

Politics and Inequality in Latin America and the Caribbean

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Introduction

Pooled time series data on income distribution and wage dispersion recently made available by the Luxembourg Income Study (LIS) and OECD respectively have stimulated a number of studies by political scientists which have demonstrated that variables of interest to the discipline such as party government and political institutions exert a strong influence on inequality, poverty, and wage dispersion in advanced industrial societies (e.g. see Bradley et al. 2003, Moller et al. 2003, Iversen 2005, Rueda and Pontusson 2000, Wallerstein 1999). By contrast, the study of causes of cross-national differences in inequality in developing countries has been neglected by political scientists.

The earliest and single most influential theoretical contribution on inequality and economic development was the work of an economist, Simon Kuznets (1955). Since its publication, the crossnational quantitative and more recently pooled time series analyses of determinants of income inequality have primarily been the work of sociologists and have been published in sociology journals.¹ The dominant debate in sociology has been about the relative contribution of economic development and related variables (education, the changing weight of economic sectors, per capita income), economic dependency, and political democracy. Other than democracy, the absence of variables tapping politics; political parties, political institutions, public policy, etc.; is striking. This is hardly due to disciplinary neglect of such variables in the theoretical literature in sociology: Most of the articles by sociologists cite the modern classic on inequality, Lenski (1966), whose explanation of the decline of inequality in the course of industrialization – Kuznet's inverted U-curve – emphasizes power and politics.

The neglect of politics in the study of inequality in the developing world is all the more striking because inequality is not only an intrinsically interesting social phenomenon and serious social problem, but recent research has argued that inequality is also causally related to two other phenomena of interest to social scientists concerned with development, democracy and economic growth. New growth theory has made the case both theoretically and empirically that more equal income distribution is related to economic growth in developing countries (Barro 1997). Observers of new democracies, particularly those in Latin America, have noted that high degrees of inequality prevent high quality democracies from emerging (UNDP 2004).

The reasons for this neglect are rather more prosaic: Studies of inequality in developing countries typically rely on data collected by international financial institutions, such as the IMF and World Bank, and international organizations, such as the ILO and the UN. The type of data utilized in the recent studies of the determinants of inequality in advanced industrial societies by political scientists cited previously – the distribution of votes, parliamentary seats, and cabinet seats across parties, the institutional

¹ Of the 24 references to journal articles on the determinants of income inequality in world wide samples of countries appearing in the list of references of three recent articles on the subject (Alderson and Nielsen 1999, Rudra 2004, Lee 2005), 16 were in sociology journals and 5 were in political science journals. Four of the authors or co-authors of these articles were political scientists; the rest were sociologists. Other than regime type, the only political variables appearing in these analyses were public expenditure in two very recent articles (Lee 2005, Rudra 2004) and government revenue in an early contribution (Rubinson 1976).

forms of government, etc. – are not collected by these organizations and thus are not readily available for a cross section of developing countries much less a pooled cross section and time series, and not even for one region of the developing world.

In this article, we analyze pooled time series data on Latin America and the Caribbean from 1970 to 1995 that include a range of such political variables collected by our research team. Latin America and the Caribbean in this period is ideally suited to investigate the relationship between inequality and the independent variables hypothesized in the economic and sociological literature on development and dependency as well as in the political science literature on the politics of inequality. Compared to other regions of the developing world (sub-Saharan Africa, North Africa and the Mid-East, South Asia, Southeast Asia, and East Asia), Latin America and the Caribbean exhibit more variation in indicators of development and democracy. For example, of the country year observations in this analysis, 37% were full democracies, 26% were restricted democracies and the rest were authoritarian regimes or colonies. Thus, for almost two-thirds of the observations there is also variation in terms of the vote and seat distribution of the parties and the political coloring of the chief executive. The per capita income varied from \$2,100 to \$19,100. The richer countries in the more recent years had an income per capita which was comparable to the less affluent OECD countries in the late 1950s and early 1960s.

Politics and Inequality in Latin America

There is strong evidence that Latin America and the Caribbean form the region with the highest average level of inequality and particularly with the highest concentration of income at the very top. This inequality has deep historical structural roots, but more contemporary political factors have reinforced rather than mitigated it. Indeed, over the past three decades of the 20th century inequality increased in most of the countries in the region for which data are available (Morley 2001: 24; IDB 1998; de Ferranti et al. 2004; ECLAC 2004).

Inequality in land holding and political power is at the center of the deep historical structural roots of inequality, originating in the colonial order. It not only cemented stark income inequality in the rural sector but also greatly contributed to the massive rural - urban migrations in the 20th century and thus to the swelling of the reserve army of unemployed that depressed wages for urban unskilled workers (Morley 2001: 63-65). Inequality in access to education and infrastructure perpetuated and reinforced income inequality in both the rural and urban sectors. Inequality in assets and income was conditioned by and reinforced inequality in political influence and thus in political institutions and policies, which in turn perpetuated the vicious cycle of inequality.

In all countries, including those outside of Latin America, such as Italy, Spain, and Prussia, where large landholders played an important role in the national economy and depended on a cheap labor force, they were determined and effective enemies of democracy (Moore, 1966; Rueschemeyer, Stephens and Stephens 1992). As long as they remained important economic and political actors, democracy had difficulty surviving. Restrictive labor legislation combined with the comparatively small size of the urban industrial sector hampered the formation of broad-based unions with sufficient

independence to challenge existing institutions and acquire economic and political clout. Weakness of democracy obstructed the formation of strong political parties in general, and combined with weakness of labor it hampered the development of parties of the left in particular and thus of forces capable of building the redistributive capacity of the state and shaping a model of political economy that would produce growth with equity. The neoliberal economic reforms of the past three decades had a further regressive impact. On the average, this impact was small, but in some countries, particularly Argentina and Chile, it was quite dramatic (Morley 2001: 152-3).

Theoretically, there is agreement on the importance of both economic and political causes of inequality in Latin America but, as noted, quantitative studies of causes of inequality have neglected political variables. The IDB Report states that “firm evidence is lacking” concerning the mechanisms through which political institutions might affect the distribution of income (1998: 104). It proposes the hypothesis that effective democracies “tend to do a better job of delivering essential social services such as health and education to low-income neighborhoods” (1998: 104) and that there may also be indirect effects of good institutions via economic growth and lower economic volatility, but it does not proceed to test these hypotheses. Instead, statistical analyses focus on education, labor force participation, demographics, and the economic environment. Similarly, the recent World Bank study (de Ferranti et al. 2004) offers a very comprehensive diagnosis of the roots of inequality and devotes much attention to taxes, transfer, and social services, and even to state-society interactions, but it examines economic, demographic, and political determinants one by one, not through multiple regression analyses. The study is extremely rich conceptually and provides a wealth of evidence for the structure and incidence of various social programs in individual countries, which can serve as a source of hypotheses about generalizable relationships.

