# Poverty Cycles

RIDLEY COLLEGE

SINCE 1889

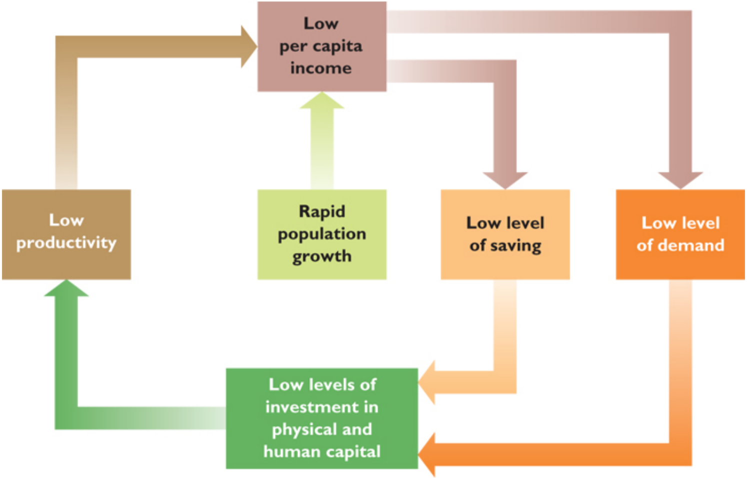
# Learning Objectives

| Specific Expectations | |
|---|---|
| AO2 | Explain the meaning of poverty cycles, also known as poverty traps |
| AO4 | Draw a diagram showing a poverty trap |
| AO3 | Evaluate the significance of each of the above factors as a barrier to economic growth and development. |
| AO2 | Explain how each of the following works as a barrier to economic growth and development.<br>- Rising income inequality<br>- Limited access to infrastructure<br>- Low human capital: limited access to education/healthcare<br>- Dependence on primary production<br>- Limited access to international markets.<br>- Informal economy, capital flight, indebtedness.<br>- Geography and landlocked countries. |

# Poverty Cycle (Poverty Trap)

- **Poverty cycle (poverty trap)** arises when low income result in low (or zero) savings, permitting only low (or zero) investments in physical, human and natural capital, and therefore low productivity of labour and of land.
  - This gives rise to low, if any, growth in income (sometimes growth may be negative), and hence low income once again.
  - A poverty cycle may occur in a family, a community, a part of an economy, or in n economy as a whole.
  - An important feature of the poverty cycle is that poverty is transmitted from generation to generation.
    - People often cannot afford to send their children to school or afford necessary medical care.
    - Large families increase the level of poverty, as income of the parents must be stretched to cover the needs of more people

# Poverty Cycle (Poverty Trap)



# Economic Barriers to Development

1. **Limited access to infrastructure**
   - **Infrastructure** refers to numerous types of physical capital resulting from investments, making major contributions to economic growth and development by lowering costs of production and increasing productivity.
   - Includes power, telecommunications, piped water supplies, sanitation, roads, major canal works for irrigation and drainage, urban transport, ports and airports.
   - The availability of infrastructure and broad access to the services it offers make major contributions to economic growth, economic development and poverty alleviation.
   - **Problems of financing** – Governments charge users for their consumption of infrastructure services. To make services affordable, prices charged have been kept below cost, resulting in insufficient revenue for the state enterprises providing infrastructure.
   - **Inadequate maintenance and poor quality** – Lack of revenues means that infrastructure facilities are often poorly maintained, resulting in low quality and unreliable services.

# Economic Barriers to Development

- **Limited access by poor** – Lack of revenue also means constraints in quantity of infrastructure facilities that can be constructed. It is generally the poor who tend to suffer disproportionately from the lack of access, both in rural area and in urban slums.
- **Misallocation of resources** – Investments may be made in infrastructure facilities that remain underused because there is not enough demand for their services (power, telecommunications), while other services (roads, or better maintenance and improvements in service quality) are neglected.
- **Neglect of the environment** – Infrastructure can have numerous negative environment effects, including the failure to adequately control unnecessary emissions, and poorly maintained irrigation facilities.

