Poverty, the state and development

Edexcel IAL Economics WEC14 sections 4.3.4-4.3.6 full package

Topic 8 at a glance

> Measure poverty and inequality, fund the state, and plan development.

- WEC14 spec sections 4.3.4 to 4.3.6.
- All worked numbers are original.

Absolute or relative poverty

Absolute

basic needs unmet

World Bank line:

$3.00 a day (2021 PPP)

Relative

below the norm

a share of median

household income

The Lorenz curve, drawn

> The poorest 80% of people earn only 50% of income.

- Shares: 5, 10, 15, 20, 50%.
- The bigger the gap, the higher the Gini.

Worked: the Gini coefficient

1. **Strips under the curve** $50 + 200 + 450 + 800 + 1500$
2. **Area** 3000 of the 10000 square: 0.30
3. **Gini** $1 - 2 \times 0.30 = 0.40$

Decision

Gini 0.40: a fairly unequal distribution.

Why inequality arises

Within countries	**Between countries**
wages and skills	growth histories
wealth and **inheritance**	institutions
the skill premium	geography

Three kinds of spending

Kind	**Example**
capital	roads, schools, hospitals
current	salaries, running costs
transfer payments	benefits: no output in return

Three tax schedules

Schedule	Incomes 10k, 40k, 100k	Average rate
progressive	pay 1k, 8k, 30k	10, 20, 30%
proportional	a flat 25%	25% for all
regressive	a 5k charge each	50% down to 5%

The Laffer curve, drawn

Revenue peaks at 100 when the rate is 50%; higher rates collect less.

- Revenue $= t(1 - t) \times 400$.
- Tax changes also hit incentives and FDI.

Deficit, debt and the cycle

Deficit vs debt

deficit: one year (a flow)

debt: the total (a stock)

Structural vs cyclical

structural: even at full employment

cyclical: only in a slump

Policy has limits

Five policy families, but bad data, risk and shocks get in the way.

- 2008: rescues, near-zero rates, QE.
- TNCs: transfer-pricing rules; firms relocate.

The Human Development Index

Education, health and income, combined by a **geometric mean**.

- Broader than GDP, but hides distribution.
- Also: water, energy, doctors, internet.

What holds development back

Economic	Non-economic
primary product dependency	**corruption**
the **savings gap**	poor governance
capital flight, debt	civil war
infrastructure, skills	terrorism

Strategies for development

Approach	**Examples**
market-orientated	free trade, FDI, privatisation, **microfinance**
interventionist	human capital, infrastructure, buffer stocks
industrialisation	the **Lewis dual-sector model**

Data response: Bangladesh per head

1. **GDP** about US$450 billion
2. **Population** about 173 million
3. **Per head** 450 billion $\div$ 173 million $\approx$ US$2,600

Decision

About US$2,600 a head: an average that hides low garment wages.

Data response: the Lewis model at work

> Surplus farm labour moves to factories, and reinvested profit keeps it moving.

- Assumes profits are reinvested at home.
- Wages rise when surplus labour runs out.

Data response: after LDC status

Long run

diversify exports

human capital

infrastructure

Short run

new trade agreements

attract FDI

safer factories

Check yourself

Question	**Answer**
Shares 5, 10, 15, 20, 50: Gini?	0.40
Taxes 1k, 8k, 30k on 10k, 40k, 100k?	**progressive**
Laffer peak?	100 at a 50% rate
Deficit or debt: which is a stock?	the **national debt**
HDI components?	education, health, income