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Inequality persistence and policymaking constraints: Explaining regional data patterns

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WORKING PAPER N° IDB-WP-1599

Inequality Persistence and Policymaking Constraints:

Explaining Regional Data Patterns

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May 2024



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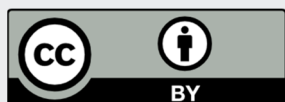
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Abstract

In well-functioning democracies, the policymaking process should in principle respond to persistent economic inequality with corrective policies. This process is set in motion through majority demands for redistributive taxation and spending that elected representatives eventually supply through policies designed to alleviate inequality. Policymaking constraints on both the demand side and the supply side have, however, considerably limited the extent of redistributive policies in Latin America. This paper explores recent data patterns from national and micro data to provide several potential explanations for the continuing high inequality observed in the region. Countries with stronger democracies have adopted more redistributive policies, even though post-tax inequality remains high in all of the region's democracies. Low citizen interpersonal and political trust both lead to fiscal policy preferences that constrain effective redistribution. Electoral participation has risen in the more democratic countries, while economically motivated protests have increased in weakly institutionalized settings.

JEL classifications: D63, D72, H20, H41, O10

Keywords: Inequality, Policymaking, Redistribution, Trust, Protests, Latin America

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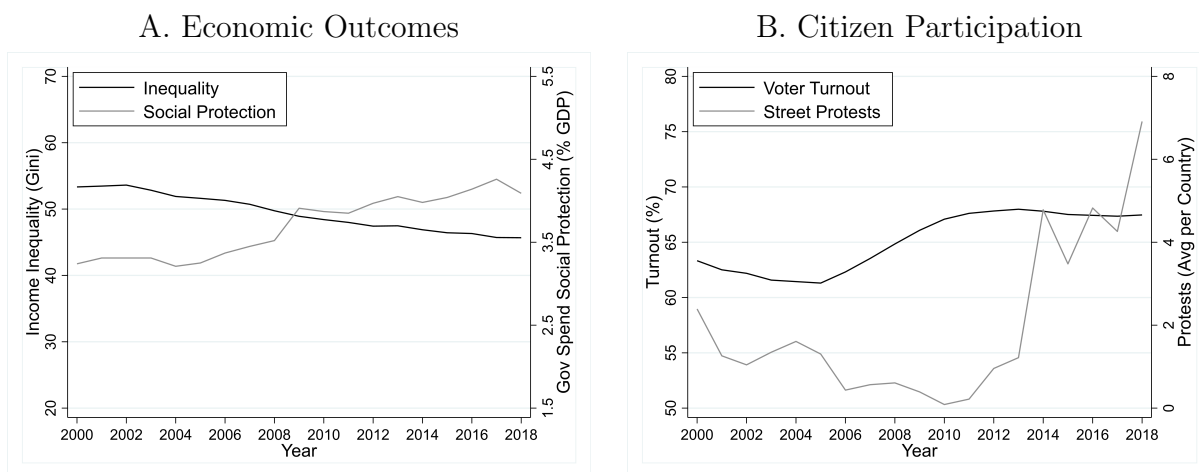
1 Introduction

Income inequality remains a persistent and pervasive problem in Latin America, with wide-ranging implications for the economic and social development of the region. According to various measures, Latin America may be the most unequal region in the world, with a high concentration of income and wealth in the hands of a few. The richest 10% of the population earn more than half of the total income, while the poorest 10% earn less than 2%. The gap between the rich and the poor has remained wide over the last three decades, even in countries like Chile, Colombia, and Mexico. The Covid-19 pandemic has exposed and exacerbated inequality in Latin America, as the most vulnerable groups have suffered more from the health and economic impacts of the crisis. Income inequality in Latin America is not simply a matter of fairness. It may also pose a challenge to democracy, stability, and growth (Busso and Messina, 2020).

In well-functioning democracies, economic inequality should to some extent be self-correcting through majority demand for redistributive taxation and spending. Democratic failures on both the demand and supply sides have, however, limited the extent of redistributive policies in Latin America. Countries with stronger democracies have adopted more redistributive policies, even though post-tax inequality remains high in all the region's democracies. Electoral participation has risen in the more democratic countries, while economically motivated protests have increased in weakly institutionalized settings.

The countries of Latin America have now experienced, with few exceptions, more than 30 years of economic policy making through democratically elected governments. The region is well endowed with natural and human resources, and most of its countries are classified as "middle income" by the United Nations. Poverty and economic inequality persist, however, as noticeable characteristics of these societies. Governments have tackled these issues using fiscal, educational, and social policies. Yet, while public policies have led to demonstrable progress in reducing income inequality, by several measures the region remains one of the most, if not the most, unequal in the world. Recurrent protests fueled by economic grievances are a regular reminder of this reality. This raises the question of why the democratic process has not been more effective in alleviating inequality. This paper presents several constraints operating in the region's democracies that may have hindered the adoption of broader inequality-reducing policies. These include biased popular perceptions of income distribution, limited demand for pro-poor policies, de jure institutional bias against redistribution, and vote buying.

Figure 1. Economic and Social Trends



Note: The Gini index is from the World Bank’s World Development Indicators. Social protection spending is from the UN’s Economic Commission for Latin America and the Caribbean. Voter turnout is for parliamentary elections and comes from the Institute for Democracy and Electoral Assistance. Street protests are the sum of general strikes and anti-government demonstrations, which are from the CNTS Domestic Conflict dataset. The Gini series is the average for each year for a set of 17 countries: ARG, BOL, BRA, CHL, COL, CRI, DOM, ECU, GTM, HND, MEX, NIC, PAN, PER, PRY, SLV, and URY. The social protection series also include BHS, BRB, GUY, HTI, JAM, TTO, and VEN, but excludes PER. The turnout and protest series are based on the 17 countries plus BLZ, GUY, HTI, JAM, TTO, and VEN.

