

Easy and Hard Redistribution: The Political Economy of Welfare States in Latin America

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Country	Gini in 2000	Gini in 2010	% change in Gini 2000-10	Change in poverty 2000-10*
Argentina	51	45	-13	-6
Bolivia	63	50	-21	-21
Brazil	59	54	-9	-11
Chile	55	52	-6	-3
Colombia	59	56	-5	-18
Costa Rica	47	48	1	-8
Dominican Republic	52	47	-9	-1
Ecuador	56	49	-13	-27
El Salvador	53	45	-16	-9
Guatemala	55	52	-5	5
Honduras	55	53	-4	-12
Mexico	52	47	-9	-11
Panama	58	52	-10	-11
Paraguay	55	52	-5	-6
Peru	51	45	-12	-16
Uruguay	44	45	2	-27
Latin America	54	49	-8	-10

Best decade ever?

- Inequality and poverty fell almost everywhere
- About half of reduction due to welfare policies

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Best decade ever?

- Except in most equal countries
 - Costa Rica & Uruguay
- Redistribution in Latin America stalled after 2010

I. Introduction

- Easy and hard/deepening phases in ISI (import substitution industrialization)
 - Hirschman and O'Donnell
- Three parallels
 - Sequencing happened in Latin America but not elsewhere
 - Policy making and implementation gets harder
 - Coalitions different in easy and hard phases

Two core arguments

- 1. Easy phase of redistribution involved layering non-contributory cash transfer programs on top of truncated contributory welfare systems
 - Easy determined both by ease of policy implementation and of coalition building
- 2. In the hard phase, labor market structure and fractured coalitions impede further deepening of redistribution
 - Hard determined both by difficulty of policy implementation and of coalition building

Some misperceptions

- Democracy is sufficient to reduce inequality
 - Meltzer and Richard may have worked in 2000s
 - but not before or after
 - Not median voter, but distinct groups
 - Divided by labor markets and by welfare benefits
 - formal versus informal (53%)
- Left government is necessary and sufficient to promote redistribution
 - Right governments redistributed too in 2000s
 - Redistribution by left has stalled in 2010s
- Stalled reduction in inequality is due to end of commodity boom
 - Problems run deeper in exhaustion of easy phase

II. Easy phase of redistribution

- Welfare states in 20th century were truncated or exclusionary
 - Contributory benefits financed through payroll taxes for a labor elite in the formal sector
 - Minimal benefits for the majority of workers in informal sector
- Non-contributory policies in 2000s expanded dramatically to cover millions of excluded families

Expansion of non-contributory transfers, 2011 (Levy & Schady)

	Noncontributory Pensions				Cash Transfers			
	People (000s)	% elderly	\$US per month	% GDP	House- holds (000s)	% House- holds	\$US Per month	% GDP
Argentina	41	1.4	248	0.03	1,876	21.1	162	0.49
Bolivia	899	100	28	1.25	972	40.2	5	0.23
Brazil	7,340	32.5	328	1.16	13,352	28.2	45	0.41
Chile	842	53.5	136	0.55	264	5.9	104	0.13
Colombia	768	15.6	33	0.09	2,438	23	33	0.22
Costa Rica	93	30.6	146	0.4	143	12.7	74	0.23
Dominican Republic					831	34.7	25	0.24
Ecuador	536	58.2	35	0.34	1,212	34	35	0.71
El Salvador	20	3.4	50	0.05	95	7.1	17	0.15
Guatemala					873	37.4	29	0.24
Honduras					412	27.7	40	0.32
Mexico	2,149	44.9	40	0.09	5,827	24.2	72	0.46
Panama	85	56.5	100	0.34	74	10	50	0.15
Paraguay	25	7.4	92	0.11	94	7.1	38	0.13
Peru	26	1.5	46	0.01	474	7.1	36	0.13
Uruguay	33	7.1	238	0.2	207	24.7	83	0.48
Latin America	12,858	33.4	178	0.56	29,143	22.6	64	0.37

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Wide and shallow

- Non-contributory programs popular across developing world
 - But, Latin America went furthest
- Total spending on average less than 1% of GDP
 - Average spending on contributory pensions is 3.1% of GDP
 - 6+% in Brazil and Argentina
 - 2/3 of Brazil's pension spending goes to richest quintile

