German counterparts.

An interpretation of these budget shares should, however, take into account that many recipients claim benefits for only part of the year (cf. Gustafsson 1993: 259-262). The yearly income data presented here thus cannot reflect different time patterns of receipt. A budget share of 50% may stand for households that have made up half of their household budgets from this source for the full year, but also for households that have been fully dependent on means-tested benefits for six months and not at all for the remainder of the year. Dynamic analyses of social assistance receipt have shown that many social assistance spells are short and that long-term receipt is the exception, rather than the rule, in most countries. Although comparative studies of social assistance dynamics remain rare, there is some evidence supporting the assumption that social assistance

spells may be somewhat shorter in Sweden than in Germany and are also likely to be shorter than in the United Kingdom (Gustafsson/Voges 1998; Leisering/Walker 1998; Ashworth/Walker 1998).[20] If this pattern should hold true, it may suggest an explanation of the low weight of means-tested benefits in the household budgets of the poor in Sweden.

5 Effectiveness of means-tested transfers

Means-tested transfers are primarily aimed at the prevention of poverty, but their exact impact is not clear. How effectively do they reduce poverty rates? How well can they improve the economic situation of poor households? How many people are brought out of poverty by these transfers and how many remain in poverty in spite of having received them?

This section will assess the effectiveness of means-tested transfers with three complementing methods. From a broad perspective, the reduction of poverty rates (head-count measure) sheds some initial light onto the effectiveness of means-tested transfers (section 4.1). Second, a more detailed account follows the effects of means-tested benefits on the income position of poor households and identifies patterns of movements from one poverty bracket to another (section 4.2). Third, the poverty gap method focuses on the intensity of poverty and monitors how closely poor households are brought to the poverty line through means-tested transfers (see section 4.3).

5.1 Change in poverty rates

A very simple measure of the impact of means-tested transfers is the reduction of poverty rates. Actual poverty rates are compared to the counterfactual of the income distribution without any means-tested transfers and monitors their change, both in absolute and in relative terms. Table 5 reports the effects of means-tested benefits on poverty rates across various poverty brackets. Please note that all poverty rates refer to a poverty line of 50% (or 30%, 40%, 60%) of median adjusted household income *after* means-tested benefits. In addition, to the portion of the population in each poverty bracket, Table 5 also reports poverty rates for the 50% poverty line, summarising poverty rates of the lower three poverty brackets.

[20] The results of the comparative study of Gustafsson and Voges (1998) are not representative for the entire social assistance systems of Sweden and Germany, but refer only to the cities of Göteborg and Bremen. However, a systematic comparison of several one-country studies suggests that these results are not unambiguous (cf. Buhr 1995: 121; Buhr/Weber 1996: 16; Olk/Rentzsch 1997: 179; Hagen/Hock 1996; Salonen 1993: 82-87, 136).

Table 5: Poverty rates before and after means-tested benefits and reduction through means-tested benefits

poverty		**Germany 1994**	**Sweden 1992**	**United Kingdom 1991**
POVERTY STATUS BEFORE MEANS-TESTED BENEFITS				
extreme poverty	*Y < 30%*	5.5	6.8	9.3
strong poverty	*30% £ Y < 40%*	2.0	2.3	4.0
moderate poverty	*40% £ Y < 50%*	4.0	6.7	8.2
near poverty	*50% £ Y < 60%*	5.2	7.6	5.9
50% poverty (cumul.)	*Y < 50%*	*11.5*	*15.8*	*21.5*
POVERTY STATUS AFTER MEANS-TESTED BENEFITS				
extreme poverty	*Y < 30%*	2.8	3.7	1.8
strong poverty	*30% £ Y < 40%*	2.2	1.9	2.4
moderate poverty	*40% £ Y < 50%*	4.1	3.2	6.9
near poverty	*50% £ Y < 60%*	6.0	5.4	8.5
50% poverty (cumul.)	*Y < 50%*	*9.1*	*8.8*	*11.1*
IMPACT OF MEANS-TESTED BENEFITS IN ABSOLUTE TERMS (PERCENTAGE POINTS)				
extreme poverty	*Y < 30%*	-2.7	-3.1	-7.5
strong poverty	*30% £ Y < 40%*	0.2	-0.4	-1.6
moderate poverty	*40% £ Y < 50%*	0.1	-3.5	-1.3
near poverty	*50% £ Y < 60%*	0.8	-2.2	2.6
50% poverty (cumul.)	*Y < 50%*	*-2.4*	*-7.0*	*-10.4*
IMPACT OF MEANS-TESTED BENEFITS IN RELATIVE TERMS (PERCENT)				
extreme poverty	*Y < 30%*	-49.1	-45.6	-80.6
strong poverty	*30% £ Y < 40%*	10.0	-17.4	-40.0
moderate poverty	*40% £ Y < 50%*	2.5	-52.2	-15.9
near poverty	*50% £ Y < 60%*	15.4	-28.9	44.1
50% poverty (cumul.)	*Y < 50%*	*-20.9*	*-44.3*	*-48.4*

