

# Can Governance Factors Explain Persistent Inequality in Latin America?

N.º 133 | June 2024

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- ➔ Governance factors on both the demand side (e.g., low voter trust) and supply side (e.g., vote buying) have limited the extent of redistributive policies in Latin America.
- ➔ Countries with stronger democracies have adopted more redistributive policies, even though post-tax inequality remains high in all the region's democracies.
- ➔ Electoral participation has risen in the more democratic countries, while economically motivated protests have increased in weakly institutionalized settings.

## CONTEXT

Income inequality is a persistent policy issue for Latin America, with wide-ranging implications for the region's economic and social development. The richest 10% of the population earn more than half of the total income, while the poorest 10% earn less than 2%. This income gap has remained wide over the last three decades, and the COVID-19 pandemic has exposed and exacerbated inequality. While economic inequality should to some extent be self-correcting through majority demand for redistributive taxation and spending, democratic failures on both the demand and supply sides have limited the extent of redistributive policies in Latin America.

## PROJECT

The project draws on both macro and micro data to shed light on the governance determinants of inequality in Latin America. The macro-data are assembled from multiple sources. Inequality indexes and government spending data are from international organizations such as UNESCO and WHO. Governance data are from the Gallup Poll and the Economist Intelligence Unit. The micro-data are from the IDB-LAPOP Survey, which asked voters in 7 countries to weigh the trade-offs between two spending alternatives, one of them more vulnerable to the biases of voter mistrust. Questions elicited preferences for redistribution and for government provision of public goods.

### Key Concept

#### INTERPERSONAL TRUST

Confidence in the motives of others that supports willingness to accept vulnerability in social interactions.





## RESULTS

### **Stronger democracies have more pre-tax inequality on average, but not more post-tax inequality, compared to weaker democracies.**

Democracy is measured as an index (averaged for 2006-18) that summarizes the quality of each country's democratic process along five dimensions: civil liberties, political culture, political participation, functioning of government, and electoral process and pluralism. Post-tax inequality drops in virtually every country, suggesting that fiscal policy has an equalizing effect across the board. On average, the Gini coefficient drops from 0.506 to 0.437, suggesting that stronger democracies more effectively reduce inequality through the tax system. Indeed, stronger democracies tend to allocate more fiscal resources to social protection (see [Figure 1](#)).

Stronger democracies in the region appear to have higher voter turnout but fewer street protests on average. Public spending on education and health, which tend to be pro-poor, correlate positively with interpersonal trust from the Gallup World Poll. The correlation coefficients are around 0.20. At the same time, low interpersonal trust is associated with weak income redistribution. Public education has a redistributive dimension, particularly primary and secondary education, as it disproportionately benefits lower-income individuals. Voters in the region, however, exhibit a low level of support for redistribution policies financed through higher taxes, even though such policies could increase aggregate welfare. One explanation is that low-trust voters believe that the government will misallocate fiscal resources.

#### Key Concept

### GINI COEFFICIENT



A statistical measure of economic inequality measuring the dispersion of income in a given population, and ranging from 0 (low inequality) to 1 (high inequality).

Respondents with lower interpersonal trust are about 8 percentage points less supportive of tax-funded government assistance to the poor, and about 6 percentage points less supportive

of progressive taxation that redistributes income from the well-off to the needy. Individuals who express low levels of trust in politician promises are about 7 percentage points less supportive of public investments in education than individuals who report high trust, and also about 7 percentage points less supportive of public investments in public security.



## POLICY IMPLICATIONS

**It is important to develop policies that overcome weak voter demand for pro-poor public spending, a particularly notable problem in low-trust environments, as voters at the low end of the income distribution do tend to vote less often and to be less engaged in the democratic process.** In addition, inequality may lead to partisan polarization, and political polarization can further increase inequality. Overcoming this vicious circle raises a challenge for the region's relatively young democracies. A public commitment to strengthening democratic institutions—in the government sector and civil society alike—and concrete policies to safeguard the electoral process and protect freedom of participation and expression, should over time improve representational outcomes, including economic equity, in these societies.

