

Taxes, Transfers, Inequality and Poverty in Latin America

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Commitment to Equity Project

- Commitment to Equity (CEQ) Initiative; Inter-American Dialogue and Tulane University's CIPR and Dept. of Economics.
- Currently: 12 countries
- 6 finished: Argentina (2009), Bolivia (2007), Brazil (2009), Mexico (2008), Peru (2009) and Uruguay (2009) (year of HH survey)
- 6 in progress: Chile, Colombia, Costa Rica, El Salvador, Guatemala, Paraguay
- To begin soon: Dominican Republic (with Lopez-Calva, WB; and Jamaica (with Ruprah, IDB)
- Multi-country project at WB: Can LA Afford Opportunities for All? (with Fiess and Molinas)

References

- Lustig, Nora (coordinator). “Fiscal Policy and Income Redistribution in Latin America: Challenging the Conventional Wisdom,” Argentina: Carola Pessino; Bolivia: George Gray Molina, Wilson Jimenez, Verónica Paz, Ernesto Yañez; Brazil: Claudiney Pereira, Sean Higgins; Mexico: John Scott; Peru: Miguel Jaramillo. , Economics Department, Working Paper 1202, New Orleans, Louisiana, 2012. Forthcoming.
- Lustig and Higgins (2012) “Fiscal Incidence, Fiscal Mobility and the Poor: a New Approach,” to be presented at *Well-being and inequality in the long-run: measurement, history and ideas*, Universidad Carlos III, Madrid, May 31 and June 1, 2012