2. **Limited access to appropriate technology**

   - **Appropriate technologies** are technologies that are well suited to a country's particular economic, geographical, ecological and climate conditions.

# Economic Barriers to Development

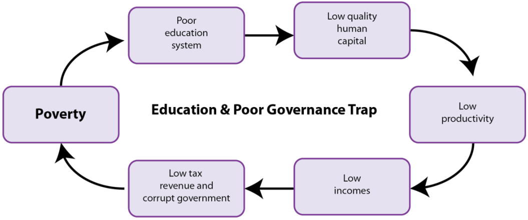
- Often used in connection with labour-abundant developing countries that require labour-intensive (as opposed to capital-intensive technologies).
- New technology contributes to improving the quality of physical capital and economic growth.
- **Labour-intensive (Labour-using) technologies** – use more labour in relation to capital. They result in increases in local employment and the use of local skills and materials, increases in income and poverty alleviation, and save on the use of scarce foreign exchange.
- **Capital-intensive (Capital-using) technologies** – use more capital in relation to labour. In developing countries with large supplies of labour they displace workers and increase unemployment, reduce incomes and throw people into poverty, and require skill levels that may be costly and difficult to acquire, as well as the us of foreign exchange for imports.
- Many of the technologies developed in rich countries are inappropriate to the climates, geography and ecological conditions of many developing countries.

# Economic Barriers to Development

- Firms in developing countries, especially in the lower income ones, have neither the resources not the markets to support R&D activities.

3. **Low levels of human capital**

- **Human capital** refers to the skills, abilities and knowledge acquired by people as well as good levels of health, all of which make them more productive.
- Increased provisions (universal access) of education and healthcare are among the key goals of economic and human development.



# Economic Barriers to Development

- There are several barriers to inclusive and equitable education in developing countries.
  - **Insufficient funding for education** – many developing countries do not have sufficient government revenues to fund education.
  - **Insufficient teachers or untrained teachers** – there are not enough teachers at the primary and secondary levels, and those that are available do not have access to necessary training.
  - **Insufficient classrooms and basic facilities** – many countries in sub-Saharan Africa do not have enough classrooms, and many of those that are available do not have running water toilets.
  - **Lack of teaching materials** – textbooks are often old and worn out, and those that are available are shared by several students.
  - **Children with disabilities excluded** – the majority of children with disabilities do not attend school while also facing discrimination.
  - **Gender discrimination** – girls disproportionately are unable to attend school.

# Economic Barriers to Development

- **Conflict or risk of conflict** – many children live in countries where there are conflicts and therefore do not attend school.
- **Distance of school from home** – it is not uncommon for a child to have to walk three hours a day to get to school.
- **Inability to pay for education** – whereas primary education is free virtually everywhere, expenses of having to buy books, pens, exam fees or other "informal fess' means that many families locked in poverty cannot afford to send their children to school.]

- Barriers to achieving good health include:
  - **Insufficient funding for health care** – there is a significant financing gap on healthcare spending.
  - **Insufficient access to health care services** – at least half of the world's population do not have access to all of the essential health care services needed.
  - **Private payments for healthcare** – many people are pushed into poverty as a result of having to make these payments while others do not receive medical treatment due to the high cost.

# Economic Barriers to Development

- **Geographical access** – healthcare facilities are often situated very far from where people live. Long distances, lack of roads and transportations means many people do not have access to healthcare facilities.
- **Insufficient number of trained medical practitioners** – even where medical practitioners are available they are often ineffective.
- **Insufficient medical facilities and medical supplies** – there are major problems of financing in order to set-up, staff and equip medical facilities to ensure access to rural populations.
- **Acceptability of modern medical practices** – in some very poor societies modern medical practices are not accepted as people prefer traditional medicine.
- **Insufficient access to clean water and sanitation** – adequate access to quality health care services is not enough to ensure good health. It is also necessary to ensure access to clean water supplies and sanitation.

