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C- The Poverty Penalty in France: How the Market Makes Low-Income Populations Poorer

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Abstract. What has come to be known as the poverty penalty–the additional cost paid for goods and services by the poor relative to the more affluent–is a familiar mechanism in emerging countries. For profoundly different reasons, however, poor people in developed countries also suffer from the poverty penalty. Quite naturally, without any particular ill will on the part of the actors in the commercial sector, the market sometimes penalizes the poor by making them pay more than other households, per unit of consumption, for the same goods and services.

Drawing on a study by the Boston Consulting Group conducted at the request of the action tank "Entreprises et Pauvreté", this paper sets out to quantify a part of the poverty penalty. The economic impact is far from incidental, as it represents, at the very least, a "double jeopardy" of an extra 2.5% of the total budget for low-income households, or some €500–more than a month's worth of "discretionary" spending.

The paper sheds light on the various underlying mechanisms that contribute to the creation of the poverty penalty. These "undesirable side-effects" of the market are of five types:

- An unfavorable cost structure
- An unfavorable price structure
- The law of supply and demand
- A lack of equipment or an unfavorable risk profile
- Insufficient objectivity to deal with scarce, imperfect or missing information.

The ultimate aim is to favor the development of compensation or annulment solutions through "positive discrimination" actions implemented by businesses; experiments currently under way offer some hope in the fight against the poverty penalty.

Keywords. Poverty in developed countries, poverty penalty, double jeopardy, social business.

1 The Poverty Penalty in France: How the Market Makes Low-Income Populations Poorer

As numerous studies have shown, poverty cannot be understood as a one-dimensional phenomenon, restricted to financial issues alone. Financial constraints remain, of course, a core concern for the poor, but these constraints are aggravated by another, perhaps even more unjust, form of pressure. Known as the "poverty penalty" or "double jeopardy", it refers to the fact that the poor often pay more per unit of consumption than the non-poor. Or as one Washington Post journalist put it, provocatively: "You have to be rich to be poor" (Brown 2009).

There are few studies that document in any detail the poverty penalty in rich countries. Indeed, as far as we are aware, no such study has ever been conducted in France. This paper sets out to change that. It is based on a study commissioned by the HEC professorial chair in Social Business and the action tank "Entreprise et Pauvreté", conducted *pro bono* by a team from the Boston Consulting Group's Paris office.

Using available statistical data, this study focused on seven sectors of activity. Its conclusions, as we shall see, are damning: on average, compared to the rest of the population, poor households pay an annual penalty of €500 in the sectors analyzed: a "double jeopardy" of 2.5%, or even as high 8% for

[1] This research is the result of a collaboration between the "Social Business, Enterprise and Poverty" chair at HEC Paris (sponsored by Danone and Schneider Electric), the action tank "Entreprise et Pauvreté", and the strategic consulting firm Boston Consulting Group. The authors would like to thank David Menascé for his valuable help throughout this project.

certain types of household. This may sound like a lot of money, and yet it is only a part of the penalty paid by poorer consumers. There are also significant penalties in other sectors, which are harder to evaluate; as we argue below, the poor are subject to "triple" or even "quadruple" jeopardy.

This is not to say that the business world has hatched some kind of conspiracy against the poor. It is simply that, left to their own devices, the market mechanisms that businesses have to deal with naturally penalize the poor. This paper looks into the idea of introducing a new system of "positive discrimination" in business, this time in favor of the poor.

2 Costing the poverty penalty

The poverty penalty is a relatively well-known phenomenon; it was described for the first time in the United States in 1963 by David Caplovitz, in the evocatively titled "The Poor Pay More". In 2004, C.K. Prahalad's book "The Fortune at the Bottom of the Pyramid" provided a striking update for the poor living in emerging countries. There are now a number of studies that quantify, at least to some extent, the size of the poverty penalty in emerging countries, but the phenomenon remains largely unrecognized in rich countries such as France. And yet the national statistical data are there to tell the tale, albeit incompletely.