Theoretically, then, we have strong reasons to believe that state action or inaction has been an important determinant of income distribution in Latin America and the Caribbean. We also know from quantitative studies of distribution and redistribution in advanced industrial societies that the welfare state can be a very powerful instrument of redistribution. All welfare states in advanced industrial societies redistribute income downward, but the magnitude of this effect depends both on the overall size of the welfare state and the structure of taxation and expenditures (Bradley et al. 2003). This structure in turn is shaped by power constellations and political institutions (Hicks 1999; Huber and Stephens 2001; Swank 2002). However, we have no quantitative studies of the effect of the size and type of social expenditures and of party political power distribution on inequality in Latin America. Here we provide the first multiple regression analysis that includes a whole range of theoretically important determinants of inequality, including strength of a country’s democratic tradition, different varieties of social spending, and political party strength.²

The inclusion of political party strength in an analysis of income distribution in Latin America and the Caribbean may require some additional justification. Why should one use a theoretical perspective that has proven useful in the analysis of inequality in

² In a companion article (author cite), we show that social spending in turn is determined in part by democratic history and political party strength.

advanced welfare states in an analysis of Latin America and the Caribbean, when many analysts have emphasized the weakness of the state and of political parties there? The first reason is that social science is cumulative and seeks generalization beyond specific regions. We certainly would want to know whether and how democracy and political forces shape social expenditures and thus income distribution under different historical and structural conditions. We do expect these factors to be important, but we also expect them to have different weights and different effects from those in advanced industrial societies.

The second reason is that there is significant variation among Latin American and Caribbean countries in the strength of the state, the magnitude and distribution of social expenditures, and the strength of political parties. Most analyses have emphasized the contrast to advanced industrial societies and the pathologies of Latin American states and party politics. However, some countries, such as Chile, Uruguay, and Costa Rica have long been recognized as having more effective states and social policies than other countries. Mainwaring and Scully (1995) clearly showed important differences in the institutionalization of party systems. In some countries, such as Brazil, stronger, more programmatic and disciplined parties have emerged more recently (Hagopian 2004). Luna and Zechmeister (2005) demonstrate on the basis of elite and mass survey evidence that the degree of programmatic orientation and coherence of political parties varies greatly between countries and between parties within the same country. Moreover, Colomer and Escatel (2004) show that citizens in Latin America find the left-right dimension meaningful for structuring politics. Finally, party affiliation and orientation has been shown to affect policy (Murillo 2001; 2002). All this evidence taken together suggests that we are justified in pursuing a theoretical perspective that assigns an important role to politics in shaping income distribution in Latin America and the Caribbean.

Literature and Hypotheses

Morley's (2001) study of the determinants of differences in inequality of income distribution between countries in Latin America combines multiple regression analyses with nine country case studies, and his variables include national income, inflation, education, economic reform indices, and land distribution. Studies of inequality in cross-regional mixed samples of developed and developing countries (Alderson and Nielsen 1999, Lee 2005), and in developing country samples (Rudra 2004) have paid particular attention to world system or globalization variables, along with demography and economic development. Alderson and Nielsen (1999), based on Nielsen and Alderson (1995) also examine the impact of sectoral differences in development, the size of the agricultural labor force, and the spread of education, whereas Rudra (2004) and Lee (2005) include government expenditures and democracy. None of them analyze the effects of power distributions among political parties. We build on these studies by adding to Nielsen and Alderson's (1995) internal-developmental model of inequality some of the indicators of investment dependence that Alderson and Nielsen (1999) examined, inflation and land distribution as used by Morley (2001), and size of the

informal sector as well as measures of the strength of the democratic tradition, two categories of social expenditures, and party political strength.

Economic Development: Theories linking economic development and inequality have been profoundly shaped by Kuznet's (1955) finding of an inverted U curve. In a comparative historical analysis of three advanced industrial societies, Germany, Britain, and the United States, he found that inequality increased with the onset of industrialization, then leveled off, and finally declined as these societies approached the advanced industrial stage.³ Most of the Latin American and Caribbean countries are at medium levels of industrialization; several of them are near the peak of the curve and a few have passed the peak (IDB 1998: 89). Thus, for the whole sample we would expect the relationship between economic development and inequality to be mildly negative or neutral.

Much statistical research has been devoted to establishing and explaining the U-curve relationship between economic development and inequality (e.g. Bollen and Jackman 1985, Crenshaw 1992, Muller 1985, 1988, 1989, Nielsen 1994, Nielsen and Alderson 1995, Simpson 1990). Alderson and Nielsen (1999) emphasize the role of labor force shifts and sectoral dualism, along with the demographic transition and the spread of education. Sectoral dualism refers to the coexistence of a low productivity traditional sector and a high productivity modern sector, the former being largely identified with the agricultural sector. The traditional assumption is that in the course of economic development, an increasing share of the labor force shifts from the low productivity agricultural sector to the high productivity modern sectors, causing initially an increase in income inequality, then a leveling off, and finally a decline, when the great majority of the labor force is in the high productivity modern sectors. Sectoral dualism then is a function of the average difference in income between sectors and is expected to have a positive effect on overall inequality in a society (Alderson and Nielsen 1999: 610).

In the Latin American context of the second half of the 20th century, though, the shift of the labor force out of agriculture did not necessarily imply a shift into high productivity modern sectors. Rather, many rural-urban migrants ended up in the low productivity urban informal sector. Thus, we cannot necessarily expect the hypothesized relationship between sectoral dualism and inequality to hold in our set of countries.

Alderson and Nielsen (1999: 610), based on Kuznets (1955) hypothesize that the shift of the labor force out of the agricultural sector is associated with increasing inequality, because the degree of inequality within the agricultural sector is assumed to be lower. Thus, size of the agricultural population would be negatively associated with inequality. However, the assumption of lower inequality within the agricultural sector for Latin America is certainly questionable, given the tradition of great inequality in landholding. Indeed, a comparison of Gini indices based on urban and rural surveys contained in the full Deininger and Squire data set (1996a, b) shows that inequality in the rural samples in Latin America is generally higher. Therefore, we would expect the

³ We should note that several advanced industrial societies have experienced a reversal of the trend to declining inequality over the past few decades. Harrison and Bluestone (1988) called this "The Great U-Turn." Since none of the Latin American societies have achieved an advanced industrial stage, we will not include the explanatory factors of this second U-turn in our discussion.

opposite relationship to hold in our set of countries; the larger the proportion of the labor force in agriculture, the higher the degree of inequality.