Politics of non contributory pensions and CCTs

- Broad coverage
- Low cost
- Easy implementation (ATMs)
 - Spending on monetary transfers grew much faster than on health care
- Financed from increasing revenues from **indirect** taxes
 - without jeopardizing other programs
 - Or raising direct taxes

Coalitions in the easy phase

- Beneficiaries become strong stakeholders
 - Non-contributory programs not demanded by mobilized beneficiaries (not like organized labor)
- Once benefit has been granted, it becomes pivotal issue in voting
 - electoral boost to incumbents in Mexico, Brazil, and Uruguay range from 5 to 14 percentage points
 - Policy entrenchment

Insiders in easy phase

- Little opposition
 - Programs were cheap and did not entail new direct taxes
 - Contributory programs for insiders not affected
- Program design generated support
 - In Brazil, 75 percent supported some redistribution to the poor
 - but only with strong conditionalities and controls

Shifting preferences?

- Some argue that preferences of insiders shifted to align with outsiders
 - Due to de-industrialization and increasingly precarious jobs in the formal sector
- But, we do not find much evidence
 - Survey data weak on identifying those in informal sector and on specifying preferences on social policies
 - We try to rely more on actual cases with revealed preferences

III. Exhaustion of the Easy Phase

- Non-contributory transfers subsidize informal work
 - Median NCP is third of minimum wage
 - Median CCT is 15%
- In principle, increasing payments through CCTs and NCPs could reduce inequality further
 - But at the cost of encouraging more workers to move to the informal sector
 - Partial evidence from Colombia, Mexico, and especially Uruguay (where benefits are more generous)
- Crucial complementarity in new welfare states

Zero sum spending decisions



- Growth in GDP generated new resources in 2000s that could be transferred to new beneficiaries
- Spending decisions in 2010s more contentious
- Dilma vetoed item in bill from congress that would have granted automatic increases to all pensioners

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- Low level of redistribution through taxes and spending
- High level of informality
- Contributory systems still out of reach for most workers
- Rich are not paying income taxes
- Public services are low quality, especially education

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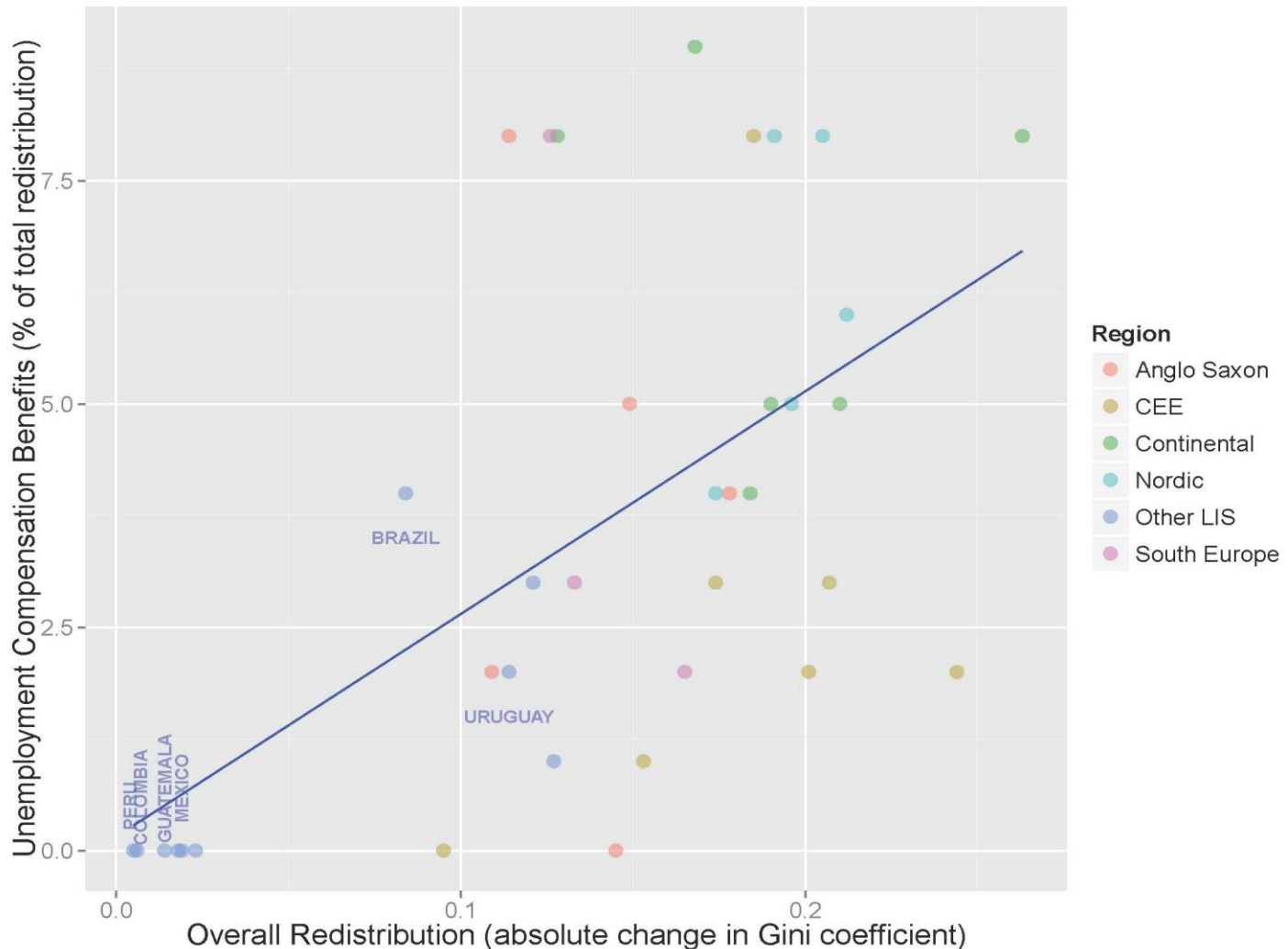
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IV. Challenges of Deepening in Harder Phases of Redistribution