2.1 A well-known phenomenon affecting the poor in emerging countries

Poverty penalties have been widely analyzed in emerging countries, probably because they are even more flagrant there than in rich countries. In Bombay, for example, Prahalad and Hammond (2002) have shown that the inhabitants of Dharavi, India's biggest slum, pay 20% more for their rice than the inhabitants of the residential district of Warden Road. Depending on the product or service, this double jeopardy can rise dramatically, reaching 100% for a minute of telephone use, and prices 10, 37, and up to 75 times higher for anti-diarrhea medication, water and credit, respectively.

The water sector provides a good illustration of the phenomenon. For people living in slums, not being connected to the water distribution network means that they have to pay much more for water of dubious sanitary quality. A World Bank study of 47 poor countries evaluated the average markup of water sector intermediaries, showing how the price per cubic meter of water shoots up from less than US$ 0.5 when purchased from public or private utilities to over $4.5 when bought from street vendors (Kariuki and Schwartz 2005).

Poverty penalties in poor countries are in large part attributable to imperfections in the *informal* market and the inability of the poor to access the same markets as the non-poor, due to institutional obstacles (lack of administrative recognition, or access to conventional banking networks) or physical barriers (non–connection to utility grids, rural isolation).

2.2 A little understood, but very widespread, phenomenon in France

Paradoxically, although they have no institutional or physical obstacles, the poor in rich countries also pay poverty penalties. The mechanisms at work may be different, but the result is the same: those in poverty are hit with a double jeopardy, in the form of higher prices per unit of consumption.

2.2.1 The first penalty: the situation of the poor in France

2.2.1.1 The traditional measure of poverty in France

The official definition is based on the threshold of 60% of median income (i.e. 880 euros a month for a single person), below which people can be considered to be poor. In 2009, the last year for which the figures are known, 13.5% of the French population was concerned, or 8.2 million people (INSEE 2011). While the size of that figure may, quite rightly, come as a surprise, it nonetheless places France in a favorable situation compared with most other European countries, as the corresponding figures are, for example, 15% for Germany and 19% for the United Kingdom (Eurostat 2010). The number of people in poverty is on the increase, however, up by more than 750,000 on 2002, when the percentage was 12.9%. The population groups most exposed to poverty are couples with 3 or more children (34%), single-parent families (33%), and young people under the age of 24 (19%) (INSEE 2011). These figures need to be handled with some precaution: as the ONPES report (2010) points out, the statistical tools traditionally used for measuring poverty do not always accurately reflect changes in poverty, mainly because of the time lag involved in collecting the data. The deterioration measured in 2009, for example, does not seem to take fully into account the sudden worsening of the situation reported in "field" observations.

2.2.1.2 Measuring what is "left-to-live-on": essential, necessary and discretionary spending

A more accurate understanding of poor population groups can be gained by analyzing their budgets, separating out the irreducible expenses they have to meet. These expenses correspond to items of "essential spending": rent, taxes, loan repayments, compulsory insurance, and utility bills: gas, water, electricity, etc. For poor households (the 1st income decile), this figure represents 31% of income. France's High Commission for Active Solidarity against Poverty estimated in 2009 that the proportion of essential spending had risen by 40% between 2001 and 2006 for the poor, whereas the percentage had remained stable for households above the poverty line (Hirsch, 2009).

The money remaining once these expenses have been met–the "left-to-live-on" amount–is a useful tool for measuring the real situation of poor households. It can in turn be subdivided into in necessary spending, discretionary spending, and saving capacity. The Boston Consulting Group study proposes the following breakdown: "necessary" spending refers to food, transportation, communication, health, school lunches, education and, finally, financial services. The rest is classed as "discretionary spending", the main items being: clothing, leisure, furniture/equipment, non-mandatory insurance, alcohol and tobacco, and, finally, hotels and restaurants. The

Table 1. Distribution of spending by income

	Poor households	Median households	Rich households
Essential & necessary spending	€ 11,994 (70%)	€ 19,994 (50%)	€ 39,710 (33%)
Discretionary spending	€ 6,378 (37%)	€ 12,406 (31%)	€ 31,701 (26%)
Saving capacity	€ -1,343 (-8%)	€ 7616 (19%)	€ 50,603 (41%)
Total income	€ 17,029	€ 39,966	€ 122,014

Source: BCG study "Double Peine" for the action tank " Entreprises et Pauvreté" February 2011; INSEE data

balance left over when total spending is subtracted from income is called "saving capacity".