Land Distribution: Inequality in land distribution obviously has a very direct effect on inequality in incomes in the agrarian sector. In addition, it has a long-term indirect effect on income inequality in the urban sector via the great numbers of unskilled migrants swelling the reserve army of unemployed in the cities and thus depressing wages at the bottom. Latin America has historically had very high inequality in the distribution of land, which accounts for some of the extraordinarily high income inequality in comparison with other regions. However, within Latin America the variation in landholding structures is not great, as only very few countries have significant regions where small and medium landholdings dominate. Thus, we cannot necessarily expect a statistically significant effect of landholding inequality on income inequality.

Informal sector: The informal sector in Latin America is very heterogeneous, but low productivity activities dominate. Accordingly, workers employed in small enterprises in the informal sector earn less than workers in the formal sector, even controlling for experience and years of schooling. The same is true for self-employed workers, the vast majority of whom are in the informal sector. Moreover, the difference between male and female earnings is larger among workers in the informal than in the formal sector and among the self-employed than formal sector workers (IDB 1998: 40). Thus, we expect a larger informal sector to be associated with greater overall income inequality.

Inflation: Morley (2001:72) argues that in periods of high inflation labor markets adjust only with a lag, which leads to a decrease in real wages, and this decrease is particularly steep for the minimum wage. Thus, high inflation drives up inequality. The IDB (1998: 100-2) and World Bank studies (de Ferranti et al. 2004: 11; 231-9) agree that macroeconomic shocks, which are typically accompanied by high inflation, have a detrimental impact on inequality. Higher income earners are better able to protect their assets, e.g. by moving them abroad, and public bailouts of failed financial institutions transfer major shares of budgetary outlays from social services to investors. Low income families often make decisions that may help their situation in the short run but have a negative impact on earnings capacity in the long run, such as interrupting the education of children to send them into the labor force.

Demography: Rapid population growth is associated with economic development in the early and medium stages via the discovery of mortality-reducing medical practices. In advanced stages, the birth rate declines also and slows population growth. Previous studies have shown a strong association between population growth and the size of the young population, and a positive impact of population growth on inequality (Bollen and Jackman 1985, Simpson 1990). Alderson and Nielsen (1999) explain this impact with the oversupply of young unskilled workers that further depresses lower incomes and increases wage differentials. Thus, we expect population growth and percentage of the population under 15 years of age to push up the level of inequality. Holding other demographic features constant, we also might expect large aged populations to be associated with higher levels of inequality, particularly given the underdevelopment of public pension systems in most Latin American and Caribbean countries.

Education: The spread of education in the population, or the improvement of human capital, is regarded as a positive factor not only for the promotion of economic development but also for the reduction of inequality. In Latin American and Caribbean countries, however, the spread of education over the past three decades has coincided with a trend towards increasing inequality. In most of Latin America and the Caribbean, primary education has been universalized since 1970 for the younger cohorts, but a large proportion of these cohorts drops out at that point. At the other end of the educational spectrum, university education has expanded rapidly as well, as have returns to university education. Thus, educational achievement is unequally distributed and contributes to income inequality. In the newly industrializing countries of Asia, in contrast, secondary education has been nearly universalized and thus educational achievement is more equally distributed than in Latin America, causing lower income inequality (Morley 2001: 51-60). Accordingly, we would expect higher levels of secondary school enrollment to have a depressing effect on inequality in Latin America and the Caribbean.

Foreign Direct Investment: The debate about the effects of foreign direct investment on growth and inequality in Latin America has a long pedigree. Modernization theorists expected foreign direct investment to promote economic growth and thus decrease inequality, whereas dependency theorists pointed to the distorting effects of foreign investment on dependent economies which included increased inequality (e.g. Klarén and Bossert 1986). Statistical studies have found that stock of foreign direct investment has a positive effect on inequality (Bornschiefer and Chase-Dunn 1985, Evans and Timberlake 1980). Tsai (1995) found that this effect is region-specific and that foreign direct investment has no significant distributional effect for Latin American countries.

Firebaugh (1992) argued that studies of the effects of stock of foreign direct investment on economic growth were flawed because they typically included measures of both stock and flow, and a measure of the foreign investment rate (flow/stock) had a significant positive effect on economic growth. Thus, he argued, the authors of these studies wrongly interpreted the negative coefficient for stock as indicating a detrimental long-term effect of foreign investment on growth, when it in fact was the result of a denominator effect and consistent with a positive effect of the foreign investment rate. The same critique, then, could be applied to studies of inequality that include both stock and flow measures.

Alderson and Nielsen (1999) test whether Firebaugh's arguments also hold for inequality and find a positive and statistically significant effect of foreign investment stock, no significant effect of flow, and a significant and positive effect of investment rate on inequality. Thus, the positive effect of stock could not be the result of its role as the denominator of the rate. They also examine regional effects and find that stock of foreign direct investment continues to have a significant positive effect on inequality net of the region variables and interactions. Accordingly, we expect a positive effect of the stock of foreign direct investment on inequality.

We also expect a positive effect of flows of foreign direct investment on inequality in Latin America and the Caribbean, because foreign investment usually brings comparatively capital intensive production that creates comparatively few but well paying jobs. In addition, foreign investors have typically opposed corporate taxation and

often been able to extract concessions at the point of negotiations about new investment. This in turn keeps tax revenue and thus the redistributive capacity of the state restricted.

Democracy: There are strong theoretical reasons to expect that length of a country's democratic experience is associated with lower inequality (Rueschemeyer, Stephens and Stephens 1992: 10). Democracy gives the powerless and underprivileged the chance to organize and use organization as a power base to gain entry into the political decision-making process. The most effective channels for underprivileged groups into the political decision-making process are political parties, as they lack the connections and funds to influence decision-makers directly. However, it takes time for parties to gain coherence and establish roots in social bases, as well as for legislatures to pass major pieces of legislation and for that legislation to be implemented. In particular, it takes time for parties representing the interests of less privileged groups to consolidate. These groups and parties need to have the freedom to organize and establish linkages with each other in order to gain representation in competition with parties representing privileged groups and enjoying a financial advantage.