- 3 cases to illustrate difficulties:
 - 1. Insider-outsider division over **unemployment insurance**
 - 2. Bottom hollowing in **housing** policy
 - 3. Top hollowing in middle class exit from public **health and education**
- Challenges related to both:
 - Policy implementation
 - More importantly, coalition building

Unemployment insurance important to higher levels of redistribution



Insider-Outsider Divisions over Unemployment Insurance

- Washington consensus on benefits of UI over severance pay
 - UI increases employment flexibility and protects workers
- Difficulties of implementation
 - Brazilian case of UI promoting informality
- Business opposition
 - High cost of transition from severance pay to UI
- Chilean case of union opposition to UI
 - Insiders feared loss of protection and dilution by inclusion of outsiders
 - Result was diluted UI that covers few workers
 - without much change to severance pay

Bottom hollowing in housing

- Housing is major budget item for families
 - Effective bottom-targeted policy could be very redistributive
- But, policy is hard to target
 - Poor do not qualify for most mortgage subsidies
 - Construction programs require honest, capable agencies
- Coalitions bias policy to middle class
 - Stronger demand for mortgage subsidy
 - Poor have benefitted from forbearance for squatting and prefer spending on services to squatter settlements

Informal equilibrium in Colombia

(Holland 2014)

- Uribe and Santos promised sweeping construction programs
 - But ended up with small subsidies to middle class and expanding squatter settlements
- Middle class prefers subsidies to construction
- Poor prefer public services in settlements to new construction
 - 74% favored granting titles to squatters
 - 52% favored greater spending on housing programs

Top hollowing in health and education

- Basic coverage is near universal, especially education
 - Policy challenge is **quality** not quantity (easy phase)
 - High economic cost in health
 - High political cost in education (teacher unions)
- Upper income groups exit public system
 - 40 % of middle class is in private education
 - Coverage by private health insurance in Brazil rose 40% 2000 to 2010 to almost ¼ of population
- Upper income deciles pay most taxes, but do not want to pay twice for health and education
 - First in private sector for their own families
 - And second time in taxes for public services for the poor
- So, public services stay bottom-targeted and low quality

V. Conclusions

- Hybrid emerging type of welfare state in Latin America?
 - Liberal style welfare state in targeted benefits
 - but low income tax
 - Conservative/corporatist in contributory system
 - For a minority labor elite
 - Many political and administrative obstacles to moving to universal, social democratic model
- Conceptually, need think of **fractured groups** rather than voters on an income scale (Meltzer & Richard)
 - Fragmented by position in labor market
 - And by path-dependent connections to welfare state

Limits to increasing minimum wages?

