

Bogdan M. Chiritoiu, MA, MSc
Assistant Professor

Poverty Alleviation: Minimum Income Guarantee

The flagship initiative of the social democratic government of Adrian Nastase, the minimum income guarantee, is tidying up the Romanian social benefits system. Moreover, the law introduces safeguard measures against to mitigate the disincentive to work commonly associated with means-tested benefits. The financial feasibility of the scheme, aimed at covering more than 10% of the population, is however in doubt. Should the central government fail to provide adequate funding, the initiative will prove again an empty promise of the national government thrown on the shoulders of an overburdened local administration.

Poverty in Romania

The poverty rate has substantially increased over the transition period. Table 1 show that both poverty rate and the harder extreme poverty rate doubled since 1995. Romania is also a laggard in regional comparison tables, registering the fourth worst poverty rate in Central and Eastern Europe. Only Albania and the former Soviet Republics of Moldova and Russia encounter a worse situation (table 2).

Table 1. Poverty in Romania, 1995 - 2000

	Poverty rate	Extreme poverty rate
1995	25.3	8.0
1996	19.9	5.1
1997	30.1	9.5
1998	33.8	11.7
1999	41.2	16.6
2000*	44.0	-

Source: Tesliuc, Pop, Tesliuc, 2001

Table 2: The Poverty in Central and Eastern Europe, 1995 - 1999

	Year	Poverty rate	
		2 USD PPP*/day	4 USD PPP/day
Moldova	1999	55.4	84.6
Russia	1998	18.8	50.3
Albania	1996	11.5	58.6
Romania	1998	6.8	44.5
Macedonia	1996	6.7	43.9
Latvia	1998	6.6	34.8
Bulgaria	1995	3.1	18.2
Lithuania	1999	3.1	22.5
Ukraine	1999	3.0	29.4
Slovakia	1997	2.6	8.6
Estonia	1998	2.1	19.3
Hungary	1997	1.3	15.4

Poland	1998	1.2	18.4
Belarus	1999	1.0	10.4
Croatia	1998	0.2	4.0
Czech Republic	1996	0.0	0.8
Slovenia	1997/98	0.0	0.7

Source: World Bank, 2000

Note: The poverty estimates use thresholds in USD/day/adult at 1996 PPP (purchasing power parity) equivalent.

Sources of poverty

Table 3 shows the breakdown of poverty in the Romanian population. Against the common wisdom, poverty is most prevalent not among pensioners, but among young families with many children, unemployed and even self-employed people. Over 80% of the families with 4 or more children live in poverty (table 4). Single parent families are also prone to living in poverty (table 5).

Table 3. Poverty rate function of the occupation of the head of household

	Poverty rate
Employee	29.7
Retired	25.6
Farmer	57.4
Private enterpriser	10.1
Self employed	53.9
Unemployed	59.8

Source: Tesliuc, Pop, Tesliuc, 2001.

Table 4. Poverty rate function of the age and number of children

	1995	1998
1. Poverty rate function of number of children:		
- no children	16.4	23.5
- 1 child	24.6	35.0
- 2 children	30.1	43.6
- 3 children	52.8	64.6
- 4 children or more	71.7	83.6
2. Poverty rate function of age:		
- under 7 years	30.2	37.7
- 7 - 15 years	37.1	48.7
- 16 - 25 years	34.3	45.5
- 26 - 35 years	21.7	31.0
- 36 - 45 years	26.0	36.1
- 46 - 55 years	23.7	32.3
- 56 - 65 years	14.5	21.0
- over 65 years	9.7	11.4

Source: Tesliuc, Pop, Tesliuc, 2001.

Table 5. Poverty rate in single parent families (1994)

	Poverty rate
Childless single	17.9

Single parent family with 1 child	51.8
Single parent family with 2 children	76.0

Source: C. Zamfir (ed.), 1995.

Poverty also correlates strongly with low education attainment. A household whose head did not attend the secondary school is 7 times more likely to live below poverty line, than a household headed by a university graduate (see table 6).

Table 6. Poverty rate function of the educational level of the household head

	Poverty rate
No schooling/primary school	42.00
Secondary school	41.00
Vocational training	40.00
High school	22.00
College	19.00
University	6.00

Source: Tesliuc, Pop, Tesliuc, 2001.

Poverty alleviation

The Romanian government has employed a wide array of instruments in fighting poverty. Most of social expenditure is now accounted for by the employment related contributory benefits, the most important being healthcare, pensions, and than the unemployment benefit. In addition, access to education services, an important poverty prevention tool, is free at point of delivery.

In what concerns the non-contributory benefits, there has been a shift from universal benefits to means-testing. The only large universal benefit existent is the child allowance. The means-tested income support was introduced in 1995. During the transition years the value of social benefits has decreased dramatically in both real and relative terms (see table 7).