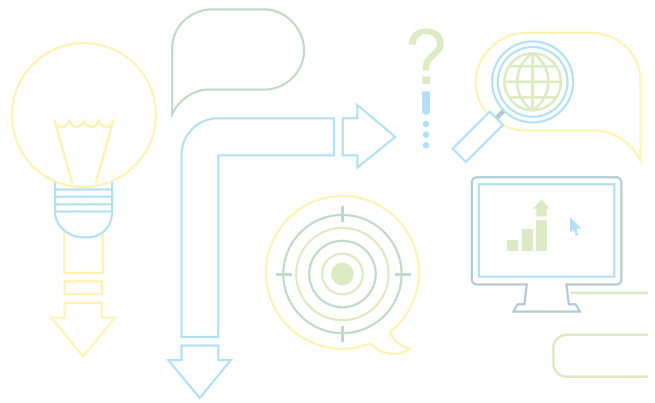
It is also possible that current redistributive policies fall short because of implementation failures in the targeting of transfers and public goods. To determine this, more granular data on fiscal outlays is needed, particularly at the local level. As several countries in Latin America use a system of fiscal decentralization based on grants to localities from the central government, local accountability for the allocation of these transfers becomes a key issue. Yet, local politicians face little accountability for efficient public spending because the cost of this spending, tax revenues, is not borne at the local level; this may lead to overspending and misallocations. A reform of fiscal institutions may be necessary to reduce these incentive problems. Decentralization of taxing authority and fiscal revenue collection would address some of these issues. These need to be accompanied by increased local state capacity to enforce fiscal obligations, for instance through digitalization of tax and fee collection.

Key Concept

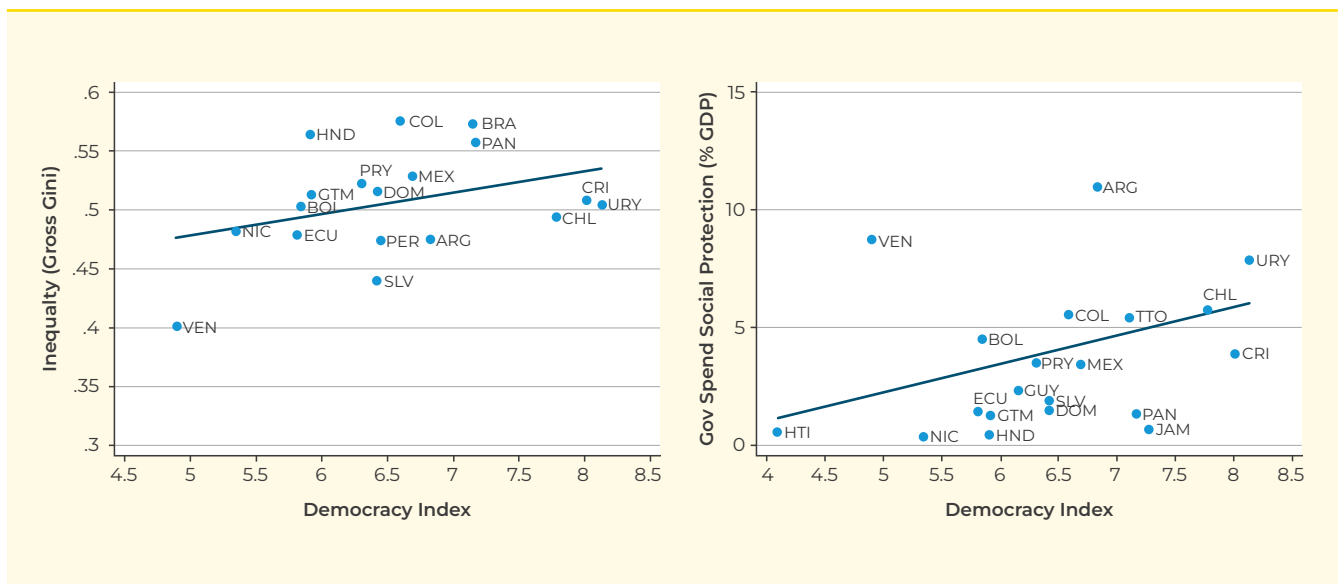
**SOCIAL PROTECTION**



Government policies intended to create an economic safety net for individuals and communities, such as cash transfers, unemployment insurance, and pensions.



