

# **The Rise and Fall of Income Inequality in Mexico, 1989–2010**

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LASA, San Francisco, May 26, 2012

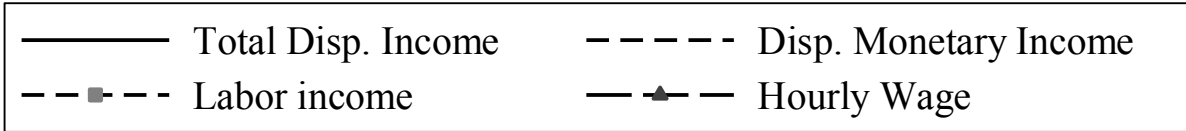
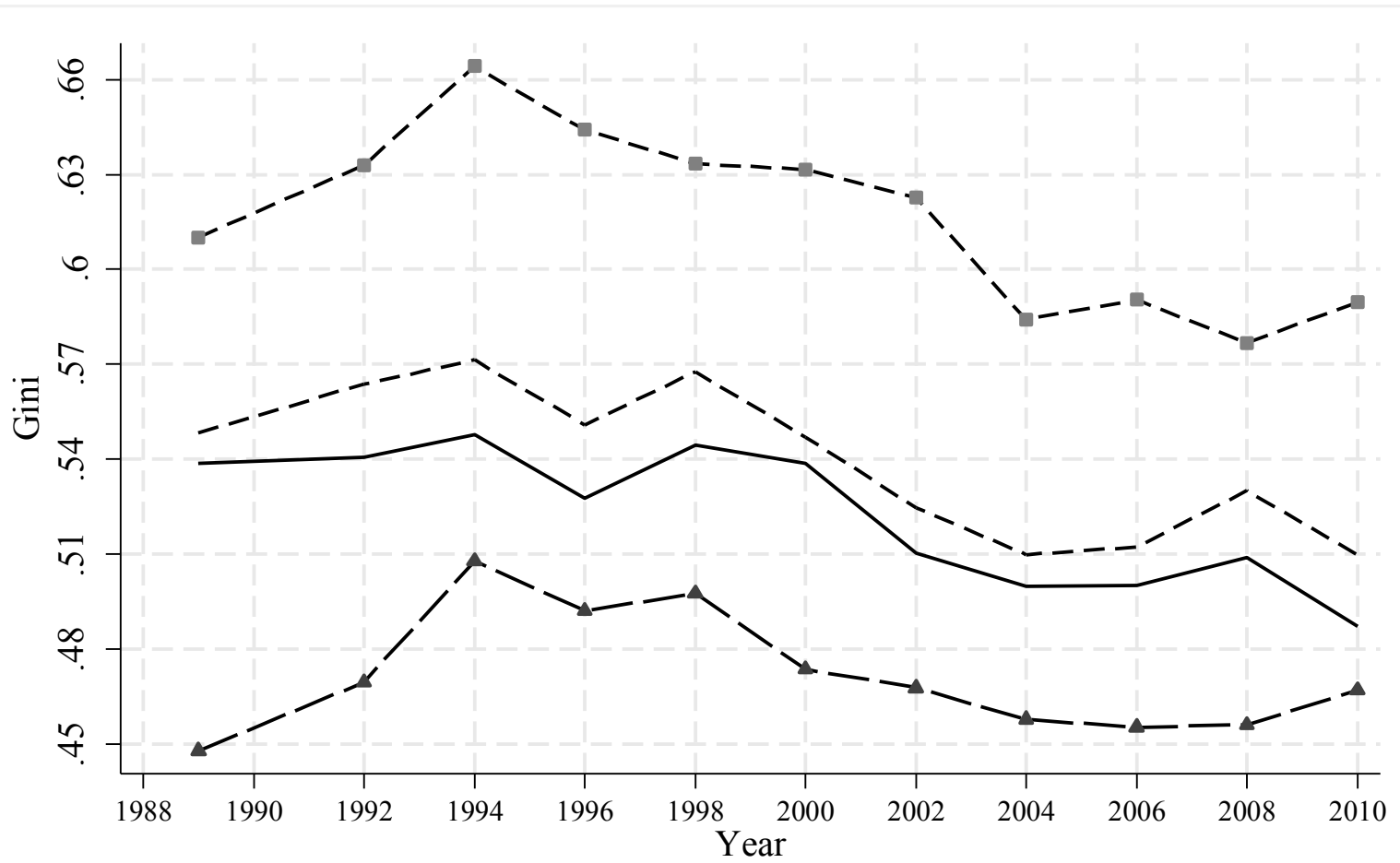
Mexico: Policy regimes, 1989-2010

