Abstract for “Unraveling Declining Income Inequality in Bolivia: Do Government Transfers Matter?”

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This paper documents and explains the remarkable decline in income inequality observed during the last decade in one of the most unequal countries in the world, Bolivia. Our analysis is based on the set of official household surveys for the 1999-2011 period, harmonized by Fundaci´on ARU.

Regarding the changes in the income distribution, we find significant differences in annual growth rates by quantile during the 1999-2011 period, much more related to the growth performance of the last half of the decade, i.e. the 2005-2011 period. While the first half was a period of relatively no growth for almost all quantiles; the second half was a period of high growth (6% on average), pro-poor growth (with average growth rates above 6% for the bottom 2 deciles and rates around 5% for the middle quantiles); but not shared by everybody (the top 10% experienced growth rates below 1% and some Pen’s “giants” even negative annual growth rates). These uneven growth patterns have caused a remarkable decline in income inequality during the last half of the decade. During the 2005-2011 period, the bottom 20% has increased its income share in more than 40% while the top 10% has reduced as much as 40% of its income share, causing the Gini index to drop in 10 percentual points, from a level of .52 to .42.

To analyze the “proximate” determinants of Bolivia’s income inequality decline, we perform a counterfactual ´a la Barros decomposition of inequality changes by income source. We find that almost all inequality changes are explained by distributional changes in labor earnings. Neither the changes in contributory transfers (pensions) nor the changes and the expansion of non-contributory social transfers (renta dignidad, bono Juancito Pinto, or bono Juana Azurduy, among others), nor the growth of remittances and of property income account for the remarkable decline in income inequality. Furthermore, an extended counterfactual decomposition of labor earnings reveals that changes in the wage distribution are much more important than changes in the utilization of the labor force (i.e. changes in the patters of participation, of unemployment and of hours of work). To explore the “ultimate” determinants of the changes in the wage inequality we also perform a counterfactual ´a la Machado-Mata decomposition of the distributional changes in wage inequality. We find that most of the decline wage inequality can be explained by an increase in unskilled labor demand that have reduced the skill premia and also by compositional shifts in the labor force. Changes in the relative supply of skilled labor have play no significant role to explained the decline in the skill premia.

From these finding we derive two important policy implications. On the one hand, we argue that, since Bolivia’s income inequality changes seems to be driven by a price effect, there

is no guarantee of continuing the declining trend in the future or even maintaining the current inequality levels. On the other hand, we argue that, since non-contributory social transfers did not play a role in the redistribution of income, there is plenty of scope to redesign programs - particularly CCT programs, to be much more progressive than they currently are.