

# A Level Economics (EdExcel)

## Theme 4: A Global Perspective

### Course companion 7: Inequality and poverty



Name: \_\_\_\_\_

Tutor group: \_\_\_\_\_

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### Specification: 4.2.2 Inequality

- a) Distinction between wealth and income inequality
- b) Measurements of income inequality:
  - the Lorenz curve (diagrammatic analysis)
  - the Gini coefficient
- c) Causes of income and wealth inequality within countries and between countries
- d) Impact of economic change and development on inequality
- e) Significance of capitalism for inequality

### Note: Factors affecting inequality between countries

In course companion 2, Development Economics, we studied factors affecting inequality **between countries**, i.e. factors which might help / hinder developing countries in 'catching up' with developed countries in terms of income and economic development. In this course companion we shall focus on inequality **within countries**.

## Distinction between wealth and income inequality

**Income** is a **flow** of money measured over a **period of time** (£ per year)

**Wealth** is a **stock** of **assets** measured at a point in time.

### Income

Give examples of sources of income for households

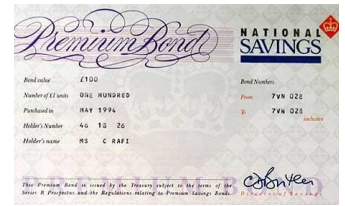


Discuss possible reasons why some UK households have a much higher income than others



## Wealth

Give examples of assets which a household may own:



Discuss possible reasons why some UK households are more wealthy (hold a greater stock of assets) than others



Explain the importance of the housing market in creating an unequal distribution of wealth

Why are the old usually wealthier than the young?



Why is it easy for wealthy individuals to increase their wealth?

Why do the poor find it difficult to increase their wealth?

Why might there be a positive correlation between income and wealth?

Evaluation: Discuss reasons why income and wealth may not be strongly correlated for all households

## **Is inequality unfair?**

### **Distinction between inequity and inequality**

The term equity means fairness. If the distribution of income is equitable it means it is fair or just. If the distribution of income is inequitable it means the distribution of income is unfair or unjust.

If someone says that the distribution of income in the UK is fair or unfair this is a normative or subjective statement. It is based on a value judgement and cannot be measured scientifically.

The term equal means the same. If the distribution of income is unequal it means that individuals have different levels of income.

If someone says the distribution of income in the UK is more equal than in the USA this is a positive or objective statement. It is a non-value judgement that can be tested using evidence.

### **Questions**

Why could it be argued that a certain degree of inequality is fair?

Why is a certain degree of inequality essential in a market economy?

What problems could arise if there are very high levels of inequality?

### **TED lecture from Richard Wilkinson: The effects of inequality**

1. Is there any relationship between gross national income per head and life expectancy:  
Between rich developed countries  
Within the UK
2. How much richer are the richest 20% of the population than the poorest 20% of the population:  
In the USA  
In the UK  
In Japan  
In Finland
3. What is the relationship between income inequality and social problems:  
Within rich countries  
Between rich countries
4. Is there any relationship between average well-being and national income in:  
Developed countries  
Developing countries
5. What is the relationship between income inequality and:  
Trust  
Mental illness  
Homicide rates  
Prisoners  
% dropping out of school  
Social mobility
6. Why does Sweden have a relatively equal society?
7. Why does Japan have a relatively equal society?
8. Does it matter how a society achieves greater equality?
9. Why does inequality lead to social problems?
10. What tasks do people find most stressful?
11. What is the link between inequality and:  
Poor health  
Violence
12. How can greater equality be achieved?

## Measurement of income inequality

### Using deciles to show the UK income distribution

In descriptive statistics, a **decile** is any of the 9 values that divide the sorted data into 10 equal parts, so that each part represents 1/10th of the sample or population.

- The 1st decile cuts off lowest 10% of data, i.e. the 10% of the population on lowest income.
- The 5th decile cuts off lowest 50% of data, i.e. 50% of the population have an income below this level, in other words the 5<sup>th</sup> decile is the **median income**.
- The 9th decile cuts off lowest 90% of data, i.e., 90% of the population have an income below this value, in other words only 10% have an income above this value.
- In the UK, **60% of median income** is defined as the '**poverty line**', those receiving below the poverty line suffer **relative poverty**.

### Comparison of UK household income distribution 2005/6 and 2008/9

#### INCOME DISTRIBUTION IN UK 2005/6

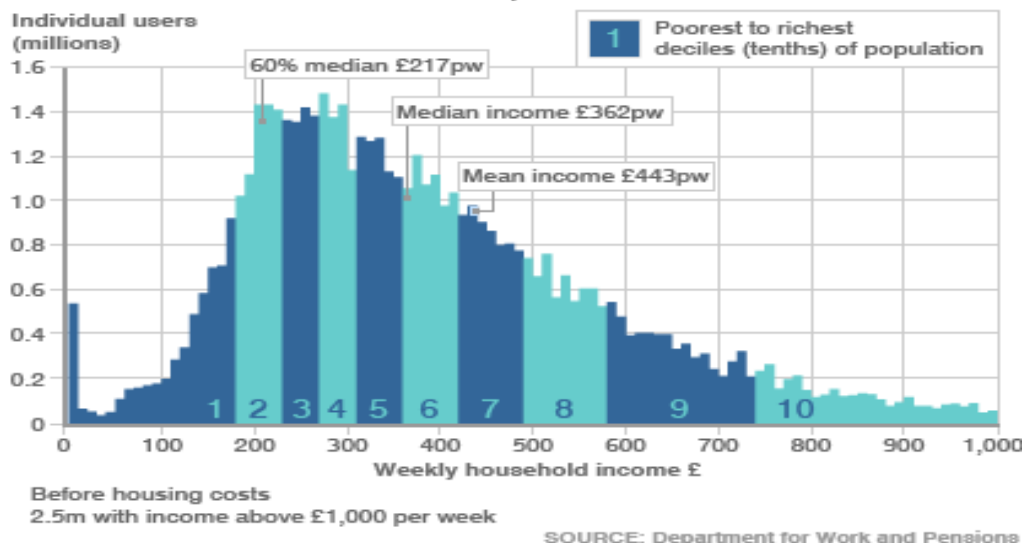
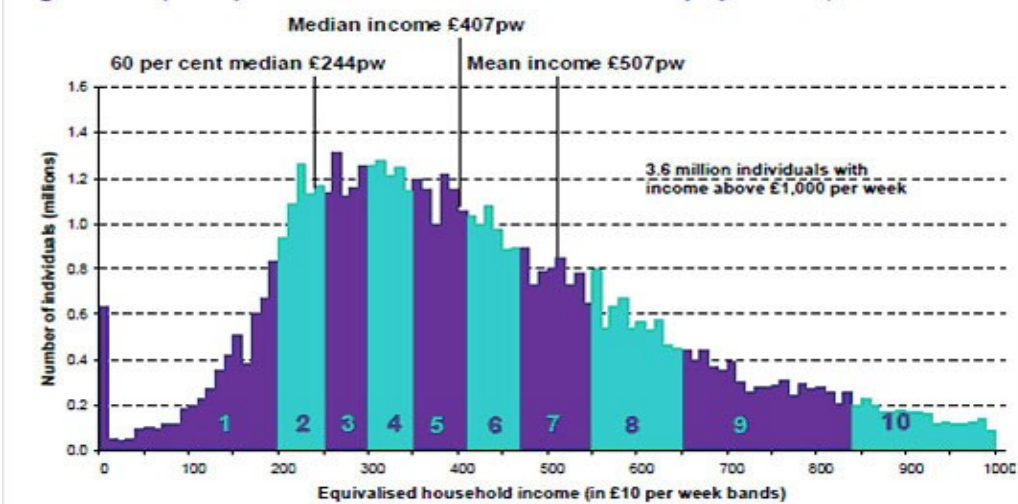


Figure 2.1 (BHC): Income distribution for the total population, 2008/09



The data shows the UK income distribution in 2005/6 and 2008/9 in £10 per week bands, for household (not individual) incomes from zero upwards. Incomes are measured after tax and before housing costs, and are adjusted for household size against a standard of a household with two adults and no children.