	1989-94	1994-2010
Macro	<p>A. Aftermath of 1980s debt crisis</p> <p>B. Contractionary fiscal and monetary policies;</p> <p>C. Quasi-fixed exchange</p> <p>D. Very low growth</p> <p>E. Inflation under control starting in 1989</p>	<p>— 1995 peso crisis and recovery</p> <p>— Fiscal discipline (balanced budget law passed in 2006)</p> <p>— Inflation-targeting by central bank since 1999</p> <p>— Flexible exchange rate regime</p> <p>— Low growth (GDP/capita growth of around 1% annually) with some inflation in the second half of 1990s; low inflation since around 2000</p> <p>— Output contracted sharply in 2008/09 due to great recession in US</p>
Labour	<p>— Minimum wages and unionization rates declined markedly</p>	<p>a. Minimum wages stable and not binding. Unionization rates stable with a slight decline since 2005</p>
Openness	<p>— Unilateral trade liberalization since 1985. Mexico joins GATT in 1986.</p> <p>— Foreign direct investment liberalized</p>	<p>b. NAFTA comes into effect in 1994. Other free trade agreements</p>

Other market-oriented reforms	<ul style="list-style-type: none"> <li>— Large scale privatizations (banks and telecommunications)</li> <li>— Deregulation</li> <li>— Dismantling of price support (and other) schemes in agriculture and elimination of general production and consumption subsidies</li> </ul>	a. Social security reforms
Social Policy	<ul style="list-style-type: none"> <li>— Very small scale targeted subsidies to <i>tortilla</i></li> <li>— Flagship anti-poverty program <i>Programa Nacional de Solidaridad</i> focused on expanding rural infrastructures (no targeted cash transfer)</li> </ul>	<p>b. Targeted Cash Transfer Programs: <i>Procampo</i> in 1995 and <i>Progresa</i> in 1997. <i>Progresas</i> changes name to <i>Oportunidades</i> in 2002 and is expanded to urban areas and includes children in high school.</p>
Inequality	Increased	<p>c. Noncontributory pensions in rural areas in 2007 (<i>Seventy or more</i>)</p> <p>d. Declined especially between 1998 and 2004; between 2006 and 2010, decline loses momentum and wage inequality slightly rises</p>