In studies of income distribution in advanced industrial democracies, democracy does not figure as a variable because there are no non-democratic cases outside of Southern Europe in the post-WW II period.⁴ In Latin America and the Caribbean, in contrast, there is great variation in the length of time for which a country has been democratic. Thus, we expect the countries with the longer democratic traditions to have lower inequality. Other studies have found such an effect (Bollen and Jackman 1985, Burkhart 1997, Rudra 2004), but they have measured the immediate presence of democracy in the year of the observation of the dependent variable or the year before, not the strength of the democratic tradition, which is theoretically more appropriate.

Political Parties: We know from studies of welfare states and redistribution in advanced industrial democracies that strength of left parties has a significant effect on the extent of redistribution effected through the welfare state (Bradley et al. 2003). Redistribution depends both on the size of the welfare state and on its structure. Both left and Christian democratic parties favor large welfare states, but left parties favor structures of transfers and services that benefit particularly lower income earners to a greater extent than do Christian democratic parties. When in office for protracted periods of time, these parties indeed structure welfare states in accordance with these preferences (Huber and Stephens 2001). In Latin America and the Caribbean, left parties have also favored redistributive policies. As noted, however, left parties on the whole have been rather weak, so they have not been able to build generous, comprehensive, and redistributive welfare states. Nevertheless, we would expect to see some impact of differences in left party strength on the level of public expenditures and thus indirectly on income distribution. To the extent that we are not able to capture the distributive structure of public programs in our measures, we would expect to see a direct effect of left party strength on inequality. We would also expect left parties to have a direct impact, not mediated by social spending, through legislative and administrative measures such as adjustments of the minimum wage, wage setting for public employees, and labor

⁴ Indeed, the vast majority of cross-national statistical analyses of welfare states in advanced industrial societies do not even include Spain, Portugal, and Greece.

laws. Center parties in Latin America and the Caribbean tend to base their appeals on commitments to democracy, the rule of law, honest government, and competent leadership, rather than a social and economic policy agenda. Accordingly, we would not expect any center party effects on inequality. Right parties, in contrast, have supported growth strategies without regard to their distributive consequences, and they generally protect the interests of upper income earners, so we would expect a positive effect of right party strength on inequality.

Social Spending: In advanced industrial democracies, size of the welfare state is strongly associated with reduction in inequality (Bradley et al. 2003). In Latin America and the Caribbean, the evidence for the distributive impact of social spending is more mixed and tends to be different for different kinds of expenditures. Social security spending, particularly the largest share that goes to pensions, tends to be regressive (de Ferranti et al. 2004). Social security schemes are typically tied to formal sector employment and benefits are tied to earnings, so the entire workforce in the informal sector is excluded. Even within the formal sector, more highly educated and more highly paid employees are more likely to be covered by social security (IDB 1998: 148). Moreover, social security benefits are very unequally distributed among those covered not only because they are earnings-related but even more so because of the existence of different schemes for different groups, with particular privileges for some, such as the military, police, upper level civil servants, judges, etc.. Thus, we expect higher social security and welfare spending to increase inequality.

Spending on health and education is spending on social services and thus its impact on income inequality is expected to have a considerable lag. Moreover, its distributive effect depends on the allocation of health and education spending. Allocation to preventive and primary care in rural and urban clinics has a much more redistributive impact than allocation to expensive curative medicine in urban hospitals. Spending on primary education is redistributive and spending on university education regressive. As de Ferranti et al. argue, the distributive impact of an expansion of services depends on the initial level of coverage or enrollment (2004: 260-1). Where initial enrollment or coverage is relatively high, an expansion will predominantly benefit the lower income groups; where it is low, the middle and higher income groups are likely to be the first to benefit from an expansion. We do not have breakdowns for these different allocations, but evidence from case studies cited by de Ferranti et al. (2004: 263-5) and from IDB analyses (1998: 190-7) indicates that the bulk of education spending is progressive and health spending slightly progressive or neutral. Thus, we hypothesize an overall depressing effect of sustained high levels of expenditures for health and education on inequality.

Measures of the Dependent and Independent Variables

We use the Gini coefficient to measure income inequality because it “combine(s) maximum coverage of countries and time periods with an acceptable level of quality” (Deininger and Squire 1996a: 567). Our Gini observations are compiled from the datasets of Klaus Deininger and Lyn Squire (1996) and Juan Luis Londoño and Miguel Székely (1997). Deininger

and Squire (1996) establish three criteria for “good quality” Gini data, namely that the observations be based on household surveys; that the data provide comprehensive coverage of the country; and that the observations fully cover all income sources (568). Londoño and Székely (1997) abide by the same stipulations for “good quality” data, and add 40 observations. Deininger and Squire (1996) and Londoño and Székely (1997) find that other technical aspects of household survey data often influence the value of Gini estimates. There are three aspects of data collection that may result in cross-national variation in Gini measures: whether data are recorded for the household or the individual, whether values are calculated based on income or consumption, and whether gross or net income sources are considered. We control for two of these potential problems by including a dummy for Gini values that are calculated for the household (1) rather than per capita (0), and for coefficients that are based on income (1) instead of consumption (0). We chose not to control for variation in the income source (gross versus net), because previous studies (Alderson and Nielson 1999) found this variable to be non-significant.

As indicators of development we use GDP per capita in purchasing power parity dollars, employment in agriculture as a percent of total employment, and sector dualism in our models. Gross Domestic Product in 1996 purchasing power parity dollars is taken from the Penn World Tables supplemented by World Bank’s (2003) *World Development Indicators* where data were missing in the Penn World Tables. Employment in agriculture as a percent of total employment is compiled from four sources (ILO 2003, ECLAC various years, World Bank 2003, and Alderson and Nielson 1999). Sector dualism measures the absolute difference between employment in agriculture as a percent of total employment and agriculture as a percent of GDP. The component parts of this measure are taken from four sources (ILO 2003, ECLAC various years, World Bank 2003, and Alderson and Nielson 1999). Where values were missing on either of the component parts, observations were extrapolated or interpolated.

To measure the spread of education, we take the net secondary school enrollment ratio, that is, the number of students of official school age who are enrolled in secondary schools as a proportion of all children from that age group. The official secondary school age is defined by each country’s education system. The data are taken from the World Bank’s (2003) *World Development Indicators*. Where values were missing, we extrapolated and interpolated observations.

To measure a country’s penetration by direct foreign investment, we include measures of inward foreign direct investment flows and stock. Foreign direct investment inflows are measured as a percent of gross capital formation. The data are compiled from the World Bank’s (2003) *World Development Indicators*. The World Bank (2003) defines inflows as “the sum of equity capital, reinvestment of earnings, other long-term capital, and short-term capital as shown in the balance of payments” (CD rom). The measure of inward investment stock is reported in millions of dollars and is taken from two sources, UNCTAD’s (2002) *Handbook of Statistics* and from the United Nations Centre on Transnational Corporations (1985). The missing values for stock of inward investment were interpolated. Since values of inflows of direct foreign investment fluctuate from year to year, interpolation is not an appropriate way to handle missing data for this variable, so the missing values were coded to the country mean for the eight country years for which there were missing data.

