World Poverty and Sustainable Development: Poverty measures lecture 3

World Poverty and Economic Development
ECRG 3240 Spring 2013
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Poverty and Inequality Measures

• What is meant by poverty and how is it measured?

• How to best to measure living standards: the “best” poverty measure.

• What about inequality—should we worry about inequality?
Two broad but very different poverty concepts

Absolute Poverty

Absolute deprivation:
less than some physical minimum (malnutrition)
- Poverty line consumption or income constant for long periods of time (50 years in U.S.)
- The U.S., UN, UK and IMF-World Bank use absolute poverty mainly (MDG 1 for example)

Relative Poverty

Relative deprivation:
inequality, not enough compared to others or social norm
- Typically 1/3 of median (middle class income or consumption.
- Europe (the EU & OECD) uses relative poverty measures.
Defining Poverty lines: practical considerations

- **Poverty implies one group needs help** from another to escape poverty, poverty perpetuates poverty, a poverty trap (*education, nutrition, health*)

- **85% or almost everyone may be poor**, but this implies a useless (not practical) poverty line.

- **For example, a $2.50/day PL makes almost 3 billion in** : but this is “too many to help” (TMTH) ...

- **A useful “national” or international poverty rate should be less than a 1/3:** (when poverty falls under 5-10%, just raise the poverty line...)  

- **How high can we go? $2 or $5/day Hans Rosling has a “sustainable development goal” for this long term poverty line, considering climate change...**
A longer View… Poverty reduction is a race between the population non-poor and the poor…

- **Poverty should fall because**, economic growth raises income per person..
- Technical progress helps bring cheaper food and better medicine to the poor, living better on the same income with antibiotics, vaccinations, etc.
- But population growth work against the poverty rate... population growth is faster among the poor...
### Absolute and Relative poverty measures:

**What to take away from Problem set #1:**

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*FGT: Foster-Greer-Thorbeck Index  H can be absolute or relative, depending on how the poverty line is defined*
Step 1: Putting Poverty and inequality trends in Perspective–

- how are the poor doing? How do we decide when someone is poor or not.
- The most widely used international poverty level of income or consumption is $1 per day and $2 per day (roughly).
- Using these conservative cut off points the World Bank estimates about 1.2 and 2.8 million people are poor....
Why is it so hard to reduce poverty....

- **Population growth** is more rapid in poor communities (see the IKEA boxes: ending poverty slows population growth.

- **Poverty Traps**: HIV-aids and Malaria + conflict and war (worse during cold war–1980s Ethiopia, civil war–Famine).

- **Geography**, the resource curse, malaria, Isolation: landlocked with bad neighbors...geographic or political isolation...

- **Conflict & governance**: institutions change slowly, extractive vs. inclusive governments hard to dislodge...
Issues in measuring poverty across countries and over time:


2. Define a poverty line: is poverty absolute or relative? Should the poverty line be fixed, over time, across countries? Or should we look at many poverty lines?

3. Which poverty indicators (example the poverty rate) are best, what are the pitfalls of relying on one indicator?
History of UK poverty is instructive: starting in 1899 with Seebohm Rowntree’s York survey

**Absolute Poverty defined:** In 1899 Rowntree conducted a survey in the village of York. His poverty line started with a minimum diet based on American biologist Atwater’s minimum nutritional requirements:

- Breakfast: porridge and skim milk
- Lunch: bread and cheese  
  Dinner: Soup (very little meat).

**Professor Rowntree**, and then his students went back to York in 1936 and 1951 poverty dropped from 31% to 3%, though 22% still relied on government transfer payments to escape poverty…
1952 UK headline: Labour Party ends poverty in the UK...poverty is no more.

- Based on Rowntree research in York, in 1952 with some fanfare, Britain’s new Labour government declared poverty and destitution defeated in UK—poverty was no more...
- But people in the UK many still thought of themselves as “poor” leading to a long (and ongoing debate) over whether poverty is really relative as opposed to some “absolute” threshold everyone can cross...
- Perhaps poverty is always intrinsically “relative” such that anyone who is “too far” from middle class living standards feels poor, even if compared to the poor in India, one is relative affluent. (see Sen’s “Poor relatively speaking” on the class web page for a very nice overview of this debate...”
Sen’s answer: poverty should reflect absolute deprivation in achievements socially defined

- The standards for poverty remain the same: a socially determined minimum set of achievements or “capabilities:” i.e., attend school, vote, housing, etc.
- The minimum achievements stay the same across nations: what changes in the goods and services required to achieve these minimum social norms (this is why the U.S. poverty line income is $5000, while in poor ctys it is 400.
- Once this social defined minimum standard of living is defined the poverty line should be fixed, absolutely over time.. this is what the U.S. and World Bank do…
- But Europe went to relative poverty rates…(see Francois Bourguignon’s article on “social exclusion”)
In 1776 Adam Smith argued the definition of necessities depends on when and where one lives… our “necessities” may be some one else’s “luxuries” (e.g. togas, vaccines, antibiotics, AZT..)

