

# Public Policies in Chile: More Spending is not Necessarily Better

**It is very important that before the State powers demand the population a new effort on resource issues, they demand the Government a greater emphasis on management, since in only five years spending increased almost 60% real, and the quality of the public policies has not done justice to it.**

In the last five years, we have probably witnessed the highest government spending increase in the recent Chilean history. In fact, between 2005 and 2010, public spending increased 58.2% real, while in the same period, the GDP increased only 17.2%. The consequence of this gap was that the size of the central government as a percentage of the GDP grew from 19.3% to 23.5%, and the additional resources in dollars 2010 accounted for US\$17,600 million. A figure of this magnitude leads necessarily to the question of what has been done with the resources and how much the effectiveness of the public policies has improved. The conclusion *a priori* speaks of a meager accountability, which is mainly explained by the fact that the budgetary discussion itself is focused on the quantity of resources rather than its quality. In conclusion, the increase of resources in specific items or programs end up being a “political triumph”, both for the government and the opposition, something that was quite evident in the last discussion about the education budget, concerning additional amounts between US\$500 million and US\$2,000 million, without clearly detailing the specific destination of the expenditure, nor a certain estimation of the effectiveness of the additional resources.

The results' evaluation process in relation to the use of resources is unfortunately quite absent in the budgetary discussion, which calls for a change of approach. It would be desirable to follow budgetary process criteria of any organization, that is, to discuss how to make more and better policies with the same resources, or how to do the same with less. This is nothing more than an efficiency and effectiveness approach in the use of resources.

The intention of the following analysis is not to make an exhaustive evaluation of government spending, but as a first approach we would like at least to show the destination of this huge increase of resources, first according to the types of expenditure, and then, a functional analysis of spending, with the aim of seeing if priorities have entailed significant improvements.

By type of expenditures, a gross analysis shows priorities that seem correct in relation to the destination, although this speaks little of its efficiency and effectiveness. The expenditure items that have most increased in this period are investment (61% real), capital transfers (95% real) and the expenditures on subsidies and transfers (87%). Table 1 shows the growth rates for different types of expenditures, by year, and the accumulated average for this period.

Table 1

### CENTRAL GOVERNMENT SPENDING (REAL GROWTH RATES)

	2005	2006	2007	2008	2009	2010	Acc. 2010- 2005
<b>RECURRENT EXPENSES</b>	<b>5.9</b>	<b>6.3</b>	<b>8.5</b>	<b>7.3</b>	<b>15.2</b>	<b>8.7</b>	<b>54.9</b>
Personnel	6.1	6.1	7.8	4.9	17.0	9.1	53.2
Consumer and Production Goods	18.4	11.1	14.1	-6.1	19.3	11.5	58.2
& Services	-3.8	-6.2	-7.4	-22.4	6.5	11.4	-20.0
Interests	6.7	7.9	14.2	19.7	16.8	8.6	87.0
Subsidies and Grants	4.8	5.3	2.7	4.6	10.8	6.9	33.9
Social Security	-79.8	-33.0	44.4	62.3	-20.4	47.2	84.0
Others							
<b>CAPITAL EXPENDITURES</b>	<b>10.3</b>	<b>10.3</b>	<b>13.4</b>	<b>12.2</b>	<b>23.9</b>	<b>1.3</b>	<b>76.1</b>
Sales of Tangible Assets	23.4	-32.3	-33.0	70.8	113.5	-47.6	-13.3
Investment	11.6	10.0	24.7	3.6	21.1	-6.6	60.6
Capital Transfers	9.0	9.4	-3.3	28.5	29.5	10.7	95.2
<b>TOTAL EXPENDITURES</b>	<b>6.6</b>	<b>6.8</b>	<b>9.2</b>	<b>8.2</b>	<b>16.9</b>	<b>7.2</b>	<b>58.2</b>

Source: DIPRES (Budget Office)

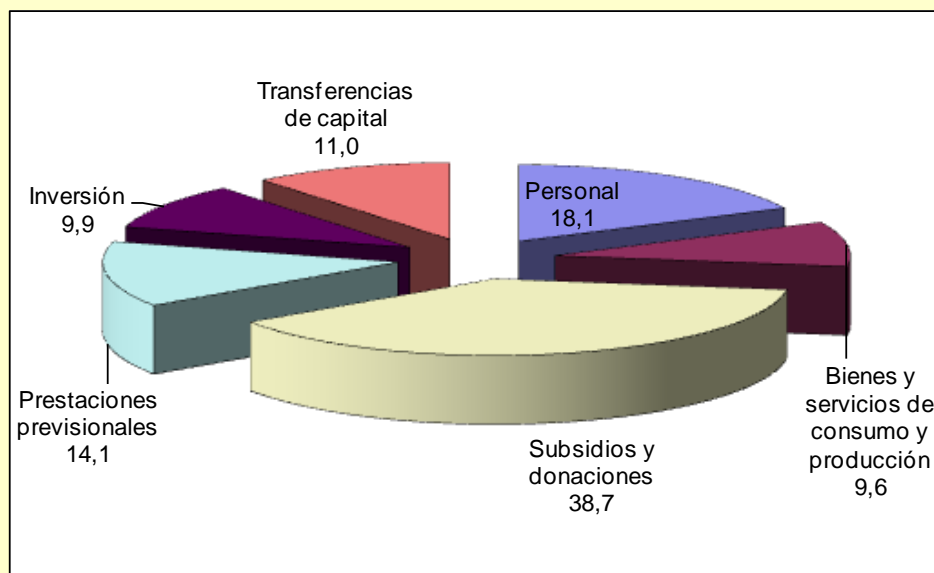
It does not seem so positive for personnel expenses, representing close to 20% of total spending, to increase 53% in this period, and the consumer and production goods and services, 58%. The latter represents almost 10% of the total, which seems a high figure for any type of organization. The fact of these types of expenditures growing at the same rate as the total does not show reasonable efficiency either.