Source: Own calculations from LIS. Y = disposable household income adjusted for household size.
Example: For the United Kingdom 1991, 9.3% of the population were extremely poor before having received some kind of means-tested transfers and 1.8% after having received some transfers. Poverty rates for this poverty bracket were thus reduced by 7.5 percentage points or by 80.6% compared to the pre-transfer poverty rate.

Under the assumption that no means-tested transfers were available in these three countries, poverty rates are expected to have been significantly higher than the actual poverty rates calculated from disposable income. In Germany, 11.5% of all households would have had an income below the 50%-poverty line if no means-tested benefits were available. An even higher percentage, 15.8% of the population would have lived in poverty in Sweden and more than one fifth of the population in the United Kingdom.

The impact of means-tested transfers can be assessed by analysing the reduction of poverty rates by means-tested transfers. The empirical results show an outstanding reduction of the poverty rates in the United Kingdom for the two lower poverty brackets. The share of the population living in extreme poverty was reduced by some 80%; and by 40% in the strong poverty bracket.

The reduction of poverty rates is considerably less marked in Germany and Sweden. For Germany, the share of the population living in extreme poverty was reduced by half in 1994. The share of the population living in the moderate or the near poverty bracket remained unchanged or even increased. Sweden, on the other hand, exhibited a more regular pattern: means-tested

benefits reduced the percentage of the population in every income bracket; but the magnitude of the reduction varies.

Poverty alleviation appears to be achieved through differing strategies in these two countries. The German means-tested benefits appear to be more effective in reducing extreme poverty, whereas the Swedish pattern distributed benefits more uniformly across all poverty brackets. Poverty reduction at the 50%- level has been most effective in absolute terms in the United Kingdom, followed by Sweden, and least effective in Germany. Measured in relative terms, means-tested benefits in Sweden appear to be almost as effective as in the United Kingdom.

5.2 Move between poverty brackets

The examination of poverty rates in the various poverty brackets shows the overall effect of means-tested transfers, but it fails to illustrate exactly how far households are pushed up the income scale from a particular poverty bracket to another.

Means-tested benefits can follow different strategies. A targeting strategy would focus social transfers on the most needy in order to bring them out of poverty. A broader transfer strategy would rather distribute transfers more equally among the poor. This section will illustrate the impact of means-tested transfers in more detail and will demonstrate how means-tested benefits push a fraction of households from a low poverty bracket (as defined earlier) into a higher bracket. It will also demonstrate that some households do not succeed in moving to a higher poverty bracket in spite of having received means-tested transfers. The moves between income brackets are shown in Table 6. The table focuses on households that actually do receive any sort of means-tested benefits; households not receiving benefits are not included. Again, poverty brackets are used to illustrate the poverty-alleviating power of means-tested benefits. The columns show the poverty status of households before means-tested transfers, and the rows the poverty status after transfers.

Table 6: Effects of means-tested benefits: move between poverty brackets (in percent of all households having received some means-tested benefits)

poverty status after m.-t. benefits ⇨ before m.-t. benefits ⇩	***extreme poverty***	***strong poverty***	***moderate poverty***	***near poverty***	***no poverty***	***total***
GERMANY 1994						
extreme poverty	25	23	21	22	8	100
strong poverty	-	13	30	27	30	100
moderate poverty	-	-	28	29	43	100
near poverty	-	-	-	64	36	100
SWEDEN 1992						
extreme poverty	17	13	14	14	42	100
strong poverty	-	18	25	19	38	100
moderate poverty	-	-	7	30	64	100
near poverty	-	-	-	12	88	100
UNITED KINGDOM 1991						
extreme poverty	8	17	31	23	21	100
strong poverty	-	3	34	32	31	100
moderate poverty	-	-	23	30	47	100
near poverty	-	-	-	38	62	100

