

Relative Poverty and Consumption Inequality behind Massive Protests in Chile



Sungwoo Hong

Ph.D., Associate Research Fellow, Americas Team
Korea Institute for International Economic Policy

Have there been any recently notable changes in the pattern of inequality in Latin America? Had it been before the massive protests in Chile in 2019, a number of experts on Latin America would have answered this question in the negative, as inequality in the region, including income inequality, has always been severe.

However, the massive protests in Chile, which led to the Constituent Assembly election in May 2020, provided the experts with an opportunity to reconsider the following issues of inequality in Latin America. Why did the Chilean uprising occur despite the fact that the absolute poverty rate in Chile has been continuously decreasing? And why was it so difficult to foresee such massive protests? I believe that there are two reasons.

First, it is likely that numerous previous studies have focused on absolute poverty rather than relative poverty. In general, the relative poverty rate is defined as the ratio of the number of people who live below 50 percent of median income, to the total number of people. Focusing only on the absolute poverty, we could misjudge a poverty issue in reality. For instance,

as the gap between the high and low income groups widens, the low-income group may feel a sense of relative deprivation. In spite of this situation, we may erroneously assume that the problems of poverty and inequality have alleviated over time, looking at the decline in the absolute poverty.

Second, in order to discuss inequality in a country, consumption inequality should be considered along with income equality. The reason is that although income is highly correlated with consumption, the patterns of income and consumption inequalities may appear differently. Consumption can be smoothed over time by savings or borrowing; by contrast it is hard for income to be smoothed over time. However, a number of existing studies have examined income inequality only and thus are unlikely to provide significant implications for inequality in a country.

Now I look into relative poverty and income and consumption inequalities to understand why the massive protests in Chile occurred. According to OECD data, the absolute poverty rate in Chile decreased by approximately 8 percentage points between 2007 and 2016; by contrast, the relative poverty rate decreased only about 2 percentage points during the same period. This implies that focusing only on the absolute poverty could provide misleading information on the income inequality of a country.

According to Chile's raw data from the Household Budget Survey (Encuesta de Presupuestos Familiares), while the relative income poverty rate rose, the relative consumption poverty rate decreased between 2011 and 2017. In other words, while the size of the low-income class increased during the period, the consumption of this class did not drop, or even rose. Therefore, it is highly likely that low-income households faced severe financial difficulties as their income declined and their expenditure did not decrease.

The goods that caused the financial burden on the low-income household would be necessity goods such as housing costs and utility fees. Expenditure on these goods accounts for a high proportion of the household spending. In addition, prices for housing and utility service are fairly high due to Chile's privatization policy, which can put financial pressure on the low-income household.

Similar to the results for the above-mentioned relative poverty rate, income inequality, defined as the ratio of income in the ninth decile to the first decile, has decreased between 2011 and 2017. By contrast, consumption inequality, which shows the ratio of consumption in the ninth decile to the first decile, has rather increased during the same period. This outcome suggests that although income inequality has worsened, the consumption gap between the high and

low-income groups has shrunk.

However, the findings that the consumption gap decreased do not imply an improvement in welfare of the low-income household. Taking into account the increase in income inequality, the outcome shows that the low-income group could be experiencing the double burden of reduced income and raised expenditure. If these financial burdens on low and middle-income groups have accumulated, the raised subway fares in 2019 could have been a trigger for the massive protests.

Previous literature on income inequality tends to investigate Latin America as a whole or rely on specific indicators such as the Gini coefficient. This approach could make it difficult to accurately grasp the situation that recently faces each Latin American country. In this context, it is necessary to examine both relative poverty and consumption inequality as complementary indicators of income inequality. In Chile, based on these two indicators, the relative poverty rate has risen, and the income gap between high and low income class has increased even though the absolute poverty rate has fallen from 2011 to 2017. However, the consumption gap between the groups has shrunk for the same period, having the result of aggravating the financial pressure of the low-income group. The massive protests in Chile seem to be led by the cumulative consequence of these phenomena. Therefore, it is important to comprehensively look into a variety of indicators when investigating the income inequality problem in Latin America. **KIEP**