The regional decline in inequality over the past two decades has occurred in the context of increased government spending on social protection, as well as increased political participation. Figure 1.A shows the time trends in inequality and social protection spending in the region. On average, inequality measured by the Gini index, as estimated by the World Bank, gradually came down from 53.3 in 2000 to 45.7 by 2018; by comparison, the Gini index in the member countries of the Organization for Economic Co-operation and Development (OECD) was 33.2 as of 2018.¹ Government spending on social protection as a percentage of GDP steadily increased from 3.24 percent in 2000 to 4.09 percent by 2018, although it remains well below the OECD average. Two of the main drivers of this trend have been expanded coverage of conditional cash transfer programs and increased availability of noncontributory pensions. Figure 1.B shows that during the same period, voter turnout in parliamentary elections had an upward movement, increasing by about 4.5 percentage points on average, from 63.2 in 2000 to 67.5 in 2018. More striking is the increase in street protests over the past decade, from about one per year to more than six per year, on average per country. Given the progress in inequality and the accommodating response in government policy, this

¹Based on the most recent data available from each country (no data are available for New Zealand). Of the 37 member countries of the OECD, the three LAC countries of Chile, Mexico, and Colombia (which joined in April 2020) had the highest Gini readings in this group, namely 44.4, 45.4, and 50.4, respectively.

last trend may seem puzzling, suggesting complexities in addressing inequality through the democratic process.

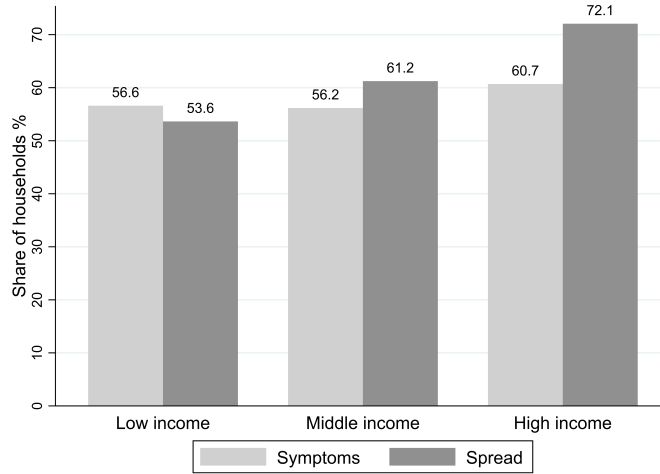
To some extent, economic inequality is a natural consequence of the market-based system that governs the economies of most of the countries in the region. The distribution of assets and income depends on the unequal distribution of initial endowments and innate abilities, and on the market returns to the different types of human and physical capital, which can be largely unpredictable in a globalized economy. The market system operates, however, within a political system. The political system influences the outcomes of the market system directly through tax-and-transfer reallocations of income or by providing essential public goods such as public health and education, or indirectly through government regulation of market activities. How the political system shapes the market system depends on several key factors: a society's preferences over economic outcomes (democratic values), the distribution of de jure political power (democratic institutions), and the distribution of de facto political power (democratic engagement).

2 Democratic Policymaking and Inequality

At a fundamental level, the more democratic a country is the more effective it should be at alleviating the inequalities resulting from the market system. One would expect the democratic process—which by design is highly egalitarian and based on the principle of “one person, one vote”—to find ways to implement policies that reduce market inequalities. In other words, in a well-functioning democracy, inequality should to some extent be self-correcting. If inequality is too high, the income of the median voter has dropped well below the income of the average voter. The decisive median voter would then support an income tax policy that would shift income from the top of the distribution to the bottom (Meltzer and Richard, 1981). Most political candidates should have an incentive to represent the preferences of the median voter, as this would be a successful electoral strategy.

Regional data do provide some evidence supportive of this mechanism. Brown and Hunter (1999) found in a 1980–92 panel of Latin American countries that democracy was associated with higher social spending per capita. Lapp (2004) reports a statistical association between democratization and land reform in Latin America. Huber and Stephens (2012) looked at several Latin American countries over the period 1970–2007 and measured democracy using how long the country had been democratic since the end of World War II.

Figure 2. Virus Knowledge by Income Level



Note: Figure plots percentage of respondents who respond correctly to questions about the symptoms and spread of the Covid-19 virus. Based on data from the IDB-Cornell online survey 2020.

A relevant finding is that a longer history of democracy is associated with more welfare and social security spending, as well as education spending, and lower income inequality. Fujiwara (2015) studied a change in voting technology in Brazil from the 1990s that made it easier for illiterate citizens to vote, leading to a major de facto enfranchisement of the poor. His data shows that the reform led to a shift of government spending in a pro-poor direction, particularly in the area of health. Baland and Robinson (2008, 2012) examined the effects of switching from the open ballot to the secret ballot in Chile in 1958, finding that the reform increased the vote share of left-wing parties, which, they argue, is consistent with increased political support for redistributive policies. While the link between democracy and redistributive policies has appeared in data from other regions, the link between democracy and inequality has proven less robust in other panel data (Acemoglu et al., 2015).

Notwithstanding the evidence showing that democracy may reduce inequality through a greater emphasis on redistributive policies, in practice, several factors may conspire against this simple democratic mechanism of redistribution. Some come from the demand side. For example, although a large fraction of the region's electorate may favor economic equality, many voters still choose not to participate in the political process through voting or joining political parties (Lijphart, 1997). Other constraints come from the supply side. For example, the political process does not accurately represent the preferences of a majority of citizens because a minority is able to capture de facto political power (Acemoglu and Robinson, 2008), or the country lacks the state capacity necessary to collect taxes or provide good-

quality primary education for everyone (Besley and Persson, 2009).