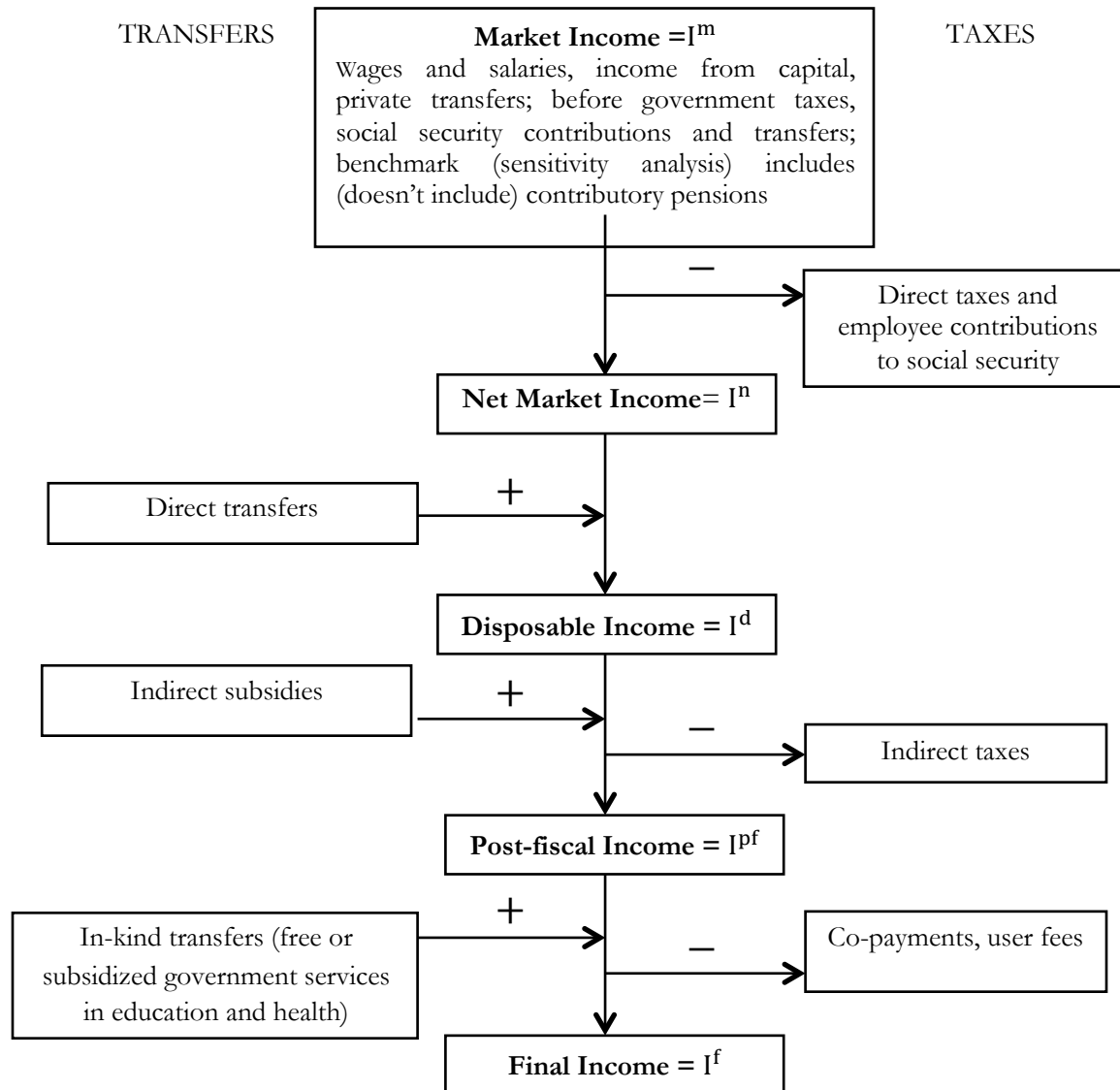
Outline

- How much redistribution LA achieves through fiscal policy? How effective are governments at redistribution?
- Standard Incidence Analysis
- Caveats, at this point:
 - No behavioral responses
 - No inter-temporal effects
 - No general equilibrium effects
 - No macro-sustainability analysis
- Most up-to-date, detailed and microdata-based analysis available

Results: A Primer

1. Lots of heterogeneity in LA
2. No clear-cut correlation between government size, the extent of redistribution, redistributive effectiveness
3. Direct taxes achieve little in the form of redistribution
4. Contributory pensions are progressive in relative terms in most countries (regressive in absolute terms)
5. Direct transfers reduce poverty the most when coverage of the poor is high and average transfer is close to average poverty gap
6. Indirect taxes can make poor people net contributors to the state and a substantial portion of the poor poorer

Definitions of Income Concepts: A Stylized Presentation



Where public *contributory* pensions go matters...

- Benchmark: *contributory* pensions are treated as market income; assumes an actuarially fair system on average
- Sensitivity Analysis: *contributory* pensions are considered as a government transfer
- Redistribution and incidence results are sensitive to the placement of contributory pensions
- Here we shall present benchmark results

Conclusions:

First, Latin America is heterogenous;
can't talk of "a Latin America"

The extent and effectiveness of income redistribution and poverty reduction, government size, and spending patterns vary significantly across countries.

