International Journal of Innovations & Research Analysis (IJIRA)
ISSN :2583-0295, Impact Factor: 6.238, Volume 04, No. 01(I), January- March, 2024, pp 23-27

ECONOMIC INEQUALITY

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ABSTRACT

For any economy, the measurement and value of its GDP is often looked at as the most important indicator of economic growth and prosperity. And while the GDP does play a large role in establishing a robust economy for any country, what is of utmost importance for its continued growth is its underlying composition. The GDP or gross domestic product of an economy refers to the sum total of value of the goods and services produced in a given economy over a given period of time, usually a year. It is also used as a measure for a nation's income. Its composition is dependent upon the contribution of the economy's different sectors and segments of the population. Economic Inequality occurs due to the uneven distribution of this income and wealth across the various population segments of an economy. The greater the unevenness of distribution, the higher the level of inequality. This inequality creates a rich - poor divide in the economy which, if not treated at an early stage through proper policy intervention, can lead to serious consequences for the economy. The population can be divided on the basis of various factors such as gender, religion and caste, geographical location, sector of employment, level of education or race to find the presence of different types of inequality.

Keywords: *Economic Inequality, GDP, Economic Growth, Geographical Location, Types of Inequality.*

Introduction

Over the last few years, India has become one of the fastest growing countries in the world. Its most recent GDP figures, as announced by finance minister Dr. Nirmala Sitharaman on 12 June 2023, state it to be the fifth largest GDP in the world, ahead even of Britain, with a value of $3.75 trillion. It is even expected to take on Germany over the next few years, whose GDP is valued at $4.3 trillion, if it continues to maintain its current growth rate of 7.2%. India's per capita GDP distribution stands at approximately $2400 and the country is hailed as a 'bright spot' in the global economy. While the above figures point to a powerful economy that is on par with its global competitors, it is important to delve deeper into the numbers and determine if all segments of the population are reaping an equal benefit. This often tells a different story. In the instance of India, one that is genuinely concerning.

Recently published reports on inequality in India by leading research institutions such as the World Inequality Lab and Oxfam all point to one thing - a crushing divide between the country's rich and poor, which is only increasing as time passes. Even though India's current purchasing power parity (PPP) rests at approximately $2400, the division is not at all an equitable one. The average income for the bottom 50% of the population is a meagre $654, which is a fourth of the national average. On the other hand, the top 10% of the population earns an average income of $14,231 which is almost six times the overall population average. An even stronger divide persists in the distribution of wealth in the country. According to a report published by Oxfam in 2022, a staggering 77% of the total national wealth is held by only 10% of the country's total population. This leaves the remaining 90% to be survived by only 23% of the nation's wealth. The bottom 50% of the population, which is approximately 670 million

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people, only saw a 1% increase in their wealth over the year while the ultra wealthy, whose net worth lies over $30 million, are expected to increase by 58.4% by 2027, stated the 'Wealth Report 2023' published by Knight Frank, taking the final figure from 12,069 in 2022 to 19,119 in 2027. It further stated that India's billionaire population is also expected to expand 161 in 2022 to 195 in 2027. The Indian high net worth population, who have an asset value of over $1 million would rise to 1.76 million in 2027 from 79,7714 persons in 2022, recording a growth of 107% over the five-year period. Tracing the distribution of wealth historically, according to data from the World Inequality Database, the share of wealth held by the bottom 50% of the population has nearly halved since 1961 whereas that of the top 10% has increased by around 50% and the top 1% saw a 180% growth in their wealth since 1961.

Economic Inequality, especially income inequality, is multifaceted in its causes and far reaching as well as devastating in its implications for any economy. Both are discussed in detail below.