**FIGURE 1. Democracy, Inequality, and Redistribution**



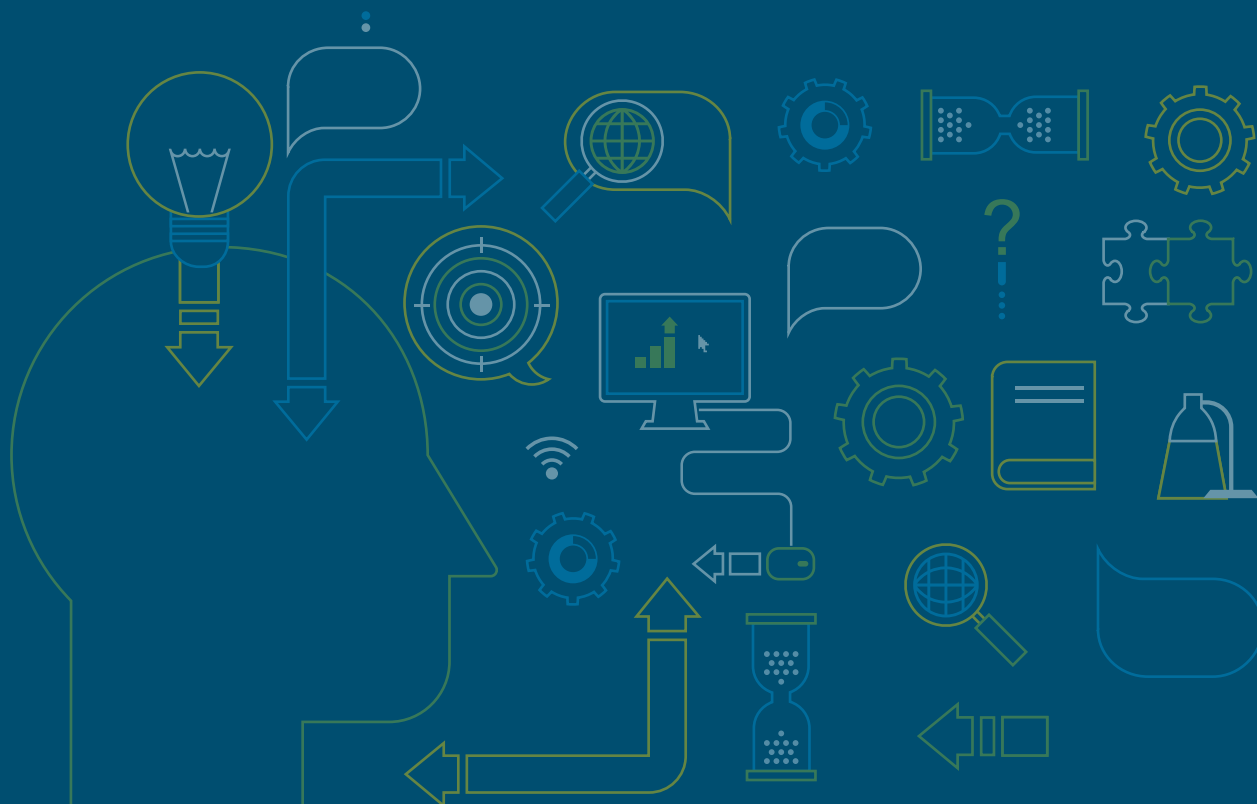
Notes: Pretax (gross Gini) is from the Commitment to Equity Institute Data Center on Fiscal Redistribution. Social protection spending is from the Economic Commission for Latin America and the Caribbean. Democracy Index is from the Economist Intelligence Unit. Democracy values are averaged for the period 2006-18.

**FULL STUDY**

[Vlaicu, Razvan. 2024. "Inequality Persistence and Policymaking Constraints: Explaining Regional Data Patterns." IDB Working Paper No. 1599. Washington, DC: Inter-American Development Bank.](#)

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