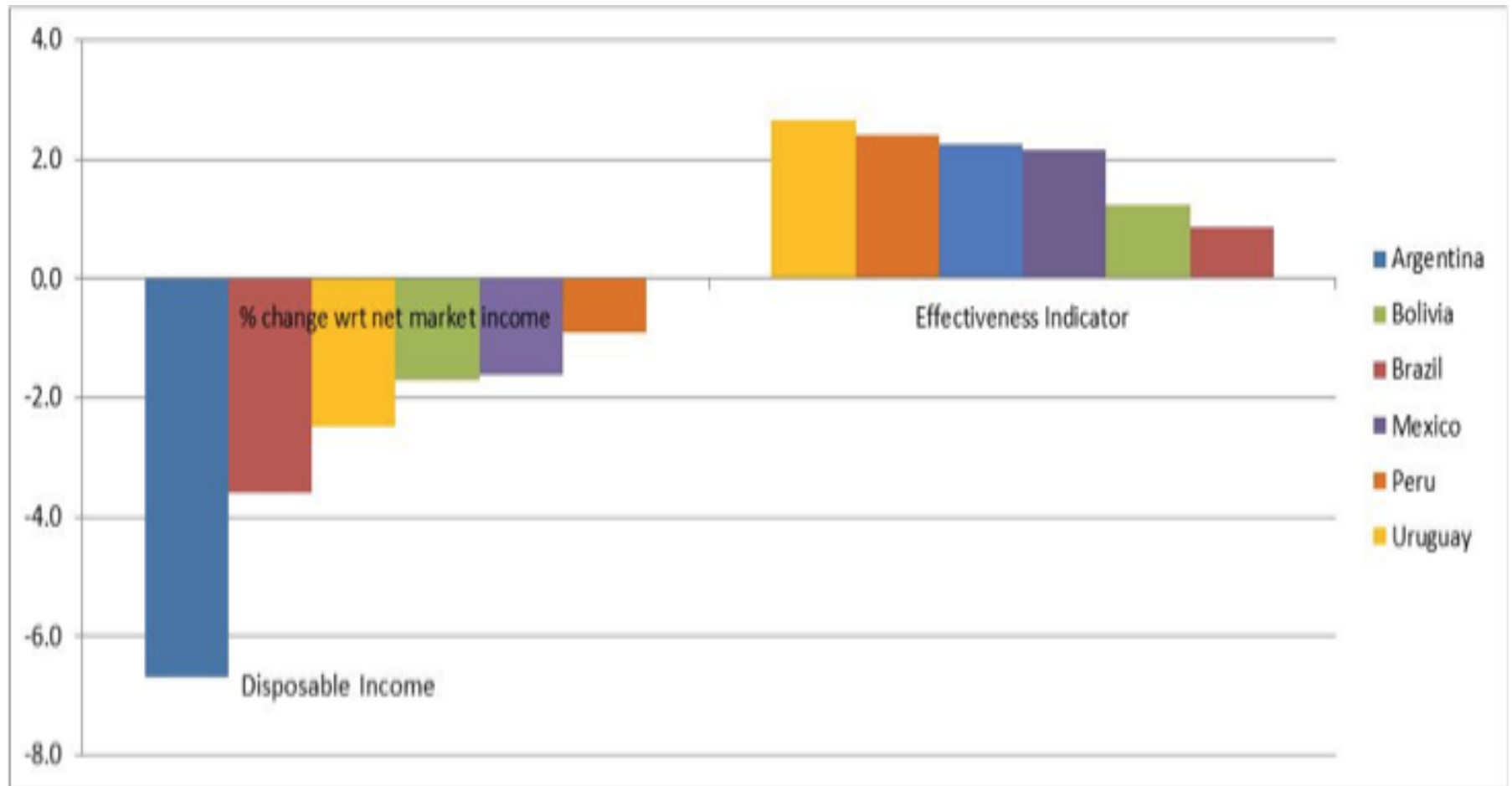
Effectiveness Indicator

Example: Gini net mkt income
& Gini Disposable income

Numerator: $Gini(\text{net mkt inc}) - Gini(\text{disp inc}) / Gini(\text{net mkt inc})$