The Covid-19 global pandemic that began in March 2020 has brought into sharp relief inequalities of information among the general public. An IDB-Cornell online survey conducted in 17 countries in Latin America and the Caribbean has found that basic knowledge about virus symptoms, spread, and prevention was less accurate at the bottom of the income distribution (Bottan, Hoffmann, and Vera-Cossio, 2020). Figure 2 reveals an income gradient for knowledge of symptoms and spread. Also, lower-income respondents were less likely to have heard of “social distancing,” a key public health strategy for preventing the spread of the disease. The information inequalities will likely filter through the political process and reflect themselves in public policies that are more favorable to those who have more economic resources and can articulate policy demands effectively.

Political mobilization through street protests has been a key accountability mechanism, particularly for those at the lower end of the income distribution, to make their policy demands heard in political systems with weak responsiveness. During the crisis, however, this mode of political participation was significantly suppressed by fear of contagion and government-mandated lockdowns.

3 Demand-Side Policymaking Constraints

A well-known weakness of democratic governance is low voter turnout and limited political interest. Because of the widespread use of compulsory voting, turnout has remained relatively high in Latin America, although enforcement is uneven. Turnout appears biased, however, in a way that is detrimental to the poor—namely, voting is less common among the less educated and less wealthy, as found by Carreras and Castaneda-Angarita (2014) in individual-level data from the 2010 wave of AmericasBarometer collected by LAPOP. This should weaken representation of their interests by elected policymakers. A related distortion in representation comes from biased popular perceptions of the income distribution. Cruces, Perez-Truglia, and Tetaz (2012) studied survey data from Argentina and found that about a third of their sampled individuals overestimated their position in the income distribution. Using a survey experiment, they showed that those with such a positive bias, when informed of their true lower ranking, tended to demand higher levels of redistribution. The Covid-19 pandemic brought to light another example of inequality of information: knowledge about virus symptoms, spread, and prevention is less accurate at the bottom of the income distribution (see again Figure 2 above).

Other research has found evidence of weak demand for pro-poor policies—such as public spending on basic public services. Bursztyn (2016) studied survey data from Brazil, where respondents were given a choice between a candidate who supports higher spending on public education and another who supports higher spending on transfers. Poorer voters should be the ones benefiting more from public education, at least in the long term, yet they were less likely to support the candidate supporting public education. In a more recent multi-country survey of individual preferences for public spending from seven Latin American capital cities, Keefer, Scartascini, and Vlaicu (2022) find a similar pattern. In addition, they document that spending on pro-poor public goods, such as public education and security, is valued less among voters with low trust in political promises or high time-discounting rates. This link appears in country-level data as well: countries with average low trust and high discounting rates spend smaller fractions of their budgets on public investments.

Sometimes redistribution can increase, rather than reduce, inequality. For example, democratization may empower the middle class to raise taxes and redistribute to itself, an effect known as Director’s Law, named for economist Aaron Director (Stigler, 1970). If the middle class is relatively closer in income to the poor than to the rich, this can worsen existing income inequality. Acemoglu, Naidu, Restrepo, and Robinson (2015) find evidence for this phenomenon in a 1960–2010 panel of 110 countries, in which many of the switches to democracy come from the Latin American wave of democratization.

4 Supply-Side Policymaking Constraints

The democratic process can also be obstructed from performing its inequality-alleviating function by distortions coming from the supply side of public policies. An important channel is the possibility that elements of the elite can circumvent de jure institutions by making investments in de facto political power—e.g., through control of local law enforcement (Acemoglu and Robinson, 2008), or campaign contributions (Campante, 2011). In this scenario, the “effective” median voter is placed much higher in the income distribution than the actual median voter.

A related constraint arises when the institutional architecture of a new democracy is chosen by actors connected with the previous regime. The chosen de jure constitutional provisions restrict the scope of redistribution that occurs under democratization. For instance, Londregan (2000) argues that the constitution imposed by the Pinochet government in Chile was designed to constrain the extent of future redistribution. Ardanaz and Scartascini (2013)

study a sample of more than fifty countries, including several from Latin America, between 1990 and 2007. They find that countries with historically more unequal distributions of wealth and income have higher levels of legislative malapportionment, which in turn are associated with smaller shares of personal income taxes in GDP. Sometimes the constraints are exogenous to the prior power structure. Campello (2011) argues that the economic threat of capital flight tied the hands of several Latin American governments from pursuing more vigorous, and therefore costlier in the short run, redistributive policies. Each of these factors would reduce the potential impact of democracy on inequality.

More recent research has suggested that vote buying, a prevalent phenomenon in many Latin American democracies, also prevents the democratic process from fully internalizing latent popular demand for redistribution in high-inequality settings. Keefer and Vlaicu (2017) show that vote buying as an electoral strategy is more common in countries where campaign promises have low credibility, such as those Latin American democracies where political parties are weak. They demonstrate that vote buying has distributional consequences, as voters targeted by attempts at vote buying before the election may receive no government benefits after the election. As poorer voters are more susceptible to vote buying, this type of redistribution crowds out redistribution through the legitimate policymaking process and becomes an imperfect substitute for the welfare state (Kitschelt, 2000).

