UNIT 3 INEQUALITY

Structure

3.1 INTRODUCTION

You have heard about inequality often, and observed it in daily life. A simple example of inequality is the income difference between an agricultural landlord and labourer, the income differences between a peon and a Class-I officer. Inequalities exist in every society. The economic structure and an individual's abilities to earn are a few among many factors responsible for inequality. In this unit, you will read about inequality: its cause, effect and remedies.

After going through this unit you should be able to

- explain economic inequality
- describe various causes and effects of economic inequality
- suggest remedies for economic inequality
- narrate the severity of income inequality in the Indian perspective

3.2 ECONOMIC INEQUALITY : MEANING AND MEASURES

Global income inequality is probably greater than it has ever been in human history. The economic inequality, largely, viewed as comprising all forms of disparities in the distribution of economic assets and income. There is a debate about whether the income inequality is getting worse or getting better. Currently, the richest 1 per cent of people in the world receives as much as the bottom 57 per cent. The ratio between the average income of the top 5 per cent in the world to the bottom 5 per cent increased from 78:1 in 1988 to 114:1 in 1993 (Milanovic 1999). One pole represents the 2.4 billion people whose mean income is less than $1000 year and includes people living in India, Indonesia and rural China. With 42 per cent of the world's population, this group received just 9 per cent of the world Purchasing Power Parity (PPP) income. The other pole is the group of 500 million people whose income exceeds $11,500. This group includes the US, Japan, Germany, France and the

UK. Combined, they account for 13 per cent of the world's population, yet garner 45 per cent of the world PPP income. The gap between these two poles is so large that it comprises the major component of the world's income inequality. The richest 25 per cent of the world's population receives 75 per cent of the world's income, even when adjusting for purchasing power parity. The poorest 75 per cent of the population share just 25 per cent. This occurs because a large proportion of the world's population lives in the poorest countries, and within the poorest regions of those countries, particularly in the rural areas of China, rural and urban India and Africa.

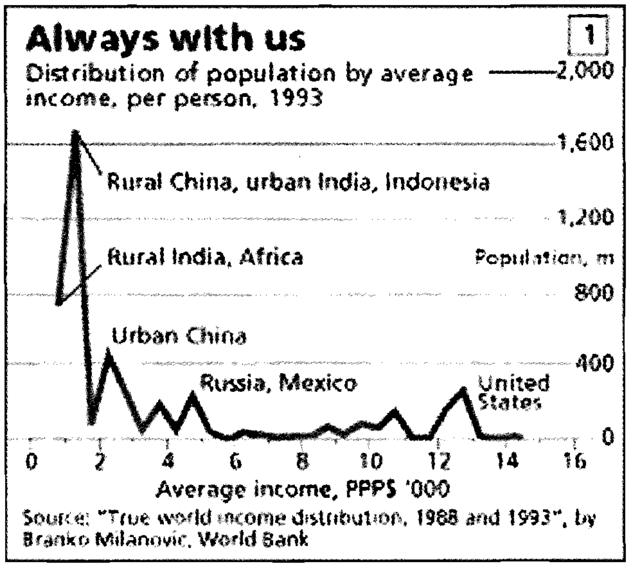

Figure : 3.1: Global Income Inequality

Figure 3.1 indicates the distribution of world population (vertical scale) against income (horizontal scale). Income here is measured by using gross domestic product per person (GDP) in US dollars compared at purchasing power parity rates.

The graph reflects both inequalities between countries and within countries. The country with higher population suffers from lower average income. In the last 25 years, some regions of the world have raised their average income per person, while others have suffered a decline in income. There is decline in real income of sub Saharan Africa and Eastern Europe. While rapid growth in East Asia was impressive, it had little effect on global inequality due to the relatively small populations involved. The rise in world income inequality is due to rapid growth in China since the 1970s, and in India since the 1980s, and the 'catch-up' process of European economies with the United States.

Economic growth that does not lead to sharp and sustained reductions in poverty may create more problems than it solves. Similarly, if rapid growth is achieved at the expense of a worsening in the distribution of resources, it ultimately becomes unsustainable, since it engenders social tensions. Let us examine the degree of inequality in India. Both the United Nations (UN) and the Central Intelligence Agency (CIA) have made lists of countries by income inequality metrics.