“By necessaries I understand not only the commodities which are indispensably necessary for the support of life, but whatever the custom of the country renders it indecent for creditable people, even of the lowest order, to be without. A linen shirt, for example, is, strictly speaking, not a necessary of life. The Greeks and Romans lived, I suppose, very comfortably though they had no linen. But in the present times, through the greater part of Europe, a creditable day-laborer would be ashamed to appear in public without a linen shirt, the want of which would be supposed to denote that disgraceful degree of poverty which, it is presumed, nobody can well fall into without extreme bad conduct. Custom, in the same manner, has rendered leather shoes a necessary of life in England. The poorest creditable person of either sex would be ashamed to appear in public without them…”
Three Steps to Measure Poverty

1. Determine how to measure well being:
   – Income or consumption? Pre or post government transfers?
   – Include wealth (education), social networks, human rights?
   – International prices vs. local prices the PPP issue.
   – By individuals or households? equivalence scales

1. Define a poverty Line:
   – Relative Poverty such as 1/3 the median consumption
   – Or Absolute Poverty line such as 2250 calories.
   – Standardizing poverty lines across countries

3. Choose an aggregate Poverty Measure:
   – Incidence: Poverty Rate $H = \frac{\# \text{ of poor}}{\text{total population}}$
   – Depth of Poverty: the Income Gap Ratio or $I$
   – Incidence and Depth: Poverty Gap or $H*I \ p(1)$
   – Severity: “gap-squared” (FGT) or Sen index…or just a lower poverty line (e.g. 75 cents per day)
Four poverty measurement axioms: every absolute poverty measure should:

1. Provide a **comparable measure** of living standards across regions, countries and provinces and over time— to identify the neediest groups -- $ppp$ factors help here.

2. Be sensitive to the **incidence** (how many are poor?) and the **depth** (how poor are they?) of poverty?

3. Be sensitive to **severity** of poverty— are some people really much poorer than others? They need more help.

4. **Rise when the status of the poor deteriorates**, but if nothing happens to the poor population the poverty measure should not change either.
The Headcount Measure (H)

• How many people are poor as a % of the total population? ..the *incidence* of Poverty.

• *Easy to understand but has limitations:*
  – Says *nothing* about the *depth of Poverty*
  – Creates an incentive to help those closest to the line
  – Severely poor could be worse off as poverty falls

• *Measurement Issues:*
  – Households or Persons?: Equivalency Scales
  – Prices/incomes must be comparable– the $ppp issue.
  – Consumption or Income? Capabilities?
  – Surveys or National accounts? A big difference…
Setting a world poverty line:

- The World Bank estimates one billion people still get by on less $1/day ($1 buys about 2250 calories).
- Raising the line to a modest $2/day raises the number of poor to 2.7 billion, about half the people alive today.
- About 70% of these very poor people live in rural areas, and mainly in Africa and Asia.
Why it is hard to reduce poverty

• Population growth is rapid in poor countries.
• Poverty Traps: Aids and Malaria + political instability in newly independent states.
• Bad development policies, e.g. the resource curse
• Lack of globalization, geographic or political isolation...
Income Gap and the Poverty Gap

• How poor is the average poor family?:
  – I is the gap between the average income of the poor and the official poverty line.

• The glass is ___% empty -- useful but:
  – 1. Says nothing about how many or poor.
  – 2. There may be great inequality among the poor.
  – 3. Not sensitive to redistribution of income among poor-- still misses the severely poor.