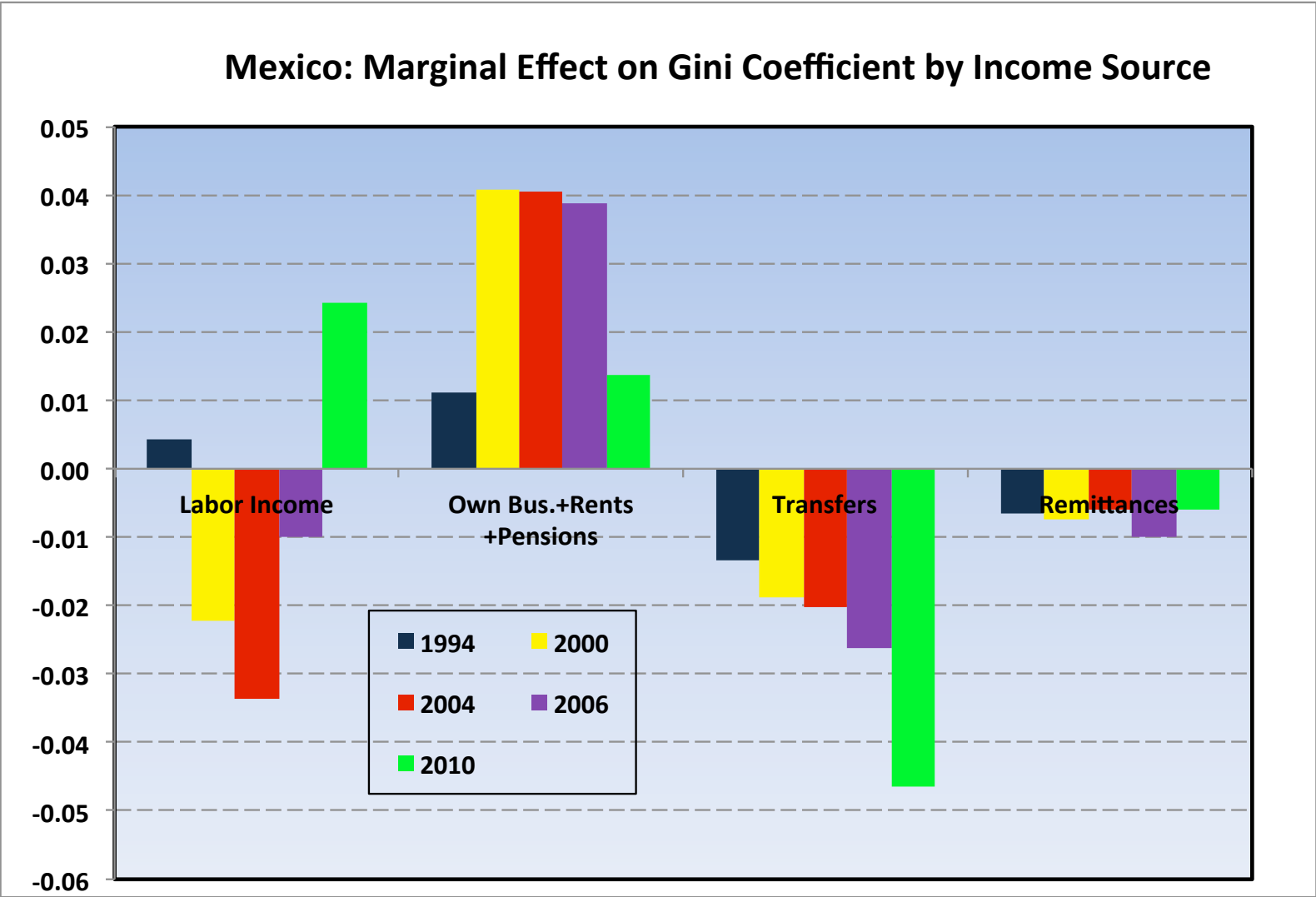
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Mexico: Evolution of the Gini Coefficient, 1989-2010



Mexico: Decomposition of overall inequality, 1994, 2000, 2004, 2006 and 2010

Mexico: Marginal Effect on Gini Coefficient by Income Source



- Labor income/wage inequality plays an important role in explaining overall inequality

- Wage inequality is affected by two main factors:
  - distribution of characteristics of workers (e.g., education, experience, gender, talent.)
  - returns to those characteristics

- Workers' characteristics, in turn, are affected by:
  - 'fate' (e.g., gender, race, talent)
  - households' decisions (e.g., to enroll children in school)
  - policy (e.g., expanding access to education).

