

Relative poverty and development traps

Abstract

This paper proposes a theory according to which relative poverty may drive the emergence of development traps, even in the absence of market imperfections. Poverty is defined as lack of or low social participation, which is source of direct benefits as well as indirect gains, whenever consumed over a threshold. We formalize poverty and behavior of poor and rich agents, considering that individuals have different characteristics and economic behavior determined by their specific socio-economic status, such that each of them behave and choose accordingly to their poverty status. We show that in economies starting largely poor inequality traps emerge, while in richer economies convergence towards a unique steady state is reached. The development traps are reinforced by the persistence of inequality as a large mass of people remains relatively disadvantaged and excluded from the benefits of societal participation.