WORLD INEQUALITY LAB

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Inequality in Latin America Revisited: Insights from Distributional National Accounts

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Overview

This issue brief describes preliminary findings from the new Latin American income inequality series presented in the November 2020 update on WID.world. First, inequality is very high in the region and is underestimated in official measures based solely on survey data. We complement survey data with tax data and national accounts to provide a more accurate picture of the true level of inequality in Latin America. Second, we find a decline in inequality since 2000 in a number of countries, including Argentina, Colombia, Ecuador and Uruguay. Although inequality remains relatively high by international standards in all of these countries, this is a fairly significant downward trend. Third, we do not find such a decline in a number of other countries, including Brazil, Chile, Mexico and Peru, where inequality was relatively stable at very high levels (Peru) or increased even further (Brazil, Chile, Mexico). Fourth, we stress the importance of significantly increasing the quality of the data on income and wealth in the region. We welcome comments and feedback from the research community on this on-going project.

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Context

Within the highly heterogeneous part of the globe usually called the *developing world*, Latin America represents a significant proportion with over 600 million inhabitants, and has been the object of intense discussions in light of the significant social, political and economical changes that the region has witnessed in the last few decades. Latin America is still among the most unequal regions on the planet, but contrary to the global trend, the concentration of income seems to have decreased during the first fifteen years of this new century according to "official" estimates from household surveys. Despite being a moderate decline, it represented a unique episode in the economic history of the continent.

Economic historians have long debated whether the high levels of economic concentration observed in Latin America have been a constant since colonial times. Or if, on the contrary, it was during the first globalisation era (1870-1914), that it really exploded. Furthermore, it is not clear whether the entire region experienced a reduction in inequality between the World Wars and the 1970s, or whether it maintained its levels throughout the last century, while in the vast majority of developed countries it declined. Since the 1970s, inequality has increased throughout the region. In this context, the recent period of a reduction in inequality is the only decreasing episode in the last 60 years and, potentially, the only event of this nature in more than a century.

What's new

Evidence from Latin America and other regions has nevertheless shown that household surveys present a number of caveats that need to be addressed, in order to properly understand income inequality levels and trends. Thus, this Issue Brief, the attached Technical Note (De Rosa, Flores, and Morgan, 2020) and the Distributional National Accounts (DINA) series presented in the World Inequality Database (WID.world, https://wid.world) for Latin America in the November 2020 update, represent the first step of an ongoing effort to provide a complete, consistent and comparable overview of the evolution of income inequality in the region.

Our estimates distribute total pre-tax national income to resident individuals. For that purpose, we combine a variety of data sources, namely harmonized household surveys, income tax records, social security registers, and national accounts. The available information allows us to study ten countries, covering around 80% of the region's population over the last two decades.

We use survey micro-data harmonized by the Statistics Division of the UN's Economic Commission for Latin America and the Caribbean (ECLAC), including ten countries for the years from 2000 to 2018: Argentina, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Mexico, Peru, and Uruguay. The information from National Accounts (NA) was obtained by scrapping the United Nations' Statistics Division database (http://data.un.org), which gathers a variety of series produced by national statistical offices. Although the macro aggregates produced by national accountants are often considered among the most reliable and internationally comparable data sources (e.g. to rank countries according to their total output, *per capita* GDP, etc.), detailed information on the income approach, which is the one we need to compute our series, is scarce in the region, to say the least. Finally, we use tax and/or social security data for all countries included in the update, available for at least part of the period under analysis.

In this Issue Brief we summarise some of the preliminary findings. The scientific assessment of our findings, as well as a detailed analysis of several important issues raised by the challenging task of distributing national income in a situation of relatively rich but particularly imperfect data, will be presented in a separate and longer paper, currently under preparation. The results of the current update should be considered as preliminary, thus subject to revision and improvement. A lot of effort has been devoted to the harmonisation of data inputs to improve comparability. Before the publication of the present series, Brazil was the only country in the region with DINA estimates in WID.world, based on Morgan (2017). Therefore, the November 2020 update includes brand new series for nine countries, as well as a revised and updated series for Brazil. It is expected that future updates will extend the time coverage back to 1990. Due to considerable (although not surprising) statistical inconsistencies across data sources, we do not currently present series for a number of countries, even if survey data is available. Such issues require more time to reconcile.

Given the complexity of the task, and the number of assumptions required for the construction of these series, in the Technical Note (De Rosa, Flores, and Morgan, 2020) we describe the impact that each stage of our adjustment procedure has on the income distribution, starting from the survey-based figures. We hope that this gives readers greater insight on the final series presented in the database. We distinguish three steps: first, we adjust for the low representativeness of top incomes using administrative records based on Blanchet, Flores, and Morgan (2018); second, we correct for the under/over coverage of income components by scaling them to national accounts aggregates (i.e., wages, capital incomes, mixed income, pensions and imputed rents); and third, we impute income from the corporate sector and the general government to the household income distribution. This allows us to fully account for the national income recorded in each country's system of national accounts. Our forthcoming paper will provide greater details.

Not surprisingly, each of the three steps of our procedure increases inequality levels, with different magnitudes depending on the country. Their impact on trends is not homogeneous either. In some countries we continue to observe the decrease in inequality during the period – such as in Colombia, Ecuador, El Salvador, Argentina and Uruguay – while in others – like Brazil, Mexico, Peru and Chile – we observe trends that gradually flatten or even revert with each step. Furthermore, in the period after 2015 it seems that the falling inequality trend comes to a halt and even reverses in several countries. We will address how these changes challenge the prevailing narrative from the literature in our forthcoming paper.