We derive our measure of democracy from Rueschemeyer, Stephens, and Stephens' (1992) democracy coding. Where values were not available, we extended the coding following the guidelines provided by the authors: colonies = 0, authoritarian regimes = 1, bureaucratic authoritarian regimes = 2, restricted democracy = 3, and full democracy = 4. These categories were collapsed into non democracy = 0, restricted democracy = .5, and full democracy = 1. To measure democratic history we cumulate the yearly scores beginning in 1945.

Our political variables are derived from Coppedge (1997). In his project, he consulted country experts to classify political parties which contested elections for the lower house or constituent assemblies in 11 countries of Latin America from as far back as 1912. His classification scheme contains two primary dimensions and several residual categories. First, it includes a left-right dimension, defined primarily in social and economic terms. He is concerned with a political party's ideology and class appeals and with its relative prioritization of growth and redistribution. This dimension is divided into five categories: left, center-left, center, center-right, and right. Second, it includes a religious dimension of two categories, Christian and secular. It distinguishes those parties which do and do not base their ideology or programs on the Catholic Church, the Bible, or religious philosophy or seek to defend the interests of the Catholic Church and to reduce the separation of church and state. Finally, his classification scheme contains three residual categories: personalist, other, and unknown. For our purposes, it is sufficient to say that these residual categories all contain parties that are not classifiable according to left-right or Christian-secular criteria.

In two respects, we directly adopted his work. First, we adopted his classification scheme.⁵ Second, we adopted his classification of parties for the country-years that fall within our sample. We use his classification scheme to expand the coverage to the full range of countries and years that fall within our analysis.⁶ After classifying each party, we summed the proportion of the seats held by each category for each country-year.⁷ This results in 13 annual series (secular left, secular center-left, secular center, secular center-right, secular right, Christian left, Christian center-left, Christian center, Christian center-right, Christian right, Personalist, Other, Unknown) for each country. Each series indicates the seat share in the lower house or constituent assembly held by secular left parties, secular center-left parties, etc. During years which are non-democratic, as defined by our democracy variable, all categories are scored as zero. For each category, we cumulated the seat share from 1945 to the year of observation. Finally, to construct each of our political independent variables, we tallied various party categories, as described in Table 1. For example, the variable "Leftist Lower House" is the cumulative total since 1945 of the proportion of seats held by secular left, secular center-left, Christian left, and Christian center-left parties in the lower house or constituent assembly.

⁵ See Coppedge (1997) for detailed category descriptions.

⁶ Unlike Coppedge (1997), we did not use expert surveys. Instead, two members of our team independently consulted numerous primary and reference materials in order to code each political party. Then, on parties for which there was a disagreement, we did seek external expert advice, and finally the entire research team convened to make a decision.

⁷ Our procedure of tallying seat shares differs from Coppedge (1997), who tallied vote shares. We make this choice on the grounds that seat shares are more consequential for policy than vote shares.

Our measures of social spending as a percentage of GDP are derived from several sources. The series for social security and welfare spending comes from two IMF volumes. In the Government Finance Statistics Yearbook (GFS) the IMF disaggregates central government spending into combined spending on social security and welfare and into combined spending on health and education.⁸ GDP is reported in the International Financial Statistics Yearbook. Both spending and GDP are reported in current local currency units. The fact that these figures include only outlays by the central government is not a problem for social security and welfare expenditures, as these programs in general are uniform across the nation and centrally financed.⁹ Social assistance programs provided by subnational units are not large enough to make a difference. This is confirmed by the fact that the data series from the IMF and our other sources are very highly correlated (.92 to .96).

For health and education expenditures, however, the exclusion of state and local spending is a major problem. Several countries administer health and education programs at sub-national levels; some have done it for a long time, in others trends towards decentralization began in the 1980s or 1990s. To deal with this problem, we compared data series from four different sources: ECLAC (<http://www.eclac.cl/badeinso/SistemasDisponibles.asp>), Cominetti (1996), ECLAC's *Social Panorama* (various years), and the IMF sources cited above. The correlations for the IMF and ECLAC series, the only two series with large numbers of observations are .85 for education and .64 for health. The *Social Panorama* series cover state and local spending where it is significant except in Mexico (ECLAC 2004: 179). Comparing the ECLAC series and the *Social Panorama* (available only for years from 1990 on) series, it is apparent that the ECLAC series also cover state and local spending. Thus, we use ECLAC for countries in which state and local spending is significant. For the remaining countries, we use the longer time series when ECLAC and IMF are consistent with each other, which is the case in all but a few cases. In most cases, the ECLAC series is longer. We filled in missing values from the other three series provided they are consistent with the ECLAC or IMF series. In the few cases in which there are discrepancies between ECLAC and IMF (other than those with significant state and local spending as noted above), we chose the series which was most consistent with Cominetti and *Social Panorama*. When the *Social Panorama* and ECLAC series overlapped and appeared similar but not identical we used the *Social Panorama* data because they are more recent and we have more information on exactly what they cover. We would also expect ECLAC to update the *Social Panorama* series. The only case in which we did not use *Social Panorama* data over ECLAC data is Mexico's health spending (1990-2000). *Social Panorama* notes that its series for Mexico does not include local spending and thus systematically underestimates spending (2004: 179). Since the ECLAC series is consistently higher, we opted for the ECLAC series.

⁸ Kaufman and Segura (2001) use the same measure and source as one of their specifications of social spending. Health spending includes those health expenditures which are provided as parts of social security and educational programs, such as health care provided as part of old age social security schemes. They use the IMF series for both social security and health and education spending.

⁹ Indeed, the bulk of spending in this combined category goes to social security. The IMF sources report the two types of expenditures separately for 179 country years only; in these observations, social security accounts for 83% of the spending.

As noted, successful investment in human capital requires a sustained effort in the form of expenditures on health and education. In addition, improvements of the human capital base only have an impact on income inequality over the medium and longer run. Therefore, we measure health and education spending as the cumulative average from the first data point to the year of observation.