Using the INSEE figures, and assimilating poor households to the 1st income decile, median households to the average of the 5th and 6th deciles, and rich households to the 10th decile, the breakdown of spending for each profile is indicated in Table 1 below.

In other words, once the essential and necessary expenses have been met, poor households (with an average of 2.2 people) are left with €420 a month to pay for clothes, furniture or entertainment. As this amount is insufficient, they fall back on borrowing–an average of €110. Clearly, for these households, the monthly gap between borrowing and saving–for "rainy days" or to improve their living conditions–is a matter of a few dozen euros either way.

The second penalty has to be seen in this context of almost non-existent room for manoeuver, which makes it all the more painful.

2.2.2 The double jeopardy: measuring the poverty penalty in France

2.2.2.1 The BCG study of February 2011

Although studies have been conducted in certain specific sectors–for example, the 2008 ADEME study on energy consumption–there was no pre-existing research, as far as we are aware, to evaluate the poverty penalty in France across the board. The BCG study set out to do just that. The analysis focused on seven key items of "essential and necessary" spending: housing, food, transportation, insurance, credit, communication and health (see box for the methodology). The study deliberately restricted itself to analyzing quantitative data from INSEE, in order to illustrate the double jeopardy in the most factual way possible. As we shall see, these methodological choices lead us to believe that the findings of this study should be seen as a lower-end estimate of the double jeopardy for poor households.

While this analysis does not find evidence for a double jeopardy in "food" and "transportation" spending, it does quantify the associated double jeopardy on the five other items. The main conclusions are summarized in Table 2 below. The additional cost ranges from 3% (insurance) to 20% (consumer loans and health). Relative to the total expenditure

Methodology of the Boston Consulting Group Study

The study conducted by the BCG draws on the latest major detailed survey from INSEE on household income and consumption in France, published in 2008.

The BCG began by analyzing the budgets of poor households, broken down into basic items of expenditure, and then selected the expenditure items most relevant to the analysis of the poverty penalty due to their significance for the budgets of poor households and their "double jeopardy" potential.

The next step was to evaluate the gap between unit prices in a selection of categories. Drawing on the detailed analysis of spending, a unit purchase price was calculated for each category and compared with the price paid by the median consumer, based on quantities consumed (e.g. rent/surface area), the price/volume curve (e.g. for energy) or a typical spending basket (e.g. food, health). These calculations were used to synthesize the "double jeopardy" effect for a poor household.

The factors that account for the double jeopardy were then analyzed. Before summarizing the data and probing, for each spending category, the levers that could be explored by business, the authors of the study examined the existing compensatory mechanisms and their triggering thresholds (aid in the form of state welfare payments, such as housing support, or of social benefits in kind, such as universal supplementary insurance cover, access to social rented housing, and social tariffs).

Table 2. Quantification of the double jeopardy.

	Share of poor household spending	Average double jeopardy	Main cause of the double jeopardy (DJ)
Rent	12.8%	8%	DJ concentrated on private tenants (+15%)
Utilities	9.1%	5%	DJ on collective charges (+16%) and domestic gas (+6%)
Insurance	6.3%	3%	DJ on home insurance (+20%)
Credit	4.4%	20%	Use of consumer credit
Communication	4.0%	7%	Use of pre-paid cards
Health	2.6%	20%	Lower supplementary cover

Source: BCG study "Double Peine" for the action tank " Entreprises et Pauvreté" February 2011

of poor households, the double jeopardies identified represent a premium of 2.5%, or about €500 in additional annual spending: equivalent to more than a month and a half of discretionary spending. Expressed on a national scale, the annual cost of the double jeopardy for the 3.5 million poor households comes to almost 2 billion euros.

