Income Inequality in Chile: 1990-2006

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Abstract

The entrance of Chile to the Organization for the Economic Cooperation and Development, as the first South American country and second after Mexico in Latin America, sets a landmark in the development path that since the beginning of the 1990s decade has seemed to lead this country to a privileged position in the region. Given the reforms taken by the military regime in the 1980s, Chile is one of the most market-oriented countries in Latin America, with Free Trade Agreements and Economical Partnerships with several countries, including Japan, the United States and China.

Nonetheless, Chile’s economic success is said to exclusively benefit a few Chileans; this is true, given the deep inequalities in the distribution of wealth.

The income inequality existing in Chile is a long-term phenomenon; it tended to increase from 1974 to 1987 and decrease from 1987. This paper focuses on the evolution of the inequality from 1992 to 2006, and investigates the reasons for the decreasing trend in income inequality. First, we show that monetary transfers focused on low-income households contributed to decreasing inequality in after-tax income. Next, causes for the decrease in inequality in before-tax income are analyzed using log variance decomposition method based on the ageing hypothesis, Skilled biased-technological change and spreading higher education hypothesis. The analysis based on ageing hypothesis shows that the reduction of income inequality between age groups greatly contributed to decreasing in total income inequality. The spreading of higher education did not have the results expected, and surprisingly has a negative effect by increasing inequality; this could be because this popularization of higher education benefits mostly richer sectors of the population. The SBTC theory is also tested, resulting in signs of a possible inverse effect. A possible explanation could be the rise in the demand of unskilled workers through globalization and the Foreign Direct Investment in sectors using unskilled labor force.

Keywords: Income Inequality, Chile, Skilled-biased Technological Change Theory

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1 Introduction

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