Exercise walk-through

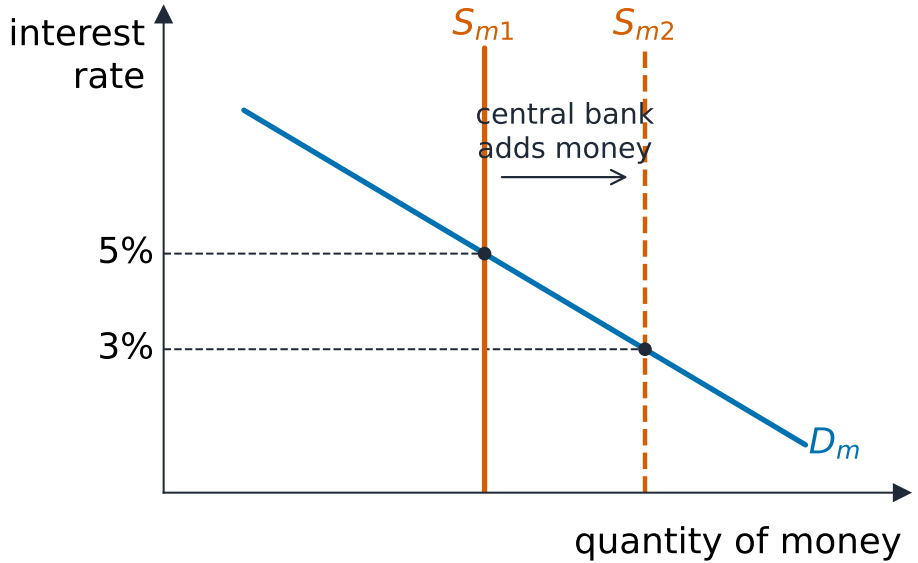
4.5
Economics of inequality and poverty

International Baccalaureate · IB Diploma · Economics · SL

The economics of inequality and poverty

- **Absolute poverty** : **income** too low to buy basic needs. The World Bank's international poverty line is 3.00 US dollars a day per person (at 2021 PPP prices).
- **Relative poverty** : income far below others in the same country, often below 50% or 60% of the median income.
- The **Multidimensional Poverty Index** (MPI) counts lack of health, education and living standards (such as clean water, electricity and cooking fuel), not only income.

Figure: Monetary policy



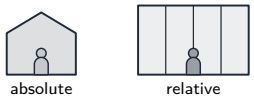
- More **money supply** lowers the equilibrium interest rate
- Read the axes and units first.

Sources for this lesson

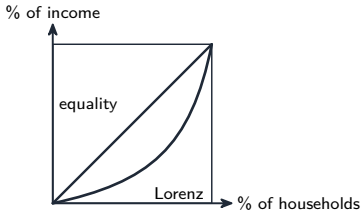
- International Baccalaureate, *Economics guide* (first assessment 2022).
- US Bureau of Labor Statistics, *The Employment Situation* (April 2020) and ***Consumer Price Index*** (June 2022).
- Board of Governors of the Federal Reserve System, FOMC statements, March 2022 to July 2023.
- International Monetary Fund, *World Economic Outlook* database.

Exercises 2.1·2.2

2.1 Distinguish between absolute poverty and relative poverty. [2]

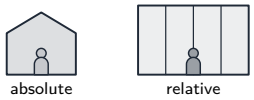


2.2 State what a Gini coefficient of 0 and of 1 would show. [2]



Exercises 2.1·2.2

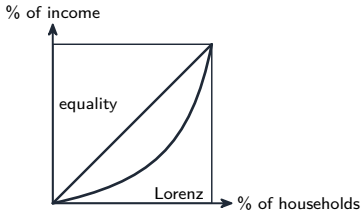
2.1 Distinguish between absolute poverty and relative poverty. [2]



2.1

absolute poverty: income too low to meet basic needs such as food, water and shelter; relative poverty: income well below the average or median income in a country

2.2 State what a Gini coefficient of 0 and of 1 would show. [2]



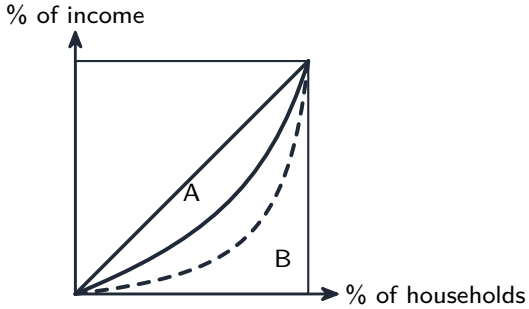
2.2

0: perfect equality: every household has the same income; 1: perfect inequality: one household has all the income

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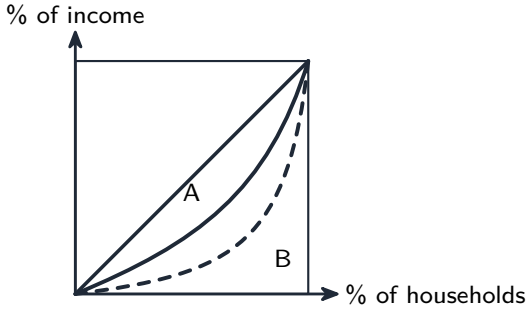
Exercise 2.3

2.3 Explain **two** reasons why the Lorenz curve of a country might move further from the line of equality. [4]



Exercise 2.3

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2.3

any two, explained: technology raises the pay of high-skilled workers relative to low-skilled; cuts in progressive taxes or benefits mean less redistribution; rising returns to capital and property increase incomes of the wealthy; weaker unions / falling real minimum wage

Exercise 3.1 (a)

3.1 A country's Gini coefficient has risen from 0.32 to 0.41 in 20 years.

(a) Describe what has happened to income distribution. [2]

Exercise 3.1 (a)

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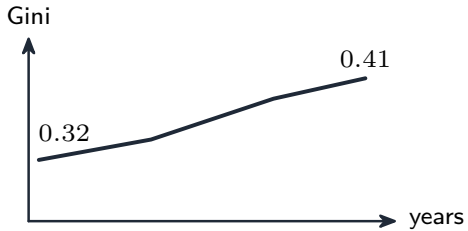
(a) Describe what has happened to income distribution. [2]

(a) income has become more unequal; a larger share of income goes to the richest households

Exercise 3.1 (b)

3.1 A country's Gini coefficient has risen from 0.32 to 0.41 in 20 years.

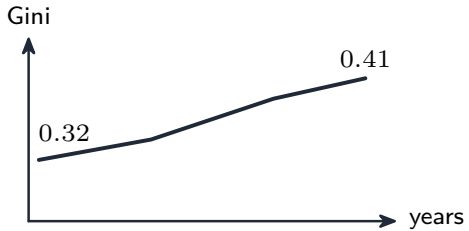
(b) Evaluate the use of transfer payments to reduce income inequality. [6]



Exercise 3.1 (b)

3.1 A country's Gini coefficient has risen from 0.32 to 0.41 in 20 years.

(b) Evaluate the use of transfer payments to reduce income inequality. [6]



(b) transfer payments (pensions, child benefits, unemployment benefits) raise the incomes of the poorest directly; they reduce poverty quickly and support spending (AD); but they are costly, with an opportunity cost for other spending, or need higher taxes; a poverty trap if benefits are withdrawn as earnings rise, reducing the incentive to work; they treat the symptom, not the causes such as low skills; judgement: needed in the short run, best combined with education and training