Causes and Implications of Economic Inequality

The most pressing and dangerous impact of economic inequality is the unequal distribution of economic benefit. Increase in GDP levels of an economy and higher growth rates, though imply a better standard of living for its citizens, do not always result in the same. Oftentimes, it is a reflection of the increase in income, wealth and consumption of the rich, while the poor continue to suffer the same as before, or are sometimes, even left worse off. The prevalence of economic inequality, combined with high levels of economic growth, often result in what is called a 'K shaped Growth' based on the shape the graph of economic growth resembles when cross sectioned on the basis of different factors of economic growth. An uneven growth trajectory results in an uneven recovery for the economy. 'K shaped recoveries' from recessionary periods are becoming more and more common over the world as economic disparities are increasing almost everywhere.

A 'K' shaped recovery exacerbates any prevailing disparities in the economy as well as results in structural changes. To understand this, one must be able to identify the cause for a divide in economic growth in the first place. These will be different on a case to case basis.

Income inequality often occurs due to preexisting social inequality, with differences based on gender, geographical location, caste, colour, creed etc. Other factors affecting income inequality are listed below:

- **Unemploymen**t - Any work is better than no work as it helps an individual earn an income, regardless how meagre. Therefore, at the time of a recession, an employed worker is more likely to have savings to dive into if relieved from a job or when inflationary pressure raises prices of basic necessities as compared to an unemployed person, who will have no savings due to his lack of an income. However, even within the employed class of individuals, there are those engaged in the formal sector and others in the informal. Those that come under the latter have little job security and do not receive any government benefits such as gratuity and provident fund. Oftentimes, workers in the informal sector work on the basis of day contracts and receive daily wages. On the days they are unable to find work, they receive no wage, largely affecting their abilities to save. In the case of a recession, they are one of the worst hit among the employed. While the salaried class of workers is able to dive into its accumulated savings at the time of a recession if they are fired from their work, the casual labourers and unemployed are unable to do so and are often left poorer than they were before the recession.
- **Education** - Education is considered an important determinant of income equality as it greatly impacts the ability of an individual to get a well earning job. A basic education is necessary for any job that requires even the most basic level of skill. Higher his level of skill and competence, higher his wage. Education is perceived as an indicator of skill. The higher an individual's level of education, the greater his level of skill and thus higher his earning potential. As a result, difference in access to education to the rich and poor, or across gender and race, religion etc is also considered a source of income inequality.
- **Technology Upgradation** - Another cause for income inequality is technological advancement. Since any development in the technology sector mostly focuses on automation of activities, it usually results in the elimination of unskilled and low skill labourers, whose job is either made redundant by machines or requires an upgrade in skill level to be done more efficiently. As a result, those with lower skill and no means of obtaining higher education are often left unemployed while there is an increase in demand for skilled labour who reap all economic benefits when their firms do well and drive economic growth.

- **Government Policies** - While the purpose of government intervention in an economy is to create an equitable distribution of economic benefit through creation and implementation of taxation policies, subsidies and other laws that benefit the poorer sections of the population, often governments end up creating the opposite impact. Countries often face wide income disparity due to uneven collection of tax from the rich and poor, with the poorer having to pay more while the rich enjoy various kinds of rebates. Laws too, most of which focus on deregulation of labour also tend to increase disparity. Their main focus is often to break down unionisation, which strips low and unskilled labour of their power to negotiate their contracts and income, leaving them mere casual labourers in the informal sector. Oftentimes when policies are formulated with a capitalist mindset, greater power lies with big corporations and the rich who invest their money in them. As a result, at times of economic hardship, the initial response of the government is to save the rich, as they are the primary driving force of the economy. Such biased policies, which do not provide additional support to the lower income level groups or don't offer at least equal help to all sections of the society, can also be a cause for income inequality.
- **Access to Financial Services** - Access to financial services and institutions can also sometimes play a pivotal role in income equality. While lending by commercial banks is often helpful in reducing inequality, as it can be regulated and directed to sectors and segments of the society who are most urgently in need of finance, market based financing often tends to have the opposite impact. Participants in the latter constitute largely of the rich, and to some extent the middle class segment of the population, who have some source of wealth. As a result, even the benefits of this financing, no matter how widespread, are restricted only to the above mentioned group of people. The income from interest earned on loans, dividends earned on shares purchased and returns on investments in large corporations are exclusively shared among the rich without tricking down to the lower rungs of society. Moreover, market based financing, not balanced with lending by commercial banks creates a capitalist economy, where investment is made in goods that can reap maximum profit rather than social benefit. As a result, investment in goods that benefit the poor often takes a backseat.

