THE IMPACT OF INCOME INEQUALITY ON THE NIGERIAN ECONOMY

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Abstract

The study is a theoretical discus of the impact of income inequality on the Nigerian economy. Income inequality is the bane of most socio-economic problems in Nigeria. It has resulted most recently in militancy in the Niger-Delta, which has caused threat to our political stability and thus divesting in the country. Other ills include social problems like alienation leading to crime; vandalism and rioting; increased financial crimes among youths and even public office holders; incessant industrial actions; unequal assess to opportunities, discouragement of certain basic norms like trust and commitment, thereby increasing business risk and increased cost of contract enforcement; as well as unnecessary educational expansion. Proper educational funding to reduce the expenses of the poor on education, ban on large political donations, equal anti-corruption measures and provision of social infrastructures in the rural areas amongst others were given as the way forward for Nigeria, the giant of Africa.

Introduction

Income inequality is the difference in per capita income of household incomes across populations within or across countries. There has been rising concern about the relationship between income inequality and economic development of developing countries. This is probably due to the fact that development efforts that neglect income inequality issues are dampened by same. There is a sure link between inequality, growth and poverty reduction but this paper is not set to provide the link empirically.

Todaro and Smith (2005) define income inequality as the existence of disproportionate distribution of total national income among households whereby the share going to the rich persons is far greater than that going to the poorer persons. This is largely due to difference in amount of income derived from ownership of property and to a lesser extent, the result of difference in earned income.

Income inequality affects economic development through such channels as the political economy, credit market imperfections, socio-political instability and human fertility/reproduction. Income inequality is affected by level of corruption, human and natural resource endowment, sectoral allocation of manpower, level of economic development and the size of government subsidies.

Nigeria, a country with increasing population, staggering per capita income, widening income disparity within and between the poor and the rich has to deal decisively with the issue of income inequality if the efforts at economic advancement are to make positive impact. Nigeria is among the first twenty countries in the world with the widest gap between the rich and the poor and this may be the reason why even the genuine efforts at development seems not to proffer solutions to issues like unemployment, corruption, youth restiveness, prostitution amongst others.

The problem of development has drawn the attention of scholars and government as well as international organizations over the years. With the recent world economic meltdown, a lot of sustained developmental efforts have to be put in place by every nation. Development of an economy connotes a multidimensional process involving major changes in social structures, political attitudes and national institutions as well as acceleration of economic growth; the reduction of inequality and eradication o absolute poverty (Lane and Erssons, 1997). It means a qualitative and quantitative stability, advancement and progressing towards attainment of social, political and economic aspirations.

Development must be sustained or rather self-sustaining whether for the developing or developed economies. Inspite of the disparities in perspectives of development, there is a general consensus that development will cause good changes manifested in increased capacity of people to have control over material assets, intellectual resources and ideology; obtain physical necessities of life; employment; gender equality; education to mention a few.

The remaining part of this paper is set to look at the measures of inequality; negative effects of income inequality; effects of inequality on Nigeria and lastly provides the way forward for Nigeria.

Measuring Inequality

While not taking too much time and space, it is important to review various ways in which inequality can be measured. These methods can be grouped according to Todaro and Smith (2005) into

- Variance method
- Axiomatic approach
- Stochastic dominance approach

The variance is the simplest measure of inequality. It is scale-dependent. The axiomatic approach defines a set of axioms that an appropriate measure must conform to. These axioms are

a. Piguo-Dalton transfer principle which says a transfer from a poorer to a richer person should register as a rise in inequality and vice versa for transfer from rich to poor.
b. Income scale independence which requires that if an individual's income changes by the same proportion then inequality should not change.
c. Principle of population which requires that a merger of two identical distributions (or populations) should not alter inequality.
d. Anonymity which requires that the inequality measure be independent of individual characteristics other than their income.
e. Decomposability which requires that if inequality rises amongst each subgroup of the population then overall inequality should rise.

