

WHAT MAKES UP A DECENT BASKET OF GOODS AND SERVICES? REVIEW OF THE LIVING WAGE EXPENDITURE CATEGORIES

Jan Bittner

Abstract

The new European legislation introduces the concept of the adequacy of the minimum wage while offering a basket-based approach for its assessment. For such purpose, the member states and other parties can use the existing research on the concepts of living wages – basket-based indicators of low wages not enabling a decent standard of living. This text presents a review of seven living wage methodologies relevant to the European context with an emphasis on the question of the creation and composition of the consumption basket, which is the basic building block of every basket-based indicator. I find that the availability and method of obtaining data for estimating the consumer baskets are the main determinants of the number of categories and the detail of the baskets. Also, a definition of the decent standard of living by the respective concepts serves as a determinant of the division of the basket. The main categories common across the concepts are food and housing, whose estimation method the authors pay great attention to. Apart from other consumer goods categories and public services, financial reserve and savings is also important category, the quantification of which is problematic.

Key words: Living Wage, Minimum Wage, Poverty

JEL Code: J31, J39, P36

Introduction

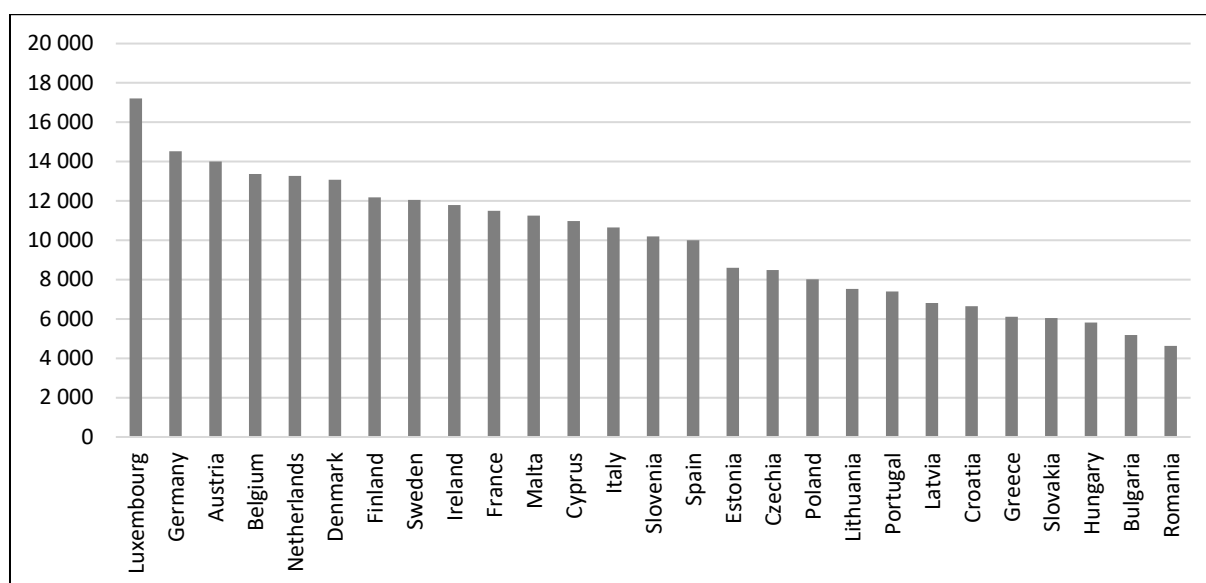
On June 16, the Council for Employment, Social Policy, Health and Consumer Protection (EPSCO) confirmed the provisional agreement of the European Commission, the European Parliament and the Council of the European Union on the proposal for a Directive of the European Parliament and of the Council on adequate minimum wages in the European Union (Committee on Employment and Social Affairs, 2022). As the name of the directive suggests, its primary goal is to ensure the minimum wage level that guarantees a decent standard of living for employees in the EU member states, supporting the efforts to fight against working poverty.