Source: Own calculations from LIS. Please note that households that do not receive any means-tested benefits are excluded from this subsample. The „no poverty" bracket has been omitted from the rows since a move out of this poverty bracket is not possible. The dotted line marks the poverty line of 50% of median household income before means-tested transfers adjusted for family size. The figures do not always add up to 100 due to rounding.
Example: In Sweden 1992, of all people living in extreme poverty before means-tested transfers, 27% remained in this poverty bracket in spite of having received some kind of means-tested benefits, 13% moved to the strong poverty bracket, 14% to the moderate poverty bracket, 14% to the near poverty bracket, and 42% to the no poverty bracket.

Table 6 demonstrates that the impact of means-tested benefits is not unambiguous. Only a small fraction of the poor are actually lifted over the 50% poverty line (dotted vertical line), many still remain in poverty. Yet it should be noted that there is a high degree of variation across countries and over time.

In Germany, only one third of the households living in extreme poverty were lifted above the 50%-poverty line by means-tested transfers, while 23% moved to the strong poverty bracket, 21% to the low poverty bracket, and 30% succeeded to leave poverty altogether. A more effective record is monitored for the strong poverty bracket, some 30% of households moving to each of the three highest poverty brackets, but 13% of households remained in this bracket in spite of means-tested transfers. From moderate poverty, more than 70% crossed the poverty line, most of whom were pushed into the „no poverty" bracket. One third of the households in the near poverty bracket could improve their situation and move out of poverty. In sum, Germany exhibits a pattern of poverty alleviation by means-tested transfers that is characterised by a relatively equal distribution of households onto higher poverty brackets. The Swedish and British patterns appear to be somewhat more clear-cut.

In Sweden, poor households in each poverty bracket are most likely to end up in the no poverty bracket after having received means-tested transfers. However, for a considerable proportion of households, means-tested transfers do not contribute to a discernible improvement of their economic situation. Especially for the extreme and strong poverty brackets, many households are

stuck in their initial position or experience a marginal improvement of their situation without crossing the 50%-poverty line.[21] The most effective impact of means-tested transfers serves the moderately poor, whose chance to escape poverty may be as high as almost 94%. For low-income households just above the poverty line, the effects of means-tested benefits are notable as well: almost 90% left the near-poverty bracket. Overall, means-tested transfers in Sweden display an ambiguous pattern: On the one hand, they managed to catapult many previously poor households out of poverty, many of whom even crossed the 60% poverty line. On the other hand, however, many households hardly improved their position at all.

The British escape rates are very high when compared to the two other countries, if movements out of the extreme and the strong poverty brackets are concerned. Almost every one of the extremely or strongly poor households have been pushed into higher poverty brackets. It is noteworthy that a large fraction of this group were at least brought into the moderate poverty bracket. The United Kingdom displays the most marked relationship between the initial and the final poverty bracket of the three countries: the higher the initial poverty bracket, the higher the households are pushed up the income scale. In the moderate poverty bracket, most households are not only pushed out of poverty, but they are most likely to even cross the 60%-poverty line, the same applies to the near poverty bracket. Households in the lowest poverty brackets, however, only have a relatively small chance to end up in the no poverty bracket.

The advantage of the poverty bracket method is the straightforward illustration of the effects of means-tested benefits. This approach is, however, quite sensitive to distribution effects. If households are not distributed evenly along the income scale, the use of poverty brackets may overstate or understate the effects of transfers, depending of the distance of household clusters from the - arbitrarily defined - poverty line(s). This problem could be overcome if more poverty lines were introduced in order to enhance the exactness of results. Another possibility is the application of a more precise measure: the poverty gap measure is able to reflect the intensity of poverty and can also be used to reflect the effectiveness of transfers.