1. Calculate the percentage change in each of the following, between 2005/6 and 2008/9:
  - a. Mean income
  - b. Median income
  - c. 1<sup>st</sup> decile income
  - d. 9<sup>th</sup> decile income
2. Comment on changes in the distribution of income in the UK between 2005/6 and 2008/9.
3. Why is the mean income significantly higher than the median income?
4. Which measure of average do you think is the best measure of the income received by the “average person” in the UK?
5. What has happened to the official ‘poverty line’ in the UK between 2005/6 and 2008/9 and why?



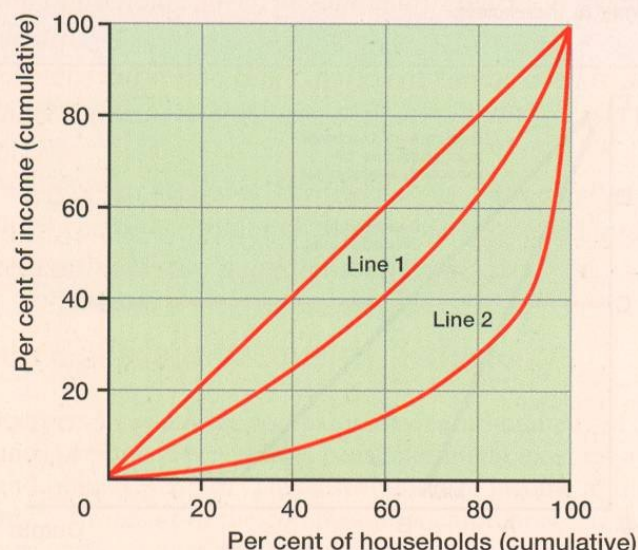
**Lorenz curve:** a graphical representation of the degree of income or wealth inequality in a society

Lorenz curves plot **cumulative share of income** (or **wealth**) against the **cumulative share of the population** with that income (or wealth).

- Straight 45° line shows position of total equality, e.g. bottom 20% of households receive 20% of total income.
- Line 1: relatively equal: bottom 20% receive 10% of income i.e. half the average income. Top 10% receive 20% of income, i.e. twice average income.
- Line 2: very unequal society: bottom 50% receive only 10% of income, i.e. half of all households receive one-fifth (10/50) of average income. Top 10% earn 60% of all income, i.e. earn 6 times average income.
- The further the Lorenz curve is from 45° line, the greater the income inequality in society.

**Figure 3 Lorenz curves**

A Lorenz curve shows the degree of inequality of income in a society. The farther from the 45° line is the curve, the greater the degree of inequality.



### Constructing Lorenz curves for the UK

	Quintile groups of households				
	Bottom fifth	Next fifth	Middle fifth	Next fifth	Top fifth
1979	10	14	18	23	35
2002-03	7	12	17	24	40
2012-13	7	12	16	23	41

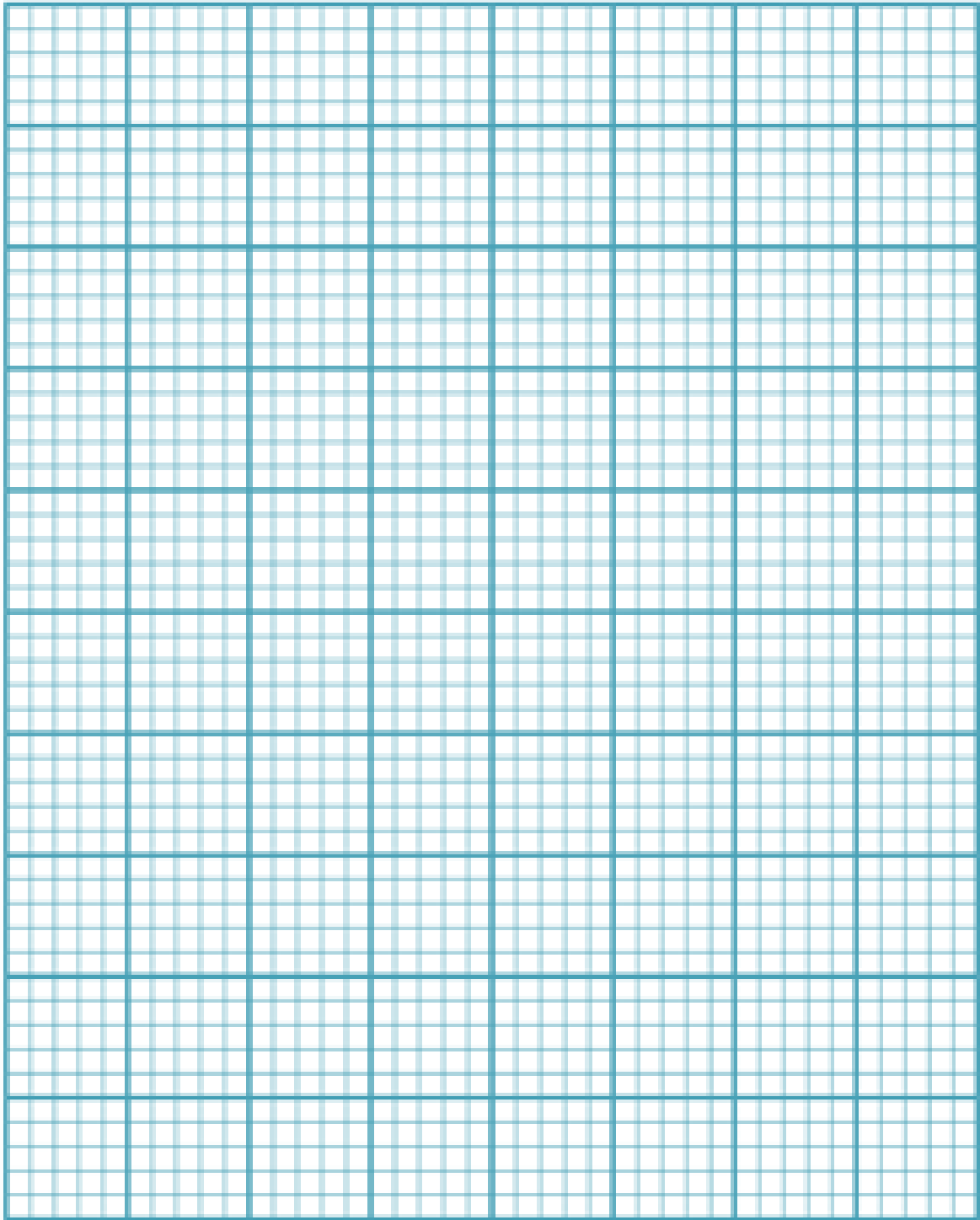
1. After direct taxes and benefits

2. Figures may not add up due to rounding.

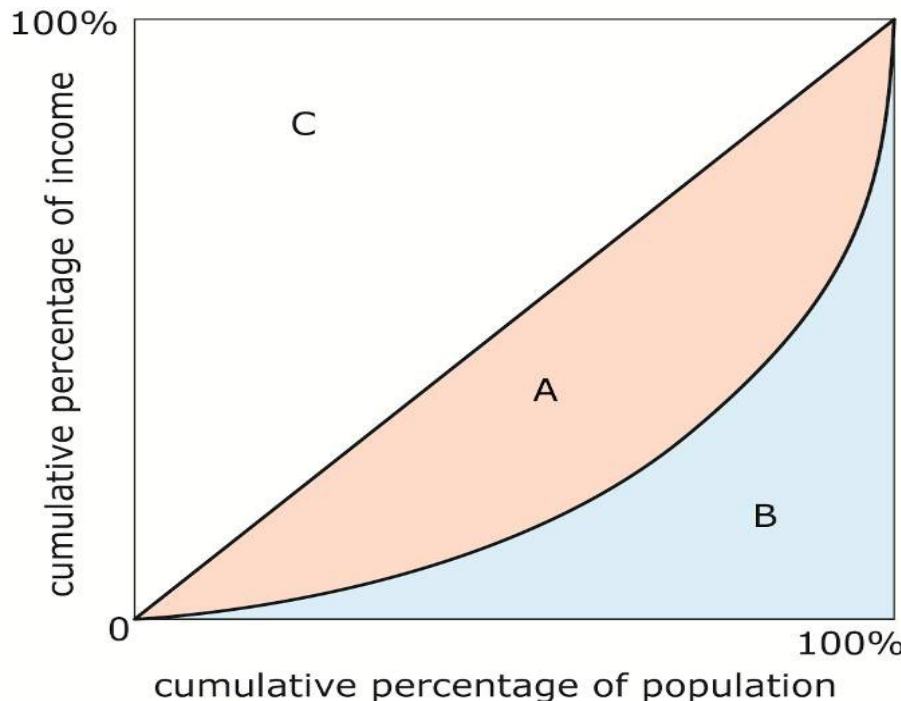
Source: adapted from [www.ons.gov.uk](http://www.ons.gov.uk), Social Trends, ONS

(a) Construct two Lorenz curves for 1979 and 2012-13 from the data above.  
(Remember to calculate the **cumulative** income for each quintile group)

(b) Has the distribution of income become more or less equal between 1979 and 2012-13?