• The poverty Gap Index or H*I address issue #1 but not limitations #2 and #3 above.
How Long the Escape from Poverty Takes depends on the Depth of Poverty and the Average Growth Rate of the country:

<table>
<thead>
<tr>
<th>Growth Rate Per Capita</th>
<th>Average Income Shortfall:</th>
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<tbody>
<tr>
<td></td>
<td>20%</td>
</tr>
<tr>
<td>4%</td>
<td>6</td>
</tr>
<tr>
<td>3%</td>
<td>8</td>
</tr>
<tr>
<td>2%</td>
<td>11</td>
</tr>
<tr>
<td>1%</td>
<td>22</td>
</tr>
<tr>
<td>0.5%</td>
<td>45</td>
</tr>
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</table>
Poverty Rate H: % below $1/day

Source: OECD, World Bank
Poverty Gap Index or H*I

Incidence times Depth of Poverty H*I

Source: OECD, World Bank
Child Malnutrition: Prevalence of Underweight
Under 5  --  Source: OECD, World Bank
A long struggle bears fruit in India…

Figure SA-1A $1/day poverty rates (H) in India

Source: World Bank, Povcalnet January 2013
(http://iresearch.worldbank.org/PovcalNet/index.htm?1)
A long struggle against poverty in India...

Figure SA-1C $1/day poverty gap (H*I) in India

<table>
<thead>
<tr>
<th>Year</th>
<th>India--Urban</th>
<th>India--Rural</th>
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</thead>
<tbody>
<tr>
<td>1978</td>
<td>11.1</td>
<td>15</td>
</tr>
<tr>
<td>1983</td>
<td>7.8</td>
<td>10</td>
</tr>
<tr>
<td>1988</td>
<td>7.7</td>
<td>8.3</td>
</tr>
<tr>
<td>1994</td>
<td>5.8</td>
<td>6.8</td>
</tr>
<tr>
<td>2005</td>
<td>5.0</td>
<td>4.5</td>
</tr>
<tr>
<td>2010</td>
<td>3.3</td>
<td>2.9</td>
</tr>
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</table>

Source: World Bank, Povcalnet January 2013
(http://iresearch.worldbank.org/PovcalNet/index.htm?1)
A long struggle bears fruit in India...

SA-5 India: Total Population of $1/day poor

A long struggle bears fruit in India...

SA-5 India: Total Population of $1/day poor

<table>
<thead>
<tr>
<th>Year</th>
<th>Total # of poor (millions)</th>
<th>Rural Poor (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1978</td>
<td>312</td>
<td></td>
</tr>
<tr>
<td>1983</td>
<td>275</td>
<td>218</td>
</tr>
<tr>
<td>1988</td>
<td>284</td>
<td>220</td>
</tr>
<tr>
<td>1994</td>
<td>279</td>
<td>217</td>
</tr>
<tr>
<td>2005</td>
<td>262</td>
<td>190</td>
</tr>
<tr>
<td>2010</td>
<td>195</td>
<td>136</td>
</tr>
</tbody>
</table>

A long struggle bears fruit in India...

SA-5 India: Total Population of $1.25/day poor

- Total # of poor (millions)
- Rural Poor (millions)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total # of Poor</th>
<th>Rural Poor</th>
</tr>
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<tbody>
<tr>
<td>1978</td>
<td>430</td>
<td>351</td>
</tr>
<tr>
<td>1983</td>
<td>362</td>
<td>276</td>
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<td>1988</td>
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<td>293</td>
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<td>1994</td>
<td>378</td>
<td>279</td>
</tr>
<tr>
<td>2005</td>
<td>406</td>
<td>290</td>
</tr>
<tr>
<td>2010</td>
<td>349</td>
<td>245</td>
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Has India already achieved MDG 1???

Figure SA-1 $1.25/day poverty rates (H) in India

Source: World Bank, Povcalnet January 2013
(http://iresearch.worldbank.org/PovcalNet/index.htm?1)
Has Indonesia definitely has... what year?

EA-1 Indonesia $1/day Poverty rate

Source: World Bank, Povcalnet January 2013
(http://iresearch.worldbank.org/PovcalNet/index.htm)
Social justice perspective

- **Social deprivation: lack of capabilities**
  (Amartya Sen all should be capable of participating in basic civil and social events, w/o humiliation (e.g. having no shoes)
  Example: MDGs are multidimensional

- **Unjust deprivation:** Rawlsian justice for example, the least of always comes first OWS??

- **Lost human capital:** poor health or education means your ideas and innovations may be lost to all of us: an inability to produce: lost potential growth.
  Example: barriers to undocumented Dreamers.. 1.5 students in the U.S. (except in California and Texas)
Why help improve the lives of others *in particular the poor*?

- **Altruism:** people feel an urge to help those less fortunate: especially during crises: Katrina, Haiti, Tsunami

- **Social justice:** helping others reveals what we value to ourselves & others... the proper role of family, government and community groups...

- **A safer more secure world:** economic insecurity breeds political instability: war, crime and terrorism... Inequality and poverty lead to political instability, terrorism, crime...
When, how and who should improve the lives of others?