What does “adequate” mean? The legislation sets out the criteria the member states should follow while deciding on their statutory minimum wage. These criteria are purchasing power, long-term national productivity levels and developments, wage levels, distribution, and growth. Even though the final decision remains within the competence of the member states, the criteria make a case for data-based policy decision-making. Generally, the income assessment of an individual of a household uses two possible sets of tools: relative and absolute indicators, both mentioned by the directive:

„Among other instruments, a basket of goods and services at real prices established at national level can be instrumental to determine the cost of living with the aim of achieving a decent standard of living. In addition to material necessities such as food, clothing and housing, the need to participate in cultural, educational and social activities could also be taken into consideration. [...] That assessment might be based on reference values commonly used at international level, such as the ratio of the gross minimum wage to 60% of the gross median wage, the ratio of the gross minimum wage to 50% of the gross average wage, which are currently not met by all Member States, or the ratio of the net minimum wage to 50% or 60 % of the net average wage.“ (Committee on Employment and Social Affairs, 2022, p. 22)

The relative approach, also known as the distribution-oriented approach, originates in the Kaitz index. Its policy application is associated mainly with the relative poverty measurements used by the European Commission for setting the poverty threshold by the relative position of an income to the 60 % of the equivalized household disposable income in the country. The commonly criticized feature of such an indicator is a missing connection to purchasing power and thus its international incomparability (Ponthieux, 2009). Based on 2020 Eurostat data, Fig. 1 shows that the purchasing power at the poverty line level is 3.7 times higher in Luxembourg than in Romania. It follows that the household of a working poor Luxembourger can have three times the purchasing power, i.e. three times bigger basket to satisfy basic needs than a non-poor Romanian household. Given the assumption that the basic material needs of a person do not fundamentally differ across the European Union, the relative indicators cannot sufficiently assess the incomes’ or minimum wages’ provision of a specific standard of living. It is why the directive mentions the purchasing power of minimum wage as an alternative way to assess their level.

Fig. 1: The purchasing power at the level of the poverty threshold (in PPS; 2020)



Source: Eurostat

The assessment of purchasing power of a wage using a basket-based approach has a reference: a living wage. The concept of a living wage responds to a situation where the remuneration for normal working hours is insufficient to ensure a decent living standard for the worker or his family. Many regional living wage concepts around the world differ in their methodology. Therefore, the nonunified concept is not internationally comparable and cannot be used to evaluate a policy across countries, such as the mentioned directive.

The first step to embedding the living wage concept in academic and political practice is a description of state of the art. The last comprehensive review was done more than a decade ago by Anker (2011), however, without much methodological detail. Since then, some new concepts have emerged, and along with the development of the availability of data sources, the existing ones have also gradually changed.

All the living wage methodologies (and all the basket-based indicators in general) start with the critical question: what makes up the basket of goods and services that enables a decent life? This text looks at a selected group of existing living wage methodologies and compares their approach to determining expenditure categories, i.e. the division of a decent consumption basket. Particularly, I study the reasoning behind the number of expenditure categories and general guidelines in their bundling. In other words, the goal is to find focal points between different approaches and reasons for their choice.

Section 1 describes the reviewed group of living wage methodologies and the method, Section 2 presents the results, followed by a conclusion in Section 3.

1 Research Method

I study the existing research on living wages following specific criteria to limit the number of reviewed concepts. The focus of this text is put in the context of European legislation. Therefore, I include all the European concepts from the United Kingdom, Ireland and Czechia. Given the history of the concept mainly in Anglo-Saxon countries, I include the concept from New Zealand as well. There are living wages in the United States and Australia, which were not included in this review. The US Living Wage Calculator, which accounts for only basic needs, is thus considered less than the acceptable minimum. The authors themselves state that it is perhaps better to define this living wage as a minimum subsistence wage (Glasmeier, 2021). As for the Australian concepts, there are multiple regional campaigns with their approaches without umbrella methodology. Apart from the national concepts, international methodologies are also relevant for the review. Firstly, Anker and Anker (2017) have developed an Ankers' methodology adopted by the Living Wage Coalition while being a referential methodology for others. Secondly, a methodology which refers to the Ankers is a worldwide methodology based on the WageIndicator project developed by Guzi and Kahanec (2019). Guzi (2021) has also created a specific European variant by altering the methodology for the concrete European context. Here, I name the reviewed concepts with the sources of their methodologies and further used abbreviations:

- The Living Wage Foundation's living wage for the United Kingdom (abbrev. UKLW) based on the methodology description of D'Arcy and Finch (2019) and the minimum income standard research publication as the data basis for the UK methodology (Davis et al., 2021).
- The Republic of Ireland Living Wage (abbrev. IELW) using their Technical Document (Living Wage Technical Group, 2021) with the methodology description.
- The Czech Minimum decent wage (abbrev. CZLW) with information about their methodology from their website (Platforma MDM, n.d.).
- Living Wage Aotearoa New Zealand (abbrev. NZLW) is the national non-European concept with the methodology described in King and Waldegrave (2012).
- The Global Living Wage Coalition adopted Ankers' methodology (abbrev. AM) for computing living wages mainly in the developing world from Anker and Anker (2017).
- WageIndicator has a couple of methodologies: the original methodology of Guzi was improved by Guzi and Kahanec (2019) (abbrev. WI), and finally Guzi (2021) used

mainly the same dataset from WageIndicator to create Europeansimilare living wage concept for the minimum wage assessment (abbrev. EULW).

I review the above-listed technical documents and match the methodologies' expenditure categories in the first step. For such purpose, I choose Classification of Individual Consumption According to Purpose (COICOP), an internationally accepted statistical classification also used by the European Commission (CZ-COICOP, n.d.). It is a neutral classification used for structuring household expenditures, which is detailed enough for those methodologies with more categories while enabling it to match with the more general ones. Nonetheless, some methodologies use "other" expenditures to cover various items from multiple COICOP categories. I call them "cross-categories" and list them as a separate category. Secondly, study the reasoning behind the detail of the categories dividing the decent basket of goods and services. The choice of this division is a methodological cornerstone. From the comparison perspective, it enables to structure the review before studying the categories in detail. The methodologies differ not only in several categories but also in their content. It is why I bundle the categories in general clusters distinguishing their essence. In other words, I search for similarities and differences and their reasoning.

2 Comparative analysis

The matched living wage categories with the COICOP classification is shown in Tab. 1. The fundamental difference between the investigated methodologies in terms of expenditure categories is their number or the detail of their focus. In this, the AM is fundamentally different from the others, with only four categories. Apart from the basic expenditure categories – expenditure on housing and food – it does not distinguish other specific areas. Even the closest methodology used for the developing countries, the WI, indicates eight categories. The first explanation is data availability. Ankers created a methodology for developing countries, where even elementary statistics, such as food prices, can be unavailable. It is why even the estimation of the two main categories, housing and food, thus consists of providing primary data based on the survey and fieldwork of researchers in the given regions. For that reason, the number of estimated categories is minimized to the most important ones. The opposite extreme is found in UKLW and IELW with 17 different categories, although having the same denominator, which is the primary data. In the case of the British and Irish variants, however, the reason for their choice is not the unavailability of an alternative, but the methodology of determining the "*minimum acceptable living standard as defined by the public.*" (Living Wage Foundation, n.d.), respectively the "*minimum acceptable standard of living*" (The Rep. of Ireland Living

Wage, 2009). Unlike the other national and international methodologies, these two rely on focus groups composed of representatives of the public who, based on the principle of consensus, agree on the definition of such a minimum. For that reason, dividing the consumer basket into many categories does not cause a data-availability problem. On the contrary, greater detail makes it easier for facilitators to focus on all conceivable aspects of consumption in particular. All the other reviewed methodologies define the decent minimum on the basis of an expert decision while using secondary data (such as household surveys and price statistics) or its own online survey in the case of WageIndicator methodologies.

The number of categories is not only a consequence of the desire for detail but may also be related to the very definition of dignity. As a result of the development of the concept, two different approaches to the meaning of dignity have developed here. The first is based on the history of the living wage as a tool in the fight for higher wages in developing countries, which is based purely on providing basic human needs (Anker, 2011). In such a case, other expenses are just a supplement to basic needs. This is exemplified above all by AMs, which differentiate between food and housing, with the remaining expenses representing an additional margin. And the methodology does not go into specifics. The approach to the food category, in some more detailed cases supplemented by a separate category of drinking water, does not differ in essence. Food expenditures follow the nutritional guidelines of the United Nations, the World Bank and others. Given the cultural differences in the diet composition, it is adjusted by the secondary data on the average diet pattern. Finally, this constructed diet is priced. In the case of the focus groups-based approach, the nutritional adequacy is input by the facilitators. Housing, sometimes divided into rents and energy, is a substantial category with a significant variety of forms, prices, availability of rental versus owner-occupied housing, the age and condition of apartments and houses even within a region. Due to its importance in family budgets, the total living wage amount is susceptible to the chosen calculation method. In general, the estimates use either a reference house type based on rich data on location or number of bedrooms (WI, EULW) or international housing standards (AM), rents distribution supplemented by energy modelling tools (NZLW) or social benefits indicators (CZLW).