Denominator: $\text{Gov. Spending on Direct Transfers} / \text{GDP}$

Decline in Gini and Effectiveness: Heterogeneous LA

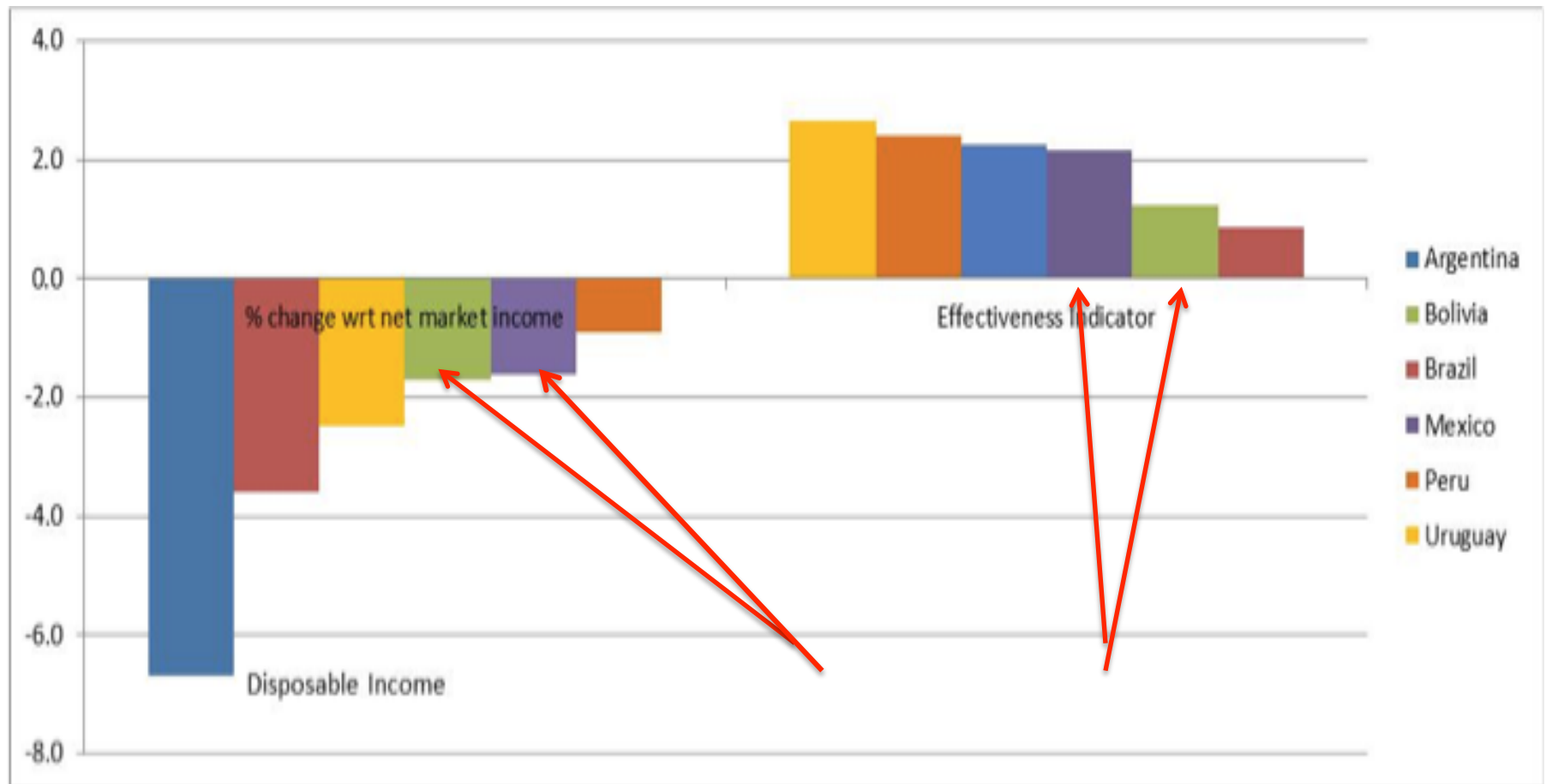


Conclusions

- Second, no clear-cut correlation between government size and the extent and effectiveness of redistribution and poverty reduction.

	Headcount		Headcount				
	Gini	Gini	Ratio Net	Ratio	Direct	Primary	
	Mket	Disposable	Mket	Disposable	Transfers as	Spending as	GDP/cap
	Income	Income	Income	Income	% GDP	% of GDP	U\$PPP
Argentina	0.50	0.46	14%	5%	2.8%	38%	14030
Bolivia	0.53	0.52	22%	21%	1.2%	37%	4069
Brazil	0.57	0.54	15%	12%	4.2%	37%	10140
Mexico	0.53	0.51	12%	11%	0.8%	22%	14530
Peru	0.50	0.49	15%	14%	0.4%	19%	8349

No clear-cut correlation between government size, redistribution and effectiveness



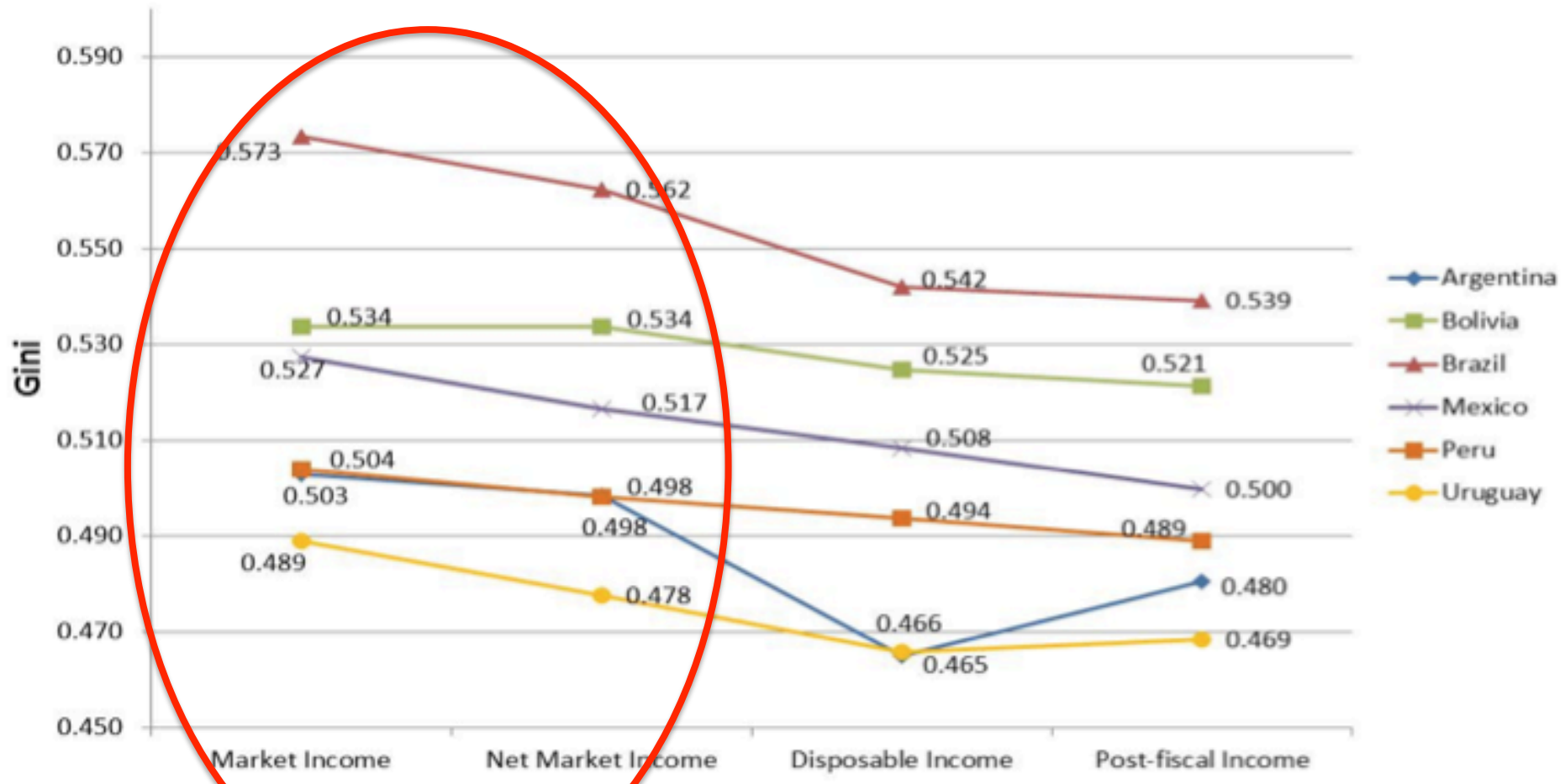
Conclusions

Third, direct taxes achieve little in the form of redistribution.