5.3 Closing the poverty gap

The poverty gap measures the distance between a household's income and a given poverty line, in other words, it assesses the resources needed to eradicate poverty. This measure can be used both on an individual and an aggregate level. The effects of means-tested benefits are calculated as a reduction of the poverty gap before and after the receipt of transfers, again only for house-

[21] In these two poverty brackets, we would expect to find many students, due to the particular household definition in the Swedish data. If single students aged 18-21 were excluded from this subsample, the movements measured would not fundamentally change, however. The percentage of households remaining in the extreme poverty bracket would be reduced from 27% to 12%, and in strong poverty from 18% to 11%, but the general pattern of moments into higher poverty brackets remains fairly constant.

holds having reported any means-tested benefits. The results are shown in Table 7 and Table 8. Table 7 shows the average resources needed to lift the poor above a poverty line of 50% of median disposable household income adjusted for household size (given as a percentage of the poverty line).[22]

Table 7: Average poverty gap and average poverty gap reduction by means-tested benefits for households who were poor before having received any means-tested transfers

	Germany 1994	**Sweden 1992**	**United Kingdom 1991**
poverty gap before means-tested benefits	.547	.340	.484
rank order (small poverty gap = 1)	*3*	*1*	*2*
poverty gap after means-tested benefits	.009	-.177	-.102
rank order (small poverty gap = 1)	*3*	*1*	*2*
absolute change of poverty gap	-.537	-.518	-.586
rank order (strong reduction = 1)	*2*	*3*	*1*
relative change of poverty gap	-98%	-152%	-121%
rank order (strong reduction = 1)	*3*	*1*	*2*

Source: LIS and own calculations. The average poverty gap is calculated as the average resources needed to lift the poor households over the poverty line of 50% of median disposable household income after means-tested transfers adjusted for family size, given as a percentage of the poverty line. Poverty gaps are negative if the average income of the poor after transfers is higher than the poverty line.

There are two possibilities for gauging the effects of means-tested benefits with a poverty gap measure. First, the average poverty gap before means-tested benefits can be compared to the average poverty gap after means-tested benefits for all households who were poor before having received any means-tested transfers. The results are presented in Table 7. They indicate that poverty gaps in Sweden and in the United Kingdom have now become negative, thus implying that, on average, household income of the previously poor is now above the poverty line. Only in Germany is the average disposable income slightly below the poverty line. The most favourable income position was reached by previously poor households in Sweden whose average income households increased to as much as almost 18% above the poverty line.

The relative reduction of poverty gaps has been greatest in Sweden, followed by the United Kingdom. Germany is clearly less efficient in relative terms. It would, however, be misleading to focus only on the reduction of the poverty gap and to ignore its absolute size. The average poverty gaps before means-tested benefits were much smaller in Sweden than in the other two countries; in other words, means-tested benefits had a smaller gap to fill. Consequently, considering the absolute reduction of poverty gaps, Sweden displays the smallest decrease in poverty gaps, whereas the United Kingdom has most effectively managed to close its previously large poverty gap. Interestingly, the poverty gap before means-tested transfers has been largest in Germany, although its reduction was not as effective as in the United Kingdom.[23]

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[22] To be sure, the poverty gap measure is not free from arbitrary decisions on the part of the researcher since a poverty line has to be defined.

[23] This result is particularly striking, given that the United Kingdom allocates a considerably larger share of social security expenditure on means-tested transfers than Germany.

The effectiveness of means-tested transfers in respect to the closing of the poverty gap could also be considered by focusing on households who are still poor after having received means-tested transfers. Table 7 above discussed analyses the effect of means-tested benefits on the overall poverty gap, although it is equally interesting to see whether means-tested households could improve the situation of households who remain poor after having received means-tested transfers. Table 8 shows the reduction of the poverty gap for this group of the population and compares it to the overall poverty gap before means-tested benefits as in Table 7.

Table 8: Average poverty gap and average poverty gap reduction by means-tested benefits for households who are still poor after having received means-tested benefits

	Germany 1994	**Sweden 1992**	**United Kingdom 1991**
poverty gap before means-tested benefits	.547	.340	.484
rank order (small poverty gap = 1)	*3*	*1*	*2*
poverty gap after means-tested benefits	.280	.281	.182
rank order (small poverty gap = 1)	*2*	*3*	*1*
absolute change of poverty gap	-.266	-.059	-.302
rank order (strong reduction = 1)	*2*	*3*	*1*
relative change of poverty gap	-49%	-18%	-62%
rank order (strong reduction = 1)	*2*	*3*	*1*

Source: LIS and own calculations. The average poverty gap is calculated as the average resources needed to lift the poor households over the poverty line of 50% of median disposable household income after means-tested transfers adjusted for family size, given as a percentage of the poverty line. Poverty gaps are negative if the average income of the poor after transfers is higher than the poverty line.