The second approach, applied mainly in developed countries, expands the basic expenses by others, perceived by society as necessary, which ensures a decent quality of life. These categories, which include clothing, household equipment and maintenance, all kinds of transport and communication, are hard to define in priceable items. With exceptions, those expenditures are estimated using household survey consumption data and artificially specified

Tab. 1: Expenditure categories

COICOP	UKLW	IELW	CZLW	NZLW	AM	WI	EULW
01 - FOOD AND NON-ALCOHOLIC BEVERAGES	Food	Food	Groceries	Food	Food	Food	Food
	Water rates					Water	Drinking water
02 - ALCOHOLIC BEVERAGES AND TOBACCO	Alcohol						
	Tobacco						
03 - CLOTHING AND FOOTWEAR	Clothing	Clothing	Clothing and footwear	Clothing and footwear		Clothing	Clothing and footwear
04 - HOUSING, WATER, GAS, ELECTRICITY AND OTHER FUELS	Rent	Housing	Housing	Actual rentals for housing	Housing	Housing	Housing
	Fuel	Household energy		Household energy			
05 - FURNISHINGS, HOUSEHOLD EQUIPMENT AND ROUTINE MAINTENANCE OF THE HOUSE	Household goods	Household goods		Household contents and services			Household maintenance
	Household services	Household services					
	Other housing costs						
06 - HEALTH		Health	Health and hygiene	Health		Healthcare	Healthcare
07 - TRANSPORT	Motoring	Transport	Transportation	Transport		Transport	Public transport
	Bus and Coach Travel						Car operation costs
08 - COMMUNICATIONS		Communications	Telecommunications	Communication		Phone	Phone
09 - RECREATION AND CULTURE	Leisure Goods and services	Social inclusion and Participation		Recreation and culture			Culture and recreation
	Other travel costs						
10 - EDUCATION	Childcare	Education		Education			Education
11 - RESTAURANTS AND HOTELS							Eating out
12 - MISCELLANEOUS GOODS AND SERVICES	Personal goods and services	Personal costs		Miscellaneous goods and services	Sustainability and emergencies		Personal care
		Household insurances					Insurance - Home
		Insurance - Health					
		Insurance - Car					
		Savings and Contingencies					
CROSSCATEGORIES			Savings	Other expenditure	Other essential expenses	Other costs	
		Free time and education					

Source: Own compilation

levels of expenditures as a concrete quartile. By listing these categories in detail, the concepts try to demonstrate areas that should not be neglected. On the other hand, their hard-to-define nature together with limited data sources leads to a uniform distribution-based approach of their estimation that does not require such detailed categorization.

A problematic area is spending on services that are, to varying degrees, provided publicly - education and health. To a large extent, these expenses are included in taxation, as they tend to be provided free of charge. However, this does not mean that households have no costs in these areas. Glickman (1999) points to the need to include in the living wage expenses related to social participation, which are desirable for a dignified life, whether it is culture, sports or civic activities. Such a concept sees poverty more broadly than material lack in vital and existential categories.

Again, a common feature of all methodologies is the effort to cover otherwise unspecified items and the creation of a financial reserve for one-off expenses, savings for old age or insurance. These categories represent a nut for maintaining the consistency and justification of any methodology, but at the same time, they tend to be an essential item. Unlike concretely defined categories, this item is usually an arbitrarily chosen percentage of total expenses. Take 5% sustainability and emergency margin in AM, WI and EULW, average household expenditures on miscellaneous goods and services (personal care, insurances etc.) in NZLW for the households between the first and the fifth decile or 5% margin for unexpected events with 7% for insurance in CZLW.