Caveat:

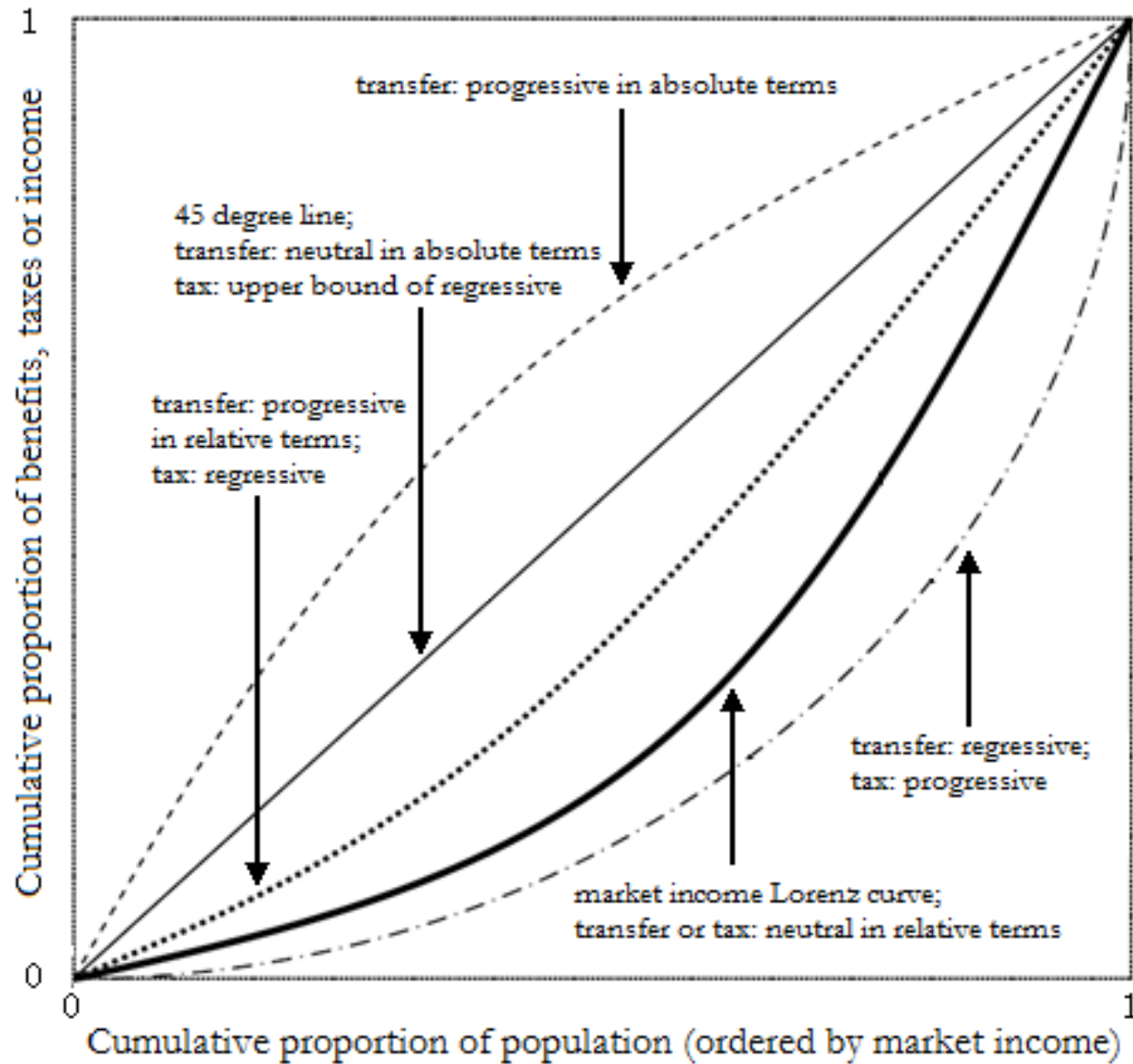
- The rich are excluded from analysis using household surveys; need governments to share information from tax returns (anonymous of course) as all advanced countries do (except for NIC's)

Fiscal Policy and Decline in Gini



- Fourth, contributory pensions are progressive in relative terms (regressive in absolute terms) in Argentina, Brazil, Mexico, Peru and Uruguay.
- The concentration coefficient is substantially lower than pre-transfers Gini.

