

Quadrant II – Transcript and Related Materials

Programme: Bachelor of Arts (Third year)

Subject: Economics

Paper Code: ECD 111

Paper Title: Growth and Development Paper I

Unit: 1

Module Name: Measures of Income Inequality

Module No: 3

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Notes

In this module we are finding the impact of rural migration on urban unemployment. Income inequality is the unequal distribution of household or individual income across the various participants in an economy. Income inequality is often presented as the percentage of income to a percentage of the population.

Simon Kuznets put forward the hypothesis that relationship between per capita national income and the degree of inequality in income distribution. Comparing highest earning households (usually defined by the upper 20%) and the income going to the lowest-earning households lowest 40% of income. The Kuznets ratio is a measurement of the ratio of income going to the highest-earning households (usually defined by the upper 20%) and the

income going to the lowest-earning households which is commonly measured by either the lowest 20% or lowest 40% of income. Comparing 20% to 20%, a completely even distribution is expressed as 1; 20% to 40% changes this value to 0.5.

It was developed by Max O. Lorenz in 1905 for representing wealth distribution. Graphical representation of an economic inequality model.

The curve is a while taking the population percentile on the X-axis and Cumulative wealth on the Y-axis. Complementing this graph would be a diagonal line at 45° angle from the origin (meeting point of the X & Y axis) indicating the perfect income or wealth distribution among the population.

As we can see, there are two lines in the graph of the Lorenz curve, the curved red line, and the straight black line. The black line represents the fictional line called the line of equality i.e. the ideal graph when income or wealth is equally distributed amongst the population. The red curve, the Lorenz curve, which we have been discussing, represents the actual distribution of wealth among the population. Diagonal line at 45° angle from the origin (meeting point of the X & Y axis) indicating the perfect income or wealth distribution among the population. The further away from the diagonal line, the more unequal the size of the distribution of income.

Gini Coefficient: The Gini Coefficient, which is derived from the Lorenz Curve, can be used as an indicator of economic development in a country. The Gini Coefficient measures the degree of income equality in a population. The Gini Coefficient can vary from 0 (perfect equality) to 1 (perfect inequality). A Gini Coefficient of zero means that everyone has the same income, while a Coefficient of 1 represents a single individual receiving all the income. Gini Coefficient = $A_1 / (A_1 + A_2)$