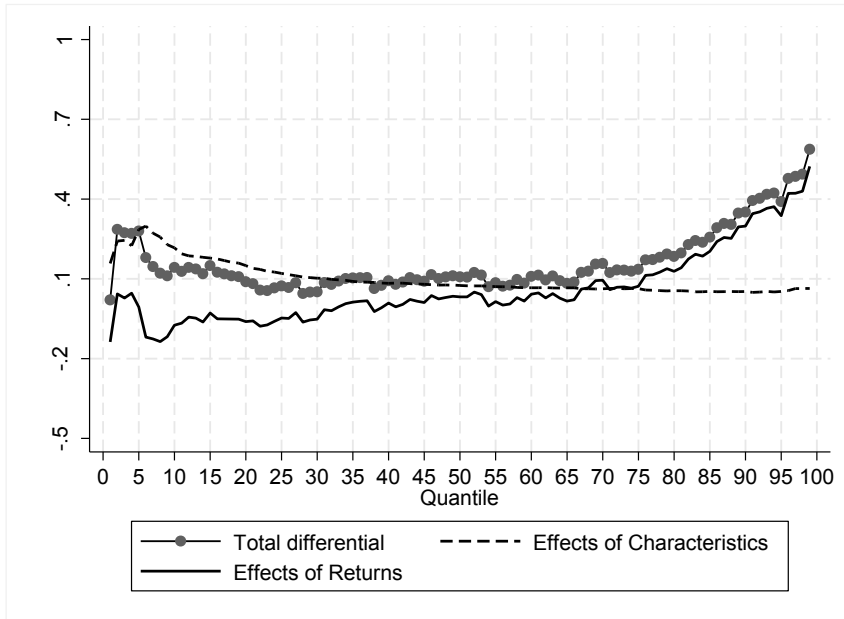


- Returns to households' characteristics depend on:
  - market forces (i.e., demand and supply of workers of different skills and experience)
  - institutional/policy factors (e.g., minimum wage policy and the unionization rate).

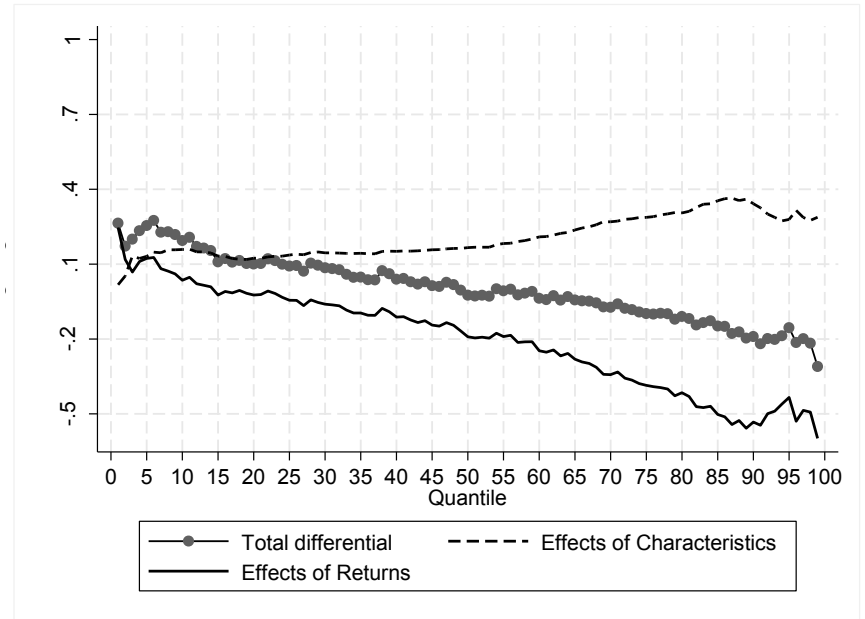
- Decompose changes in wage inequality into a returns (aka skill premium; aka wage gap) and a characteristics effect (distribution of skills)