**Gini coefficient:** a statistical measure of inequality of income. Its value ranges from 0, where there is perfect equality of income, to 1 where income is highly unequal with 1 person having all the income and everyone else having no income. The Gini index is the Gini coefficient times 100.



$$\text{Gini Coefficient} = \frac{\text{Area A}}{\text{Area A} + \text{Area B}}$$

**The closer the Gini Coefficient is to 1, the higher the degree of inequality**

#### Recent trends in

#### income inequality in the UK (IFS report 2017)

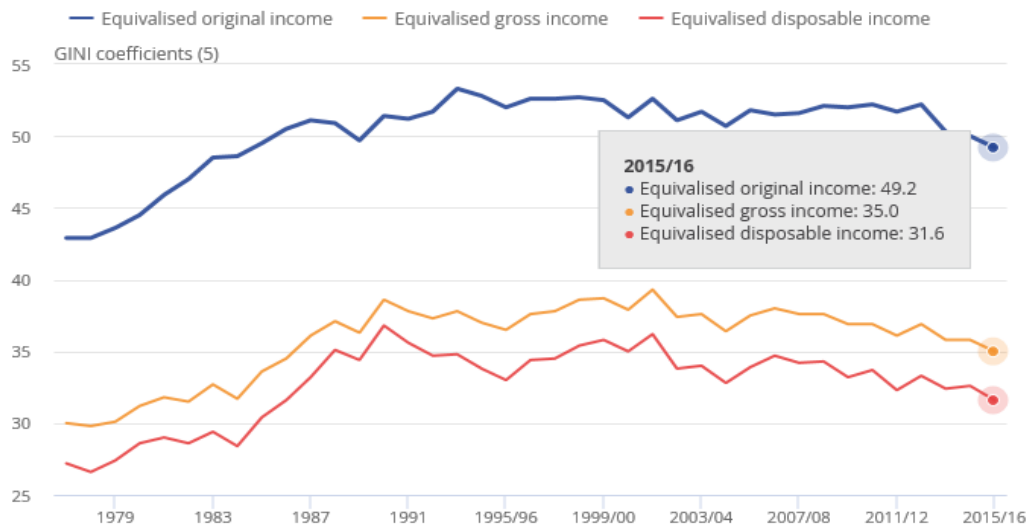
Income inequality in the UK changed little in 2015–16, meaning inequality remains lower than before the Great Recession. Since 2007–08, incomes have grown by 7.7% at the 10th percentile and 3.7% at the median (50<sup>th</sup> percentile), but have fallen by 0.6% at the 90<sup>th</sup> percentile. The reduction in income inequality largely occurred between 2007–08 and 2011–12, due to rising benefit income and falling real earnings. Since then, income growth has been relatively even across all levels of income, leaving inequality largely unchanged. Overall inequality is no higher than in 1990, though the top 1% continued to pull away until the Great Recession. According to the Gini coefficient, inequality is around the same level as it was 25 years ago, albeit considerably higher than in the 1960s and 1970s. This stability is the result of two offsetting factors: inequality across most of the population has fallen slightly since 1990, but the share of income going to the top 1% continued to rise. Trends in top incomes since the recession are less clear, but there are reasons to think they may have fallen back in recent years

#### Future trends for inequality

Projections produced by the Institute for Fiscal Studies (IFS), published in March 2017, suggest income inequality in the UK is likely to increase over the coming years to 2021/22 assuming no change in government policy. Looking first at income before housing costs (BHC), growth in inequality between 2015/16 and 2021/22 is expected to reverse the fall in inequality observed after the economic downturn in 2008. Firstly, cuts in the real value of working-age benefits are expected to reduce the real incomes of poorer households. Secondly, forecast growth in real earnings (particularly from 2019/20) is expected to mostly benefit higher-income households.

## The Gini coefficient for the UK

**Figure 5: Gini coefficients for the distribution of income at each stage of the tax-benefit system for all households, 1977 to financial year ending 2016**

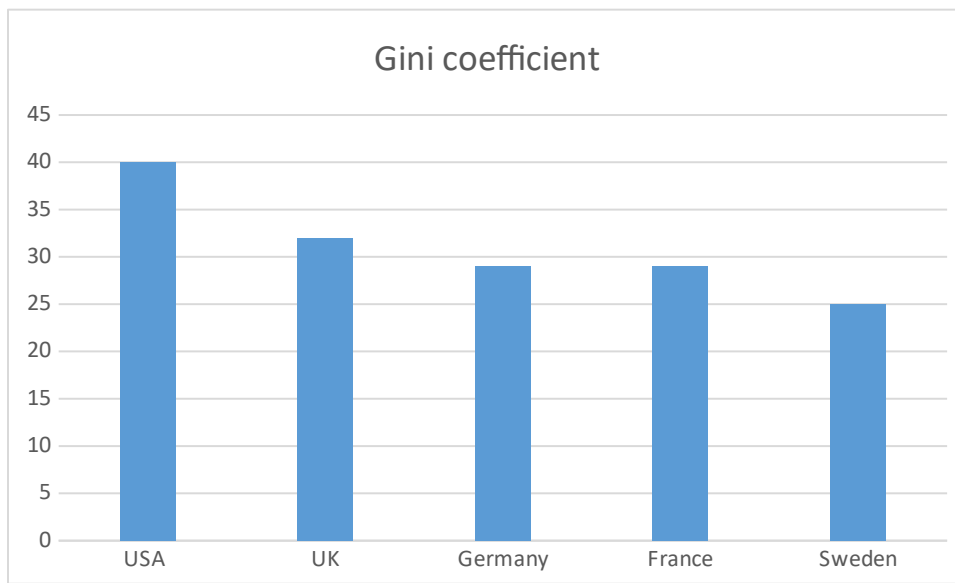


Source: Office for National Statistics

### Questions – Use the diagram above and the text on the previous page

1. Describe how the Gini Coefficient has changed over time
2. Explain why the Gini has fallen in recent years.
3. What factors may lead to the Gini Coefficient rising by 2022?