It is important to remember that these figures are averages, obtained by analyzing statistical aggregates. For a fuller, more tangible, understanding of the extent of the double jeopardy, the BCG study also offers an interesting comparison between three families in typical configurations: a family on a median income and two families living in poverty (one of them owning its own home, the other renting). Table 3 highlights the cost differences per unit of consumption between median households and poor households, and the double jeopardy for each spending category. In the configurations considered, the annual cost of the double jeopardy totals €1025 for the tenant family and €1139 for the home-owning family. In either case, this represents more than 5% of household income and the equivalent of more than two and a half months of discretionary spending. In reality, poor households soon reach a double jeopardy of 8% of income.

2.2.2.2 Towards a definition of "triple" and "quadruple" penalties?

The BCG study is rich in insights, and its quantified findings are already highly significant. And yet, by its design, the study minimizes the amplitude of the double jeopardy. On the one hand, the set of sectors analyzed covers only 2/3 of the total consumption of poor population groups. Extending it to all of the goods and services consumed by poor households would logically lead to a concomitant increase in the body of data adduced. On the other hand, the method focuses on statistically attested double jeopardy; the study does not detect a double jeopardy either in food or transportation, categories which nonetheless represent 15.4% and 9.4% respectively of total consumption by poor households. Does this mean that there is no double jeopardy in these two categories? That seems unlikely.

For food, the double jeopardy is expressed, for example, in the inferior nutritional quality of "low-end" foodstuffs. This inferior nutritional quality can have significant health consequences, because the food is in principle of lower quality, or because greater quantities have to be purchased, and ingested, for the same nutrient and vitamin intake. For transportation, the question of the double jeopardy arises directly when carmakers practice cutthroat competition on the price of new cars and keep their dealerships afloat by pushing up their margins on used vehicles, or when the cost of the technical inspection and the obligatory repairs that follow is borne disproportionately by the poorest households.

In either case, one could speak of a "triple penalty" when discussing the inferior quality of the goods purchased (in food, for example, but also in other categories such as domestic appliances) or the induced additional functioning costs (for transportation, for example, but other categories, such as heating for poorly insulated houses could also be cited). Admittedly, these additional costs could be integrated into the double jeopardy, but their indirect and often unpredictable nature argues for a separate conceptualization. Evaluating this "triple penalty" would call for an altogether more onerous methodology, notably with longitudinal monitoring of a panel of poor households.

Finally, it may be legitimate to speak of a "quadruple penalty" when one considers that exposure to the media–especially television–is far higher among the poor than among more affluent groups. An INSEE study on the consumption of TV programs clearly shows that the least affluent socioeconomic groups (manual workers, non-manual workers, pensioners) watch more television than mid-level occupations, middle managers, and senior managers and professionals (INSEE 2005): 51% of non-manual workers, 61% of manual workers and 73% of pensioners watch more than two hours of television a day, whereas these figures fall to 43% for mid-level occupations and 27% for middle managers and for senior managers and professionals. The consequence of over-exposure to television is clear: poor households are the first victims of a frustration effect, bombarded with the new

Table 3. Cost per unit of consumption

	Median households	Poor households	% double jeopardy
Rent	€ 45 / m²	€ 52 / m²	15.6
Utilities	€ 0.44 / m²	€ 0.51 / m²	13.7
Domestic gas	€ 84.9 / MWh	€ 89.6 / MWh	5.6
Home insurance	€ 80 / room	€ 96 / room	20.0
Property loans	€ 96 / m²	€ 107 / m²	11.5
Consumer loans	€ 1041 / n goods	€ 1374 / same goods	32.0
Mobile telephone	€ 15 / hour	€ 19 / hour	26.7
Health	€ 389 / n treatments	€ 486 / same treatments	24.9

Source: BCG study "Double Peine" for the action tank "Entreprises et Pauvreté" February 2011

goods and services showcased every day by the media. This psychological quadruple penalty is hard to quantify, but it is nonetheless real.