We have taken the Gini coefficients as measured by the CIA and the UN. The Gini coefficient is a number between 0 and 1, where 0 corresponds with perfect equality (where everyone has the same income) and 1 corresponds with perfect inequality (where one person has all the income, and everyone else has zero income). The Gini coefficient is calculated with the help of a Lorenz Curve which provides a graphical representation of a nation's income distribution.

The Gini coefficient is equal to the area between the line of equality and the Lorenz curve divided by the total. According to the data given in the Table-1, we find that, among five countries, China has the highest income inequality followed by US and Japan. The Gini coefficient for India is only 36.8 as measured by the UN and the CIA.

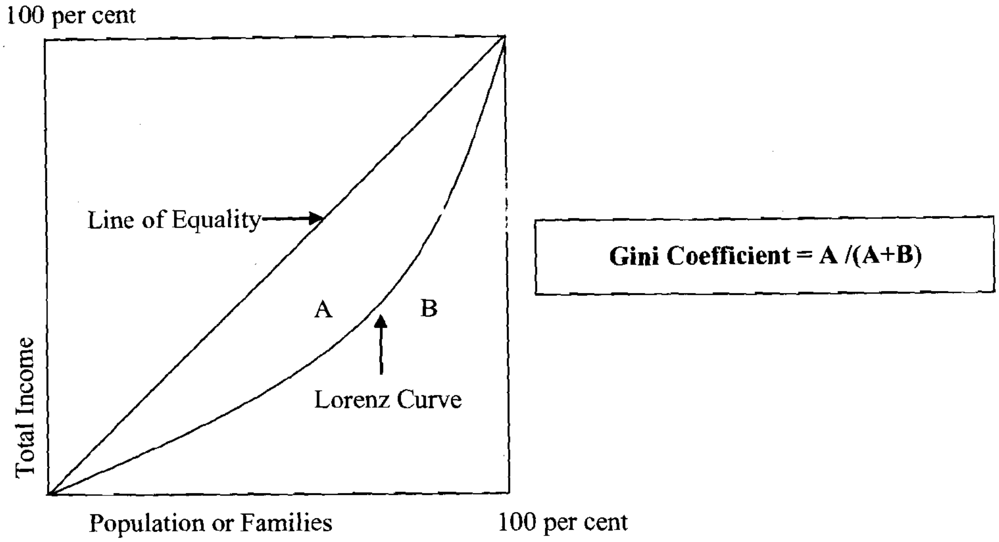

Figure 3.2 : Gini Coefficient

Table.-1: Gini Index of Countries

Country	Year	R/P -10	R/P -20	UN Gini Index	CIA Gini Index
USA	2007	15.9	8.4	40.8	45
UK	2005	13.8	7.2	36	34
Japan	2002	4.5	3.4	24.9	38.1
China	2004	21.6	12.2	46.9	46.9
India	2004	8.6	5.6	36.8	36.8

Note: R/P10=Richest 10% to poorest 10%; R/P 20= Richest 20% to poorest 20%; Gini index is estimated from Central Intelligence Agency's World Fact book, R/P-10 and R/P-20 are estimated from data given by United Nations Development Programme

Gini Ratio

There are many instruments that measure inequality of income. The most widely used ones are the Gini coefficient, and the Lorenz curve which draws the cumulative percentage of distribution of income corresponding to cumulative distribution of households. Table-2 shows the comparative degree of inequality. The degree of inequality is about the same in the case of Japan and India, but in the case of Brazil, it is substantially higher. Such a relationship can be easily understood from the fact that income received by the bottom 20 per cent of household is 8.1 per cent in

India, 8.7 per cent in Japan but only 2.4 per cent in Brazil. Similarly, income received by the bottom 40 per cent is 40.4 per cent in India, 21.9 per cent in Japan, but only 8.1 per cent in Brazil. The Gini coefficients are estimated as 0.31 for India, 0.27 for Japan and 0.54 for Brazil.