To measure land distribution, we calculated a Gini coefficient of land inequality using the Lorenz curve. The United Nations' Food and Agriculture Organization reports land holding size as percent of all holdings (share of holdings) and the distribution of holding area as a percent of total area (share of area). Using these two series, we plotted the Lorenz curve and calculated the Gini coefficient of land inequality (FAO, various years). Since land holding patterns have a high degree of stability, we interpolated and extrapolated missing data points. The exceptions are cases where governments instituted land reform,

We calculated the size of the informal sector, that is, workers classified as informal; including independent workers, domestic workers, and small enterprises; as a percentage of the non-agricultural labor force, on the basis of data from Portes (1995) and the International Labor Organization (ILO, various years). Missing values are interpolated and extrapolated. The International Labor Organization's data on informal sector employment contained no information for the four English speaking Caribbean countries, Bahamas, Barbados, Jamaica, and Trinidad and Tobago. Unlike the two other variables for which we had incomplete information (land distribution and FDI inflows), informal sector proved to be significant in the baseline model with no political variables. In order not to lose the 18 Caribbean observations or, alternatively, drop the informal sector variable from subsequent models, we developed a trichotomous version of the variable and estimated the values of the 4 countries based on our knowledge of the domestic economies. Barbados and the Bahamas were estimated to have low informal sector employment and Trinidad and Jamaica were estimated to have medium informal sector employment.¹⁰ The trichotomous measure of informal sector proved to be a stronger predictor of inequality for the observations for which we had both variables.

Analytic Techniques

We use an unbalanced panel data set with 113 observations from 18 Latin American and Caribbean countries: Bahamas, Barbados, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Panama, Peru, Trinidad and Tobago, and Venezuela. The inequality data were available for varying numbers of time points for the countries. The data span the period 1970 to 1995. A central problem in estimating regression models from panel data is that the assumption of independence of errors across observations is unlikely to be satisfied. As a result OLS produces incorrect standard errors for the regression coefficients (Greene 1993). There are several strategies to deal with correlated errors in panel data. One approach assumes serially correlated errors within each unit (country) obeying a unit specific autoregressive process (which may optionally be constrained to be the same across units). This approach requires what Stimson (1985) calls temporally dominated time-series of cross-sections, i.e., data structures consisting of

¹⁰ The results of the statistical analyses were substantially the same when this variable was deleted from the analysis.

relatively few units observed over many equally spaced time points (Beck and Katz 1995:635-4; Beck 2001). Since the average number of time points (7) is much smaller than the number of units (18), our data set precludes this approach.

Another approach is to estimate a random effect model (REM) in which the error term contains a unit-specific component that differs across units but is constant over time for a given unit. Such an error structure would arise if unmeasured unit-specific causes, such as systematic measurement differences or other overlooked aspects of the social and cultural makeup of a country, affect the dependent variable in the same way at each point in time over the period of the data. The stable unit specific component implies that observations for the same unit at different time points are all correlated by the same amount, ρ . The REM strategy is feasible with our data; one attractive feature of REM is that it allows estimating the value of ρ . However, REM requires relatively strong assumptions, such as equal correlations among errors within units.

Because it is not substantively essential in this study to measure ρ , we adopt an alternative estimation strategy that addresses the correlation problem while requiring a minimum of assumptions on the behavior of the errors. We combine OLS estimation of the regression coefficients, which provides consistent estimates of the regression coefficients, with the use of a *robust-cluster* estimator of the standard errors. The standard (i.e., non-cluster) Huber-White or "sandwich" robust estimator of the variance matrix of parameter estimates was discovered independently by P. Huber (1967), White (1980) and others (see Long and Ervin 2000 for a detailed description). It provides correct standard errors in the presence of any pattern of heteroskedasticity (i.e., unequal variances of the error terms) but not in the presence of correlated errors (i.e., nonzero off-diagonal elements in the covariance matrix of the errors). The robust-cluster variance estimator is a variant of the Huber-White robust estimator that remains valid (i.e., provides correct coverage) in the presence of *any* pattern of correlations among errors *within* units, including serial correlation and correlation due to unit-specific components (Rogers 1993; see also Sribney 1998; StataCorp 1999: 256-260). Thus the robust-cluster standard errors are unaffected by the presence of unmeasured stable country-specific factors causing correlation among errors of observations for the same country, or for that matter any other form of within-unit error correlation.¹¹

The robust-cluster estimator of the standard errors is only impervious to correlations of errors *within* clusters. It requires errors to be uncorrelated *between* clusters. The latter assumption might be violated if unmeasured factors affect the dependent variable in all units at the same point in time. Global economic fluctuations, such as the debt crisis period in Latin America in the 1980s, could produce such contemporaneous effects. To evaluate the potential impact of such unmeasured period specific factors we re-estimated the models with indicator variables for the debt crisis (1983-89) and for the 1990s (1990-1995); the baseline category corresponds to 1970-82. These period dummies were not significant so they were dropped from the analysis. In order to check for robustness, the models were also estimated with

¹¹ Long and Ervin (2000) find that the alternative robust estimator HC3 proposed by MacKinnon and White (1985) performs better than the standard Huber-White robust estimator in small samples in the presence of heteroskedasticity. However HC3 is not defined for clustered data and not impervious to correlated errors within clusters. Thus HC3 is not suitable for our data.

panel corrected standard errors (PCSE), OLS, and REM. The results were substantially the same using these alternative techniques. The robust cluster estimates proved to be the most conservative.

Population growth, the proportion of the population over 64, and the proportion of the population under 15 proved to be very highly intercorrelated. When two of these three variables were entered together with the other independent variables, the independent variables were multi-collinear. When entered alone, youth population and population growth carried the wrong sign. The aged population was correctly signed but not significant. Since the aged variable had the highest variance inflation factor value, it was dropped from the analysis. Since population growth theoretically works through the size of the young population in influencing inequality, we also dropped this indicator and only retained size of the young population.

Similarly, strength of democracy and party strength are very highly correlated, particularly left party strength ($r=.88$), for the theoretical reasons outlined above. This means that we cannot enter them in the same regression because of multicollinearity. Thus, we produce models with controls and democracy, with controls and democracy and spending, and with controls and spending and parties.

Results

The results of our analyses are presented in Table 2. Model 1 includes all non-political variables and the dummies to correct for difference in methodology. Model 2 drops two non-significant variables for which we have incomplete data, land distribution and foreign investment inflows. This helps us gain 16 observations. Model 2, then, is the baseline for the analysis of the political variables. Model 3 adds democracy to the baseline model. Model 4 adds social spending; model 5, parties; model 6, social spending and democracy; and model 7, left parties and social spending; to the baseline model. The drop in variation explained from model 1 to model 2 is entirely due to the change in the observations included: If model 2 is estimated only for the cases included in model 1, the R^2 is identical to model 1, .74. Multi-collinearity forced us to exclude right and center parties from model 7.