3 The mechanisms behind the poverty penalty

The debate about the impact of the market on the situation of people in poverty all too often boils down to a clash of ideological positions: for some, the market tramples on the right to dignity of vulnerable people, while for others it enables everyone to fulfill his or her individual potential. Ideology aside, the study of the double jeopardy sheds light on a "natural" mechanism of the market: without calculation or ill will, the market has *undesirable side effects.* It effectively penalizes people in poverty. Poverty penalties can be analyzed as a collateral result of designing offerings of goods and services for the median population or more affluent classes. This phenomenon can be attributed mainly to five factors. Three of these involve the double jeopardy observed when people in poverty buy the same goods or use the same services as the non-poor; the other two derive from the fact that they consume different products, or consume the same products in different ways.

3.1 Double jeopardy for the same product and the same usage

3.1.1 An unfavorable cost structure

The first factor is the cost structure, which is unfavorable to small-quantity purchases, since the unit cost of certain goods or services produced in small quantities is higher for the business. Poor households, which mainly buy things in small quantities, are therefore directly penalized. This is the case, for example, with financial services, where the fixed administration costs have a strong impact on the overall interest rate for loans of small amounts.

3.1.2 An unfavorable price structure

The second factor is an unfavorable *price* structure. In this case, the cost to the business of producing the product or service does not change, but the way it is priced negatively impacts the purchasing cost for the poor. Home insurance, for example, works out more expensive per room, or per euro insured, when small volumes are involved. Being generally smaller than average, the homes of poor households therefore incur a double jeopardy on their insurance of +20% per square meter.

The distinction between unfavorable cost structure and unfavorable price structure is an important one. In the first case, the business simply passes the additional cost on to poorer consumers. In the second, it could be accused, at the very least, of negligence towards the underprivileged. However, it is not always easy to make an *a priori* distinction between an unfavorable cost structure and an unfavorable price structure. Mobile telephony is a case in point: being unable to afford a subscription, with its high face value and long-term commitment, poor households tend to opt for prepaid cards, which cost more to put on the market (notably because of the distribution network involved). A minute of talk time is billed 15 to 50% higher for prepaid cards than for subscriptions. What proportion of this additional charge is due to the difference in cost to the operator? Only a detailed analysis of the sector, and indeed of each operator, could provide a precise answer to that question.

3.1.3 The law of supply and demand

Sometimes the law of supply and demand puts upward pressure on the prices of goods and services consumed in small quantities, the market being tighter when volumes are small. Of course, as economic theory tells us, the differences should even out in the long term. But the reality is sometimes different, and the housing market provides a perfect illustration:

small dwellings are traditionally more sought after, and this is reflected in the price. The purchasing price per square meter is on average 5% higher for poorer households. Two additional factors push the cost up even further: firstly, mortgage rates are less advantageous for poor borrowers, who have little to bargain with: the difference can be as much as 3 percentage points. Secondly, poor households tend to be passed over for the best-value offerings in the private rental market because of their higher risk profile: the corresponding additional cost is in the order of 10%.

3.2 Different products, or different ways of consuming

3.2.1 Lack of access to special offers

Poor households do not always have access to the best offers, because they do not have the necessary equipment, or because they have the wrong risk profile, or because the upfront price is dissuasive. For example, lack of access to the Internet discriminates against the poor in as much as online telephone operators offer prices 30% lower than conventional operators. Likewise, having efficient appliances, or an apartment with high-quality insulation, allows for substantial energy savings.

3.1.2 Lack of access to information

Finally, poorer consumers sometimes lack the necessary objectivity to handle or decipher complex and at times opaque information. This often leads them to make poor trade-offs, notably between purchase costs and running costs. Who can say with certainty that buying a major-brand tire saves money in the long run because it lasts longer and is fuel-efficient? And there is rarely anything in the wording of special offers about the longer-term impact of a purchase on the household budget.