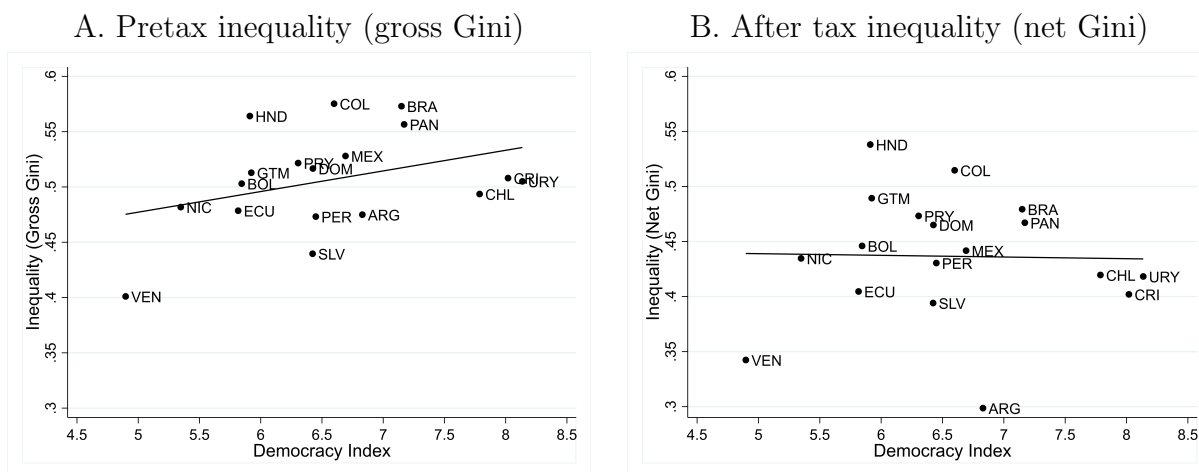
5 Recent Inequality Data Patterns

Recent inequality data for Latin America can shed light on the broad contours of the relationship between government policymaking constraints and income distribution. Below I consider several relevant dimensions of the policymaking process: tax policies, social protection, citizen trust, and citizen activism.

5.1 Tax Policies

Regional data appear to indicate that stronger democracies have more pretax inequality on average, but not more post-tax inequality, compared to weaker democracies. Figure 3 plots the pretax (gross) Gini coefficient and the after-tax (net) Gini coefficient against a democracy index (averaged for 2006–18) that summarizes the quality of each country’s democratic process along five dimensions: civil liberties, political culture, political participation, functioning of government, and electoral process and pluralism. This yields a continuous

Figure 3. Inequality Relationship with Democracy



Note: Pretax (gross) and after-tax (net) Gini are from the Commitment to Equity Institute Data Center on Fiscal Redistribution. Democracy Index is from the Economist Intelligence Unit. Sample includes 18 countries; codes shown in the figures. Gini coefficients are from the early 2010s. Democracy values are averaged for the period 2006-18.

index from 0 to 10, with higher values indicating stronger democracies. Three types of democracies can then be distinguished: hybrid (index between 4 and 6), flawed (index between 6 and 8), and full (index between 8 and 10).

Figure 3.A suggests that market-based incomes tend to be more unequal in the stronger democracies, such as Costa Rica or Uruguay, than in the weaker democracies, such as El Salvador and Venezuela. The correlation between pretax inequality and democracy is 0.361. Perhaps this is due to the more diversified economies and open-market policies of the former group. Comparing Figure 3.A to Figure 3.B, inequality levels after taxes drop in virtually every country, suggesting that fiscal policy has an equalizing effect across the board. On average, the Gini coefficient drops from 0.506 to 0.437, a decline of 13.6 percent.² The drop is not uniform, however, as more democratic countries experience more equalization than others. The result is that strength of democracy is no longer positively correlated with inequality. The correlation in the second figure is slightly negative, at -0.023 .

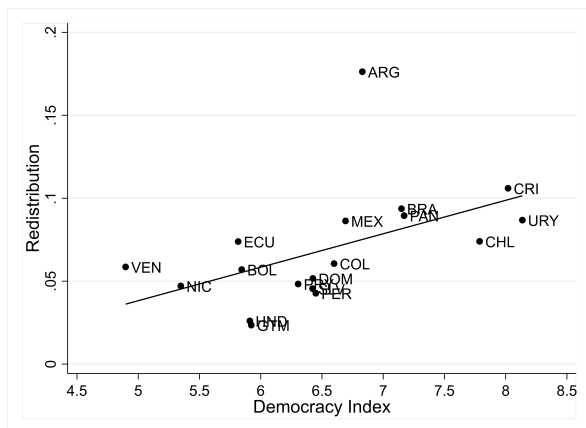
5.2 Social Protection

This pattern suggests that stronger democracies are better at reducing inequality through the tax system. Figure 4 shows some evidence that this may be the case. Figure 4.A plots the degree of fiscal redistribution against the democracy index. Fiscal redistribution equals

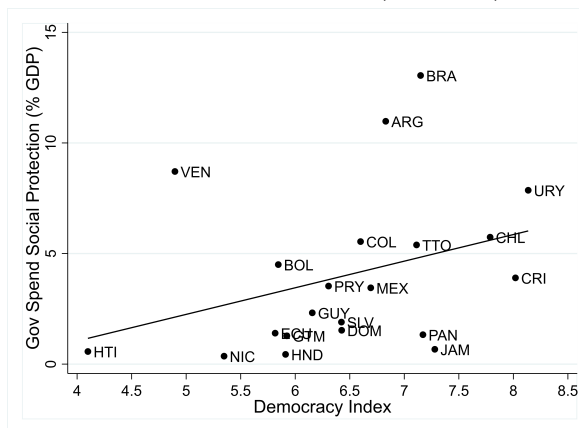
²As Izquierdo, Pessino, and Vuletin (2018) have documented, this is significantly lower than the figure for the OECD.

Figure 4. Inequality Policy Relationship with Democracy

A. Redistribution



B. Social protection (% GDP)



Note: Redistribution is the difference between the gross and net Gini coefficients, which are from the Commitment to Equity Institute Data Center on Fiscal Redistribution. Social protection spending is from the Economic Commission for Latin America and the Caribbean. Democracy Index is from the Economist Intelligence Unit. Sample includes 18 countries in panel A, 21 in panel B. Gini coefficients are from the early 2010s. Social protection values are as of 2018. Democracy values are averaged for the period 2006-18.