Table -2: Cumulative Shares of Household Income by Quintile Class

Income Size Class	Cumulative frequency			
	Households	India	Japan	Brazil
I	20	8.1	8.7	2.4
II	40	40.4	21.9	8.1
III	60	36.7	39.4	18.8
IV	80	58.7	62.5	37.4
V	100	100	100	100
Gini Coefficient	--	0.31	0.27	0.54

Source: Das, Kumar (1997) Asian Profile of Underdevelopment and Poverty, *Asian Profile*, Vol.25 (1) ,Canada

The fact of gross inequalities is very much evident from several estimates. An estimate made from time to time leaves no doubt about the existence of large inequalities in India. It is seen from Table–3 that in 1994, 20 per cent of the households at the lowest rung of the income ladder receive only 9.2 per cent of the national income. At the other end, 20 per cent of households at the highest rung enjoy as much as 39.3 per cent of the national income. If one takes up the lowest 10 per cent of the households at the lower end and highest 10 per cent at the upper end, the fact of inequality is more glaring with the lowest getting as little as 4.1 per cent and the highest getting as much as 25 per cent of the national income. The trend and magnitude of inequality in India can be perceived over the years by the data given below.

Table – 3: Income Inequalities

Year	Bottom 20 %	Top 20 %
1955-56	34(bottom 10%)	9.6(top 25%)
1975-76	49.4	7
1989-90	41.3	8.8
1992-93	42.6	8.5
1993-94	39.3	9.2

Source: Das, Kumar (1994) Paradox of Poverty and Planning in India, *Economic Quarterly*, Berlin

Some remark that inequality in newly liberalized economies has significantly increased. India has been experiencing dramatically increased income inequality. This is not a surprise to most people. The rise in inequality is explained in terms of an increase in the relative share of output going to capital as compared to labour, a drop in the rate of labour absorption and the rapid growth of the services sector. The truth is that while a small percentage of the population (around 20 per cent) has indeed benefited greatly from the economic policies and processes of the last decade, for the majority of the rural population and a significant part of the urban population, things have got worse. The most dramatic and remarkable improvement in consumption has been of those who were already the richest people in India - that is the top 20 per cent of the urban population.

By contrast, the bottom 40 per cent of the urban population per capita consumption has increased by 14 per cent since 1989-90. But the most dramatic evidence is for the bottom 80 per cent (nearly 600 million) of the rural population whose per capita consumption has actually declined since 1989-90. In other words, even the official statistics of the government still show that more than half of India has

lower consumption per person than more than 10 years ago, after a decade of impressive economic growth.

3.3 CAUSES OF ECONOMIC INEQUALITY

The income distribution pattern shows that there are glaring inequalities in India. The main causes of income inequality in Inui... ...e as follows.

(i) **Differential Regional Growth:** the post reform period is characterized by widening regional inequality. Regional disparity is the major reason for income inequality. The economic disparity has a geographical facet. A large majority of poor people live in backward regions/states of the country. The rich are more in percentage in the advanced states and regions. There is also intra state income inequality. But that income inequality is still sharper in poor states. It is because the advanced states grow rapidly. They have performed well, both in agriculture and industries. Their per capita income also rises very fast. On the contrary the poor states lag behind. Due to slow economic growth, the poor states continue to be inhabited by poor people with low per capita income. Statistical convergence among states in terms of inequality, poverty, and real mean consumption is weak.

(ii) **Unequal Asset Distribution:** income flows from wealth. Assets like land, cattle, labour, training, education, and shares represent the wealth of households. Asset distribution is very uneven, both in rural and urban areas of India. Few people are land owners, but a majority are land tillers. Therefore, income distribution is highly skewed. Asset formation in different regions has been very asymmetric. The accumulated assets pass on from generation to generation. This inequality in wealth enables few people to get income in the form of rent, interest, and profit. But the majority of people in the villages and urban areas do not possess any income generating assets. Private ownership of property has no limit. It is the cause of the concentration of economic power.