Regarding the expenditures on personnel during this period, the total number of public employees increased by 21.5%, going from 167 thousand to 203 thousand. We observe that the wage bill increased by 26% real in

five years, which results in a quite generous figure of 4.7% real per year. This figure is much higher than the adjustment given at the end of each year, which means that besides the adjustment, the policy for different bonus and allowances is being quite generous. In a previous survey we show that, using the results of the CASEN survey, the income situation for public employees has increased more than that of private workers. The figure above tends to confirm this result. Obviously, the fact of having well-paid public employees is not a negative aspect *per se*. The problem is that these salary gains are not associated to performance factors, but to political pressures. We are not talking about giving lower adjustments, but changing the incentive structure within the public sector. It is highly relevant to radically change the performance evaluation system and to eliminate the rigidity generated by the Administrative Statute.

Chart 1

### PUBLIC SPENDING INCREASE 2005-2010: RELEVANCE BY TYPE OF EXPENDITURE



Source: DIPRES

From the total spending increase of US\$17,600 million, recurrent expenses represent 79% and capital expenditures, 21%. Subsidies and transfers represent 38.7% of the total, followed by the expenditures on personnel, with 18.1%, social security, 14.1% and capital transfers with 11%. Chart 1 shows the share of the different items in the spending increase for this period.

Table 2

## FUNCTIONAL CLASSIFICATION OF PUBLIC SPENDING

	Weighting in the Total 2005-2010	Relevance within the Spending Increase
<b>TOTAL SPENDING</b>	<b>100.0</b>	<b>100</b>
<b>General Public Services</b>	<b>6.3</b>	<b>6.6</b>
Executive and Legislative Org., Financial, Fiscal and Foreign Affairs	3.6	4.4
General Services	0.7	0.8
Basic Research	0.6	1.1
General Public Services (unspecified)	0.2	0.0
Public Debt Transactions	1.3	0.3
<b>Defense</b>	<b>5.7</b>	<b>4.4</b>
Military Defense	5.7	4.4
Research & Development related to Defense	0.0	0.0
<b>Public Order and Police Security Services</b>	<b>6.9</b>	<b>7.4</b>
Police Services	3.2	3.4
Fire Fighting Services	0.1	0.2
Courts of Justice	2.7	3.0
Prisons	0.9	0.8
<b>Economic Affairs</b>	<b>14.4</b>	<b>15.1</b>
General Economic, Commercial and Labor Affairs	0.5	0.5
Agriculture, Forestry, Fishing & Hunting	1.5	1.0
Fuels and Energy	0.3	0.3
Mining, Manufacturing and Building	0.2	0.1
Transport	9.5	10.3
Communications	0.1	0.1
Other Industries	0.1	0.1
Research & Development related to Economic Affairs	1.0	1.0
Economic Affairs (unspecified)	1.3	1.7
<b>Environment Protection</b>	<b>0.3</b>	<b>0.4</b>
Contamination Reduction	0.1	0.1
Biological Diversity and Landscape Protection	0.2	0.3
Environment Protection	0.0	0.1

(unspecified)		
<b>Housing and Community Services</b>	<b>1.4</b>	<b>1.9</b>
Urbanization	1.1	1.6
Water Supply	0.3	0.3
Housing and Community Services (unspecified)	0.0	0.0
<b>Health</b>	<b>15.9</b>	<b>18.7</b>
Hospital Services	11.7	14.1
Public Health Services	0.3	0.2
Health (unspecified)	3.9	4.4
<b>Recreational Activities, Culture &amp; Religion</b>	<b>0.8</b>	<b>1.1</b>
Recreational and Sport Services	0.4	0.6
Cultural Services	0.3	0.5
<b>Education</b>	<b>17.7</b>	<b>18.9</b>
Preschool, Primary & Secondary Education	13.3	12.7
Tertiary Education	1.9	2.0
Education not imputable to any level	0.1	-0.1
Education Auxiliary Services	1.7	3.3
Education (unspecified)	0.7	1.0
<b>Social Security</b>	<b>30.7</b>	<b>25.5</b>
Old Age	21.1	12.8
Family and Children	3.0	4.1
Unemployment	0.4	0.4
Housing	4.5	6.1
Research & Development related to Social Security	0.1	0.1
Social Security (unspecified)	1.6	2.0

Source: DIPRES

A second approach for analyzing the expansive fiscal policy of the last five years is through the spending functional composition. Although in this case it is neither possible to determine the exact efficiency problems, it allows seeing which sectors are receiving a major priority, and if these priorities seem the conceptually correct ones.