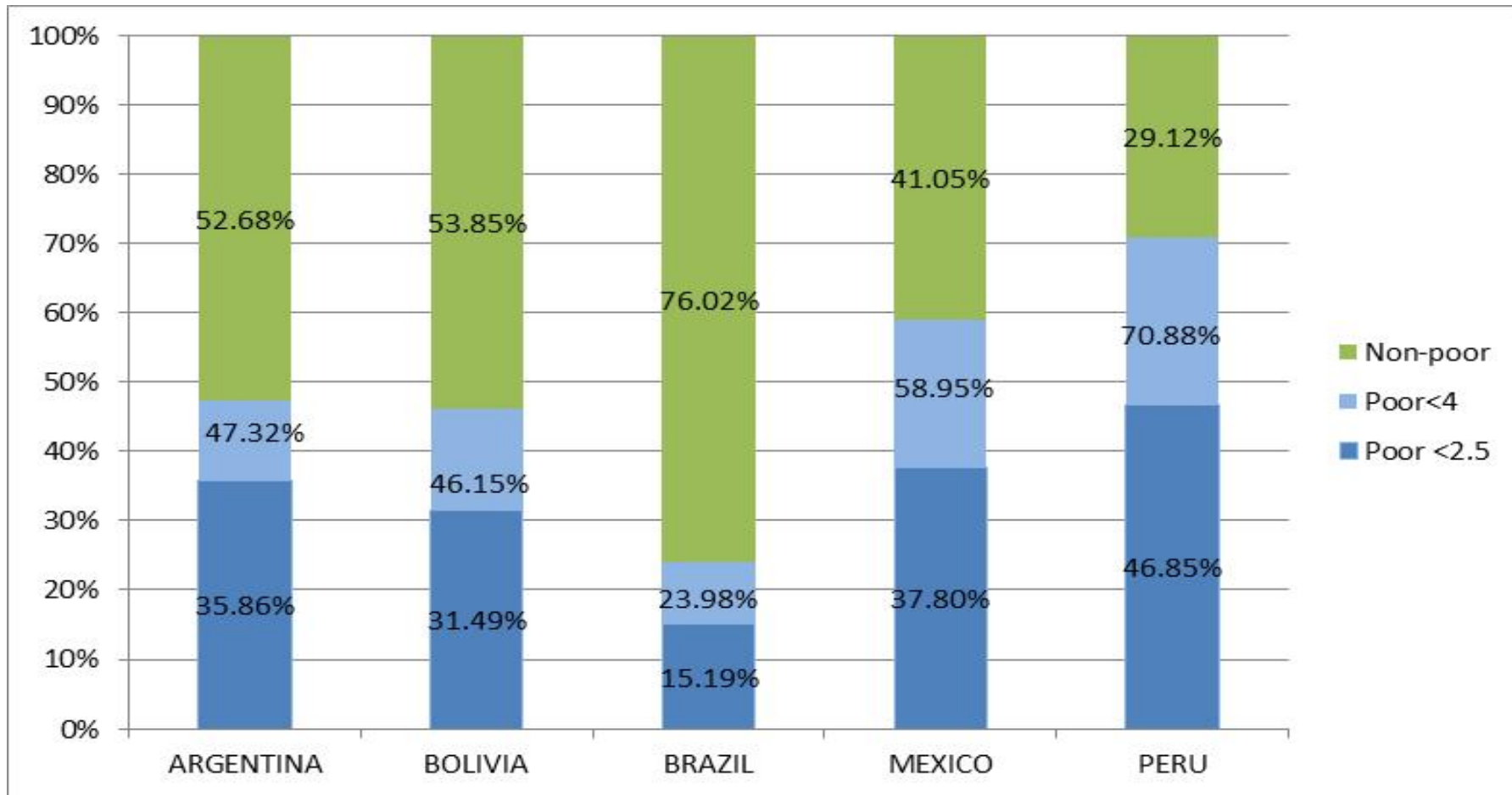
Concentration Curves for Progressive and Regressive Transfers (Taxes)