The difference between the gross Gini and the net Gini that were shown in Figures 3.A and 3.B. The plot reveals a strong positive association between redistribution and democracy: stronger democracies engage in more extensive redistribution. The correlation is 0.502.³

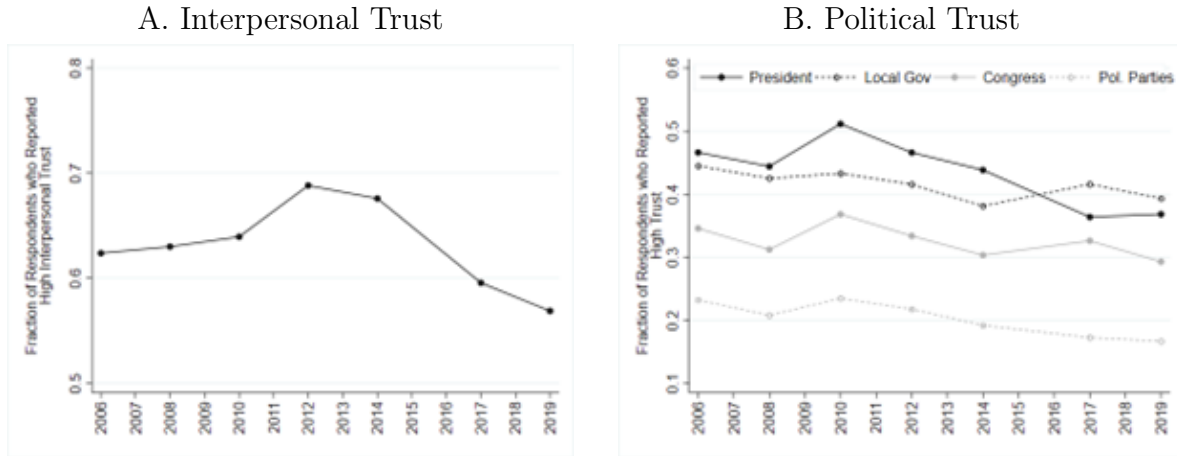
Consistent with this observation, stronger democracies also tend to spend a larger fraction of their GDP on social protection programs. Figure 4.B plots the most recent values of government spending on social protection as a percent of GDP, against the democracy index. The pattern of these data resembles the one in the redistribution plot: stronger democracies tend to allocate more fiscal resources to social protection. The correlation is 0.334. This may be partly due to the better state capacity of these democracies—e.g., their ability to collect taxes—or it may be due to the more effective channeling of popular demand through the democratic process, along the lines of the arguments made above.

5.3 Citizen Trust

Among world regions, Latin America displays some of the lowest levels of citizen trust. Recent survey evidence from a large set of Latin American countries confirms that citizens

³A similar analysis using Gini data from the OECD reveals a correlation between redistribution and democracy of 0.325. The sample consists of all 36 member countries in 2018, where the Gini data is from the mid to late 2010s.

Figure 5. Citizen Trust in Latin America



Note: Based on LAPOP 2006-2019 Database. The trust series is the average for each wave for a set of 18 countries: ARG, BOL, BRA, CHL, COL, CRI, DOM, ECU, GTM, HND, JAM, MEX, NIC, PAN, PER, PRY, SLV, and URY. Interpersonal trust values range from 1 to 4, where 1 is no trust in people and 4 is trust a lot, high trust is defined as options 3 or 4. Trust values range from 1 to 7, where 1 is no trust in political institution and 7 is trust a lot, high trust is defined as options 5 to 7.

express low trust in government and political institutions. The Latin American Public Opinion Project (LAPOP) at Vanderbilt University carries out one of the most extensive public opinion surveys in the region. The survey collects a representative national sample of voting-age adults approximately every two years in each country within Latin America and the Caribbean.⁴ In the survey, respondents answer questions about their trust in others, and in different political actors, such as the president, local governments, congress, and political parties. Answer options are consistent across countries and waves.⁵

Figure 1 presents trends of citizens' trust in each other and in political actors from 2006 to 2019. Trust levels increased slightly in 2010 and followed a gradual decline in subsequent years. Trust in local governments and congress decreased by around 10%, while trust in the president and political parties decreased by 17%, from 2006 to 2019. This evidence indicates that the lack of trust in government and government institutions is a longstanding problem in the LAC region. In 2019, nearly 40% of respondents reported that they trusted the president and the local governments, but only 30% reported that they trusted the congress, and 18% reported trust in political parties.

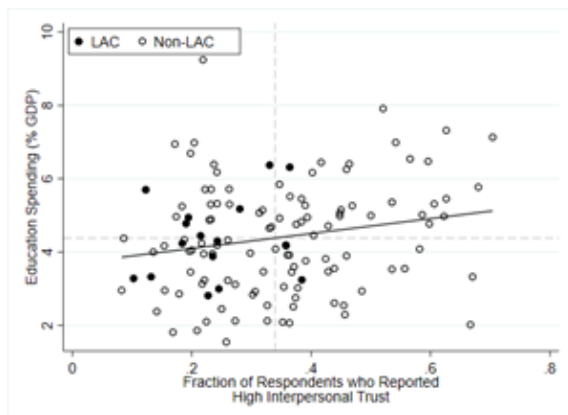
While trust in political institution is a more general global phenomenon, the trends in Latin America are more pronounced. Based on World Values Survey data (not shown here),

⁴LAPOP data are available beginning in 2004; however, the first wave did not conduct interviews in more than 60 percent of LAC countries. To construct a balanced panel of countries, only waves from 2006 to 2019 that include all LAC countries are being considered.