- **When and how?** what NGO/government policies help? foreign aid, in-kind donations, conditional cash transfers minimum wages: what can be done?

- **Who should do it:** Private charities, national governments (bilateral aid) or international institutions: IMF, World Bank, United Nations... WTO, ILO, UNCTAD & so on.
Poverty reduction now main metric of economic well-being: MDG goal 1 is to reduce 1990 $1/day poverty rate (H) in half everywhere– can we do it?

Physical and social deprivation should be reduced whenever and wherever possible. But if most people are poor the idea of poverty as one group helping another may not be operational or feasible.

Absolute poverty relative is a relatively new metric of human progress...practically speaking the poor should be less than 50% and more that 5% of the total population...
How to draw a poverty line? start with some minimum diet... for example

- **Official U.S. poverty definition:** Income less than $20k year for an urban family of 4 (or roughly $50/day in 2006)

- **UN/World Bank international poverty line:** 2250 calories per day or $1/day in consumption spending (same for all poor countries – except perhaps LatAm where $2/day) – to make prices comparable in various countries, ICP surveys different countries: rents and wages are lower in poor countries, the new 2005 survey is just coming out this year... a mess but good for you, and me).

- In $2005 raised to $1.25/day and switched to urban
Concern about poverty starts with prosperity…

1. **Absolute poverty** involves physical deprivation: malnutrition is a universal poverty indicator: absolute measures always start with some biologically defined but socially acceptable minimum diet and then adds a bit more: some clothes, shelter, etc.

2. **Relative poverty** focus on relative deprivation: no one should be too far from average or the middle household... this is why for example the U.S. and India use very different poverty lines, Europe uses a relative poverty measure... mixes ideas of inequality, fairness and poverty... a 2nd order concern?

3. **Poverty fighting policy is a by-product of mass affluence:** the notion that one large group should help another large group is only feasible in an age of mass affluence: economic prosperity makes it politically and economically feasible for one group to help another (not philanthropy where the very rich help the very poor) not about millionaires helping the poor, it is about the middle class in Sri Lanka, Brazil, India, the U.S. and China taxing itself to make transfers to the poor...
Europe takes inequality as seriously as poverty…

- **European poverty measures are relative**, a % of the median income, no one should be more that 50% below the median.
- **Growth cannot reduce relative poverty**, only redistribution in the bottom half of the income distribution can: make everyone “middle class”
- **Eurostat measures how long people are poor**: the persistence of poverty: chronic vs. transitional poverty.
What about inequality?

- **Inequality is a relative not an absolute concept:** my group’s “share” of the pie, not dollars or stuff...social as opposed to physical deprivation... I am or feel poor compared to ...

- **Inequality may reflect social exclusion which can cause persistent poverty and limited mobility:** quite literally in New Orleans, compare Bronx’s 29% poverty to 28% in New Orleans: in New Orleans 85% of poor are African American– same poverty rate but NY is an immigration entry point. India’s caste system or the “Roma” peoples of Europe.

- **Key point: mobility tempers inequality and poverty:** low unemployment, lots of entry level jobs) or with progress of previously excluded groups... witness B. Obama and C. Rice.. persistent poverty or inequality is less acceptable.. e.g., indigenous peoples of Bolivia
How to draw a poverty line (cont.) Sen’s capabilities approach:

- **Capabilities:** Sen argues consumption is not an end in itself, but a means to some common ends we all value: the ability (“freedom) to read, be healthy, participate in community, vote etc. Amartya Sen calls these abilities “capabilities”:

- The UN Millennium Development Goals (MDGs) are examples of minimum standards: primary school attendance, access to clean water, low U5MR, etc. – e.g. “development as freedom”
A longer View… Poverty reduction is a race between the population non-poor and the poor…

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- Technical progress helps bring cheaper food and better medicine to the poor, living better on the same income with anti-biotics, vaccinations, etc.
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Alternative measures of Absolute and Relative poverty....

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Why it is so hard to reduce the poverty rate...

- Population growth is rapid in poor countries (see the 7 IKEA boxes), ending poverty slows population growth.
- Poverty Traps: Aids and Malaria + conflict and war (worse during cold war– 1980s Ethiopia, civil war– Famine).
- Geography, the resource curse, malaria.
- Integration: Lack of globalization, geographic or political isolation...
- Poor governance.
The great poverty reversal from 85% to 15% between 1820 and 2005

In 1820 the world $1/day poverty rate was 84%, today (2005) it is about 15%: this is the great poverty reversal: the majority of the World’s population was poor but now they are not: Indians, Chinese and Koreans, teach poverty alleviation to others.