### Comparing the Gini coefficient in different countries

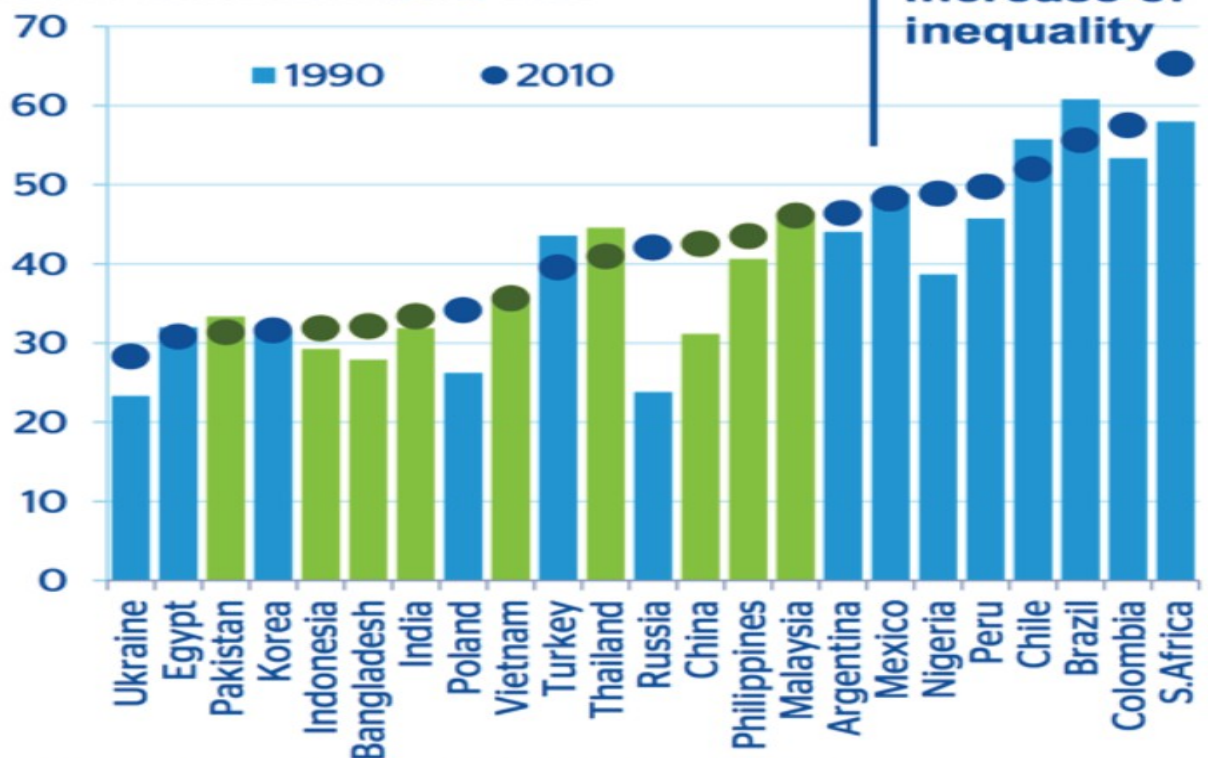


#### Questions

1. Which country has the most equal distribution of income?
2. Why is this?
3. Which country has the most unequal distribution of income?
4. Why is this?

## Gini index in the 90s and 00s\*

Source: BBVA Research, WB, OECD



\*As continuous data for the Gini index is not available, averages are computed around the starting (1986-1990) and ending point (2006-2010)

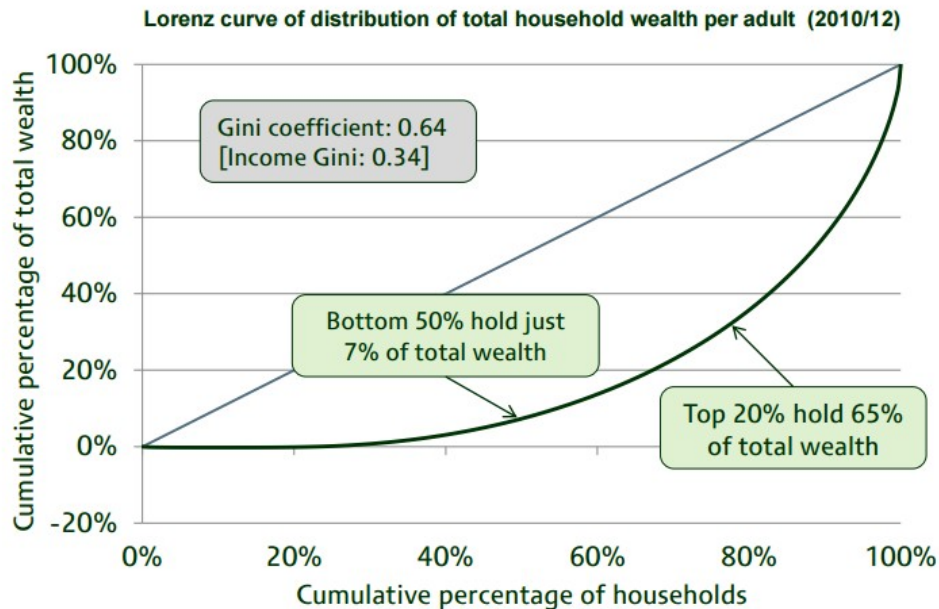
Source: tutor2u

1. Which three countries in the data set had the most equal societies in 1990? Suggest a possible reason for this.
2. Which three countries saw the biggest rise in inequality between 1990 and 2010? Suggest possible reasons.
3. Which three countries had the most unequal societies in 1990?
4. Which three countries had the most unequal societies in 2010?



## Measuring wealth in the UK

### Wealth is distributed very unequally...



Notes: Total wealth = net property wealth + net financial wealth + pension wealth  
Source: Crawford, Innes and O'Dea (Figure 3) – using Wealth and Assets Survey 2010/12

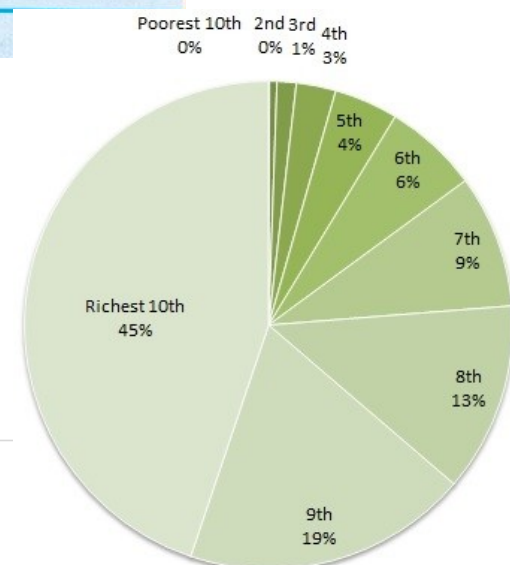
**Table 4 Distribution of wealth**

Percentage of marketable wealth owned by:	1911	1954	1971	1981	1991	2001	2003
Most wealthy 1%	69	43	31	21	17	22	21
Most wealthy 5%	-	-	52	40	35	42	40
Most wealthy 10%	92	79	65	54	47	54	53
Most wealthy 25%	-	-	86	77	71	72	72
Most wealthy 50%	-	-	97	94	92	94	93
Least wealthy 50%	-	-	3	6	8	6	7

Source: adapted from *Social Trends*, Office for National Statistics.

Pie chart shows: Household, wealth, 2012-2014 [ONS](https://www.equalitytrust.org.uk/scale-economic-inequality-uk),  
source: <https://www.equalitytrust.org.uk/scale-economic-inequality-uk>

Wealth in Great Britain is even more unequally divided than income.

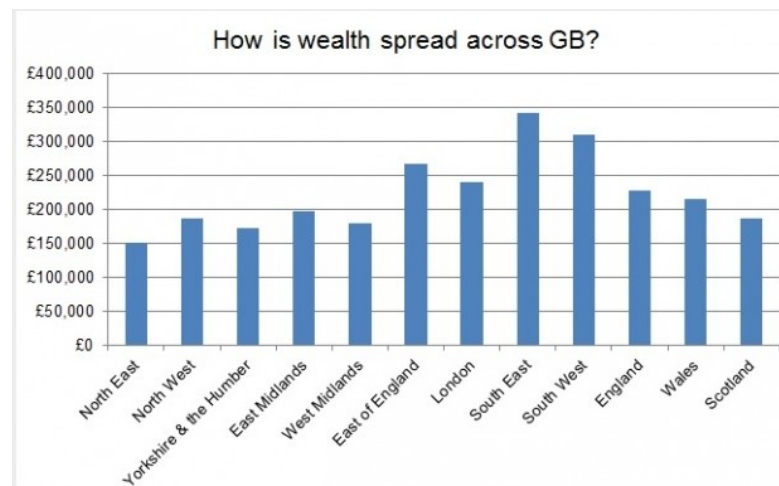


Wealth is also unevenly spread across Great Britain. An average household in the South East has almost twice (183%) the amount of wealth of an average household in Scotland<sup>7</sup>.

Compared to the other OECD countries the UK has a relatively equal distribution of wealth. The UK has a wealth GINI coefficient of 67.8% compared to an OECD average of 71.8%.

In July 2012 to June 2014:

- Aggregate total wealth of all private households in Great Britain was £11.1 trillion.
- The wealthiest 10% of households owned 45% of total aggregate household wealth.
- The least wealthy half of households owned 9% of total aggregate household wealth.
- Private pension wealth was the largest component of aggregate total wealth.
- Half of all households had total wealth of £225,100 or more.
- Households in the South East had the highest median wealth (£342,400).



Bar chart shows: Median household wealth for regions of the UK

1. Use the evidence to describe the distribution of wealth. How does the distribution of wealth compare to the distribution of income?
  