(iii) **Technological Dualism**. There is technological dualism in India. Very advanced technology, high technology, and nano technology are proudly adopted in different sectors and industries. But the old bullock cart and hand pulled rickshaw are widely used in different parts of India. High tech users maintain their high economic status, while the agricultural workers toil in the field with primitive technology and drudgery–ridden practices. As a result of the rise in technological dualism, income inequality increases.

(iv) **Educational Disparity**: the educational system in the country is inefficient and defective. It does not help in skill formation of the weaker section. It is not effective enough to build human capital. It also discriminates against the poor.

The high dropout rate is associated with high push out rates in primary schools in remote villages. There are two types of education: education through English medium schooling, and education through the medium of regional languages. The former education is very expensive. It is an investment which is not affordable by the majority of the people. The latter is an expenditure for households. The poor villagers and labour class consider education, and, particularly, a girl's education as wasteful, having no return. There is inequality in training and skill building.

(v) **Inadequate Welfare Measures**: the problem of unemployment is becoming very severe. The country is adopting capital intensive technology in the name of the modernization process. Welfare measures of the government are treated as relief measures. This promotes a dole culture which maintains inequality. Welfare measures are not adequate for the lower class and to eradicate inequality. They do not help to create jobs, or provide training in skills among the deprived classes.

(vi) **Inappropriate Government Policy**: the policy of the government lacks any perspective. It does not discourage the profit–seeking business class and rent-seeking groups in their habit of accumulating wealth. The tax authority is ineffective in curbing this trend. The credit policy and the laws governing inheritance are also defective. The government needs to follow appropriate income–policy, which keeps the ratio between the highest income and lowest income at a socially acceptable figure. The government's top-down approach to development is the main reason for the low trickle-down effect. Rising prices reduce the purchasing power of poor people. The poor are left with nothing to save and reinvest, and are also not in a position to provide education to their children. The poor fall into a vicious circle, so, the rich becomes richer, and the poor get poorer.

(vii) **Lack of Skills**: unskilled labour in India is mainly engaged in the manufacturing and the agricultural sector. The daily wages offered to the labourers in eastern India is substantially lower compared to what is offered in the northern parts of India. The agro-based industries are not growing in India. The average income of an agriculturalist in Punjab or Haryana is more than that of any state. The privatization process in India is accompanied with lucrative salaries for the few, and increases in the price index which reduces the standard of living of the majority. Employment opportunities are shrinking. The real income of the majority in the rural areas is falling.

(viii) **Growth of the Informal Sector:** inequality arises out of the differences in the capabilities and ownership of assets. There is growth of the informal sector in India. The informal sector is unregistered, unregulated, and unprotected. India's labour force is about 390 million. Out of this, only 7 per cent work on regular salaries. About half are unionized. During the 1990s, the unregistered workforce increased from 89 per cent to 93 per cent. The informal economy, comprise 60 per cent of net domestic product, 68 per cent of income, 60 per cent of savings, 31 per cent of agricultural exports, and, even 41 per cent of manufactured exports. However, the informal sector is viewed as a shock absorber, but it has become the source of exploitation, too. Exploitation of women and children is very common in this sector.

(ix) Level of Corruption: corruption is one of the important causes of inequality. India suffers from high levels of corruption in different spheres. People misuse their office and power to make money and assets by illegal means. There is less punishment for larger corruption. The legal procedure takes a very long time to punish wrongdoing. Gradually, illegal activities are finding permissiveness. Therefore, illegal accumulation of money in one generation results in wealth for succeeding generations. Thus, inequality of income and wealth prevails in the long run.

Till now, you have read about the meaning as well as the causes of its existence. Before we proceed further, you should answer the questions given below, in order to Check Your Progress-1.

Check Your Progress 1

Note: a) Write your answer in about 50 words.

b) Check your progress with possible answers given at the end of the unit.

1) What is trend for global income inequality?

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2) Give the comparative picture of income inequality.

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3) What are the main causes of inequality in India?