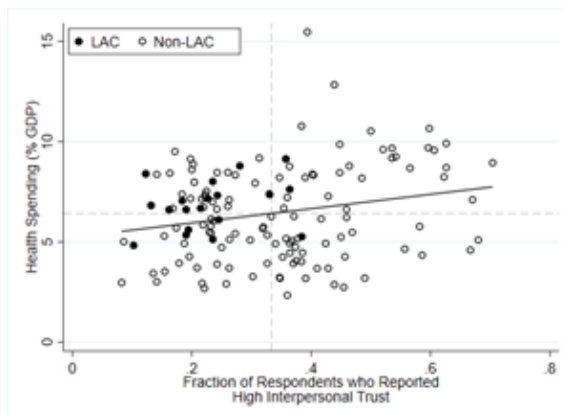
⁵For comparison purposes, the graphs present values rescaled into the unit interval.

Figure 6. Interpersonal Trust and Public Good Provision

A. Education Spending



B. Health Spending



Note: Figures based on UIS UNESCO 2006-2019 Database, WHO 2000-2018 Database; and Gallup World Poll 2018 Database. Education spending represents the average for the period 2006-2019, missing values replaced with interpolated values. The health spending presents the average for the period 2000-2018. Interpersonal trust ranges from 1 to 4, where 1 is no trust in neighbors and 4 is trust a lot. Low trust in neighbors is defined as options 1 to 3, and high trust as the complement. Sample includes 126 countries in left-hand side panel and 139 countries in right-hand side panel.

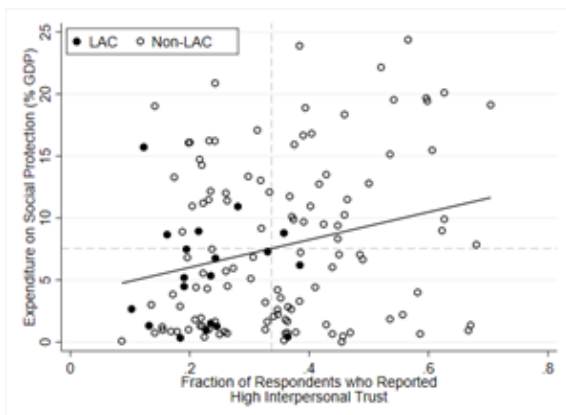
OECD countries experienced a more moderate decline in trust. That means that pre-existing differences in trust are widening. Citizens in OECD reported around 20 percentage points more trust in congress and 8 percentage points more trust in political parties than respondents in Latin American countries. These data suggest high impediments to policymaking through the democratic process in the Latin American region.

Keefer, Scartacini, and Vlaicu (2018) arrived at a similar conclusion of low trust in political institutions using the IDB-LAPOPOP 2017 survey. They elicited opinions about whether politicians and public officials keep their promises and obey the law. They also inquired about public policy expectations regarding, for instance, hypothetical policies that increase taxes for redistribution to the poor and increase water service prices for pipe maintenance. Although the survey was conducted in only seven Latin American countries, the results align with the low trust in political actors in the region. The data suggest that only 22% of respondents reported trust in the promises of politicians and public officials. This low trust in government actors also reduces public policy expectations; the survey revealed that, on average, only one out of four respondents were confident that the revenues from the hypothetical tax redistribution and pipe maintenance service fees would reach the poor or finance infrastructure maintenance (Perilla, Vlaicu, and Keefer, 2022).

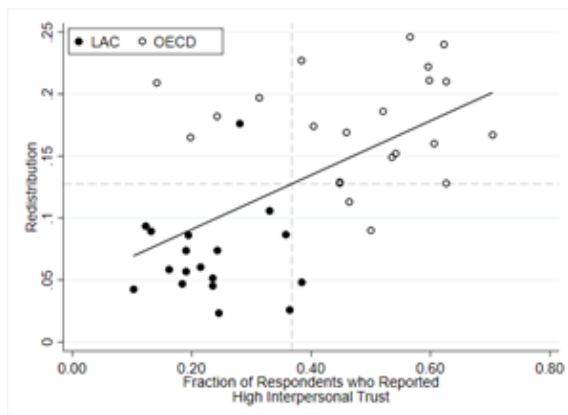
The following data patterns suggest a relationship between low interpersonal trust and suboptimal policy outcomes. First, cross-country data indicate that low interpersonal trust

Figure 7. Interpersonal Trust and Income Redistribution

A. Social Protection



B. Gini Differential



Note: Figures based on ILO Database, Commitment to Equity Institute on Fiscal Redistribution Database, and Gallup World Poll 2018 Database. The social protection spending presents the value for the most recent year. Redistribution is the difference between the gross and net Gini coefficients, calculated with the most recent data. Interpersonal trust ranges from 1 to 4, where 1 is no trust in neighbors and 4 is trust a lot. Low trust in neighbors is defined as options 1 to 3, and high trust as the complement. Sample includes 135 countries in left-hand side panel and 40 countries in right-hand side panel.

is associated with low public good provision. Figure 6 shows that public spending on education and health, as a percentage of GDP, correlates positively with interpersonal trust, from the Gallup World Poll. The correlation coefficients are around 0.20. The samples consist of about 130 countries, including Latin American countries represented by solid dots. They tend to feature low interpersonal trust and low public good spending relative to the size of their economies.

Second, low interpersonal trust is associated with low income redistribution. Figure 7 plots the relationships between interpersonal trust and two measures of redistributive policies, based on country-level data averaged for 2006-2019. Figure 7.A shows government expenditure on social protection as a percentage of GDP for a sample of 135 countries. The correlation with interpersonal trust is 0.25. Figure 7.B shows redistribution measured as the difference between the pre-tax and post-tax Gini coefficients for a sample of 40 countries from Latin America (solid dots) and OECD (hollow dots). The correlation with interpersonal trust is 0.58. Notably, Latin American countries tend to appear in the lower left quadrant. Public education also has a redistributive dimension, particularly primary and secondary education, as it disproportionately benefits lower-income individuals. In the Latin America region, however, voters exhibit a low level of support for redistribution policies financed through higher taxes, even though such policies could increase aggregate welfare. One explanation is that low-trust voters believe that the government will misallocate fiscal

resources meant for social welfare policies (Keefer, Scartacini, and Vlaicu, 2018).

