

## Is Inequality that High in Chile?

**When considering the effect of social policies through monetary subsidies in housing, health and education, we observe that inequality levels in Chile are not bad. Actually, they are comparable to the levels of European countries. It is not true either that social policies are in the doldrums, since we observe that younger generations show increasingly better income distributions, a phenomenon which cannot be observed when considering the aggregate data.**

We are used to hear that inequality in Chile is very strong, that it does not get better, and that it is responsible for great deal of the social dissatisfaction. This argument has justified the proliferation of countless redistributive policies which today represent the greatest part of public spending, impairing spending on public goods and even, in certain cases, economic growth. It is curious that, after several years in which the State's main social policy has consisted in increasing spending on these programs, the inequality levels are still as alarming as shown by official indicators. As a matter of fact, these indicators tend to consider the families' earned incomes and monetary incomes, but they do not reflect the fact that their total consumption level is much higher due to the effect of social policies, which allow the poorest families in Chile to have free access to housing, health and education. Evidently, the indicators not taking into account these non-monetary transfers do not appropriately reflect inequality in terms of quality of life.

### **Incomes Considering the Fiscal Policy**

In Chile, the higher-income families earn many times more than the lower-income ones. However, this comparison is incorrect because while the lower-income families receive free or highly subsidized health, education and housing services, the higher-income families

have to finance these services on their own, which represent an important fraction of the family budget. With the information of the survey on National Socioeconomic Characterization (CASEN, in Spanish), it is possible to get an idea of a family's consumption of health and education subsidies. These services can be valued on the basis of the spending they imply for the State. In the case of housing, the CASEN survey assigns a rent value for the house occupied by the family. With these values we have a corrected total income which better reflects the family's standard of living, considering the effect of the quite generous social policy in Chile.

Table 1 shows the inequality index 10/10<sup>i</sup> in Chile for different types of family incomes, which allows appreciating the effect of social policy on the income distribution. The index 10/10 shows how much more, on average, a person pertaining to the richest 10% of the population earns compared with a person of the poorest 10%.

We observe that in the case of earned incomes, that is, the incomes generated by the families themselves, the dispersion is quite high and we do not appreciate a downward trend. When considering the monetary incomes, corresponding to the earned incomes plus the monetary subsidies received by the families, the income difference is significantly reduced, and it also shows a significant improvement between 2000 and 2006. When considering the monetary incomes plus the allocated rent, we observe an additional reduction of this index. Finally, when we include the subsidies which the families obtain in education and health, the index 10/10 reaches levels comparable to those of European countries, who characterize for their low income dispersion.

Table 1

### INDEX 10/10 FOR DIFFERENT TYPES OF INCOME

Type of income	1990	2000	2006	2009
Earned Income	46.7	54.3	41.2	52.4
Monetary Income	40.7	45.7	30.8	29.4
Mon. In. + Allocated Rent	34.4	38.0	26.5	25.4
Mon. In. + All. Rent + Education and Health Subsidies	15.0	18.3	13.9	13.5

Source: Prepared by L&D with data of the CASEN Survey 2009<sup>ii</sup>

Table 2

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### INDEX 10/10 IN EUROPE, 2009

Country/Region	Index 10/10
European Union	22.3
Denmark	14.6
Spain	13.6
France	7.0
Germany	7.1
Italy	8.9
Latvia	13.1
Portugal	10.4

Source: Prepared by L&D with data from the European Union

Table 2 shows the index 10/10 for a number of European countries and the European Union (EU) as a region. We see that the inequality index incorporated by social policies in Chile reaches levels comparable to those of Denmark or Spain. Although the comparison between the values of Tables 1 and 2 is not so direct, because the values of Table 2 do not consider the effect of social policies in their respective countries, the comparison is by all means reasonable, since in these European countries the education and health subsidies cover the entire population, while in Chile they play an important role as income redistribution mechanisms. The EU has an index 10/10 which is greater than that of each one of its members. The reason is that the countries integrating the European Union are fairly heterogeneous among them. The value of the index 10/10 of the European Union is comparable to the value it has in Chile considering only monetary subsidies and allocated rent.

### Evolution of Inequality

Regarding the evolution of the inequality indices in Chile, there is a tendency to see with concern that they do not show improvements over time. Nevertheless, a more detailed data analysis, carried out by the economist Claudio Sapelli, reveals that new generations do have increasingly lower inequality levels, a fact which is not perceived when analyzing data in an aggregated manner. Chart 1 shows the evolution of the average Gini by cohort in Chile. We observe that the younger generations have much lower inequality levels than before, and there is a downward trend. Although the data in Chart 1 combines different effects which have an influence on inequality,

Sapelli shows in his book that once the cohort effect is isolated, we still observe a decreasing inequality pattern during the last decades.

Chart 1

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### EVOLUTION OF THE AVERAGE GINI BY COHORT



Source: Sapelli (2011), *Chile, ¿Más equitativo?*, UC Editions.

Although it is true that there are important social differences in Chile, figures indicate that (i) the effect of the current social policy is significantly reducing them at levels comparable to the European countries and (ii) it is not true that we are in the doldrums in inequality matters. The younger generations show increasingly lower inequality levels, corresponding to a long-run structural process.

The main inequality problem in Chile is related to self-generated incomes, which are very scarce in the poorest decile, and not to the families' standard of living. This puts forth a completely different scenario for public policies than the traditional redistributive policies. These policies, which have significantly increased in the last decade, actually disincentivize the generation of own-account incomes. The challenge for public policy is not allocating more resources for the less favored sectors, but making that these sectors increase their

productivity and participation in the generation of resources, thus reducing their State-dependence.

Successful social policies must lead to increasingly lower social spending. Consequently, to keep increasing the redistributive spending would not be consistent with a real disposition to uproot poverty, reduce dependence and improve equal opportunities.

### Conclusion

When considering the effect of social policies through monetary subsidies in housing, health and education, we observe that inequality levels in Chile are not bad. Actually, they are comparable to the levels of European countries. It is not true either that social policies are in the doldrums, since we observe that younger generations show increasingly better income distributions, a phenomenon which cannot be observed when considering the aggregate data.

The most significant inequality in Chile is related to the incomes generated by the families themselves, and not to their standard of living. This puts forth a different scenario for public policies, since to continue with the income redistribution disincentivizes the generation of own-account incomes. The challenge for public policy is to stimulate productivity and participation of the most vulnerable sectors, which should entail increasingly lower spending on redistributive programs and the adoption of economic policies which foster the creation of new employments.

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<sup>i</sup> The indices 10/10 for the earned and monetary incomes differ from the official figures, because to make them comparable with international values, the deciles were built based on individuals and not households.

<sup>ii</sup> The allocated subsidies correspond to preliminary estimations of an ongoing research from Henoch and Valdivieso.