Not just income but quality of life: medicines and knowledge of the rich now available cheaply to the great majority: antibiotics, vaccines, even ART for HIV-Aids.

UNICEF’s “patent injustice” When basic inexpensive treatments are not available those in need: vaccines, ART, ORT
$1/day poverty fell from 1820 to 2004: but the number of poor rose until 1980 (or 1950 see the dotted line trend)

Figure 1: World $1/day Poverty Rates

Turning point… the number of poor started to fall about 1980…

Great poverty reversal: from 85% to 15% poor…
Poverty fell fastest in the 1960s and since 1980...

Annual percentage point fall in World $1/day Poverty

<table>
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<th>Period</th>
<th>Poverty Fall</th>
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<tr>
<td>1820-1850</td>
<td>0.1%</td>
</tr>
<tr>
<td>1850-1870</td>
<td>0.4%</td>
</tr>
<tr>
<td>1870-1890</td>
<td>0.2%</td>
</tr>
<tr>
<td>1890-1910</td>
<td>0.3%</td>
</tr>
<tr>
<td>1910-1929</td>
<td>0.5%</td>
</tr>
<tr>
<td>1929-1950</td>
<td>0.05%</td>
</tr>
<tr>
<td>1950-1960</td>
<td>1.1%</td>
</tr>
<tr>
<td>1960-1970</td>
<td>0.8%</td>
</tr>
<tr>
<td>1970-1980</td>
<td>0.3%</td>
</tr>
<tr>
<td>1980-1992</td>
<td>0.8%</td>
</tr>
<tr>
<td>1992-2002</td>
<td>0.7%</td>
</tr>
<tr>
<td>2002-2004</td>
<td>0.9%</td>
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Patent injustice, “passive atrocities”: artifacts of global affluence...very low cost ways to ameliorate the worst effects of poverty... e.g. ART or ORT

- Malnutrition and famine...always a government failure.
- ORT: ten cent treatment for dehydration also antibiotics for common respiratory, diarrheal and vaccine preventable illnesses, vitamin A deficiency
- unsafe water, lack of basic sanitation
- ART treatment for HIV-1 (anti-retroviral drugs, PEPFAR,
Why and how we help reflects as much our values as characteristics of the poor….

- **Motivations change:** but remain complex: a “great society” fairness, a social safety-net, social insurance: still some compassion, fear, guilt, but perhaps less vanity, evangelism, altruism, power or noblesse oblige (not that philanthropy is bad) (cf. *Groundhog Day* or Benabou & Tirole, 2005)

- **Social justice:** equal opportunity and fairness: a level playing field: equality of opportunity not outcomes...

- **Economic efficiency:** poverty not efficient, reducing it is win-win for poor and non-poor alike, spreading risk: helping the poor is good business, they make things we buy and buy things we make... aid for trade... economically active population increases innovation and growth...
How best to help? (our values key here)

- **In-kind transfers** (food, vaccines, medicine and other “in-kind” transfers)
- **Conditional cash transfers:** require work (workfare) or education or health service use...
- **Free public services/benefits** social policy, pensions ealth services, education, schools, HIV/aids drugs...
- **Market access**—trade not aid, aid for trade: Doha Trade Round?... Bangladesh an example.
- Special programs for excluded groups (affirmative action gender, race or handicap...).
- Provide security, protect human rights, enforce international laws against genocide, piracy proliferation, arms trade, child trafficking etc.
Over the past 200 years world population increased 6-fold – to about 6.4 billion in 2004
But incomes rose even faster so the world $1/day poverty rate fell from about 84% to about 15%..
$1/day world poverty in 1820 vs. 2004: but the number of poor rose until 1980 (or was it 1950?)

Turning point… the number of poor started to fall about 1980…

The great poverty reversal
And since 1996, the poverty rate is falling everywhere…even in Africa, but...
$2/day poverty rates are much higher, but still falling...

Figure 3: Poverty in Developing Countries

Source: Chen and Ravallion (2004) "How the Poor have fared since the 1980s" World Bank Poverty Net and GEP 2006 Table 1.3 page 9.
Capitalism and globalization made about a billion of us rich, two billion remain poor and about 3 billion are in the “new middle class”

- Still, too many remain in severe poverty in the world... according to the World Bank, about 1.1 billion people still get by on less $1/day.
- Poverty defined in absolute terms: $1 per day only buys about 2250 calories of coarse cheap grain (no meat, few clothes).
- Poverty contributes to global inequality and conflict: reducing severe poverty is not easy but not impossible, “ending poverty” in your lifetime.