2. Why do you think wealth is unequally distributed?



## Causes of income and wealth inequality within countries

### Causes of income inequality in a developed country: UK

<http://www.tutor2u.net/blog/index.php/economics/comments/explaining-inequality-in-the-uk>

Watch the video clip in which CEP Director, John Van Reenen, explains recent changes in inequality in the UK.

Take notes on:

1. Reasons for increasing inequality, including:
  - a) Policy changes



- b) Globalisation

- c) Technology

- d) Decline of trade unions

2. Possible solutions

**Wealth inequality in a developed country - UK:**  
**Why younger people can't afford a house: money became too cheap**  
Dominic Frisby, Guardian, 12/4/16

House prices have risen by 10% in the last year, the Halifax announced last week. What that means is that the intergenerational wealth divide just rose by another 10% – and anyone born after 1985 is going to find it 10% harder to ever buy a home. There is perhaps no greater manifestation of the wealth gap in this country than who owns a house and who doesn't.



The standard solution is: “we need to build more”, but this is not a simple supply-and-demand issue. Between 1997 and 2007 the housing stock grew by 10%, but the population only grew by 5%. If house prices were a function of supply and demand, they should have fallen slightly over this period. They didn't. They rose by more than 300%.

The cause of house price rises is the unrestrained supply of something else: money. Mortgage lending over the same period went up by 370%, thinktank Positive Money's research shows. It was newly created debt that pushed up prices in a decade of extraordinarily loose lending, which gave birth to a national obsession. Houses were no longer places to live, but financial assets. Property owners became immensely wealthy without actually doing anything. And this great, unearned wealth saw the rise of a new rentier class: the buy-to-let landlord.

When you have runaway inflation such as this, the Bank of England has a responsibility to quash it, usually by putting up interest rates. But – and here is the great sleight of hand – the Bank has seen fit not to include house prices in its measures of inflation. So, throughout the 90s and 00s, they could then “prove” inflation was low or moderate and interest rates meandered lower. Meanwhile, more and more mortgages were issued, and so more and more money was created, and it pushed up prices. The government didn't mind. Homeowners vote and homeowners were happy – they were getting rich. The fraud persists today. The Bank of England says inflation is 0.3%. Really? With house prices up by 10% last year?

When you make money this cheap, you create bubbles. Combining a money system that requires ever-expanding debt to function with a national policy of ignoring where that money goes is asking for trouble. And trouble is what we have. 2008 gave us the crisis we needed to address the problems inherent in our money system – how is money created? Who gains and who suffers by this system? – but our leaders chose not to. Instead interest rates were slashed, so mortgages and other debts became incredibly cheap to service (great if you already had a mortgage). We got the great obfuscation that is quantitative easing; £375bn of newly printed money flowed into the financial sector and on into the London property in which it mostly lives. Asset-owners were bailed out and the next generation was made to pay the price.

Then we got help-to-buy, which is just another way to get new money into the market. And where lending has tightened in the UK, it hasn't abroad, and so we have vast sums of money created overseas now entering our housing market and further driving up prices. Today in London everywhere you look there is a crane. There is no shortage of newbuild, yet we still have a crisis, because prices are so high. People associate debt with the poor. But large, cheap debt is, in fact, a luxury of large corporations, of the rich and of governments. It has created this unholy alliance between the three and with it an international culture of keeping debt costs low and asset prices high, whatever the consequences.



Planning laws are the second part of the problem. All this money is pouring into a market that is restricted in how it can expand. Just 1.1% of rural and urban land in England and Wales has domestic property on it, according to the 2011 National Ecosystem Assessment. 1.1%! Another 1% has commercial property and 2% is roads. The rest is not built on. You could almost double the housing stock of England and Wales, using little more than 1% of available land. But planning laws prevent that. An acre of rural land worth £10,000 becomes an acre of land worth as much as £1m once it has planning permission. That is an expensive and needless cost of government. The 1947 planning act was founded on the laudable aim "that all the land of the country is used in the best interests of the whole people". The opposite has happened. The act reinforced the monopoly of the landowner and we now have a situation where more than 70% of UK land is owned by just 6,000 or so landowners (the Crown, large institutions and a few rich families). The act has led to huge concentrations of capital and people in areas that are already built up – especially London – bringing vast unearned wealth to those who own at the expense of those who don't. It has actually caused the wealth gap to grow.

Explain how the housing market has contributed to wealth inequality in the UK.

What are the causes of high house prices?

Briefly outline three policies to reduce inequality in the housing market

## Country example of a developed country - USA:

### Causes of inequality in the USA

<http://www.tutor2u.net/economics/blog/joseph-stiglitz-on-inequality-june-2015>

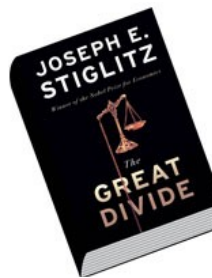
Listen to Professor Stiglitz and take notes on his arguments including:

1. How bad economic theory has contributed to inequality

2. Changes in median income



3. Land and real estate (including monopoly profits and deregulation of banks)



4. Wages, productivity and the 'American Dream'.

5. Action required to improve equality.

## Country example of a developed country: USA

### Enriching the rich in the US - but what about the rest?



Linda Yueh Chief business correspondent, BBC, 13 February 2015

Has the land of opportunity created a society of haves and have-nots? Is the US economy now just enriching the rich? Inequality has been noticeable since the recession, but the income gap has been growing for decades. During the economic boom of the 1950s in the United States, the top 1% gained a bit more than the rest - grabbing some 5% of the incomes gained during expansions. But now the top 1% accounts for 95% of the income gains after the great recession of 2008, leaving the bottom 99% with just 5% of the income gains. It's usually low interest rates and cheap money that drive a recovery, and that usually boosts stocks. US markets have hit numerous record highs since the 2008 crisis, and those gains now predominantly go to the top 10% - because they own 91% of all stocks. It used to be more equitable in that half of US households owned stocks. Those are the immediate reasons why inequality has risen in the US, but inequality has been on the rise for far longer.

Inequality fell after the first Gilded Age during the 1920s, especially during the 1950s and 1960s when per capita GDP grew strongly during what's called the Golden Age of the US economy. But starting in the 1970s, the income gap ceased narrowing and then started rising sharply after 1980 - reaching the present where it is more unequal than ever before.

In Talking Business, we discussed the longer term causes of inequality. Panellists including former US Labor Secretary Robert Reich argued that there are several forces driving up inequality.

Firstly, globalisation has driven down median wages and those who gain from trade - the skilled workers and owners of capital - have earned more while the middle- and lower-skilled lost out, which has widened the gap.

It is also due to what economists call skill-biased technical change. As the US economy becomes more technologically driven, it is again skilled workers who benefit. The two are related of course, as the US can specialise in the higher-skilled technical fields since it can import what it no longer produces from overseas.

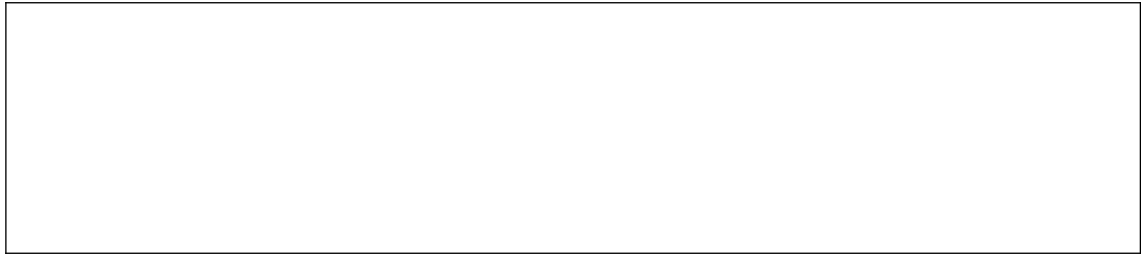
Robert Reich also says that decreased unionisation weakened workers' bargaining power over wages, while Dean Baker, co-founder of the Center for Economic and Policy Research, points to monetary policy favouring low interest rates over targeting employment.



As Jason Furman, the chairman of President Obama's Council of Economic Advisers, points out, the rise in inequality in the US is the greatest amongst advanced economies.