5.4 Citizen Preferences and Engagement

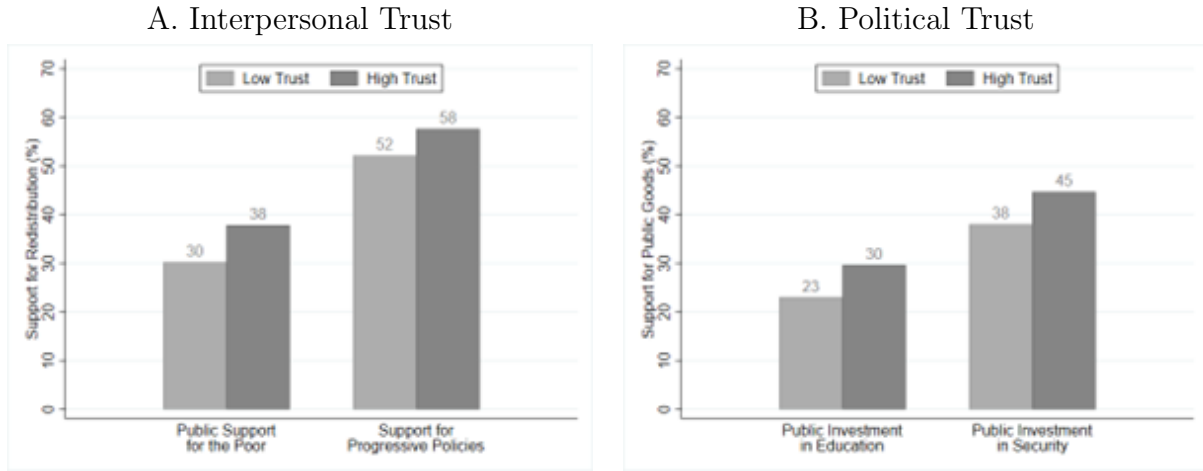
Prior research indicates that voter mistrust in policymakers should create a bias away from broad-based public policies with long-term benefits by affecting voter policy preferences. Algan, Cahuc, and Sangnier (2016) and Gründler and Köllner (2020) showed positive relationships between social or political trust and social welfare spending at the individual level as well as country or municipality levels. One explanation is that voters with low interpersonal trust believe that others will misreport their income for tax purposes, avoiding contributing their share to government revenues; consequently, low-trust voters perceive their tax burden to be unfairly large (Algan, Cahuc, and Sangnier, 2016).

The policy differences between new and old democracies provide further evidence of the importance of citizen trust in government. In new democracies, the organizations that can build citizen trust in politicians are weaker (e.g., political parties). Hence, candidate promises lack credibility with citizens. Consistent with this, governments in new democracies over-provide targeted transfers and under-provide public goods (Keefer, 2007). Voters elect politicians who promote policies that are contrary to economic growth, such as vote-buying and under-provision of public goods (Keefer and Vlaicu, 2017). In the Latin American region, Keefer, Scartacini, and Vlaicu (2022) found that trust in politician promises is associated with preferences on government spending: citizens who reported low trust in political promises were more likely to prefer targeted transfers to public goods.

A unique survey taken in 2017, the IDB-LAPOP Survey, asked voters to weigh the trade-offs between two spending alternatives, one of them more vulnerable to the biases of voter mistrust.⁶ Some questions elicited preferences for redistribution, and others elicited preferences for government provision of public goods. For example, one of the questions asked whether the citizens preferred higher taxes to fund public education spending or lower taxes so that households could self-fund their children's education. A different question offered a choice between higher taxes to fund government spending on security and lower taxes so households could provide for their own security. Distrustful voters should be less likely to support government spending on two public goods, education and security, because they discount more politician promises about converting tax revenues into good quality education

⁶The survey elicited policy preferences of 6,040 respondents from seven countries: CHL, COL, HND, MEX, PAN, PER, and URY.

Figure 8. Citizen Trust and Policy Preferences



Note: Figures based on based on IDB-LAPOP 2017 Database. In panel A, respondents chose between a preference for higher taxes for the poor and progressive tax policies, or lower taxes for the rich to create jobs and lower taxes for economic growth to reduce poverty. In panel B, respondents chose between a preference for increased taxes to boost spending in education, and security, or lower taxes to allow households to spend more on private education, and security, respectively. Interpersonal trust ranges from 1 to 4, where 1 is no trust in most of the people and 4 is trust a lot. Low interpersonal trust is defined as options 1 to 3, and high trust as the complement. Trust in politicians ranges from 1 to 4, where 1 is no trust in politicians promises and 4 is trust a lot. Low trust in politicians is defined as options 1 or 2, and high trust as the complement.

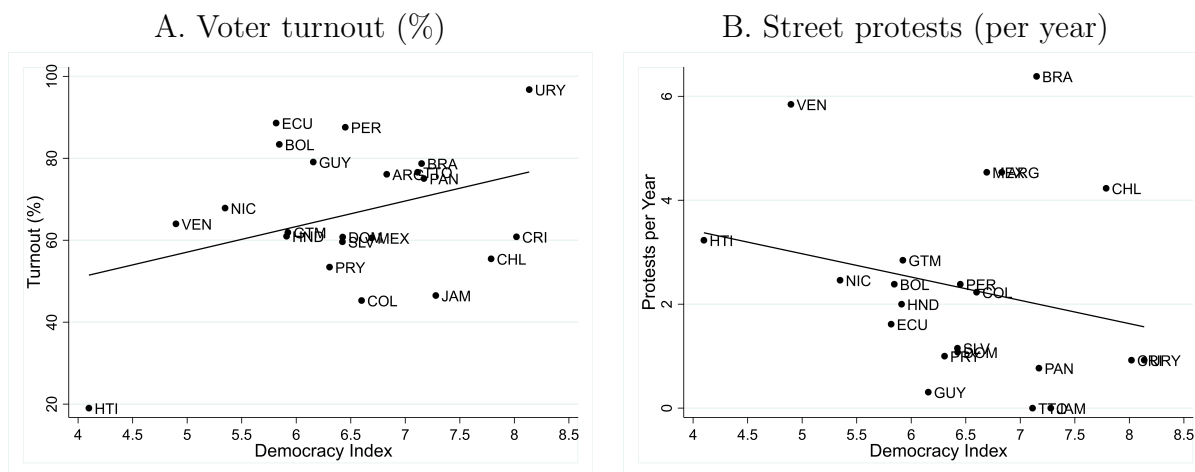
and reliable public security.