Table 7. Social benefits as percentage of average wage

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
The average public social insurance pension	46.4	44.7	45.1	43.6	45.2	42.6	40.8	38.6	40.3	37.2	35.9	34.3
Child allowance	10.5	9.7	7.2	5.4	4.9	4.2	4.3	3.9	7.4	6.2	4.3	3.2
Supplementary allowance for the 2nd child*	-	-	-	-	-	-	-	-	13.7	10.1	7.0	5.5
Income support		-	-	-	-	-	21.3	14.0	15.6	13.2	10.6	7.7
Support allowance (post unemployment benefit)		-	-	20.0	16.1	14.4	18.6	15.7	15.4	14.7	16.8	12.9
Employment subsidy	-	-	-	-	-	24.7	20.1	17.0	18.8	17.9	21.9	17.4

*Since 1997, a supplementary allowance for families with 2 or more children was introduced

Source: ICCV

Minimum income guarantee

The minimum income guarantee has been one of the key campaign pledges of the new administration of Adrian Nastase. The Parliament has swiftly enacted it through the Law 416 / 18 July 2001. The income support will from 2002 bridge the gap between

the guaranteed minimum income and the actual income of the family, other social benefits included. There is a supplementary heating allowance for income support recipients, and the universal child allowance is substantially increased.

The minimum income guarantee integrates a number of social benefits:

- income support, burial support and emergency relief, funded from the local budget.
- child allowance, and the allowance for the wives of conscripts, funded from central budget.

The income support will continue to be provided by the local government, but overall 80% of funds are expected to come from the central government, through defined destination grants. Apart from cash transfers, the income support could include goods or services.

Poverty-trap

The problem commonly associated with means-tested benefits is the disincentive to work. Because any increase in income is offset by the decrease in the amount of the social benefit, the marginal utility of labor is very low. The result is the so-called 'poverty trap': people do not find worthwhile to take the pain of a regular job, and therefore do not acquire the experience necessary for advancing to better paying positions.

Luana Pop from ICCV (a research institute) had found little support for this theory in Romania. Due to low administrative capacity, the Romanian government is not able to verify the income statements of the applicants for social benefits. The higher probability result in Romania would be to channel the recipients of social assistance towards the black market, rather than idleness.

However, the law includes safeguards for this situation. The bodily able recipients are required to perform up to 72 hours per month community work, and those legally employed receive a 15% higher income support.

Implementation problems

The Achilles' heel of Romanian income support has been its reliance on local administration. Tables 9 and 10 paint a dramatic picture of the ability of the local government to implement means-tested benefits. In 1995 the distribution was dealt with by the central government. Since 1996 it was taken over by the local administration. Faced with an administrative and especially a budgetary challenge, the local government failed to implement the measure. In 2000 the number of families receiving income support represented only 6% of the number of 1995 – see tables 9 and 10.

Table 9. The number of families receiving income support (end of year, compared with 1995)

Year	1996	1997	1998	1999	2000
%	49%	26%	22%	15%	6%

Source: MMSS

Table 10. The dynamic of the real expenditure for social benefits (1995 = 100%)

Year	1996	1997	1998	1999	2000
%	144.2%	47.6%	30%	14.8%	-

Note: The 1995 expenditure covered only the last 3 months of the year.

Source: MMSS

In 1994 the estimated number of households qualifying for income support was estimated at 659,000, or about 12% of the population. By 1998 only 50,000 households, representing 0.5% of the population, were actually receiving income support.

The minimum income guarantee could have the same fate. The Ministry of Labor and Social Solidarity estimates that those covered by it will amount to 600,000 – 750,000 a comparable number to those entitled to income support in 1995. Under a comparable administrative and budgetary challenge local administration might crack again.

By 2000, most of local authorities, especially in rural areas, had practically stopped distributing the income support. Under the present provisions of the law, a large share of the beneficiaries of the minimum income guarantee will come from rural areas (e.g. pensioners from the former socialist farming system). This will create a huge pressure on the local government from rural communities, which are already the big losers from the financial de-centralization reform introduced by the previous government.

Financial feasibility

In 1994 income support covered 87% of the extreme poverty threshold, and 58% of the poverty one. By 1998 its real value has eroded to only 48% of the extreme poverty threshold, respective 32% of the poverty one.

In 1997, income support amounted to only 0.05% of GDP. Now the government expects the minimum income guarantee to raise this amount to 0.4% of GDP, an 8 fold increase.

Conclusions

- The minimum income guarantee confirms the orientation of Romania towards means testing, and away from universal benefits. This option is consistent with the dire financial situation of the country.
- The minimum income guarantee includes measures to mitigate the disincentive to work that is associated with means-testing.
- The minimum income guarantee is part of a complex approach to poverty alleviation. It combines cash benefits with in-kind provisions (e.g. school allowance for pupils), and special measures for high risk social groups (e.g. Roma). This approach should be furthered by developing social assistance programs, as an alternative to cash benefits.
- The government is right in identifying the link between children and poverty. The substantial raise in child allowance is welcome from this perspective.
- The Romanian social benefit system is well targeted to reach the poor. Its main problem has been the lack of resources. Would be consistent with the

philosophy of means-testing to abolish the child allowance as a universal benefit, and instead transform it in a means-tested one. Another option is to take into account, when establishing the minimum income guarantee, the difference in the cost of living between rural and urban areas, and employ different thresholds. This would also ease the burden on the local authorities from rural communities.

- Based on the experience since 1995, if the central government will fail to provide the resources for income support, local administration will be unable to cope with the burden, and the whole policy will turn in an empty promise that will foster frustration. Should the situation of public finances turn worse, the government would be better advised to narrow down the scope of the policy from over 10% of population at present to a more manageable number.