1. What percentage of income gains after 2008 have gone to the top 1%?
2. Describe how inequality has changed in the USA since the 1920's.
3. With reference to the text and your own economic knowledge, discuss how the following factors may have increased inequality in the USA:

Globalisation
Technological change
Decreased unionisation
Monetary policy: low interest rates and quantitative easing

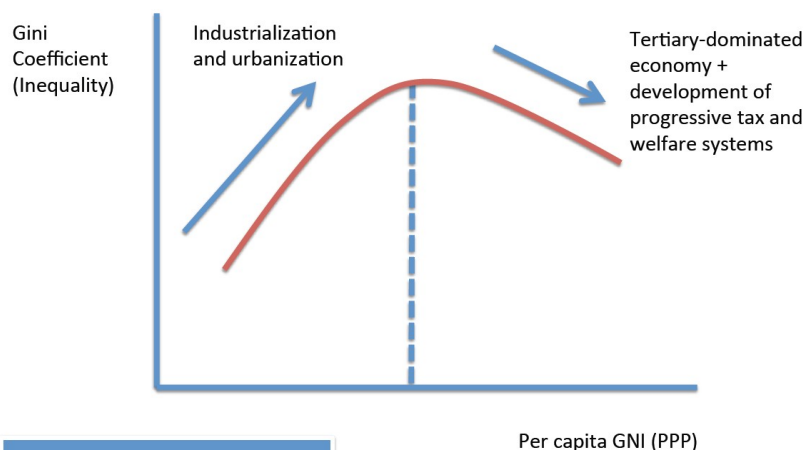


## Impact of economic change and development on inequality

Kuznets argued that as a country develops and its GDP grows from a subsistence economy, inequality initially increases and then decreases:

- Industrialisation results in increased inequality as workers move from the lower productivity and lower paid agricultural sector into the higher productivity manufacturing sector.
- However, at some point, inequality starts to decrease. This may be because governments have more resources to redistribute income through the tax and benefit system.

### Is Rising Inequality Inevitable with Development?

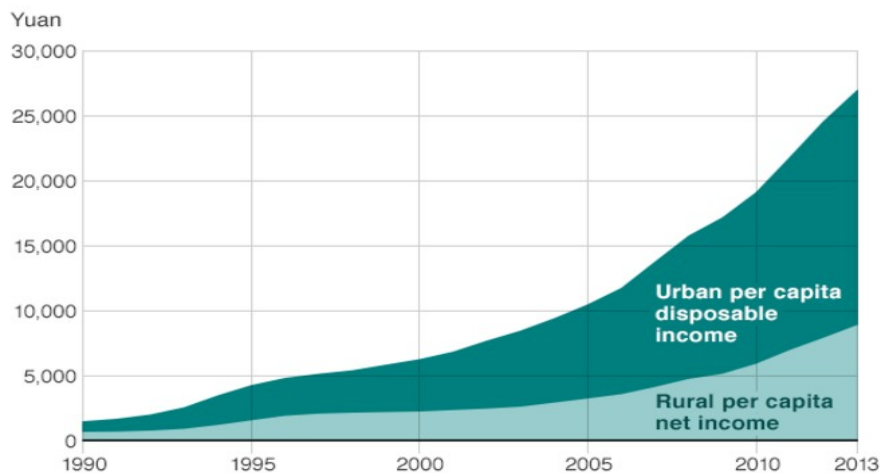


### The Kuznets Curve

Country example of developing country: China



### Rural - urban divide in spending power



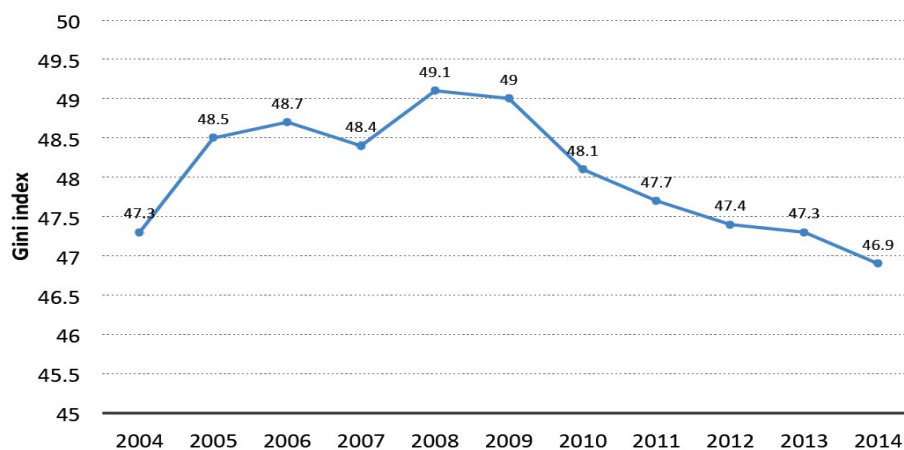
Source: National Bureau of Statistics of China, 2014 yearbook

BBC

Source: <http://www.bbc.co.uk/news/world-asia-china-33802777>

Inequality of income distribution in China based on the Gini index 2004-2014

### Gini index: inequality of income distribution in China from 2004 to 2014



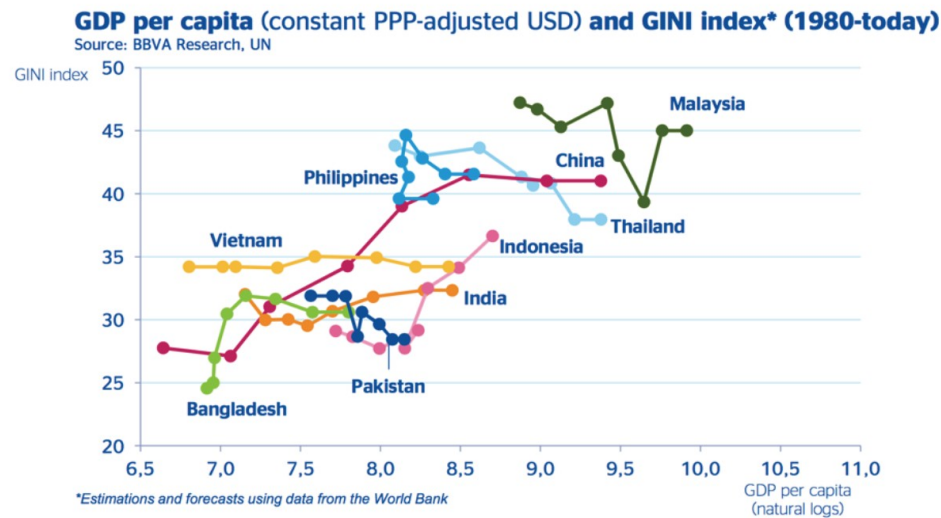
Source:

tutor2u

1. Comment on changes in inequality in China from 2004 to 2014.
2. Does the data support Kuznets theory?
3. Evaluate the limitations of the data provided.



## Evidence on Inequality for Developing Countries



To what extent does the data above support the Kuznets curve theory?

### The significance of capitalism for inequality

How much inequality is too much?

BBC, 8 January 2016

The richest 10% of Americans earn half of all of income.

In Britain, the top 10% hold 40% of all the income.

Inequality isn't just an issue for rich countries: a billion people have been lifted out of poverty since 1990, but inequality has also been rising in many countries too.

Four experts talk to the BBC World Service Inquiry programme about the effect inequality has on growth and prosperity.



Deirdre McCloskey: Capitalism is not the enemy

*Deirdre McCloskey is Distinguished Professor of Economics, History, English, and Communication at the University of Illinois at Chicago. The daughter of a Harvard Professor, her brother became a university cleaner.*

"You can't force people to take advantages that are placed in front of their nose, and that's my brother's case. No amount of income redistribution or socialist schemes to give my brother more opportunities would have made any difference at all to his life. If people strive, some of them succeed and get rich, at least momentarily until other people strive and compete with them. This striving turns out to be good for all of us. The percentage of people in the world living on \$2 (£1.30) a day - an appalling level of income - has halved in the last 30 years. That's not by foreign aid or redistribution. It's by letting the economy function



in a more innovative way. The wrong way to cure inequality is to attack the people who are taller, or have better parents, or live in richer countries. The way to do it is to uplift the poor. I approve of being taxed to help the very poor. But I don't want to kill the goose that laid the golden eggs. Capitalism is not the problem, it's the solution. The growth in the last couple of centuries has been astounding. It's a factor of 30 - about 3,000% per head for the average English or American person. Explosive, unprecedented growth. Meanwhile, inequality has gone up and down a little bit. If you were to make a rule that the chief executive could only earn 50 times the shop floor employee, that would not reduce inequality substantially. I'm very relaxed about [inequality] as long as it's not force or fraud that caused it.