The stochastic dominance approaches are of three types namely

a. The 1st order stochastic dominance
b. The 2nd order stochastic dominance
c. Mean-normalized 2nd order stochastic dominance

The 1st and 2nd order stochastic dominance are actually for ranking social welfare because they are sensitive to the mean of the distribution. The mean normalized 2nd order stochastic dominance compares the Lorenz curves of two distributions drawn from the same population. However the most popular measure of inequality uses the Gini coefficient (Lorenz curves).

Negative Effects of Income Inequality

Classical Economists were in favour of income inequality. They felt income equality discourages savings as higher income for the working class will raise their consumption level which will further lead to a rise in population. The Classicals believed therefore that inequalities in income were necessary to provide the needed incentive for economic growth. Keynes however opined that inequality will reduce the consumption capacity and contract demand causing secular stagnation, leading to a fall in production and a slowing down of economic stability. (Jhingan, 2005).

Inequality which was previously conceived as occupying the cold periphery of economic analysis, has been revived as a discus which if neglected, would destroy developmental efforts in Least Developed Countries (LDCs). Income inequality has a number of negative effects as sited in literature and some of these are true for Nigeria.

Inequalities of opportunities is the first effect of income inequality. This happens overtime and across generations and through economic, political, social and cultural mechanisms, have hampered the development objectives of nations across the globe. For example a girl child born into a poor family in LDCs is very likely to end up illiterate, unemployed and given out in early marriage!

The inequality of income across the globe is seen in the UNDP (1998) report which documented that the three richest people (Bill Gates, Paul Allen and Warren Buffet) have assets totally US $156 billion which exceeds the combined GDP of the 48 least developed nations of the world! Poverty is exacerbated by income inequality through inequality in opportunities.

Inequality exists both between the poor as well as between those above the poverty line. Extreme income inequality leads to economic inefficiency. This is partly because at any given average income, the higher the inequality, the smaller the fraction of the population that qualifies for credit. (Todaro and Smith, 2005). This further deprives the poor of education and development of their human capital which could break off the vicious cycle of poverty in which they are locked. This induces the poor to forgo human capital investments even if such investments offer high rates of return. Thus, high income inequality lowers the stock of human capital in an economy.

High inequality affects the overall rate of savings in an economy negatively. Saving out of marginal income is common among the middle class as rich elites spend much of their income sustaining a luxurious lifestyle especially through purchase of imported luxury goods. This does not add to the nations resources.

Growing income inequalities is opportunistic. It perpetuates the vested interests and maintains the *status quo* of the economic and political elites of developing nations at the expense of a greater majority of the population.

Inequality leads to an inefficient allocation of assets. It draws unnecessary emphasis on higher education (as in the case of Nigeria) at the expense of quality primary education. This in turn begets more income inequality.

Extreme income disparities undermines social stability and solidarity. High inequality strengthens the political as well as economic bargaining power of the rich. Among the rich, high inequality facilitates rent seeking including actions such as excessive lobbying, large political donations (which 'tie' the hands of true democracy), bribery and cronyism; diverting resources from productive purposes that could lead to faster economic growth. Among the poor, high inequality may lead the poor to support populist policies that are self-defeating. (Bourguignon and Morrison, 1998).

With high inequality, the focus of politics is to redistribute the existing national economic pie rather than on policies to increase its size. This increases crime, social unrest and political instability.

Reducing relative poverty should be a goal of government. Inequality can often be a cause of social problems like alienation leading to crime, vandalism and rioting. It also results in inequalities of opportunities as discussed earlier. Those in low income are often unemployed and lack education and skills.

High inequality threatens the political stability of a country as more people are dissatisfied with their economic status. This goes down to increase the risks of investing in a country and so, its development potentials are undermined.

High inequality limits the use of important market instruments like changes in prices and fines. In the face of inequality, a slightly higher rate of say electricity bill, causes deprivation amongst the poorest citizens.