# Mexico: Decomposition of differences in the distribution of earnings: 1989-2010

## A: 1989-94

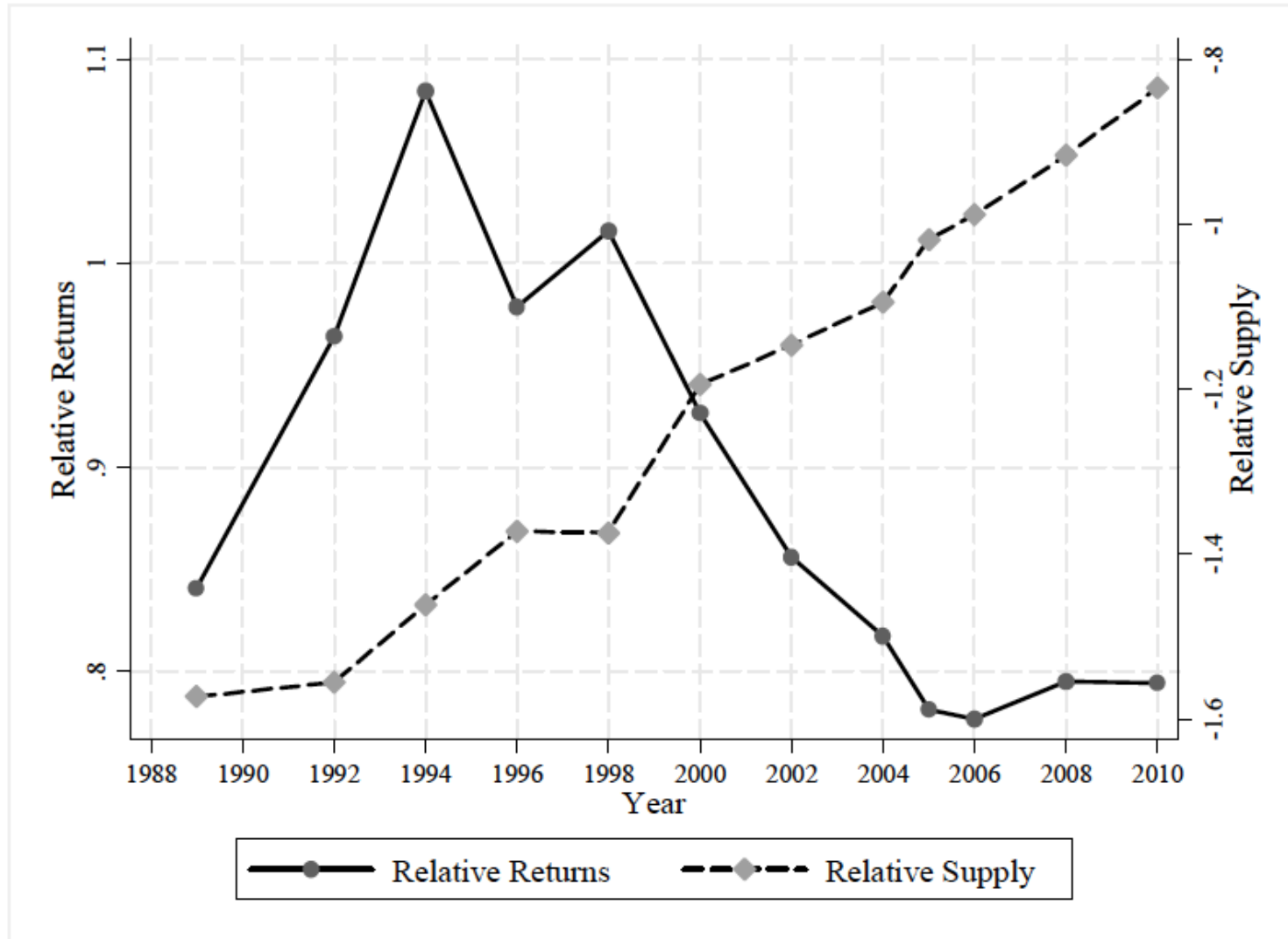


## B: 1994-2006



- Changes in the distribution of characteristics were flat in the first (1989-1994) and unequalizing in second period (1994-2010)
- Changes in the relative returns or skill premium were unequalizing in the first (1989-1994) and strongly equalizing in the second period (1994-2010)

Mexico: Relative returns and relative supply, 1989-2010  
(High school and more vs. secondary or less)