**Jared Bernstein: Inequality impedes growth**

*Jared Bernstein is a senior fellow at the Center on Budget and Policy Priorities in Washington DC, and a former economic advisor to President Obama.*

I was a member of the President's economics team during the worst recession we've had since the Great Depression. The responsibility to try to turn that around was huge. This wedge of inequality between growth and the income of working families undermines the basic incentive that hard work will be rewarded. I call it the shampoo cycle - bubble, bust, repeat. And because middle and low income families lack the income growth they used to see, they borrow to make the difference. That creates large leverage bubbles which explode and hurt growth. Once wage inequality gets too high, and you have lots of low income people stuck in tough neighbourhoods that are segregated by income and race, and they have fewer libraries and a more difficult learning environment, you begin to see this connection between high levels of inequality and barriers to opportunity.

You don't necessarily see that in today's economy because that's a cumulative process, but it's very possible that we'll see that in economies 20 years from now when these children come into the job market. If you go back to the period where productivity and incomes for middle class families were growing together - in the US that would be back to the mid 1970s - you'll see that the top 1% held about 10% of all income. Now it's 20 times that. That's too much. I'm not saying we necessarily have to get back to the late 1970s level, but I do think that a good metric here would be that the income of middle income families would grow closer to the rate of productivity growth, and that's something that we haven't seen for a while.

**Jonathan Ostry: Opportunity more important than inequality**

*Jonathan Ostry is deputy director of the Research Department of the International Monetary Fund.*

We don't have a threshold level for how much inequality is too much. We don't have a magic number. Sometimes a rise in inequality is perfectly compatible with healthy growth and prosperity, and in other cases the rise has gone way too far. When China opened up, it not only took off in terms of economic growth, but there was a marked and quite significant increase in income inequality. I'd be prepared to venture that was a good increase in inequality. Sometimes you need to have a little bit more inequality in order to get growth going as part of deregulating of your economy.

Bolsa Familia programme to tackle poverty was a centrepiece of former Brazilian President Lula's social policy. Think of the very high levels of inequality that prevailed in Brazil when President Lula came to office, and the steps he took with the Bolsa Familia conditional cash transfer programmes. His policies were successful

without jeopardising economic growth. I would want to be sure that in a country with a lot of inequality those at the bottom still had opportunities to be well-educated, to have adequate nutrition, and were not shut out from credit and banks. Likewise if there was a fair degree of equality, but nevertheless those at the bottom didn't have adequate opportunities, I'd be concerned. So for me it would be more a question of whether there were adequate opportunities for the less well-off in society. Provided that was the case I wouldn't be overly concerned that a given level of inequality was causing great harm.

[However] it turns out that income equality is an important factor in separating countries that have been successful at sustaining growth for long periods, versus those that have enjoyed spurts of growth which have fizzled out rather quickly. Too much inequality can undercut the ability to sustain growth. In more equal societies, those that are more socially cohesive, governments are able to take measures that have buy-in from the population at large. Therefore they can right their economies more quickly. In more unequal, less socially cohesive societies, people don't buy the notion that if the economic ship is righted, everyone will benefit. They're more likely to oppose the painful short-term measures that governments need to take to right the economic ship. And so righting that ship becomes much more difficult in less equal societies.

### **Branko Milanovic: Beware rising inequality within countries**

*Professor Branko Milanovic has spent his career studying inequality, and is now a visiting professor at the City University of New York.*

We need inequality. Perfect equality, everybody having the same income, doesn't exist anywhere, nor has it. Obviously some countries - maybe China during the cultural revolution - came relatively close, but some inequality has always existed. Without inequality you lack incentives to do practically anything - to work, to invent new things or to invest. Nobody is going to do things for nothing and we know that monetary rewards are really crucial, so this is the good part of inequality. We should not forget that inequality is indispensable for the development of a society.

Globalisation has been very good for the middle classes in the emerging markets - China in particular, parts of India, Thailand, Indonesia. They are still not level in terms of income with the middle class in the rich world, but it's improving. On the other hand, we have essentially a stagnation of middle class incomes in rich countries, a very interesting and a potentially politically destabilising development.

The economic disparity between the wealthiest and poorest in China is stark. If the gaps keep on increasing as they've increased in the last 20 years, you would end up with two types of societies within a single country. If there is no sufficient middle

class and if the poor really are very far from the rich, then you really cannot speak of a single society. We could end up with a kind of a global plutocracy, this global one per cent or even half a per cent that are very similar among themselves, but really belong to different nations.

We might have a situation that most of global inequality is due to inequalities within

nations which was more or less the situation 200 years ago. So we may be really going back to the situation that existed before the industrial revolution.

Pod cast of radio programme on BBC World Service related to this article:

<http://www.bbc.co.uk/programmes/p03d52kp>



Is inequality an essential part of capitalism, required for economic growth?  
 Read the articles above and fill in the table below:

Analyse ways in which inequality may be essential/inevitable in capitalism, and required for economic growth	Evaluation: To what extent is it inevitable/ desirable? Disadvantages/limitations? Is inequality a threat to capitalism/growth?

## Absolute and relative poverty

### Specification

#### 4.2.1 Absolute and relative poverty

- Distinction between absolute poverty and relative poverty
- Measures of absolute poverty and relative poverty
- Causes of changes in absolute poverty and relative poverty

### Distinction between absolute poverty and relative poverty

**Absolute poverty:** absolute poverty exists when individuals do not have the resources to be able to consume sufficient necessities to survive.

- United Nations has defined absolute poverty as:
- A condition characterised by severe deprivation of basic human needs, including food, safe drinking water, sanitation facilities, health, shelter, education and information. It depends not only on income but also on access to services.
- The World Bank recently defined the new absolute poverty line as the percentage of the population of a country living on less than \$1.90 a day (PPP) at constant 2011 prices.
- In 2015, just over 700 million lived in absolute (extreme) poverty according to World Bank figures.

**Relative poverty:** poverty which is defined relative to existing living standards for the average individual.

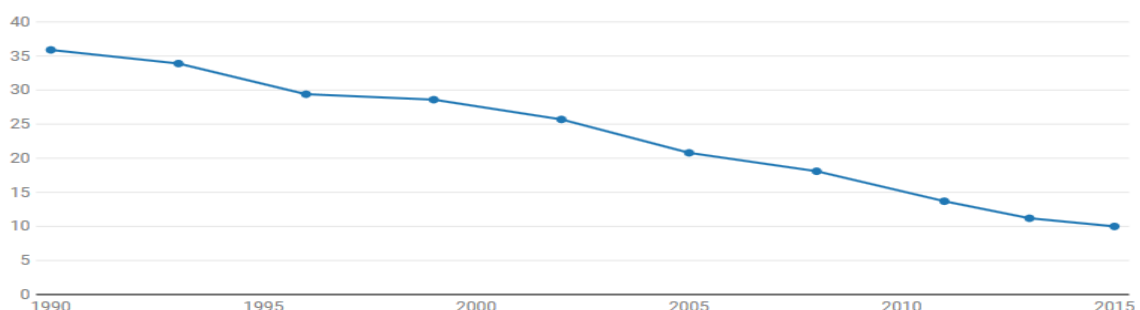
Relative poverty – this is measured in comparison with other people in the country and will vary between countries. People are considered to be in relative poverty if they are living below a certain income threshold in a particular country. For example, in the UK and the EU, people falling below 60% of median income are said to be ‘at-risk-of poverty’ and are said to be relatively poor.