The results displayed in Table 8 indicate that means-tested transfers have helped to close the poverty gap of poor households, even if their income does not surpass the poverty line. Households being poor in Britain after means-tested transfers have the best income positions in this group of countries, their incomes are on average less than 20% lower than the poverty line, whereas their counterparts in Sweden and Germany have to live on an average income that is 28% lower than the 50%-poverty line.

6 Conclusion

The evaluation of the impact of means-tested benefits has brought forward some thought-provoking results, both in the dimension of variations across countries and over time. It has been able to shed some light on the question of how well means-tested benefits are achieving their major goal, the alleviation of poverty. The results of this analysis have illustrated that the receipt of means-tested benefits is no guarantee for leaving poverty. There are distinct patterns of poverty alleviation through means-tested benefits, with considerable cross-national variations. The empirical evidence for Germany, Sweden and the United Kingdom confirms earlier expectations in part, but also challenges some views about means-tested benefits in these countries.

The United Kingdom seems to achieve the most marked results of means-tested benefits with an astonishingly high degree of effectiveness, especially among the lower poverty brackets. These patterns confirm earlier insights into the British pattern of income redistribution, which claimed

that the British welfare state was very effective in preventing harsh poverty, but less effective in the moderate poverty sphere (Mitchell 1991: 43-78). Obviously, means-tested benefits substantially contribute to the effectiveness of total redistribution in the United Kingdom. This good performance cannot, however, fully be explained by the fact that means-tested transfers play a much larger role in the British welfare state than they do in Germany or Sweden. British poverty rates before means-tested transfers were higher than in the other two countries, but the poverty gap to be filled by means-tested transfers was even larger in Germany than in the United Kingdom. The United Kingdom has then, from this perspective, been most effective in closing the poverty gap.

Sweden exhibited medium poverty rates before transfers, but a considerably smaller poverty gap than in the other two countries. This indicates that social insurance benefits are relatively effective in preventing poverty, even before means-tested benefits come into play. Means-tested transfers in Sweden are less explicitly targeted on the very poor than in the United Kingdom, but distributed relatively evenly onto the recipient population. For a relatively large fraction of previously poor households, poverty was effectively prevented by these transfers. Others, however, could only marginally improve their income position. The Swedish data should, however, be interpreted with caution due to the differing household definition.

The record of means-tested benefits in Germany is far less impressive. The German social insurance benefits leave relatively low poverty rates, but a large poverty gap to fill. The effectiveness of means-tested benefits was rather weak, especially for the poverty gap measure. The average income of formerly poor recipients of means-tested benefits still remained lower than the poverty line after transfers, although their position slightly improved over time. However, the overall performance of the German welfare state in terms of the prevention of poverty is relatively good, but this must be attributed rather to the impact of social insurance than to means-tested benefits.

The use of the LIS data for this analysis has highlighted both the potential and the limitations of this database for the evaluation of the effectiveness of means-tested transfers. It has identified considerable cross-national variation in the alleviation of poverty through means-tested benefits across countries. However, there are some serious methodological problems associated with this kind of data. Therefore, further research should complement these quantitative data with qualitative information on the means-tested benefits of each country. This would not only allow for a cross-check of the plausibility of the results of this analysis, but also for a better understanding of the causes behind these figures.

7 Appendix

Table 9: Overview on LIS data sets used

Country and year	Number of cases	Type of data	Source
Germany 1994	4.197	(panel) survey	Socio-Economic Panel Study (SOEP)
Sweden 1992	12.435	survey and tax records	Inkomstfördelningsundersokningen (HINK)
United Kingdom 1991	7.030	survey	Family Expenditure Survey (FES)

Source: OECD 1995: 25-29; LIS Institutional Database. The number of cases shown here is not the total sample size of the LIS database, but the data set used in this study (excluding households with zero or negative disposable incomes).

Table 10: Overview on household definitions

	Household Definition
Germany 1994	Persons living together or single
Sweden 1992	One or two adults (over 18) with or without children (under 18)
United Kingdom 1991	A person living alone or a group of people living at the same address and having meals prepared together; with common housekeeping

Source: OECD 1995: 124, 128-134, LIS Institutional database.

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