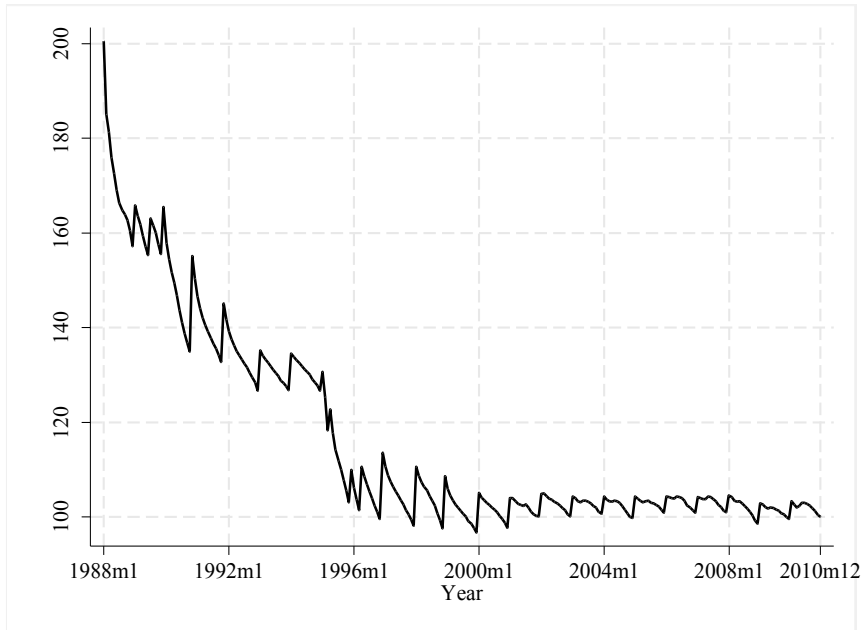


# Explaining the rise and decline of skill premium

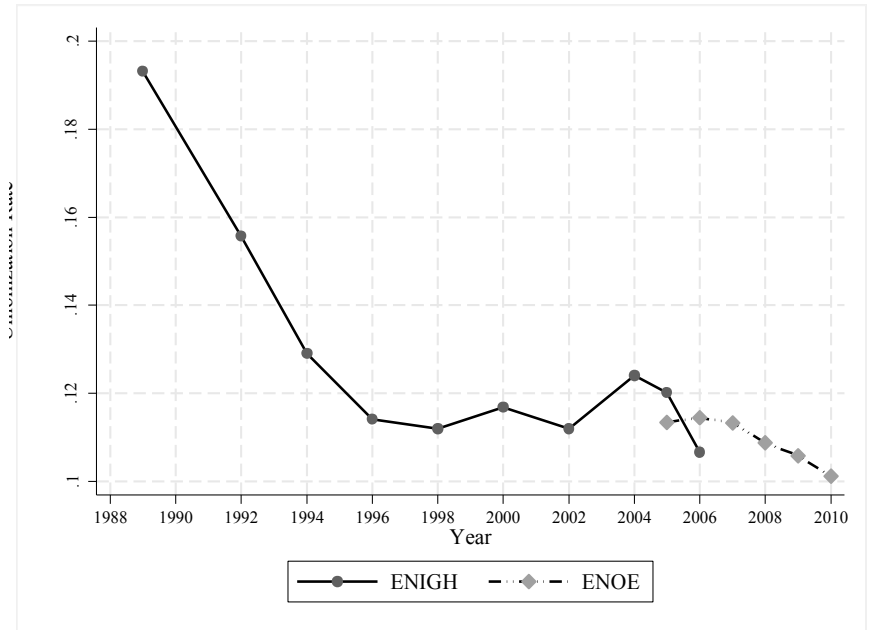
- Demand for skilled labor
- Supply of skilled labor
- Institutional factors: minimum wages and unionization rates