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3.4 EFFECTS OF ECONOMIC INEQUALITY

Inequality affects society as well as the economy. Some of the effects of inequality are given below.

i. Social cohesion: The prevalence of economy inequality affects the social cohesiveness. In a more equal society, people are more likely to trust each other. Erse Uslaner and Mitchell Brown, in their study, have found that there is a high correlation between the amount of trust in society and the amount of income equality. Inequality leads to crime and theft in society. Society which is more unequal, the marginalized section will adopt to crime bring economic egalitarianism in the society. The Neapolitan (1999) cross national research on homicide found positive association between income inequality and homicides.

ii. Effect on Health: income has a positive association with health. The country with a high degree of income inequality would experience more mortality and morbidity as income enables an individual to have access to qualitative health care services. In the Indian context, studies have shown that in the poorer states, like Orissa and Bihar, a large proportion of people use public healthcare facilities while in Punjab, a high percentage of people use private health care services which is efficient and better quality services. Richard Wilkinson, J Lynch and GA Kaplan have found that socio-economic status strongly effects health.

iii. Effect on education: there is a strong correlation between economic status and education. Wealthy people can offer higher education to their children. Globalization, which has enhanced income inequality, enables only the economically well-off to acquire higher educational qualification from private educational institutions. In the Indian context, one of the educationists has remarked that 'education is a luxury for the poor'. This income inequality affects educational opportunities in general and higher education in particular.

iv. Economic welfare and distributive effectivity: economic inequalities may reduce distributive effectivity within society. It is a fact that the marginal utility of a rupee or a dollar is high for the poor as compared to the rich. An additional, a rupee earned by a poor labourer is likely to be spent on the basic necessities like food, clothing, shelter, healthcare, etc. This may not be in the case of a rich person. This economic inequality affects economic welfare, as also distributive justice. According to Pigou, a welfare economist, income generally benefits the rich by making them wealthier than other people, whereas the poor benefit in absolute terms.

v. Economic growth: the relationship between growth and inequality is a complex one. A number of researchers have derived conflicting results. Some are of the view that inequality has a positive effect on growth, while others are of the opinion that inequality produces a positive impact on growth. Robert Barrow in his paper argued that inequality reduces growth in poor countries and promotes growth in rich countries. G.A. Cornia and J. Court (2000) have concluded that too much equality negatively impacts growth due to incentive traps, free-riding, labour shirking, and high supervision cost. On the other hand, lush levels of inequality negatively impacts growth due to incentive traps, erosion of social cohesion, social conflicts, and uncertain property rights.

3.5 REMEDIES FOR ECONOMIC INEQUALITY

Measures for curbing inequality of income are as follows.

i. Curbing the concentration of income and wealth: inequality in income can be reduced by curing the process of wealth accumulation.

ii. Land reforms: land reforms are warranted to redistribute the land from the rich landlord to the actual land tillers and poor peasants.

iii. Redistribution of assets: inequality can be reduced by making redistribution of other productive assets.

iv. Employment opportunities: creation of employment opportunities for the majority and poorer class can reduce income inequality.

v. Small scale industries: promotion of small scale industries and village level industries can generate jobs for the village people. Agro-based industries can generate income employment for the unskilled people.

vi. Social security measures: government should devise appropriate social security measures to reduce income inequality.

vii. Tax reforms: appropriate taxation system of the government can bring redistribution of the income from the rich to the poor.

viii. Educational reforms: the educational system should be efficient and fair. It should give equal opportunity to all. It should be accessible and affordable. It should be meaningful for the livelihoods of the people.

ix. Inheritance laws: changing the inheritance laws of the country is necessary. The son and daughter difference in practice of inheritance of property of the parents should be fought with morality and legality.

x. Public sector reforms: the public sector should be revitalized and modified to reduce inefficiency and corruption. It can increase the production and income level of the poor people. Good performance by the public sector can reduce income inequality in India.

You have read about the effects and remedies for economic inequality, apart from the concept, measurement and causes of economic inequality. Now attempt these questions in order to Check Your Progress-2.

Check Your Progress 2

Note: a) Write your answer in about 50 words.

b) Check your progress with possible answers given at the end of the unit.

1) Write down a few important effects of economic inequality.

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2) Suggest a few remedies for the removal of income inequality.