3 Conclusion

The European Union is close to legislatively anchoring the adequacy of minimum wages. Despite the non-binding proposal for the minimum wage level, the directive offers tools for an assessment of the wage policies. This study focused on the basket-based approach to wage assessment, enabling us to compare the purchasing power of the minimum wages across the continent. The well-known tool for such exercise is a living wage. This review contributed to the existing research on living wage by comparing existing approaches towards creating the basket of goods and services. I found that the authors decide on the detail of the basket on the basis of the data availability and the method of their collection. The unavailability of data makes the estimation process difficult while making the authors reduce the number of expenditure categories to minimum. The methodologies using focus groups as the basket creation method, on the other hand, use detailed categories in order to facilitate the process. The methodology of creating the basket is also directly linked to the definition of decency or, in the context of the

European legislation, adequacy. Further research can follow up with deepening the categories analysis with the quantitative analysis of the actual estimates.

References

- Anker, R. (2011). *Estimating a living wage: A methodological review*. ILO Geneva.
- Anker, R., & Anker, M. (2017). *Living wages around the world: Manual for measurement*. <https://doi.org/10.4337/9781786431462>
- Committee on Employment and Social Affairs. (2022). *Provisional agreement resulting from interinstitutional negotiations: Directive on adequate minimum wages in the European Union*. https://www.europarl.europa.eu/meetdocs/2014_2019/plmrep/COMMITTEES/EMPL/AG/2022/07-11/1258585EN.pdf
- CZ-COICOP. (n.d.). Klasifikace individuální spotřeby (CZ-COICOP). Retrieved 11 December 2021, from https://www.czso.cz/csu/czso/klasifikace_individualni_spotreby_cz_coicop-
- D’Arcy, C., & Finch, D. (2019). The calculation of a living wage: The UK’s experience. *Transfer: European Review of Labour and Research*, 25(3), 301–317. <https://doi.org/10.1177/1024258919847313>
- Davis, A., Hirsch, D., Padley, M., & Shepherd, C. (2021). *A Minimum Income Standard for the United Kingdom in 2021*. <https://www.jrf.org.uk/report/minimum-income-standard-uk-2021>
- Glasmeier, A. (2021). *LIVING WAGE CALCULATOR User’s Guide / Technical Notes*. <https://livingwage.mit.edu/articles/99-a-calculation-of-the-living-wage>
- Glickman, L. B. (1999). *A living wage: American workers and the making of consumer society*. Cornell University Press.
- Guzi, M. (2021). *Cost of Living, Living Wages, and Minimum Wages in EU-27 countries*. https://wageindicator.org/documents/publicationslist/publications-2021/study-en_020621.pdf
- Guzi, M., & Kahanec, M. (2019). *Living Wages Globally*. WageIndicator Foundation. https://wageindicator.org/documents/publicationslist/wageindicator-org-publications-2019/report_intro_pdf.pdf
- King, P., & Waldegrave, C. (2012). *Report of an investigation into defining a living wage for New Zealand*. https://d3n8a8pro7vhm.cloudfront.net/nzlivingwage/pages/129/attachments/original/1434872250/Living_Wage_Investigation_Report.pdf?143
- Living Wage Technical Group. (2021). *Living Wage Technical Document: Calculating a Living Wage for the Republic of Ireland*. <https://www.livingwage.ie/>
- Platforma MDM. (n.d.). *Minimum decent wage*. Minimální Důstojná Mzda. Retrieved 30 April 2022, from <https://www.dustojnamzda.cz/minimum-decent-wage/>
- Ponthieux, S. (2009). The working poor as a statistical category: Methodological difficulties and exploration of a notion of poverty in earned income. *INSEE*. <https://www.insee.fr/en/statistiques/1380803>

Acknowledgement

This article is provided as one of the outputs of the research project European Minimum Wage and Consumption No.39/2021, which is financed by the Faculty of Business Administration, Prague University of Economics and Business.

Contact

Jan Bittner

Prague University of Economics and Business

W. Churchill Sq. 1938/4

130 67 Prague 3 – Žižkov

Czech Republic

jan.bittner@vse.cz