# Real Minimum Wage and Unionization: 1988-2010

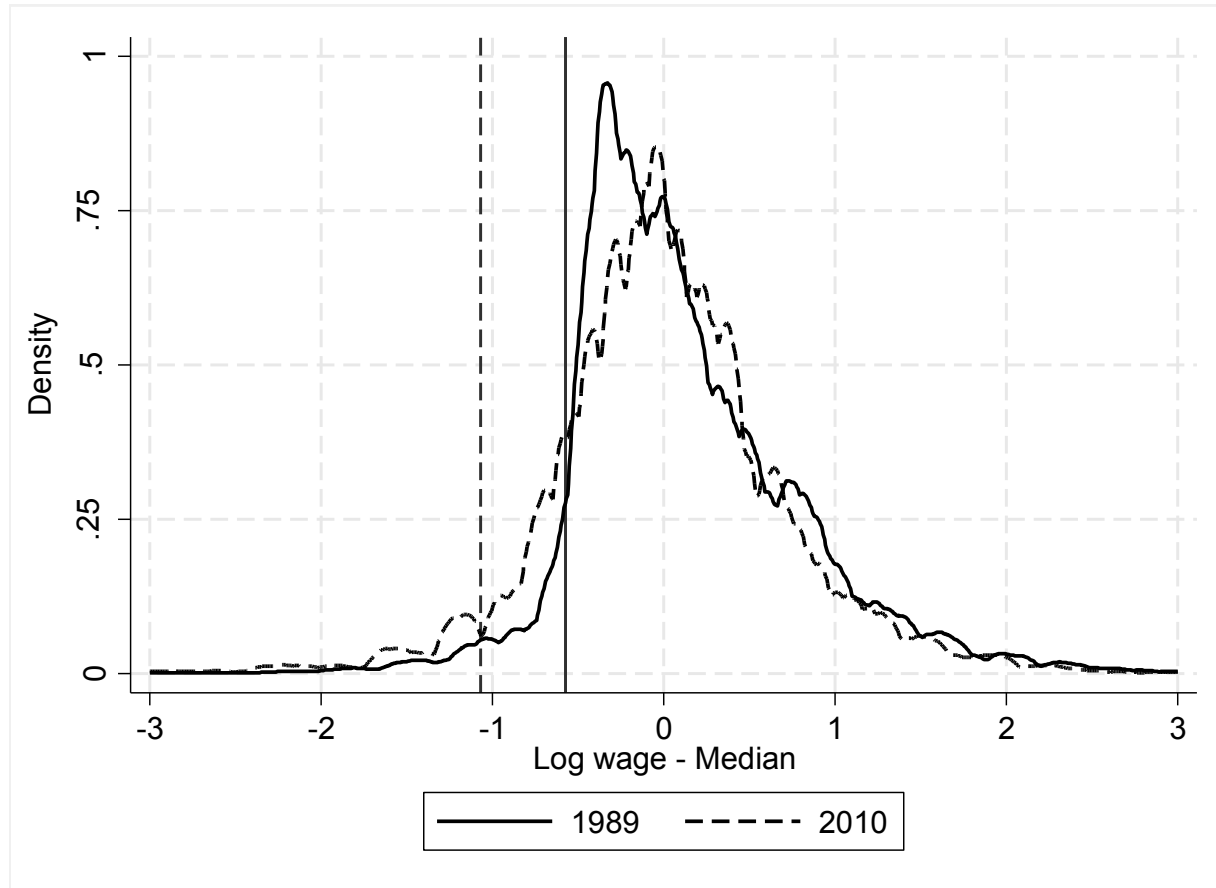
A. Real Minimum Wage Index (December 2010=100)



B. Unionization Rate



Mexico: Wage distribution with respect to median wage, 1989 and 2010





Mexico: Effects of supply on relative wage, 1989-2010

	Change Returns	Supply	= Rest
Panel A. $\sigma=1$			
1989-94	0.240	0.111	0.351
1994-2006	-0.310	0.474	0.164
2006-10	0.020	0.154	0.174
Panel B. $\sigma=2$			
1989-94	0.240	0.055	0.295
1994-2006	-0.310	0.237	-0.073
2006-10	0.020	0.077	0.097

Source: Authors' estimates based on ENIGH, several years.

- Rising earnings inequality (1989-1994):
  - Institutional factors played a role
  - Demand for skilled labor outpaced supply
- Declining earnings inequality (1994-2010):
  - Institutional factors in labor market not important
  - Expansion of access to education increased the relative supply of skilled workers above demand

# Government Transfers

- Targeted Cash Transfers: Progresa/Oportunidades; Temporary Employment Program(PET); noncontributory pensions (70 o más); PROCAMPO
- Increased in coverage significantly over time, especially Oportunidades (around 5 million beneficiary households)

Mexico: The impact of cash transfers on inequality and poverty, 1996, 2000 and 2010

		Net market income	Disposable income
1996	Gini	0.522	0.520
	% change with respect to net market income	—	-0.4%
	Headcount index (\$2.5 PPP)	30.2%	29.9%
	% change wrt net market income	—	-1.0%
2000	Gini	0.544	0.539
	% change wrt net market income	—	-0.9%
	Headcount index (\$2.5 PPP)	22.1%	21.6%
	% change with respect to net market income	—	-2.3%
2010	Gini	0.503	0.495
	% change wrt net market income	—	-1.7%
	Headcount index (\$2.5 PPP)	13.8%	11%
	% change with respect to net market income	—	-20.1%