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3.6 LET US SUM UP

In this unit, we dealt with the definition, causes, and effects of inequality. Economic inequality is measured with the use of the Gini coefficient. It is glaring in underdeveloped countries like India. The differentials in regional growth, unequal asset distribution, technological dualism, educational disparities are a few important causes of economic inequality. Economic inequality produces effects on social cohesion, education and health. Several steps can be initiated for the removal of economic inequalities. In nutshell, it is enemy of development.

3.7 KEYWORDS

Gini Coefficient : It is commonly used as a measure of inequality of income, or wealth. It has also found use in the study of inequalities in disciplines as diverse as health science, ecology, and chemistry.

Lorenz Curve : Lorenz curve is a graphical representation of the cumulative distribution function of the empirical probability distribution of wealth.

Human Development Index (HDI) : The index used to rank countries or regions by their level of human development. It also indicates whether a country or region is developed, developing, or underdeveloped based on 1) life expectancy at birth; 2) knowledge and education; 3) and, standard of living.

Purchasing Power Parity (PPP) : Purchasing power refers to the value of currency expressed in goods and services that one unit of money can buy, whereas purchasing power parity (PPP) refers to an estimation of exchange rate between countries based on their currency's purchasing power. The purchasing power parity theory uses the long term equilibrium exchange rate of two currencies to equalize their purchasing power.

Technological Dualism : Hans Singer (1970) introduced the concept of international technological dualism, by which he meant essentially unequal developments in the area of science and technology, between rich and poor countries

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3.9 CHECK YOUR PROGRESS: POSSIBLE ANSWER

Check Your Progress-1

1) What is trend for global income inequality?

Answer. Global income inequality is probably greater than it has ever .Currently, the richest 1 per cent of the people in the world receive as much as the bottom 57 per cent. The ratio between the average income of the top 5 per cent in the world to the bottom 5 per cent increased from 78:1 in 1988 to 114:1 in 1993) One pole represents the 2.4 billion people whose mean income is less than $1000 year and includes people living in India, Indonesia and rural China. With 42 per cent of the world's population, this group received just 9 per cent of the world income. The other pole is the group of 500 million people whose income exceeds $11,500. This group includes the US, Japan, Germany, France and the UK. Combined, they account for 13 per cent of the world's population, yet garner 45 per cent of the world income. The richest 25 per cent of the world's population receives 75 per cent of the world's income.

2) Give a comparative picture of income inequality

Answer. The degree of inequality is about the same in the case of Japan, UK, and India. But, in the case of USA and Brazil, it is substantially higher. Such a relationship can be easily understood from the fact that income received by the bottom 20 per cent of household is 8.1 per cent in India, 8.7 per cent in Japan but only 8.4 per cent in USA and 2.4 per cent in Brazil. Similarly income received by bottom 40 per cent is 40.4 per cent in India, 21.9 per cent in Japan but only 8.1 per cent in Brazil. The Gini Coefficients are estimated as 0.31 for India, 0.27 for Japan 0.45 for US, 0.34 for UK and 0.54 for Brazil.

3) What are the main causes of inequality in India?

Answer. Regional imbalance, educational disparity, unequal asset holding, technological duality, and inefficiency are the main causes of inequality. Welfare measures are inadequate. The policy of the government lacks any perspective. It does not discourage the profit seeking business class and rent-seeking group in their habit of accumulating wealth. Employment opportunities are shrinking due to lack of skill and education. The real income of the majority in the rural areas is falling. The growth of the informal sector is viewed as a shock absorber, but it has become the source of exploitation too. Exploitation of women and children is very common in this sector. A high level of corruption leads to wealth inequality, which prevails in the long run.

Check Your Progress-2

1) Write down a few important effects of economic inequality.

Answer. The important effects of economic inequality on society as well as on the economy are social cohesion, health, education, economic welfare, distributive effectively and economic growth.

2) Suggest a few remedies for removal of income inequality.

Answer. Some important measures, or remedies, are: curbing the concentration of income and wealth, land reforms, redistribution of assets, employment opportunities, small scale industries, social security measures, tax reforms, educational reforms, inheritance laws, and public sector reforms.