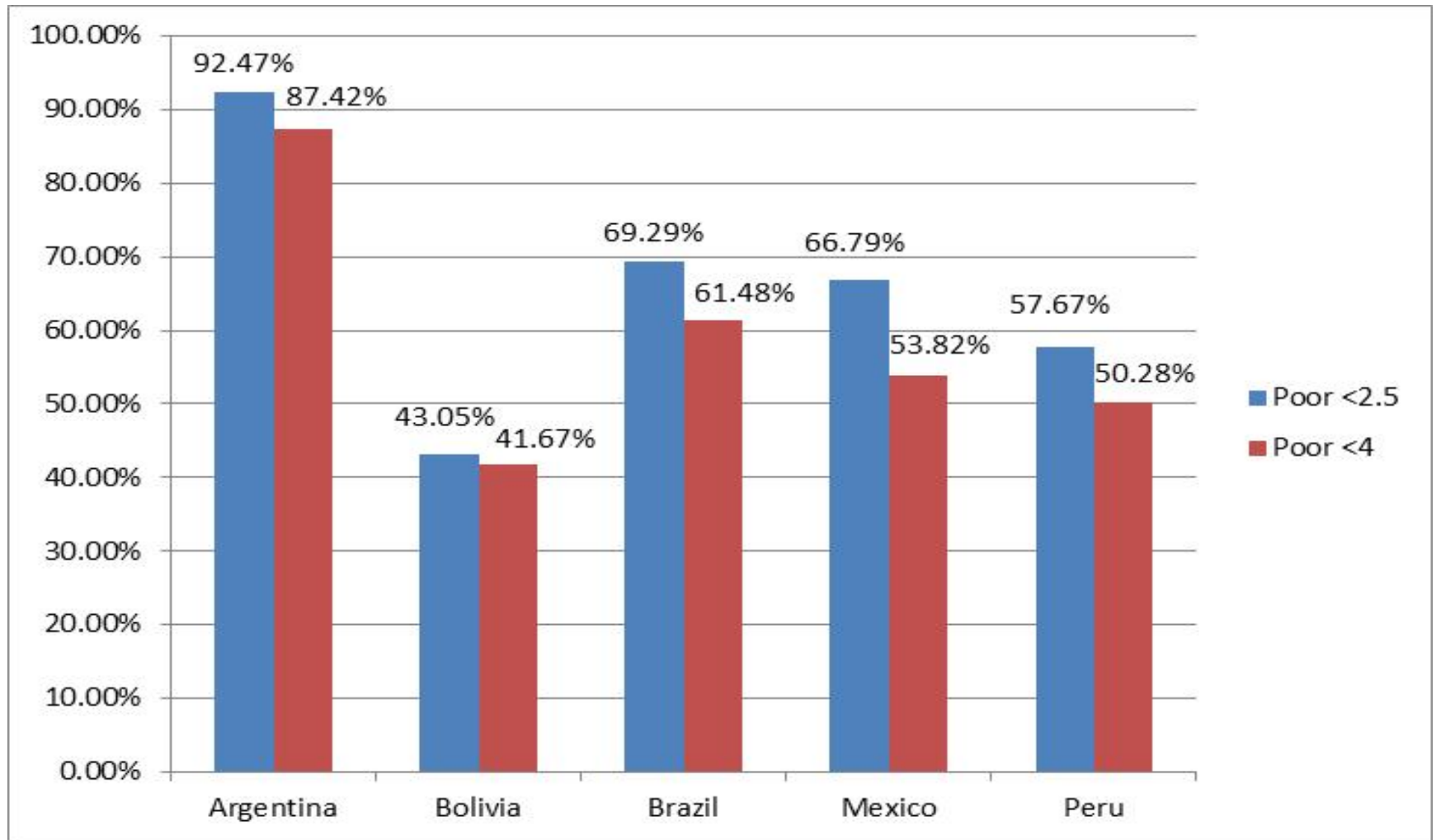
Conclusions

- Fifth, large-scale targeted cash transfers can achieve significant reductions in extreme poverty.
- The extent of poverty reduction depends on:
 - size of per capita transfer (related to leakages to nonpoor)
 - coverage of the poor