### Absolute poverty in the developing world

1. With reference to the data, describe the changes in absolute poverty since 1990

#### Global poverty rate, 1990-2015

Share of people who live below \$1.90 a day (%), 2011 PPP

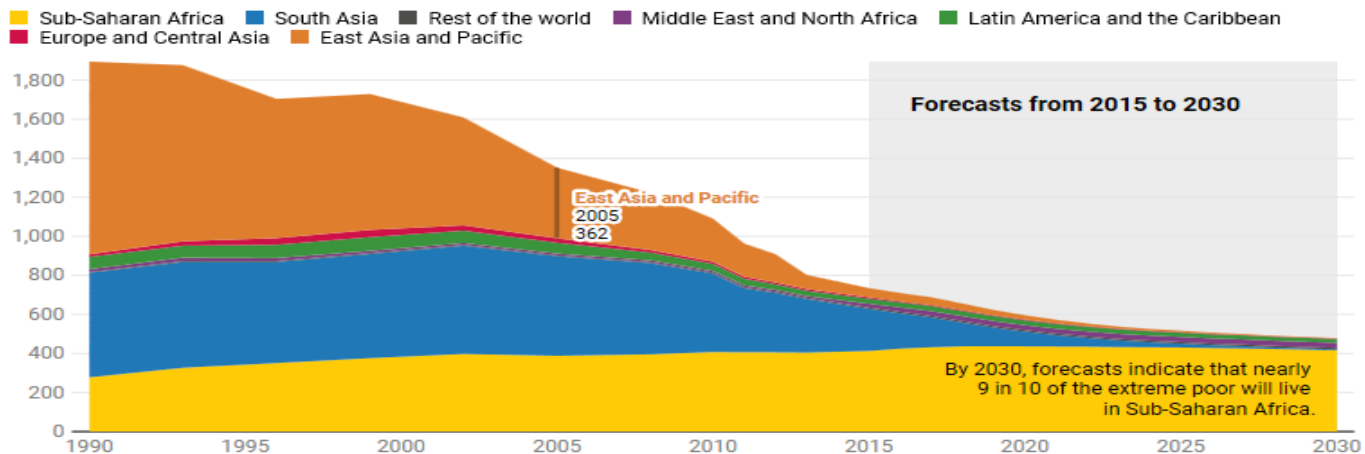


Note: PPP = Purchasing Power Parity

Source: Most recent estimates, based on 2015 data using PovcalNet

## Share of global poverty in different regions of the world

People in extreme poverty (millions)



Source: World Bank PovcalNet and Poverty & Equity Data Portal

2. With reference to the data, comment on changes in the share of global poverty in different parts of the world since 1990.

3. What share of global poverty is forecast to be in Sub-Saharan Africa in 2015?

Why has poverty fallen faster in China and India than in Sub-Saharan Africa?

<https://www.youtube.com/watch?v=HEB4tvIRTXo>

**Country example of a developing country: Nigeria** Nigeria is Africa's second largest economy and has the highest production of oil and gas in Africa. More than 62% of Nigeria's population are under 25 and its growing middle class makes up 23% of the population.

The 2014 re-based GDP figures that showed an increase in the size of the Nigerian economy have drawn attention to official poverty statistics and concern about their accuracy. Data from the last comprehensive household survey (NHLSS) in 2009/2010 indicated that the official poverty rate has not sufficiently fallen and stands at 46% of the population (adult equivalent approach), or 62% in per capita terms. The majority of the poor (66%) are to be found in the north. Poverty is also more prevalent in rural areas. Robust growth over the past decade has been accompanied by increasing inequality and vulnerability.

Two major patterns manifest themselves in the Nigerian economic space: inequalities between urban and rural areas and between different geopolitical zones. The urban centres tend to have a disproportionate share of public facilities to the detriment of rural areas. The over concentration of infrastructure induces rural-urban drift. Rural residents leave the relatively neglected rural sector for urban centres in search of better living standards. Available statistics prove the existence of the rural-urban disparity in the level of development. For example, the baseline survey on National Water Supply and Sanitation indicated that 75% of residents in urban areas have access to safe water compared to 45% in the countryside. According to the 2010 Nigerian Education data survey, it was found that 60% of children in urban areas attend secondary schools against only 36% in rural areas.

Conflict is both a result and a driver of regional inequalities. The lack of economic opportunities and poorly performing education and health-care systems lead to widespread dissatisfaction, which is often a precursor to conflict. Likewise, the lack of investment in conflict-affected areas serves to perpetuate regional inequalities. The Niger Delta is arguably the richest but one of the least-developed regions in the country, suffering from widespread poverty, insecurity and severe environmental degradation. There are efforts currently underway to develop a regional development plan in the North-East region as part of a developmental security response to the insurgency of Boko Haram's terrorist activities. The wave of terror and its accompanying political instability has held back the region's economy.

Using the text, and your knowledge from earlier discussions of Nigeria, explain three factors that have contributed to the high level of absolute poverty in Nigeria. Explain how each factor might lead to poverty.



## Country example of a developing country: Absolute poverty in India

Malnutrition is seen as a key indicator of absolute poverty. Watch video clip 'Urgent call for action: Malnutrition in India' and take notes on reasons for malnutrition, problems & possible solutions

<http://www.tutor2u.net/blog/index.php/economics/comments/unit-4-macro-malnutrition-and-economics-development>



## Country example: India (continued)

Watch video clip 'India urged to offer universal healthcare' (Al Jazeera, July 2012) and take notes on issues with health care provision

<http://www.tutor2u.net/blog/index.php/economics/comments/unit-4-macro-limited-healthcare-access-constrains-india>

## Poverty video – Hans Rosling

1. What is the United Nations goal 1.1?
2. Explain the difference between absolute and relative poverty
3. Describe the standard of living for the family living in absolute poverty in Malawi
4. What % of the world population are living in absolute poverty in:  
1800                                  1970  
1850                                  1990  
1900                                  2015  
1950
5. What was the UN's goal for absolute poverty in 1990? Was this achieved?
6. What happened to the world population between 1800 and 2000?
7. What happened to the total number of people living in absolute poverty between 1800 and 1970?
8. What happened to the total number of people living in absolute poverty between 1970 and 2015?
9. Describe the global distribution of poverty in:  
1800  
1900  
1950  
1990
10. What is the average number of children per woman in:  
Families in extreme poverty  
Families who are not living in extreme poverty
11. Why is average family size important for ending extreme poverty?
12. Should we encourage families to have fewer children to end poverty?

## **Country example of developed country: Absolute and relative poverty in the UK**

The key UK government measures take **60 per cent of median income** as the **poverty line**.

### **Who are the poor?**

The groups most likely to include people living in poverty are:

- Those without employment or those in part-time employment
- Those on low pay
- Those with disabilities or those who have long-term illness
- Young people not in employment, education or training
- People experiencing homelessness
- Children
- Pensioners
- Women
- People in lower social classes
- People from ethnic minority backgrounds

Source: <http://www.bbc.co.uk/education/guides/zspttfr/revision>

- In 2013, 7.8% of the UK population were considered to be in persistent income poverty, equivalent to around 4.6 million people. Persistent poverty is defined as being in relative income poverty both in the current year and at least two out of the three preceding years.
- In 2013, the UK persistent poverty rate was less than half the overall relative poverty rate of 15.9%. By comparison, in many other EU countries, the persistently poor make up a higher proportion of those in poverty. Since 2008 (the first year for which comparable EU longitudinal data are available), the UK has consistently had a persistent poverty rate lower than the EU average.
- Almost a third (33%) of the UK population experienced poverty in at least one year between 2010 and 2013, equivalent to approximately 19.3 million people. In contrast, across the EU as a whole, a quarter (25%) of people were in poverty at least once during that period.
- Almost 40% of those aged 65 years and over in the UK experienced poverty at least once between 2010 and 2013, compared with around 30% of those under 65.
- In the UK, 60% of those living in single parent households and almost half (46%) of those in single adult households experienced poverty at least once in the four years between 2010 and 2013 compared with less than a third of those living in households with two or more adults.

Source: <http://webarchive.nationalarchives.gov.uk/20160105160709/http://www.ons.gov.uk/ons/rel/household-income/persistent-poverty-in-the-uk-and-eu/2008-2013/index.html>

1. What percentage of the UK population lived in relative poverty in 2013?
2. How do levels of relative poverty in the UK compare with other EU countries?
3. Explain 3 reasons why a household might suffer relative poverty in the UK.

<https://www.trusselltrust.org/news-and-blog/latest-stats/end-year-stats/>

Watch the video in the link and answer the questions:

1. How many people in the UK received 3 days emergency food from the Trussell Trust in 2019?
2. What were the main reasons for people needing emergency food?
3. Explain why food banks in the UK are helping to prevent absolute poverty.