The addition of democracy (model 3) significantly increases the variation explained when compared to the baseline, from 63% to 70%. The democracy coefficient is highly significant and substantively meaningful: A standard deviation increase in democratic experience (11.2 years) is associated with a 2.3 unit decrease in the Gini index. Adding social spending to the baseline also significantly increases the variation explained (model 4). Both variables are highly significant and correctly signed. A standard deviation in education and health spending (2.1%) is associated with a 1.9 unit decrease in the Gini while a standard deviation increase in social security and welfare spending (2.7%) is associated with a 2.3 unit *increase* the Gini. Adding parties to the baseline equation also results in a significant increase in variation explained over the baseline (model 5). The coefficients for left and right parties are correctly signed, but only the left parties coefficient is significant; as predicted, center parties are not significant. A standard deviation increase in left party legislative strength (7.7) is associated

with a 3.0 unit decrease in the Gini.¹² In model 6, both democracy and social spending are added to the baseline control variables. Health and education spending falls to non-significance but social security and welfare spending retains significance with the inclusion of democracy, which is consistent with our companion analysis of the determinants of social spending. There, we find that democratic experience is a significant determinant of health and education spending but not of social security and welfare spending (author cite). Model 7 shows a similar effect in the case of left party strength; health and education spending is now not significant, which is consistent with our finding that left party strength is related to health and education spending but not to social security spending. On the contrary, we found that right party strength was a significant determinant of social security and welfare spending.

Among the substantive control variables, only inward stock of foreign investment is correctly signed and significant in every equation. Secondary education, employment in agriculture, and inflation are correctly signed and significant in five of the seven models. Sector dualism is correctly signed but significant in less than half of the models. Youth population is significant in six of the seven models but incorrectly signed. GDP per capita is incorrectly signed but significant in two models only. It is worthwhile exploring further the magnitude of the effect in the case of education and inflation because these two variables are at least in part under the control of governments. Using the coefficient of model 2 or 3, a standard deviation increase in the percent of an age cohort enrolled in secondary education (21.7%) is associated with a 3.0 unit decrease in the Gini index. Estimated on the basis of model 2, a standard deviation reduction in the level of inflation (351%) is associated with a .6 unit reduction in the Gini index, quite a small difference.

In the case of the methodological controls, only the income vs. expenditure dummy was consistently significant. Our results indicate that the income based studies result in a Gini index that is 4.5 to 8.0 higher than is the case of expenditure based studies. This squares very well with the results of Deininger and Squire's (1996a) analysis of a world wide data set and Londoño and Székeley's (1997) analysis of Latin American and Caribbean data, both of which suggest that the income based Gini will be 6 units higher than the expenditure based Gini.

Discussion and Conclusions

Our analysis has clearly demonstrated the importance of politics in shaping the extent of economic inequality in Latin American and Caribbean countries. Strength of the democratic record, the political coloring of the legislature, and policy instruments all had significant effects on income distribution. The addition of democracy to our baseline model increased the variation explained by seven percentage points, and democracy had a substantively important effect. The cumulative record of strength of different parties in the legislature, as well as social spending on health/ education and on

¹² With an identical left-center-right measure of executives, we got the same result: Cumulative left executive (coded 1 for each year of a left president or prime minister) resulted in a significant reduction of inequality while center and right executives, though correctly signed in the case of right executives, were not significant.

social security/ welfare, if added separately to the baseline model, had virtually the same explanatory power as strength of the democratic record.

Of the two spending variables, social security and welfare spending had a larger substantive effect in increasing inequality than the long-term average of health and education spending had in decreasing it. This has to be expected, given that social security and welfare spending entails direct cash transfers whereas health and education spending works indirectly, through medium and long-run improvements in the human capital base that increase the earnings capacity of the previously less educated and healthy. When democracy and the two spending variables were entered into the same model, social security and welfare spending retained significance whereas health and education spending lost its effect, and democracy retained a highly significant effect. This indicates that democracy works partly through higher expenditures on health and education, but that democracy also has other effects that lower income inequality. To begin with, the structure of expenditures matters tremendously; health and education spending lowers inequality if it is allocated to primary and secondary education and to basic preventive health services. One can assume that democracies are more likely to follow such expenditure patterns than authoritarian regimes in Latin America and the Caribbean, since the overwhelming majority of authoritarian regimes have been of the right-wing variety. In addition, democracies can be assumed to be more likely to engage in a variety of economic regulatory policies, particularly in the labor market, that affect income distribution in a progressive way.

Among the political parties, only parties of the left showed a significant impact on lowering inequality. Parties of the center and right had no statistically significant effects on inequality. As in the case of democracy, when left party strength and the two spending variables were entered into the same model, social security and welfare spending retained significance whereas health and education spending lost its effect, and left party strength remained highly significant. Again, this indicates that the effect of left party strength, like the effect of democracy, works in part through the amount of expenditures on health and education and in part through the structure of these expenditures and a range of other redistributive policies.

The most consistently significant among our control variables are foreign direct investment (significant in all seven models), secondary education, inflation, and sectoral employment (each of them significant in five of the seven models). There is a long research tradition, originating with the dependency school, that has emphasized the inegalitarian consequences of foreign direct investment. This investment tends to be more capital intensive than domestic investment and it creates relatively few jobs, all in the formal sector. In addition, foreign investors have leverage concerning demands for tax breaks, which may constrain the government's resource base and thus its ability to pursue redistributive policies.

Expansion of secondary education is an indicator of skills improvement among the lower income earners. Once primary education is universalized, as it has been in Latin America and the Caribbean, expansion of secondary education will come to include children from less privileged families. Indeed, one of the differences in

educational policy that is held to account for greater educational and thus income inequality in Latin America and the Caribbean than in East Asia is precisely that East Asian countries invested in expansion of secondary education in addition to primary education, whereas Latin American countries put stronger emphasis on expansion of university education (IDB 1998: 45). Obviously, this argument applies to differences between Latin American countries as well; countries with larger secondary enrollment have lower inequality.

Inflation has a statistically significant but substantively not very large effect. The explanation has to be sought in the nature of inflation in Latin America. Many countries had moderately high levels of inflation over long periods and developed mechanisms of indexation of wages and benefits to deal with them. What destroyed these mechanisms and hurt the poor and the middle classes more than the richest groups – and thus increased inequality – were episodes of runaway inflation. Thus, one standard deviation in inflation (351%) does not show a very large effect, but the bouts of hyperinflation of 1000% or more suffered by some countries in some years had much stronger effects.