Table 2 shows the different functions together with their weighting within total expenditure, compared with each one's relevance in explaining the spending increase during the analyzed period.

This table evidences a relatively greater priority for the health, education and transport functions, while the relevance of the defense function decreases. In the case of health, emphasis is given to hospital services, which on its own represented 14.1 of the spending increase, with very little

effectiveness if we analyze the results of the health sector in that period. This seems to demonstrate the management problems in public hospitals. In the case of education, the increase is mainly explained by the education auxiliary services, comprised by *Becas Chile* (scholarships) and the *Junta Nacional de Auxilio Escolar y Becas* (JUNAEB, in Spanish - National board responsible for schools grants and assistance). This increase is mainly explained by the increase of resources for higher education maintenance grants. A somewhat lesser emphasis is observed in preschool, primary and secondary education. Likewise, the greater relevance of the transport function is explained by the resources allocated to *Transantiago*, demonstrating that a greater amount of resources does not necessarily improve the quality and efficiency of public policies.

In the same period, a greater emphasis is observed in spending on legislative and executive organisms, and on the face of the citizens' opinion, this has not entailed a policy quality improvement.

### **Year 2009**

The circumstances of 2009 deserve special attention, since almost 40% of the spending increase of US\$17,600 millions for the five-year period took place in this specific year, as a result of the anti-cyclical fiscal policy implemented in view of the crisis. The first thing that calls our attention is that, in spite of the fact that government spending increased by almost 17% real, the economy GDP dropped 1.7%, so the effectiveness of the policy is doubtful. This does not contradict what is expectable in an economy with flexible exchange rate and which succeeded in maintaining the access to external capital flows. In this case, the government spending increases, more than generating net economic activity increases, end up being equivalent to a transfer from tradable sectors of economy towards those favored by the public spending increase, as a result of the drop of the real exchange rate generated by the policy. It is important to take this consideration into account if a more expansive fiscal policy is finally necessary in 2012, in view of an external scenario which could turn out less favorable than expected. This space must be delimited, as set forth by the Corbo Commission Report, not over 0.5% of the GDP, that is, around US\$1 billion, and with a clearly transitory nature. This was not observed in the spending increases of 2009. If we look at Table 1, in 2009 all items increased in a very significant way, including the administrative kind of expenditures (personnel and service and production goods, with real growth rates of 17% and 19.3% respectively), and none of it was reversed in the following year. What happened that year shows how difficult it is to implement transitory-nature expenditures; therefore, this policy should be used only under very exceptional circumstances.

### Conclusions

In the current scenario, with a considerable pressure put on increasing the size of the public sector, it is interesting to analyze what happened in the period 2005-2010, when the size of the central government increased by 4 points of the GDP. Although in gross terms, priority was given to subsidies and grants and capital expenditure, we can also conclude that the efficiency degree of this process leaves much to be desired. Several examples for that period show that more resources do not necessarily entail better public policies, and the *Transantiago* example is not the only one.

The considerable increase registered by the wage bill per employee in that period calls our attention, since it is quite beyond the given nominal adjustment. The growth and relevance of the administrative costs (service and production goods) seem also questionable.

Finally, in view of the current circumstances, it is essential to look more attentively at the situation of 2009, when, as a consequence of the external crisis, a spending increase of 17% real was implemented, and the objective of a transitory increase was not in the least accomplished.

It is very important that, before the State powers demand the population a new effort on resource issues, they demand the Government a greater emphasis on management, since in only five years spending increased almost 60% real, and the quality of the public policies has not done justice to it.

In brief...

**WHERE DID THE EXPLOSIVE PUBLIC SPENDING INCREASE BETWEEN 2005 AND 2010 END UP?** (It increased 58.2% real, while the GDP increased only 17.2% in that period)

- **Public employees:** it is not positive for the personnel expenditures, representing close to 20% of the total spending, to grow 53% in that period and neither that, in the same term, the total number of employees increased by 21.5%, going from 167,000 to 203,000. The wage bill increased by 26% real in five years, which results in a quite generous figure of 4.7% real per year.
- **Consumer goods and services:** the expenditure on consumer goods and services increased by 58%, which represents nearly 10% of the total, a figure that any organization would consider high.
- **Public hospitals:** with regard to health, emphasis is given to hospital services, which on its own represented 14.1% of the spending increase, with very little efficiency if we analyze the results of the health sector for that period. This seems to evidence the management problems within public hospitals.
- **Higher education scholarships:** in the case of education, the increase is mainly explained by the education auxiliary services, comprising *Becas Chile* and the JUNAEB, mostly due to the increase of resources for higher education maintenance grants. A somewhat lesser emphasis is observed in preschool, primary and secondary education.
- **Transantiago:** likewise, the greater relevance of the transport function is explained by the resources allocated to *Transantiago*, demonstrating that a greater amount of resources does not necessarily improve the quality and efficiency of public policies.