Wealth reflects savings. It is the accumulation of an individual's assets, returns on investments and savings from income. Even if one assumes that the rich and poor consume and save their incomes in the same proportion, the absolute value of savings for the richer households will far outweigh the poor. In reality, the rich save in a proportion greater than the poor as they have a larger income left after expenditure on necessities. A greater income implies greater savings and greater savings reflect higher wealth accumulation. This is often the reason most countries around the world experience a greater wealth inequality as compared to income inequality.

On the other hand, consumption inequality is usually always less severe than income inequality. This is because, some level of consumption is always required to be undertaken by an individual, irrespective of his level of income. This is expenditure on essentials such as food, water, basic clothing and cooking fuel. Individuals with lesser income simply consume a greater proportion of their income than the national average and save less, while those with no income are often forced into debt.

Another impact of economic inequality is social incoherence. Social Cohesion is the extent of solidarity a community or society feels for its other members. With rising levels of economic inequality, the level of trust between members of the society gradually fades and erodes. This leads to increased incidences of violence, rebellions and social conflict which eventually hamper the growth of the economy.

Economic inequality also has an impact on the health of an economy's population. Health is a factor of an individual's quality and standard of living. Those capable of eating healthy and nutritious food, or at least filling their stomachs, and have access to clean drinking water, those able to afford proper clothing, live in areas that are regularly cleaned and sanitised are better suited for maintaining good health than those who can't. For a country with high levels of income inequality this translates to a greater part of the population who cannot work well because of substantial health issues such as cholera, typhoid, food poisoning and malaria. Inability to work due to poor health further contributes to an increasing income divide.

Causes of Economic Inequality in India

The extent of economic inequality in India in terms of income and wealth has already been explored previously in the chapter. There are various social causes that have cultivated this inequality in the country.

- **Geographical Location** - Even now, almost 66% of India is still largely rural, which houses more than 64% of the country's total population. This rural population is at a significant disadvantage as compared to the rest of the country because of its lack of opportunities, infrastructure and facilities. As stated in an article published by the NCBI, India's present health scenario is a toxic combination of uneven quality, high cost, frequent errors and limited access for marginalised population. Only 13% of the rural population has access to primary health care centres, 33% to sub centres and only 9.6% to a hospital. However, the quality of service provided at these state run facilities is considerably poor. Almost 70% of the rural population has no access to specialist healthcare as over 80% of the country's specialists reside in urban areas. As a result, poorer health in rural areas often drives down the rural population's ability to earn income. Rural areas also lack adequate employment opportunities. Most of India's rural population is engaged in farming and other agriculture related activities. However, most of this population, while seemingly employed, faces a problem of disguised unemployment. This refers to a situation when more than required number of personnel work the same job, making the contribution of the additional workers negligible. Creation of additional employment opportunities would not only provide rural households with alternative sources of income other than farming, but would also increase the wage rate for farm labour with a significant reduction in their supply. As a combined result of all this, the average urban settler earns twice as much as someone living in a rural area.
- **Gender** - Women are at a disadvantage when it comes to economic equality. More than 75% of India's workforce consists of men, who earn, on an average, 23% more than women. This could largely be attributed to the patriarchal mindset in India and the lack of adequate resources and facilities for women in the workspace. Many households actively dissuade women from pursuing higher education or entering the workforce as they consider both to be an unnecessary act for a woman. They are of the mindset that a woman is best as a housewife and nothing else. The women that do enter the workforce, often have to face discrimination at work, especially in promotions as they are believed to be unable to contribute fully to their jobs due to familial responsibilities. Women's safety too raises a concerning issue. Women are often harassed at work and sometimes refuse to work late for fear of being assaulted on their way back home. Women also have unequal access to finance and financial knowledge. While only 20% women do not have any bank account in India, the funds deposited in them are usually not under their direct control. They are often controlled and managed by the men in the family, who use them for their own benefit, rather than the women.
- **Informal Working Sector** - More than 92% of India's workers are part of the informal sector and receive no benefits such as pension, gratuity or provident fund nor do they have a formal contract of employment, implying they have no job security. There is a significant gap in pay for workers in the informal sector, compared to the formal sector with the same skill, for the same work. This wage gap increases as the level of skill required for the job decreases, which means that even among those working the least paid jobs, workers in the informal sector earn even less, contributing to economic inequality.