High inequality may discourage certain basic norms of behavior such as trust and commitment among economic agents. With this comes higher business risks and higher costs of contract enforcement. (www.economicshelp.org, 2007)

As earlier stated some factors cause inequality in income. They include

* Human and natural resource endowment

  Bourguignon and Morrison (1998) showed that the share of skilled workers in total labour force and availability of land resources exert significant income equalizing effects thereby reducing level of inequality.

* Corruption

  The benefits from corruption accrue to the well-connected at the expense of the poor. Anti-corruption measures tend therefore to reduce inequality where they are sincere and effective.

* Fiscal actions

  Fiscal actions include expansionary and Contractionary fiscal policies of government. Contractionary fiscal policies (like tax increase) increases the level of inequality as the income of the poor is further reduced.

Effects of Income Inequality on Nigeria

The high level of inequality is evident in every facet of the Nigerian economy. It has resulted amongst other in

i. high level of financial crimes in a bid to meet up with the Joneses.
ii. unnecessary educational expansion
iii. Niger-Delta militancy resulting from neglect of oil producing areas while government officials have expensive fun-packed parties which are shown on air while the poor are left to die of starvation.
iv. strike actions embarked upon by various trade unions and incessant agitation for salary increase because the politicians are having almost every share of the national cake.
v. corruption and inflation of contract figures at all levels of government.
vi. unequal social and infrastructural development where oil wealth is used to develop non-oil producing areas leaving the producing areas to rot with bad roads, no good water and no employment for the teeming population.
vii. unequal life expectancy at birth which ranged between 36.6 in Kaduna and 61.4 in Lagos as at 1997.
viii. unequal educational attainment ranging between 1.9% in Sokoto state and 51.7% in Imo state as at 1997.
ix. human capital flight (migration) in search of greener pastures. Migrants are ready to be locked in metal containers and carried across the high seas just to be away in another land where they feel there are equal opportunities. This has led to brain drain at all levels work status.
x. development of slums and ghettos in cities.

The Way Forward

a. The fight against corruption by the Economic and Financial Crimes Commission (EFCC) and Independent Corrupt Practices Commission (ICPC) should be thorough and free from political and social class bias. Their activities should be void of governmental interference.
b. Social infrastructures should be provided in the rural areas to stern the tide of rural-urban migration which aggravate social vices in the urban centers.
c. Public institutions of higher learning should be well funded so as to reduce fees paid by the poor who cannot afford private institutions. It will also curb strike actions by workers in these sectors.
d. Jobs should exist irrespective of educational attainment of the individual. This will remove unnecessary educational expansion for example, where a cleaner or office messenger has to have a first school leaving certificate does not arise until the government is sure that that generation of people are out.
e. The government can stand as guarantors for the poor to get loans for education and provide job for same to offset the loan after graduation.
f. To remove the incidence of tying the hands of true democracy, huge political donations must be banned in Nigeria.
g. Policies that encourage low number of births per family should be put in place. For example, special scholarships can be given to children from small but poor families.
h. To curb incessant strike actions, the salary structure of political office holders should be relatively fair compared to other government workers. This will also curb the excesses of such political office holders.

Conclusion

Inequality in income is not a stimulant to growth as the Classicals claimed. It is a cankerworm which if left unattended, renders developmental efforts of governments useless. Income inequality is heightened by corruption, poor governance and mismanagement of public funds in Nigeria.

In Nigeria, inequality has led to incessant industrial actions by trade unions in the form of strike actions, militancy in the Niger-Delta, increased level of financial crimes, human capital flight, unequal social indices and unnecessary educational expansion which has led many to look for certificates at all cost even for non-existent jobs.

The fight against corruption at all levels is needed to reduce income inequality while encouraging economic growth. The exuberance of public office holders needs to be checked while discouraging the younger generation from such luxurious lifestyles at the expense of their fellow countrymen.

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