

Economic and social impact of income inequality



**ASSIGN
BUSTER**

\n[[toc title="Table of Contents"](#)]\n

\n \t

1. [2. 0 The Degree of Income Inequality](#) \n \t
2. [3. 0 Effects of Income Inequality](#) \n \t
3. [3. 1 Economy](#) \n \t
4. [3. 2 Social](#) \n \t
5. [4. 0 Ways to Combat Income Inequality](#) \n \t
6. [5. 0 Conclusion](#) \n

\n[/toc]\n \n

Globalisation has revolutionised the world in many great ways. Heshmati (2003) defined globalisation as the free movements of goods, services, and capital across countries, thus, enabling individuals and organisations to connect with the world in a faster and more economical way as compared to before. However, the rapid growth of globalisation can also be viewed from a different perspective; as they say there are two sides of the same coin. Although globalisation has widened opportunities for organisations to operate internationally and improve economic growth, it does create pressures which would lead to the increase of inequality and poverty in some countries (Duncan, 2000).

Income inequality is the disparity of income distribution between the rich and the poor within an economy. Income inequality is also linked to relative poverty, where individual or household income falls below the average income level set by the country which determines the people's status. The Gini coefficient is the most common method used to measure income

inequality. It is based on the Lorenz curve which compares the distribution of a specific variable with the line of perfect equality. According to Slack and Rodrigue (2009), the Gini coefficient ranges from 0 to 1; where 0 represents perfect equality while 1 means complete inequality. Most countries in the world have a Gini coefficient ranging from 0.25 to 0.6.

The degree of income inequality, its effect on social and economics, as well as methods to overcome the matter will be discussed further in this report.

2.0 The Degree of Income Inequality

Sachs (2008) mentioned in his book that inequality is one of the devastating crises that the world has been experiencing for the past two decades, although it has been around for centuries. The Human Development Report 2002 proved that in 1820, Western Europe's per capita income was approximately three times greater than the per capita income of Africa. However, by 1992, the difference has increased up to 13.2 times. This situation reflects the well-known phrase 'the rich getting richer and the poor getting poorer'. Income inequality has become a very serious issue because the increasing gap between the rich and the poor is too great to ignore. This gap exists either because the rich are getting much wealthier or the poor are falling behind, or even both.

Now the question is why are the rich getting richer? There are a few reasons to name, but the main drive of inequality is due to the increase inequality of labour earnings. High pays are usually rewarded to skilled workers as well as those with tertiary education qualifications, whereas unskilled workers become the victims of inequality. Unskilled workers are struggling to survive

with the mere low wages they earned that does not commensurate with the long hours of work performed. In the worst case scenario, their work might get taken over by immigrants who are more than happy to accept such amount of wage. Stiglitz (2002) quoted:

The Westerns may feel working at Nike as exploitation because they receive low pays, but for many people in developing countries, working in a factory is better than staying down on the farm.

Not only that, but with the advancement of technology and innovations, computers nowadays are capable of developing productivity in many sectors, thus, creating a high possibility of unskilled labours to be substituted off.

Labours who are skilled with machineries and computers on the other hand are in demand for employment.

Another reason why the rich are getting richer is owing to corruption.

Corruption as defined by the Oxford dictionary is a dishonest or fraudulent act by those in power, which includes but is not limited to embezzlement, bribery, extortion, and fraud. In poor countries, those ranked at the top of the hierarchy are controlling money for their own gain instead of distributing for the society's welfare. Exploitation of natural resources in the third world country by the rich countries also leaves the poor in poverty as the large amount of money received was not returned to the people. Afrikan (2011) quoted Kwame Nkrumah, the leader of Ghana, saying ' foreign capital is used by the western powers for exploitation rather than developing the less fortunate countries'. In other words, the increase of foreign investments in

less developed countries unfortunately does not reduce the gap between the rich and the poor countries.

Therefore, yes, income inequality is a very serious matter that should be taken into account because it is directly related to the welfare of society in a country. While it might be argued that inequality creates a positive result in terms of a healthy competition and as motivation to lead a better life, the truth remains that income inequality is nothing but a burden towards society.

3. 0 Effects of Income Inequality

As mentioned earlier, income inequality is a growing concern not only within a country but is a serious global issue. In this section, the effects of growing income inequality on a country's economy and social development will be discussed.

3. 1 Economy

Through the years, economists and policy makers have argued on the possible effect of income inequality on economics. According to Kuznets' theory, the relationship of economic growth on income inequality can be illustrated by an inverted-U graph. When a country develops economically, the income inequality of that country worsens. A few decades later as a country grows wealthier with the rich investing more in the economy, the level of inequality reduces. However, the Kuznets' theory seems to only apply on developed countries because studies on the third world countries have shown contrasting results (Samanta and Heyes, 2006).

Human capital is a great asset to a country's development because knowledgeable and skilled labours are the drivers of economy. In most poor countries, their economic growth is stunted by the high percentage of unemployed and unskilled labours due to the lack of education. Yet, in actuality, among those who are unfortunate to receive proper education, there are a great number of them who have potential to lead a better life. Regrettably, they do not have the opportunity to pursue education in order to contribute to the development of economy. As a result, the poor are not capable of providing goods and services to the economy that would generate high returns.

Other than that, the vicious circle of poverty also affects the economy. This vicious circle is a self-perpetuating process which returns to its initial point with no development from when it begun (Gary, 2010). The vicious circle of poverty is when a person earns low salary, they do not have enough money for savings, and thus, they are restricted to invest which then results in low productivity. Once again, low productivity causes low income, and the cycle repeats itself again continuously. In addition, when income is low, consumption decreases as well. Due to this, the government are spending a large amount of money to eradicate the problem instead of investing on the country's development, thus causing the drop in economic growth. If the cycle persists in long-term, the economy of the country would face greater risk.

