

# DISTRIBUTION OF INCOME AND WEALTH

# 11

## MULTIPLE CHOICE

- |      |       |       |       |
|------|-------|-------|-------|
| 1. A | 6. D  | 11. B | 16. D |
| 2. B | 7. C  | 12. C | 17. D |
| 3. D | 8. B  | 13. A | 18. C |
| 4. A | 9. A  | 14. C | 19. C |
| 5. C | 10. C | 15. A | 20. C |

## SHORT ANSWER QUESTIONS

### Question 1

(a) Gini Coefficient =  $\frac{A}{A+B}$

(b) Gini Coefficient =  $\frac{A}{A+B}$   
=  $\frac{30}{30+75}$   
= 0.29

(c) The Lorenz curve would shift to the left towards the line of perfect equality.

(d) An answer to this question may include any three of the following:

- Those who are employed in production receive wages in exchange for their labour.
- The self-employed and business owners receive profit in exchange for their entrepreneurial skill.
- Those who lend money to others receive interest in return for providing capital.
- Land-owners receive rent in exchange for the lease of their land.
- Those who meet certain criteria, such as unemployment or disability, will receive income from government transfer payments.

(e) Age is a key factor determining income, with young people receiving the lowest income of all age groups. Aboriginals and Torres Strait Islanders suffer from the lowest income levels amongst ethnic groups, receiving significantly lower income than non-indigenous Australians. Single parent families receive the lowest income of all family structures. In terms of gender, women still tend to earn lower wages than men, receiving two-thirds the male wage on average.

**Question 2**

- (a) Income is the funds that flow to an individual or household in return for their contribution to the production process. This differs from wealth, which is a measurement of the stock of assets owned by an individual or household at a particular point in time.
- (b) Those individuals receiving a higher income have a greater capacity to accumulate assets and so create wealth. These assets may then generate income for the individual, such as a stock of savings that generates income. As a result, wealthy individuals tend to receive a higher income.
- (c) Despite a slight reduction in Australia's Gini coefficient from 2000-01 to 2002-03, Australia's long-term trend is towards increasing inequality in the distribution of income from the mid-1990s to the early 2000s. The two bottom quintiles have experienced the greatest decrease in their income share while the highest quintile's share has grown.
- (d) Unemployment is a key factor contributing to income inequality, as this unemployed must rely on government benefits for income. These benefits are often set below wage levels to maintain the incentive to work. As a result, income inequality will increase during periods of high unemployment.

**Question 3**

- (a) An answer to this question may include any two of the following:
- Social class divisions between high and low income earners may result from inequality, creating tension and social instability.
  - Income inequality may result in high levels of relative poverty, which can constrain economic opportunities and perpetuate existing inequality.
  - Inequality may result in higher levels of crime as individuals seek to improve their economic situation through illegal means.
  - Income inequality may result in psychological problems such as depression, suicide and family breakdown for those overwhelmed by their economic situation.
- (b) Income inequality provides an incentive for lower income earners to work harder in order to improve their living standards. It will likewise encourage individuals to invest in education and training to improve their earning potential, provided affordable training options exist. The potential for higher incomes also promotes labour mobility, though this may disadvantage certain regions deprived of skilled labour. As high-income earners have a higher marginal propensity to save, inequality may increase the national savings rate.
- (c) On a cyclical level, expansionary macroeconomic policy can reduce income inequality through stimulating aggregate demand and job growth. As low income earners tend to be borrowers while high income earners are savers, lower interest rates will reduce inequality as it lowers the return on capital while reducing debt-servicing payments. From a structural point of view, fiscal policy can address inequality through a progressive taxation system and transfer payments which redistribute income to the unemployed.