“Leakages” to Non-poor



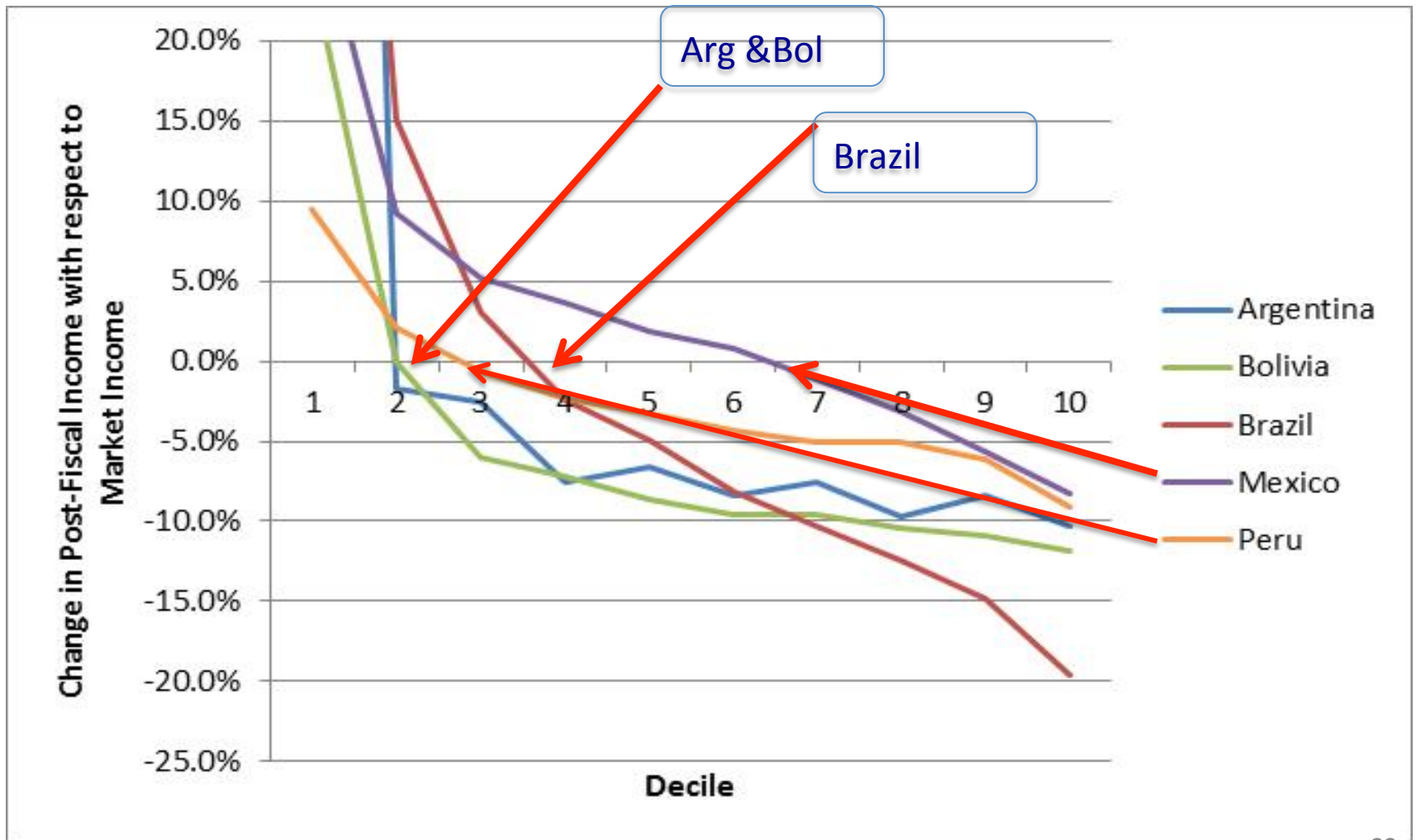
Coverage of the Extreme and Total Poor



Conclusions

- Sixth, when indirect taxes are taken into account
 - The moderate poor and the near poor become net payers to the fiscal system (except for Mexico, 2008)
 - A significant share of the moderate (extreme) poor become extreme (ultra) poor in some of the countries; results for Brazil are striking

Impact of Indirect Taxes



Indirect Taxes and the Poor in Brazil (Lustig and Higgins, 2012)

- Indirect taxes make around 11 percent of the non-poor poor, 15 percent of the moderate poor extremely poor, and 4 percent of the extremely poor “ultra-poor” despite any cash transfers they receive
- We would have missed this with standard analysis:
 - extreme poverty and inequality indicators decline
 - overall taxes are progressive

Fiscally-induced Upward and Downward Movement (in %): Brazil

Fiscal Mobility Matrix for Brazil

Market Income groups	Post-Fiscal Income groups						Percent of population	Mean income
	y < 1.25	1.25 <= y < 2.50	2.50 <= y < 4.00	4.00 <= y < 10.00	10.00 <= y < 50.00	50.00 <= y		
y < 1.25	69%	21%	6%	3%			5.7%	\$0.74
1.25 <= y < 2.50	4%	81%	10%	4%			9.6%	\$1.89
2.50 <= y < 4.00		15%	75%	9%	1%		11.3%	\$3.24
4.00 <= y < 10.00			11%	86%	3%		33.6%	\$6.67
10.00 <= y < 50.00				15%	85%		35.3%	\$19.90
50.00 <= y					32%	68%	4.5%	\$94.59
Percent of population	4.3%	10.7%	13.5%	35.8%	32.5%	3.2%	100%	\$14.15
Mean income	\$0.86	\$1.91	\$3.25	\$6.61	\$19.34	\$88.70	\$12.17	

Note: Mean incomes are in US\$ PPP per day. Rows may not sum to exactly 100% due to rounding. Zeroes are omitted from the matrix for enhanced readability. Differences in group shares between the “before” and “after” scenarios are all statistically significant from zero at the 0.1% significance level.

Source: Lustig and Higgins (2009) based on POF (2008-2009).

Thank you