# Economic Barriers to Development

4. **Dependence of production and exports on the primary sector**
    - **Primary sector** is a part of the economy that produces primary commodities and is dominated by agriculture, also including fishing, forestry and all extractive activities (such as mining).
    - Developing countries, tend to specialize in the production and export only a few goods, which usually are primary commodities.
    - The prices of primary commodities are more volatile (fluctuate more) than the prices of manufactures products because they have low price elasticities of demand and low price elasticities of supply.
    - As product prices fluctuate, so to do farmers' incomes, along with agriculture investment, employment and wages of agriculture workers.
    - Producers are unable to plan, as they are unable to determine the future profitability of investments.
    - When the product is exported, fluctuating prices also contribute to unstable export earnings, affecting the country's balance of payments and ability to import.

# Economic Barriers to Development

- Price fluctuations also affect government's revenues with negative consequences on its efforts to plan for growth and development and undertake necessary investments in merit goods (healthcare, education, and infrastructure).

5. **Limited access to international markets**

   - The inability to access international markets refers to difficulties encountered by developing countries in their exports to developed countries.
   - **Developing countries face high tariff barriers** – tariffs remain high for products of interest to developing countries, which include agricultural products, textiles and apparel.
   - **Tariff escalation** – both developing and developed countries impose low tariffs on raw materials, and much higher tariffs on processed products.
   - This makes it difficult for developing countries to undertake **vertical diversification** and move into manufacturing that makes use of domestically produced inputs.

# Economic Barriers to Development

- **Agricultural trade and rich country subsidies** – agriculture is one of the most protected sectors of developed countries, justified on the grounds that farmers earn low incomes and must therefore be assisted.
- This protection has major negative consequences for many developing country primary product exports and for poverty alleviation.
- **Global misallocation of resources** – higher prices received by developed country farmers due to price supports, as well as production subsidies, result in overallocation of resources to the production of protected goods in the developed countries, and therefore excess production and surpluses.
- When these goods are exported they artificially lower the international price of the goods, making it more difficult for farmers in developing countries to compete.
- **Global inefficiency** – developing countries can often produce certain agriculture products at a far lower cost than developed countries, yet because of protection, the more inefficient developed country producers continue to produce, capturing global market shares from the more efficient developing country producers.

# Economic Barriers to Development

- **Lower export earning of developing countries** – developing countries that export products receiving protection in developed countries suffer due to lower exports, as well as lower prices (due to the rich-country subsidies), and therefore have lower export earnings; this can contribute to balance of payment difficulties and increased debt burdens.
- **Increased poverty among affected farmers** – low exports and low prices received by developing country farmers and the inability to compete with the farmers of developed countries means lower incomes, lower investment possibilities for farmers, lower employment opportunities for farm workers and increased poverty.

6. **Informal economy**

- A **formal economy** refers to part of an economy that is registered and legally regulated; an **informal economy** by definition lies outside the formal economy, and refers to activities that are unregistered and legally unregulated.
- Workers are unregistered and the government loses tax revenues.

- Workers are vulnerable to exploitation; environmental dangers and health hazards; no access to credit for workers; limited possibilities for education and training; no social protection including pensions.

7. **Capital flight**
   - **Capital flight** refers to the large-scale transfer of privately-owned financial capital (funds) to another country resulting from fear and uncertainty of holding domestic assets.
   - It involves the loss of financial capital that could have been invested domestically.
   - It consists of the sale of domestic currency (in order to purchase foreign exchange that leaves the country), it exerts a downward pressure on the value of the currency, often forcing governments to devalue or allow the currency to depreciate.

8. **Indebtedness**
   - Rising debt levels are creating concerns that some countries debt may be increasing to unsustainable levels, with serious negative consequences for theri growth and development prospects.

# Economic Barriers to Development

- **Debt relief** refers to the cancellation or forgiveness of all or a portion of a country's debt. The World Bank and International Monetary Fund (IMF) facilitate debt forgiveness in developing countries.

9. **Geography and landlocked countries**

- Landlocked developed countries (LLDCs) are particularly disadvantages since in order to access ports for their exports and import activities they depend on their neighbouring countries, which they may sometimes have poor relations, or which may have poor road infrastructure, or they which may face conflict and political instability.