

# The capability approach to economic inequality: economic capability \*

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## Abstract

The relationship between capabilities and access to economic goods is the subject of the present paper. My focus is in particular how the capability approach can be applied to the analysis of economic inequalities within a country. The capability approach makes clear that material riches - opulence - is not the sole target of economic development, nor should opulence be the sole focus of economic policy in developed countries. On the other hand, the material standard of living neither can nor should be entirely absent from capability analysis. In particular, inequalities in income and wealth within and between countries must always be of importance. The important question is how to relate material standards of living to capabilities. The paper defines economic capability as a modification of ‘full income’.

## 1 Introduction

The relationship between capabilities and commodities does not seem straightforward. Sen clearly thinks of commodities - and hence also income, which buys commodities - as inputs into capabilities, as seen by his often used example of pregnant women needing more food. On the other hand Nussbaum has the right to own property and to engage in paid work on her list of minimum or threshold capabilities. Similarly, on his list of basic socio-economic capabilities, Peter Ulrich has the ‘Capability to earn a living wage’.<sup>1</sup> These

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\*Draft. Comments welcome, but please do not quote

<sup>1</sup>Ulrich 1997, quoted from Knobloch 2002

rights seem to correspond to a capability of earning an income; the capability of acquiring commodities.

The two approaches are not necessarily contradictory: one capability may well be an input into another capability.

We acquire commodities in various ways. They can be received in kind, as when foods and other consumption goods are shared in a family, or as handouts of rations in famine relief. We can produce them ourselves, as in subsistence farming or unpaid housework. But the most widespread way of acquiring commodities in the modern economy is by earning an income and using the income to buy commodities; this is in any case true for adult men.

These ways of acquiring commodities are not of equal worth. Women's struggle for economic emancipation from their husbands, or brothers, or fathers was not - at least, not only - a struggle to obtain more consumer goods. It was a struggle for economic independence and power: economic capability. It might also be called economic autonomy. Being able to earn your own living by means of a socially acknowledged contribution to society is also an important part of what John Rawls calls 'the social bases for self-respect', a primary good.

Economic autonomy in this connection must not be understood as the libertarian right to dispose of 'the fruit of one's labour.' The implication is that something called the fruit of a particular individual's labour can be identified, found and measured, and that, as Nozick writes: 'Things come into the world already attached to people having entitlements over them.' (Nozick 1974: 160)

But there is no such thing as human production without human social cooperation. It is both theoretically and practically impossible to identify, let alone measure, the product of one single individual. Economic independence, autonomy, in the libertarian individualistic sense is nonsense. The economic capability of an individual will always be determined by factors largely outside the control of that individual.

What we can hope to measure are legally enforceable, individual rights to economic goods. The rights must, as Nussbaum stresses, be individual. They are not the rights of a family, a household, a clan or an ethnic group, but of each individual belonging to one or more of such groups.

In addition to autonomy and legal rights, security is an important aspect of economic capability. Security may be thought of as insurance against loss of job or working capability, in other words social or private insurance against unemployment, sickness, disability and old age. Such insurance may or may not be included in ordinary wages.

Finally, economic capability must measure economic options, a set of feasible choices, not outcomes of choice.

The closest approximation I can find to economic capability is individual full income, determined by available time, real wage and non-labour income; and extended to include rights to economic goods in forms that are not usually thought of as ‘income’.

## 2 The conventional definition of income

The standard definition of income in economic literature is due to, among others, the English economist John Hicks:

The purpose of income calculations in practical affairs is to give people an indication of how much they can consume without impoverishing themselves. Following out this idea, it would seem that we ought to define a man’s income as the maximum value that he can consume during a week, and still be as well off at the end of the week as he was at the beginning. (Hicks 1961: 172)

There are three important two aspects of this definition.

Firstly: it connects income and wealth: they are two of a kind, both being means of financing consumption (commodities). The concept of wealth will, however, not be discussed in the present paper.<sup>2</sup>

Secondly, the definition emphasises income as *possible* consumption; in this sense the standard definition measures options.

Thirdly, the definition implies that any person who consumes ipso facto receives an income. That consumption implies income is explicitly stated in a famous quote from Vilfred Pareto:

Even the poorest man must be regarded as having sufficient income to keep him alive. It doesn’t matter whether this sum comes from the fruit of his work, or whether it comes to him from charity, or indeed whatever source, legal or illegal.

According to Hicks and Pareto<sup>3</sup> then, the child, the thief and the beggar all have an income, as does the housewife who receives pocket-money from her husband. The conventional definition of income does not distinguish between the passive receiving of commodities and the active earning of an income. The standard measure in distributional analysis is household income corrected for household size, usually called income per equivalent adult. This measure ascribes equal ‘incomes’ to all household members. It is a measure of

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<sup>2</sup>See e.g. Bojer (2003), Chapter 9: Income and Wealth.

<sup>3</sup>Note that both Hicks and Pareto assume that the receivers of income are men

Figure 1: Full income and the allocation of time  
(figure to be supplied)

possible consumption assuming equal shares within the household, but not of the options of the individual household members. In this respect, therefore, the conventional concept of income does not make it suitable as a concept of individual economic capability.

Nor is the problem altogether solved by measuring individual income instead of household income. Hicksian income measures options in regard to material commodities, but not options regarding time use, for instance the choice between work and leisure. This is where the concept of full income is useful.