4 Combating the double jeopardy: possible solutions

Compensatory mechanisms (financial assistance, social services, reduced tariffs) are in place that reduce budget constraints and therefore, indirectly, the double jeopardy that poverty generates. However, not all poor households benefit from these aids, and it might be worth considering the implementation of specific mechanisms to combat the double jeopardy. After all, the double jeopardy is a *market* effect, and could therefore be corrected, at least in part, by commercial sector players. Could we not devise a system of "positive discrimination", this time in favor of poor consumers?

Businesses could put in place innovative solutions to provide the first building-block of "economic justice", namely the abolition of the double jeopardy. In association with the "Social Business" chair at HEC, the action tank "Entreprises et Pauvreté" is a non-profit organization that campaigns for the implementation of innovative business solutions to combat poverty. It is currently working to define concrete operational strategies that businesses can leverage to correct the poverty penalty.

Where the cost structure is unfavorable, the action tank suggests restructuring the offering via a "low-cost" approach for small quantities. If it is the price structure that is unfavorable, the pricing policy can be adjusted so as to obtain the same level of profit margin, over and above the direct cost per unit of consumption, for all customers. In the energy sector, businesses could, for example, act on their billing systems (subscriptions). With regard to the law of supply and demand, it would be useful to participate in designing an alternative, complementary offering; businesses could apply this recommendation, for example, to the housing and rental market, in order to align the offering with the modes of consumption of poorer households.

There are two levers for addressing the problems of lack of equipment or of bad risk profiles. The first is to rethink the offering so as to facilitate access for financially fragile households, for example by creating commitment-free telephony packages. The second is to put in place a support system to help people meet the acceptance conditions, along the lines of the guarantee systems required to obtain credit. Where there is insufficient objectivity to handle complex information, the key lies in clearer, easily accessible information, and perhaps dedicated assistance where necessary. Businesses could, for example, set up a program to help poorer consumers choose a telephony package or a loan that truly corresponds to their needs and resources.

The concrete application of these solutions has already begun, with the launch of three experimental projects to combat poverty and its "double jeopardy", in coordination with Entreprises et Pauvreté.

- "*Optique Solidaire*" is an experiment conducted by leading spectacle lens manufacturer Essilor aimed at reducing the excess fee for progressive glasses for over-60s whose incomes disqualify them from France's universal health cover scheme (CMU). The pilot project is starting in Marseille. Between 100,000 and 120,000 people in France are potentially concerned;
- "*Telephonie Solidaire*", is an experimental project led by Emmaüs Défi with telephone operator SFR in Paris. It seeks to reduce the cost of telephony for people in financial difficulty through the use of low-cost prepaid cards and guidance in choosing the right package for their needs and resources;
- "*Programme Malin*" is an experiment implemented by baby food manufacturer Bledina and the Red Cross, designed to enable mothers living below the poverty line to benefit from special prices for infant formula.

These experiments work on the "Social Business" principle developed by 2006 Nobel Peace Prize winner Professor Muhammad Yunus (Yunus 2007). They are clearly still at the startup stage, and their innovative character means that success is far from guaranteed. However, they represent a remarkable step in the right direction. We call upon businesses everywhere to participate in initiatives such as these.

Conclusion

At a time when public policies are under severe budget constraints, and when labor costs cannot be increased for fear of harming business competitiveness, a new awareness of poverty penalties ("double", "triple" and "quadruple" penalties) will enable us to identify levers that are both legitimate, in terms of social justice, and efficient, in economic terms, for combating poverty in France.

The end objective is clear: to put in place mechanisms capable of reducing poverty penalties, in every economic sector, by addressing their characteristics and root causes.

Initiatives are already in place, mobilizing businesses, public institutions and non-profit organizations to implement innovative solutions. They prove that nothing is written in stone, even in these times of crisis, and that a precise, quantified analysis of underlying causes can lead to the definition of targeted strategies.

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