In a country suffering from high income inequality, there is a possibility that political instability will occur and would then lead to social unrest that could affect the country's economy. An example is the current issue in Egypt;

<https://assignbuster.com/economic-and-social-impact-of-income-inequality/>

where the citizens were dissatisfied with the high levels of corruption, low wages, and poor living conditions. As a result, they protested against their President and government, and it caused serious social unrest. This political instability could discourage domestic and foreign investments; hence, underdeveloped economy.

3. 2 Social

The inequality affects people's quality of life greatly when there is a gap between those with high and low income. However, the wealthier people of a country are not affected by the problem at all; instead they are enjoying their wealth in ways we can't even imagine. Take China as an example; there are thousands of people with low living standards in mainland China working in factories with low wages, but people in cities like Shanghai on the other hand are living their lives luxuriously. This situation shows that the income inequality of China is relatively high with a Gini coefficient of 0. 42 in year 2007, as stated by the Central Intelligence Agency (CIA). In other words, income inequality affects a country's social development negatively in terms of living standards, health, education and crime rates.

Living standards is a measure of material welfare of a population in a certain geographic area. For people with low income, they face difficulties as the living standard would be relatively high for them in order to support their daily necessities as well as their families. Hunger and malnutrition is a very common problem among those unemployed as money is a limited factor. Based on the Food and Agriculture Organization of the United Nations (FAO) 2010 report, most of the world's hungry are from developing countries which consist of 16% of the population.

<https://assignbuster.com/economic-and-social-impact-of-income-inequality/>

The second impact of income inequality is on the society's health. When there is inequality, it is clear that the less fortunate are affected greatly as they lack access to safe drinking water, exposed to unhygienic environment, and receives inadequate medical services. Some of the common diseases that affect the poor in third world countries are malaria, tuberculosis, kwashiorkor, pneumonia, and AIDS. The unavailability of clinics and medication supplies in certain geographic areas worsens this condition. Not only that, but ignorance in birth control and contraception increases the rate of those suffering from HIV/AIDS. Due to this reasons, the mortality rate in those areas will keep increasing terrifyingly unless safety measures are taken into action.

Thirdly, the social effect of income inequality is on education. With limited money to invest, most people with low income do not have the chance to enrol their children into school to obtain proper education. Even if they do have the opportunity, they couldn't afford to continue to the tertiary level without any monetary support. Due to that, most of the poor are trapped in the vicious circle as mentioned earlier. For example, if a man is a low income worker, his son who lacks proper education would have to take up low income works as well; and the cycle of unskilled workers in the man's family will run through the next generation continuously if there is no government intervention.

The final social effect on a country's development is the increase of crime rates. When money is scarce and an individual is desperate for survival, one would do absolutely anything in order to continue living. Theft and robbery is a major problem in most countries as crime is the only way for them to

obtain material goods instead of using proper methods. This is because the income inequality that affects the poor has forced a high level of stress upon them, which leads them to committing crimes.

Therefore, it is apparent that the crisis of income inequality affects negatively in a country's development either in terms of economic growth or social welfare.

4.0 Ways to Combat Income Inequality

Countries worldwide have already taken action to reduce the wide gap between the rich and the poor by adopting new policies. The government of a country plays an important role in order to overcome the problem of income inequality. The first method to combat inequality is the government should manage their budget system relevantly. The government's main source of income comes from the tax paid by the people of a country as well as foreign investments into the country. Apart from investing on the country's economy development and welfare expenses, the government should allocate and contribute money to the less fortunate too. One way of contribution is through unemployment benefits which were imposed in some countries such as Australia, Ireland, United Kingdom and Japan.

Unemployment benefits are payments to the unemployed by the government or an authorised body of a country. Although the pay is not much, it is sufficient for them to fulfil their basic necessities. With the aid of this benefit, the rate of unemployment and poverty decreases, thus, reduces the gap of inequality.

My second recommendation is to provide training to unskilled labours that has great potential to work in high income jobs. By providing proper education and skills to the poor community, chances of them to break free from the poverty trap are higher. As mentioned earlier, there are actually quite a number of people with potential who are not given the opportunity to display their true potential because they lack education. Therefore, by establishing a program where potential people from the poor community are given training to work in sectors other than agriculture and industrial, will allow them to live their lives a little wealthier than before.

The next step to overcoming income inequality is by providing education to the less fortunate with the government's support. Such as building schools in less developed areas, allocate accredited teachers to these areas to educate them, and providing scholarships so that they can move on to tertiary level education. It seems that obtaining a certified education is the only way to demolish the inequality between them and the wealthy. With proper education, it is not impossible for the poor to join the workforce alongside those people whose parents are wealthy enough to support them to study. In other words, education is able to reduce income inequality because they will then be earning the same salary and also automatically improves their living standards.

The last possible approach in combating income inequality is through standardising minimum wage per hour for unskilled workers. By standardising minimum wage, living standards of the poor can be recovered and also stimulate consumptions. However, there are arguments indicating this policy would be a disadvantage to a country because foreign investors

<https://assignbuster.com/economic-and-social-impact-of-income-inequality/>

would opt to invest in other countries which do not apply such policy. Though there is truth behind these words, if countries worldwide practice this policy together, it would provide positive outcomes to the less fortunate.

5. 0 Conclusion

Throughout this report, I have discussed that the rising of income inequality is indeed a serious matter in which its impact can be seen to affect both economy and social development of countries globally. The disparity of income between the rich and poor ought to be reduced in order to achieve an equal and better living standard among society. Although I am aware that income inequality cannot be solved overnight, I believe that steps should be taken to overcome the problem. Therefore, in conclusion, special policies and global efforts are required to combat income inequality in order to accelerate economic and social development.