Based on the aforementioned survey data, Figure 8 shows the percentage of respondents who support redistributive policies, in panel A, by level of interpersonal trust, and support for public goods spending, in panel B, by level of trust in politicians. Respondents with lower interpersonal trust are about 8 percentage points less supportive of tax-funded government assistance to the poor, and about 6 percentage points less supportive of progressive taxation that redistributes income from the well-off to the needy. It suggests that those who express a low level of trust in electoral promises indicate less support for public goods than those who express high trust. Individuals who express low levels of trust in politicians' promises are about 7 percentage points less supportive of public investments in education compared to individuals who report high trust, and also about 7 percentage points less supportive of public investments in security.⁷

We noted at the outset of this paper the sudden rise, starting in 2014, in street protests (general strikes and anti-government demonstrations) throughout the region (see Figure 1.B).

⁷Higher average support for security relative to education may reflect awareness that private markets cannot adequately provide public safety. Helsley and Strange (1999) showed that private markets seeking to address the under-provision of security may increase the overall crime rate.

Figure 9. Citizen Engagement and Democracy



Note: Voter turnout (as a percentage of the voting-age population) is from the Institute for Democracy and Electoral Assistance. Street protests are the sum of general strikes and anti-government demonstrations, which are from the CNTS Domestic Conflict dataset. Democracy Index is from the Economist Intelligence Unit. Sample includes 22 countries from the region. Voter turnout, street protests, and democracy index are averaged for the period 2006–2018.

Against the backdrop of steady expansions in government allocations to social protection, the trend raises the possibility that protests are an important mechanism through which the electorate’s demands for more redistribution are met. The data, however, do not seem to support this conjecture.

Stronger democracies in the region appear to have higher voter turnout but fewer street protests on average. Figure 9 plots country-level averages of these variables for the period 2006–2018. In Figure 9.A, voter turnout is positively associated with democracy; the correlation is 0.351. In Figure 9.B, street protests are negatively associated with democracy; the correlation is -0.240 .

As stronger democracies are more effective at reducing inequality (see Figure 3) and engage in more fiscal redistribution (see Figure 4), it appears that voter turnout is more plausible than street protests as the main mechanism for resolving inequality through the democratic process. As Machado, Scartascini, and Tommasi (2011) have found, protests are often a way to express voter demands in weakly institutionalized settings. There may be exceptions to this pattern, perhaps the cases of Brazil and Chile, both of which score relatively high on the democracy scale but have nevertheless witnessed a marked increase in economy-related protests in the past few years.

6 Conclusions and Open Questions

While there is some evidence that stronger democracies in the Latin American region are more effective at alleviating income inequality, when compared to other regions in the world, inequality remains high. Stronger democracies do appear to engage in more redistribution and social protection, particularly through conditional cash transfers and noncontributory pensions. Some of the constraints to further reducing inequality may come from the demand side—e.g., biases in voter turnout toward higher income and education, or lack of trust in the political process. Others may come from the supply side—e.g., *de jure* institutional constraints on redistribution, or vote-buying strategies that supplant government provision of essential pro-poor public goods such as quality primary education and health services. More research is needed to identify which of these constraints operate in which contexts, and the appropriate policy reforms to overcome them. The data shown above support the view that well-functioning democracies fare better overall in the extent of their redistribution.

It is also possible that current redistributive policies fall short because there are implementation failures in the targeting of transfers and public goods. To determine this, more granular data on fiscal outlays are needed, particularly at the local level. As several countries in Latin America and the Caribbean use a system of fiscal decentralization based on grants to localities from the central government, local accountability for the allocation of these transfers becomes a key issue. Yet, local politicians face little accountability for efficient spending because the cost of this spending, tax revenues, is not borne at the local level. This may lead to overspending and misallocations.⁸

Another remaining puzzle is the higher prevalence of pretax inequality in the region's more advanced democracies. The greater reliance on market-based economies seems to suggest an efficiency-equity trade-off. It is not clear, however, why this trade-off cannot be circumvented with well-designed regulatory policies that allow market competition to thrive while creating an equitable distribution of economic and social returns to the different factors of production.

Finally, it is important to understand how to overcome weak voter demand for public spending that favors the poor, a significant problem especially in low-trust environments. Voters at the low end of the income distribution do tend to vote less often and to be less engaged in the democratic process. Some have raised the possibility that poverty and in-

⁸The IDB has dedicated one of its recent flagship reports to carefully measuring and discussing issues of fiscal misallocation; see Izquierdo, Pessino, and Vuletin (2018).

equality are democracy's main weaknesses (UNDP, 2005), with the less well off becoming more and more disengaged with the democratic process that is supposed to represent their interests. Inequality may lead to partisan polarization (Vlaicu, 2018), and political polarization can further increase inequality (Bonica et al., 2013). Overcoming this vicious circle raises a challenge for the region's relatively young democracies. A commitment to strengthening democratic institutions—in the government sector and civil society alike—should over time improve representational outcomes, including economic equity, in these societies.

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