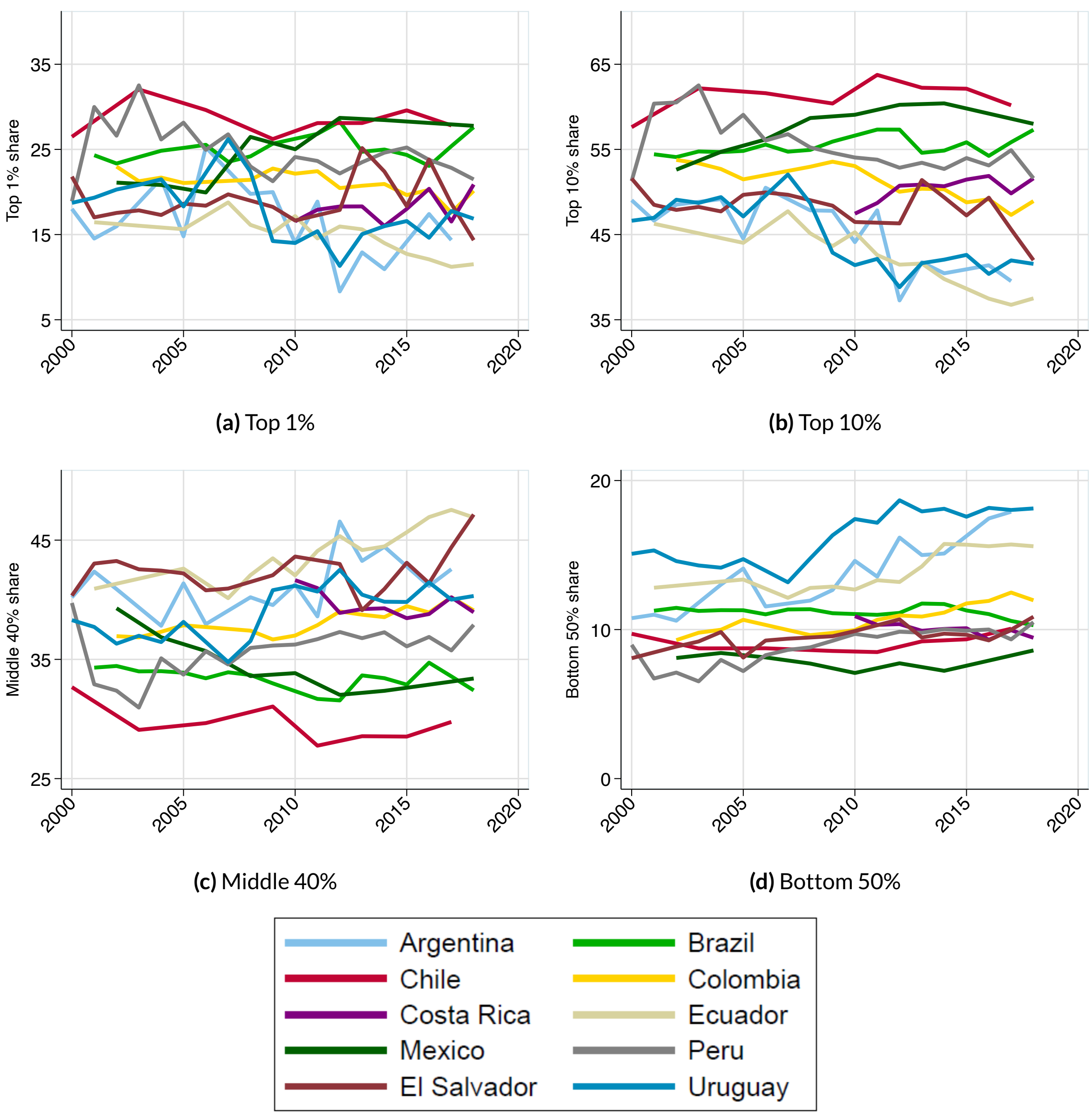
What we find

Some of the key preliminary results are presented in Figure 1, depicting the evolution of top 1%, top 10%, middle 40% and bottom 50% pre-tax national income shares. Our main distributional estimates rank individual adults by increasing intervals of income. After all data sources were combined, our preliminary series show much more heterogeneous trends than what was previously thought.

Despite the ongoing effort to improve the quality of the series presented and to provide a more detailed and complete explanation of these complex social phenomena, it is clear that inequality is still extremely high in the continent. Our preliminary results show that it is definitely higher –as expected– than what is shown by household surveys and that the downward trend in inequality was either milder than previously reported or non-existing.

The current economic crisis triggered by the covid-19 pandemic will cause what ECLAC forecasts to be the worst economic downturn since the beginning of the 20^{th} century. In this context, it is clear that an ambitious large-scale public policy effort is required to prevent yet another increase in income inequality in this already extremely unequal region. Moreover, it is of capital importance to improve the quality of the data in several countries, as well as to move forward in terms of data on aggregate wealth and its distribution in the region.

Figure 1. Pre-tax national income shares



Note. Own elaboration based on ECLAC's harmonized surveys, United Nation's Statistic Division database and country's tax data. Details of the estimation procedure discussed in (De Rosa, Flores, and Morgan, 2020).

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The World Inequality Lab

The World Inequality Lab aims to promote research on global inequality dynamics. Its core mission is to maintain and expand the World Inequality Database. It also produces inequality reports and working papers addressing substantive and methodological issues. The Lab regroups about twenty research fellows, research assistants and project officers based at the Paris School of Economics. It is supervised by an executive committee composed of 5 co-directors. The World Inequality Lab works in close coordination with the large international network (over one hundred researchers covering nearly seventy countries) contributing to the database.

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