

Precision – **Equity vs. equality**

An 'equitable distribution of income' does not necessarily mean that everyone receives the same income. Rather, it means that income is distributed in a way that is considered fair or just according to societal values.

This distinction requires understanding the difference between equity and equality.

- **Equality** means that everyone receives the same share of income, wealth, or resources regardless of their circumstances, efforts, skills, or needs.
- **Equity** means that income is distributed according to some conception of fairness. This may involve unequal incomes if those differences are considered justified. An equitable distribution can, therefore, contain substantial inequality if society judges that inequality to be justified.

To determine what degree of (in)equality can be considered just, economists weight multiple concerns:

Substantial equality is beneficial, because it:

1. **Reduces poverty.**

A more equal income distribution can reduce the number of people living below the poverty line. Many people consider this fair because all members of society should be able to meet their basic needs, such as food, housing, healthcare, and education. If some individuals lack access to necessities while others enjoy extreme levels of wealth, the distribution of income may be viewed as inequitable. Reducing poverty therefore promotes both higher living standards and a greater sense of social justice.

2. **Improves equality of opportunity.**

Greater equality can help ensure that life chances depend more on talent, effort, and personal choices than on family background or inherited wealth. Many people regard this as fair because individuals do not choose the circumstances into which they are born. When access to quality education, healthcare, and opportunities is determined primarily by parental income, outcomes may reflect privilege rather than merit. A more equal distribution of income can therefore create a fairer starting point while also allowing the economy to make better use of its human resources.

3. **Increases human capital.**

When lower-income households can afford education, training and healthcare, the quality of the labour force improves. This can increase labour productivity, innovation and long-run economic growth. Thus, equality may contribute not only to social objectives but also to economic efficiency.

4. **Improves marginal utility of income.**

A rise in income will generate a large increase in utility for a poor household and a relatively small increase in utility for a very wealthy household. Therefore, transferring income from high-income to low-income groups may increase total welfare in society. This forms the basis of many arguments for progressive taxation and redistribution.

5. Reduces social problems.

Economists and policymakers often associate large income inequalities with crime, social unrest, political instability and reduced social cohesion. A more equal society may experience lower enforcement and security costs and greater social trust.

6. Prevents concentration of market power (HL only)

High levels of inequality can lead to the concentration of economic power in the hands of a small number of firms or individuals. Large corporations and wealthy individuals may be better able to influence prices, wages, and market outcomes, reducing the degree of competition in the economy. This may reduce **factor mobility** because lower-income individuals may lack access to education, training, housing, or relocation opportunities needed to move between occupations or regions.

7. Protects democratic processes and social inclusion.

Excessive inequality may allow wealthy individuals and interest groups to exert disproportionate influence over political decision-making through lobbying, campaign financing, media ownership, or privileged access to policymakers. This can result in policies that favour narrow interests rather than the broader public interest.

8. Reduces leakages (HL only).

A more equal distribution of income may increase aggregate demand because lower-income households generally have a higher marginal propensity to consume than higher-income households. Redistributing income towards lower-income groups increases consumption expenditure, causing aggregate demand to rise. This can stimulate economic activity, increase real GDP, and reduce cyclical unemployment.

At the same time, *some inequality can be beneficial* because it:

1. Creates incentives to work

Higher potential earnings encourage people to work harder, work longer hours, acquire skills and accept difficult jobs.

2. Create incentives for education and training

Acquiring human capital often involves substantial costs due to university tuition, foregone earnings and time and effort. Income differentials provide rewards for these investments.

3. Create incentives for entrepreneurship

Entrepreneurs take risks when they create new businesses, develop new technologies and introduce new products. The possibility of earning significantly higher incomes provides motivation for innovation and risk-taking.

4. Encourages labour mobility

Differences in wages can signal where labour is most needed. Income differences therefore help allocate resources more efficiently.

5. Generates savings and investment

Higher-income households generally save a larger proportion of their income. These savings provide liquidity in the money market and enable investment, business expansion and technological development.