### 3 Full income

The concept of full income is not new; it was introduced by Gary Becker (1965). Full income as a theoretical concept is widely applied in e.g. labour market economics and fertility analysis, but has not to my knowledge been empirically measured and applied in analysis of economic distribution. The difference between full income and standard income is that full income includes leisure as an item of consumption. In symbols:

$$FI = wT + MI \tag{1}$$

where  $T$  is available time, say 24 hours a day. Available time is divided between three different pursuits: paid work ( $L$ ), unpaid work ( $H$ ) and leisure ( $F$ ). The hours spent in paid work, together with non-labour income, determine the person's options when it comes to acquiring market commodities.

$$FI = wT + MI = wL + wH + wF + MI = C + wH + wF \tag{2}$$

Equation 2 shows that the trade-off between leisure ( $F$ ) and (possible) consumption,  $C$ , is the real wage rate  $w$ .

Figure 1 illustrates the available options, and one possible choice.

Full income is determined partly by personal endowment (human capital), measured by the wage rate, partly by social and economic features of the surrounding society. These features of society determine to which extent figure 1 illustrates real choices.

Figure 2: The cost of children: time and money  
(figure to be supplied)

## 4 Unpaid work

Unpaid work is one constraint on available time. Now, unpaid work is, of course, sometimes chosen voluntarily, and may be difficult to distinguish from leisure pursuits (hobbies). Technically, the criterion used in empirical work to distinguish unpaid work from leisure is the third-person criterion: an activity is unpaid work if it is technically possible to hire someone else to do it for you. Baking bread is unpaid work, a work-out is leisure. Another possible criterion, more difficult to observe, is the possibility of choice: leisure is *free time*, when you have a free choice of activities. Caring for children and infirm or sick dependants is work according to both criteria. It has to be done by somebody, whether the person cared for is able to pay for the care or not. Children, in particular, can never pay for themselves. Parents must either do the work themselves or pay someone else to do it for them. Indeed, leisure, free time, is an extremely scarce commodity for parents (mothers) in modern society.

I have argued elsewhere (Bojer 2002) that not all care for children can or should be professional. Children's need for time measured in hours is absolute, and does not depend on the parents' income. The money value of the time will, however, vary with the real wage of the parents. Time needed for child care consists of two parts: necessary time spent by the parents and time hired from a third person (day care centre, nanny). Both must be deducted from time available when estimating full income. The price of the parents' time will be his or her own wage rate, the third-person time will be priced at the market wage for child carers. This wage, may or course, be higher than the wage rate of one or both parents.

The care cost can be expressed in time or in money, as shown in figure 2. The care cost of children and other dependants, I shall call socially necessary unpaid labour.

## 5 Different needs

The standard examples of different needs used by both Sen and Nussbaum are differences in nutritional needs. These are, of course, of great importance to people living on or near subsistence level. They are not, however,

of importance to people with normal incomes in affluent societies.<sup>4</sup> But there are many other cases of different needs which are of importance at all levels of wealth: differences due to chronic illness and/or physical and mental handicaps. This is where people need different quantities and qualities of commodities in order to obtain basic capabilities like mobility or seeing. These needs can be measured in money, namely the cost of medicines and or physical equipment needed. The monetary values of commodities needed are generally already known, more or less approximately, since in many countries, the supplementary costs are covered by governmental or private insurance, at fixed rates. There are a limited, though large, number of different cases. In each case, the necessary sum must be deducted from FI in order to compute the individual's real options.

Medication and other medical aids may enable the person to undertake paid work, and are therefore both a result of, and an input into, economic capability.

A different kind of differences in needs is the presence of children (or other dependants) who need both commodities and care. There is a considerable literature on the problem of determining the cost of children. The main body of this literature is devoted to computing the sums that parents actually, on average, spend on their children. But actual expenditure is an outcome of choice. The capability approach would be to estimate a minimum necessary expenditure. This minimum is not necessarily a small sum. It should represent some kind of societal consensus on what the legal and moral obligations of parents are towards their children.

## 6 Economic capability

Economic capability in the short term as measured by extended full income is the sum of different income streams.

1. Earnings capability: equals the net wage rate multiplied by available time. Available time equals 24 hours a day minus socially necessary unpaid labour.
2. Rights vested in social security arrangements arising from paid work: the rights to unemployment benefit, old age pension, disability pension, sickness benefit, paid parental leave.

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<sup>4</sup>In Norway, the average household spends less than 20 per cent of its (monetary) income on food.

3. Rights vested in other social security benefits: child benefit, public health services, and other welfare arrangements.
4. Actual transfers received from social security under the above arrangements.
5. Government allowances to cover special needs due to permanent or temporary disability.
6. Rights vested in, and payments received from, private insurance covering the same fields.
7. Income from assets (capital income)
8. Legally based private transfers (alimony, payments for children)
9. Less the cost of special needs like medication and physical equipment.

## 7 Commodities and capabilities

Economic capability in the sense I have defined it, is not necessarily the same as material opulence. Two people with equal economic capabilities may have unequal cash incomes, depending on how they choose to spend their time. Nevertheless, it is not necessarily *the* final good. Economic capability is an end in itself up to a certain level, but not necessarily beyond. In the paper 'Poor relatively speaking' (Sen 1984), distinguishes between two kinds of capabilities. Some, such as adequate nutrition, are obtained by an absolute quantity of commodities. Some, such as social participation in various ways, depend on acquiring commodities in quantity and/or quality relative to what other members of the society possess. As Sen writes:

The temptation to think of poverty as being altogether relative arises partly from the fact that the *absolute* satisfaction of some needs might depend on a person's *relative* position vis-a-vis others. (Sen 1984: 333)

The fact that satisfaction of needs often depends on one's relative economic position, is in my view a powerful argument for economic equality. It also makes a good case for further research into the complex relationships between economic and other capabilities.

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