The effect of the relative size of agricultural employment is consistently positive, that is, it is enhancing inequality. This is in accordance with our expectation for Latin America, but contrary to the expectations of authors who have worked with mixed samples of developed and developing countries (Alderson and Nielsen 1999). In Latin America and the Caribbean, the distribution of land has been so highly unequal that it created not only greatly unequal earnings from land ownership but also a surplus poor rural population that kept rural wages very low, much below the urban sector. Thus, a larger agrarian sector means a larger proportion of very poor people, which increases the degree of inequality at the national level.

Our discussion of the agricultural sector in Latin America and the Caribbean raises the question why land distribution did not have a significant effect on income distribution. In fact, the land distribution Gini was significant in REM, OLS, and PCSE estimates. Still, the effects were small; a standard deviation change in the land Gini (3.1) was associated with a .76 unit change in the income Gini. However, this should not be taken as evidence that land distribution has little effect on income distribution in Latin America and the Caribbean; rather, it is the result of the fact that land distribution varies very little among the country-years in the analysis: The land Gini varies from a low of 86 to a high of 96. The one country in the region for which we have data and that shows a large decline in the land Gini is Saint Lucia (which is not included in this analysis because of missing data for the dependent variable). In that country, the land Gini declined from 89 in 1973 to 71 in 1996. The land Gini coefficient in the model indicates that a decline of this magnitude would be associated with a 4.1 unit decline in the income Gini, a very substantial change. This would indicate that comprehensive land reform could have a substantial impact on income distribution in Latin America and the Caribbean.

It is worthwhile to compare our results with those of recent pooled time series analyses of income distribution in world wide sets of countries (Nielsen and

Alderson 1995, Alderson and Nielsen 1999, Lee 2005), less developed countries (Rudra 2004), and Latin American and Caribbean countries (Morley 2001). All of these studies except Nielsen and Alderson, which was in press before the data set was released, use the Deininger and Squire World Bank data set on inequality that was the source for most of our data on inequality. Morley adds the Londoño and Székely (1997) data, as we do.¹³ Nielsen and Alderson, Alderson and Nielsen, and Lee all find that secondary education is negatively related to inequality and inward stock of foreign capital is positively related to inequality, confirming our results for Latin America in world wide samples. Their result for size of the agricultural sector, a significant negative effect on inequality, contrasts to ours. As we stated in the hypothesis section, we expected this contrasting result based on the very high degree of concentration of land in Latin American countries. Lee (2004) finds, as we do, that sector dualism, though correctly signed is not significant once government spending is entered into the equation. Lee finds that the impact of aggregate government spending on inequality depends on the political regime: It is positive in authoritarian regimes and negative in democracies. Our results suggest that differences in composition of government spending are one reason for this difference. Alderson and Nielsen and Lee find no significant effect of democracy on inequality while Rudra finds that it has a negative effect, as we do. One reason for our stronger results for democracy may be the difference in the measures: Their measure is for one time point whereas ours is history of democratic rule. It makes sense that democratic history would have a stronger impact on democracy than regime form at the time point of the inequality observation. Finally, we confirm Morley's finding that inflation increases inequality in Latin America and the Caribbean and find at least some evidence supporting his finding that land distribution is related to income distribution in the region.

Our results for Latin America and the Caribbean partly square with but partly strongly contrast with the results for advanced capitalist democracies. Alderson and Nielsen (2002), and Gustafsson and Johannson (1999) find that social spending is very strongly related to income *equality* in advanced capitalist democracies, and Bradley et al. (2003) show that it is very strongly related to governmental redistribution. Numerous studies that break down the LIS micro data for various countries by program show that almost all welfare state transfers, including pensions, have an equalizing effect on income distribution, some more than others.¹⁴ By contrast, the few studies of micro data on income distribution in Latin America show that social security transfers go disproportionately to upper income groups (IDB 1998, Ferranti et al. 2004). Pensions make up the overwhelming majority of these transfers and most of them go to formal sector employees and even among these recipients, upper income groups, such as military officers, upper level civil servants, and judges, receive particularly generous pensions. By contrast, these same studies indicate that health and education spending is mostly progressive, which squares with our finding. Thus, similar to the studies of advanced capitalist democracies (see especially Bradley et al. 2003), we find that left party strength

¹³ Morley adds the urban samples from the Deininger and Squire data but then also provides an analysis for the national samples only. Our 113 observations are a subset of his 134 national sample observations, because we lose observations on independent variables that he does not use.

¹⁴ These are too numerous to cite. A large number of them appear in the LIS working paper series which can be accessed at <http://www.lisproject.org/publications/wpapers.htm>.

is associated with higher levels of health and education spending (author cite) and that left parties have both a direct effect and an indirect effect via health and education spending on income distribution.

The central implications of our results are that the deep historical structural roots of inequality in Latin America and the Caribbean weigh heavily on income distribution at the beginning of the 21st century, but that they are not immutable. We have shown that politics do make a difference. Prolonged periods of democratic rule allow for the articulation of the interests of the underprivileged. Democracy does not guarantee that these interests will be articulated, much less that they will be protected. However, democracy does increase the probability that this will happen in Latin America, where the alternative has not been communist authoritarianism but rather capitalist right-wing authoritarianism. The articulation of interests of the underprivileged through left parties can – if left parties grow sufficiently strong to achieve legislative influence – shape a whole range of policies to reduce inequality. A prominent form that this has taken in Latin America has been investment in human capital.

So far, the strength of the democratic record and of left influence in the legislatures has been insufficient to allow for major departures in strengthening the fiscal base of governments and increasing and restructuring public expenditures with an emphasis on primary and secondary education, preventive and basic health care, and redistributive transfer programs. Left parties have been developing proposals for basic social safety nets in the form of non-contributory, tax-financed transfers to the working-age poor with children and to the elderly poor, but generating new resources through tax reform has been as politically difficult as restructuring the old inegalitarian social security systems. Privileged groups have a political advantage not only under authoritarianism but also under democracy – it is just not quite as strong and durable under democracy.

Given the high level of inequality in Latin America and the Caribbean – the mean Gini in our data set is 50 compared to 28 in advanced capitalist democracies – the estimates given above for the effects of our political and policy variables may seem to the reader to be small. However, they indicate that, were a country to move in an egalitarian direction on all of the variables for a sustained period of 15 or 20 years, inequality could be reduced very substantially. A sustained period of left government (1) in a democracy (2) during which the government increased spending on education and health and directed it to lower income groups (3), increased secondary school enrollment (4), restructured social security spending to direct it to lower income groups (5), held inflation in check (6), and carried out a land reform (6) would result in a very substantial reduction in inequality.

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