BOX 2.2

What is happening with global income inequality? Grotesque levels, ambiguous trends

Human Development Report 2002 noted that while the definition of global income inequality is fuzzy and its trends ambiguous, there is widespread consensus on its grotesque levels. This has not changed. Incomes are distributed more unequally across the world's people (with a Gini coefficient of 0.66) than in the most unequal countries (Brazil, for example, has a Gini coefficient of 0.61). (The Gini coefficient is a measure of income inequality that ranges between 0, indicating perfect equality, and 1, indicating complete inequality.) The richest 5% of the world's people receive 114 times the income of the poorest 5%. The richest 1% receive as much as the poorest 57%. And the 25 million richest Americans have as much income as almost 2 billion of the world's poorest people (Milanovic 2002, pp. 51–92).

Monitoring and containing income inequality are essential not only to increase opportunities for as many people as possible, but also to reduce social friction in areas (usually urban) with high inequality. As globalization deepens and access to information becomes cheaper and more widely available, awareness of global inequality is increasing. People no longer compare themselves only to their fellow citizens: they are also aware of international gaps, making divergence across countries increasingly harmful—and dangerous. To reduce growing tensions, it is crucial that the tide of development lift all boats.

Findings on global inequality vary considerably depending on the approach used to analyse it. Inequality can be calculated across countries (using average national incomes), across the world's people (regardless of national boundaries) and across people within countries.

Inequality across countries

International inequality is generally measured by comparing national per capita incomes. Countries with the highest per capita incomes in the early 1800s are still today's richest countries, indicating persistence in the structure of international inequality.

In 1820 Western Europe's per capita income was 2.9 times Africa's—and in 1992, 13.2 times (Maddison 2001). In the 1990s per capita incomes increased slowly but steadily in high-income OECD countries, but many transition countries in Central and Eastern Europe, particularly the CIS, many parts of Sub-Saharan Africa and some countries in Latin America and the Caribbean experienced economic stagnation. At the same time, highly populated developing countries such as China and India achieved rapid growth.

As a result per capita incomes have been converging in rich countries, while in developing countries the pattern is mixed. But when income data are weighted by population—to capture the relative importance of each country's performance—average incomes across countries appear to be converging. Highly populated developing countries drive such trends: fast-growing China and India are catching up with parts of the industrialized world, such as North America and Western Europe.

Inequality across the world's people

Some studies have tried to capture trends in true global inequality—that is, the distribution of income across citizens of the world, regardless of national borders. Income surveys suggest that when measured this way, global inequality increased between 1987 and 1998. The main forces behind this divergence were:

- A widening income gap between the poorest and the richest people due to slow growth in rural incomes in populous Asian countries relative to rich OECD countries.
- Faster progress in urban China relative to rural China and to India.
- Shrinkage in the world's middle-income group (Milanovic 2002, pp. 51–92).

But these conclusions are not entirely robust due to the limited timeframe covered and the use of purchasing power parity (PPP) rates, which are often unsuitable and do not accurately reflect international price differences (see box 2.3).

Using alternative methodologies, other analysts have reached more optimistic conclusions suggesting convergence in global individual incomes: that after peaking in 1970, the gap in 1995 had returned to the level in 1950 (Dollar and Kraay 2002, pp. 120–33; Bhalla 2002; Sala-i-Martin 2002). A driving factor in this debate is the measure of inequality used to draw conclusions. When measured using single summary indicators such as the Gini coefficient, incomes appear to be converging. (Because of the Gini coefficient's construction, it gives more weight to middle-income groups and less to the extremes.) Still, in recent decades there has unquestionably been a widening gap between the incomes of the very richest and the very poorest.

Inequality across people within countries

National income inequality is the concept used for country-level analysis. This concept is suitable for analysing the correlation between a country's policies—typically economic openness or redistribution measures—and its distribution of income.

In many countries inequality in assets and especially income appears to be on the rise. Numerous studies have tried to capture trends in income distribution over time across large samples of countries. Cornia and Kiiski (2001) estimate that between the 1980s and the mid- to late 1990s inequality increased in 42 of 73 countries with complete and comparable data. Only 6 of the 33 developing countries (excluding transition countries) in the sample saw inequality decline, while 17 saw it increase. In other words, within national boundaries control over assets and resources is increasingly concentrated in the hands of a few people.

Though not the case for all these countries, in many inequality began increasing during the debt crisis of the early 1980s (Kanbur and Lustig 1999). Since then inequality has soared, particularly in the Commonwealth of Independent States (CIS) and south-eastern Europe. And in many Latin American countries inequality remains extremely high. If sharp increases in inequality persist, they may have dire effects on human development and social stability (including violence and crime rates; see Fajnzylber, Lederman and Loayza 1998 and Bourguignon 2001).

Source: Ravallion 2002; Schultz 1998, pp. 307–44; Korzeniewicz and Moran 1997, pp. 1000–39; Sprout and Weaver 1992, pp. 237–58; Maddison 2001; Milanovic 2002, pp. 51–92, 2003; Dollar and Kraay 2002, pp. 120–33; Kanbur and Lustig 1999; Bhalla 2002; Sala-i-Martin 2002; Cornia and Kiiski 2001; UNDP 2002e; Fajnzylber, Lederman and Loayza 1998; Bourguignon 2001.