Other Factors that have Contributed to India's Income Inequality Include

- **High demand for Low Skill Labour by Foreign Corporations** - India is often called a cheap source of labour, and has attracted numerous multinational corporations to set up their manufacturing units and customer care services on the basis of the same. While this has significantly helped reduce the unemployment rate in India, it has simultaneously also degraded the quality of employment in the country. During the period of deregulation and liberalisation undertaken by the Indian government in 1991 to integrate the economy better with the world economy, the labour laws too were relaxed to promote India as a suitable destination for Foreign Direct Investment. This included the informalization of the working sector. As a result, even though work was available, it was mostly intermittent and casual. Moreover, these MNCs created opportunities for low and unskilled workers, who were continuously replaced due to technological advancements and automation of jobs. As a result, the job opportunities available for the unskilled have always been highly non-rewarding in terms of income.
- **Taxation Policy** - As has already been stated above, India faces severe wealth inequality which is only expected to rise over the next five years. One reason for the same could be the government's tax regime. Up until 2015, the last existing wealth tax rate was 1% on net wealth

exceeding Rs 3 million, but was replaced with an additional 2% surcharge on the super rich whose earnings are greater than Rs 10 million annually. On the other hand, multiple studies allege that the wealthy underreport their income, giving them an unfair advantage over the rest of the population. According to a paper published by the Delhi School of Economics, titled 'Do The Wealthy Underreport their Income?' The total income reported by the wealthiest 0.1 percent of families is only about a fifth of the returns from their capital, and at least 80 per cent of their capital income goes unreported in the income tax returns. It further went on to show the wealthier a household, lesser is the income disclosed by it relative to its wealth. The Income tax is a far bigger burden on the poor as compared to the rich on the proportions of their income. Furthermore, over the last decade, there has been an increase in share of direct and indirect taxes in the economy coupled with a decrease in the rate of corporate taxes.

Conclusion

Over the years, India has experienced significant economic growth and has been a firm believer of the 'trickle down theory' of distribution of benefit from the growth. However, empirical evidence suggests a completely different reality than what was expected. The benefits of India's stellar economic growth are not showing in the lives of its poor and it is only the rich who are getting richer. India needs to implement significant changes for ensuring a more equitable distribution of opportunity, which would gradually facilitate equality in income as well as wealth. First and foremost, India needs to improve the standard and access of its education and health services to the poor. The two form the most crucial building blocks of human capital in any economy, whose quality is directly proportional to the level of income an individual earns. Secondly, there should be greater emphasis on wealth taxes, such as capital income taxation, net wealth taxation, and transfer taxation (inheritance tax, estate tax, and gift tax). These would generate tax revenue that could allow greater investment in health, education and infrastructure, all of which would create greater equality of opportunity. This will also strengthen the foundations for a more dynamic economy as these would be investments in raising the overall growth potential. Thirdly, India should focus on strengthening its social security nets for the poor and vulnerable. They should focus on providing them with viable employment opportunities, an income allowance for some time in the event of losing a job to ensure sustenance and providing health insurance to the poor so they can afford the treatments they require without accumulating debt or going bankrupt.

India has a long way to go before it achieves income inequality and might even transition to the 4th largest GDP in the world before it becomes a state with equitable distribution. However, the effort to reduce economic inequality must begin now, before the gap increases to irreparable distances and becomes a cause of social unrest and agitation within the country.

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