Wage Inequality in Latin America: Understanding the Past to Prepare for the Future

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Latin America’s remarkable story
It is possible to grow with equity

![Graph showing Real GDP (USD) and Income Inequality from 2002 to 2011. The x-axis represents years from 2002 to 2011, and the y-axis represents US (Billions) and Gini points, average. The graph shows a decrease in Real GDP (USD) and an increase in Income Inequality from 2002 to 2011.]
Key findings

- Wage inequality fell throughout Latin America—unique in the World

Why?
- Growth
- Education
- Other Forces

The future with lower growth
- Slower wage inequality reduction
- Further progress will require extra work
Latin America’s reduction in wage inequality in the 2000s

Facts
LAC sharply reduced wage inequality, going against the global trend

Wage inequality across regions relative to 2002

Regionwide phenomenon (in 16 out of the 17 countries)
How did wage differences between workers narrow?

Wage inequality and real wages

South America

Central America and Mexico

Index of real hourly wage

Gini points, average

Wages for the bottom 10%

Wages for the top 10%

Wage Inequality
Wage gaps fell between low and high-skilled workers, but also between workers with the same skill level.

More than half of the inequality reduction occurred between workers with the same skill level who worked in different firms.
To summarize

- Stronger reduction in South America
- Faster wage growth for low than high skilled workers
- More equal wages across firms (within skill groups)
Latin America’s reduction in wage inequality in the 2000s

Causes
1. Growth

- Pattern (not just level) of growth mattered

- Real exchange rate appreciation in South America caused by the commodity boom and other forces

- Contributed to the reduction in wage inequality within skill groups
Growth in South America fueled employment in both the tradable and nontradable sector.
Growth, through real exchange rate appreciation, led to more equal wages across firms

Two channels

• Expansion of the nontradable sector, where wages are more similar across firms

• Decline in export participation reduced wage dispersion across employers
2. Education

- It wasn't just growth
- Remarkable expansion of access to education
- More equal wages by skill
In 25 years, Latin America achieved close to full gross enrollment of girls in high school. Today the average education level of the labor force is 9 years, in 1990 it was 6 years.
Education ties together the reduction in inequality in low and high growth countries

Returns to education in Latin America and the Caribbean, 1993-2013

Difference in pay between less and more educated workers fell as bottlenecks in access were removed, but remains very high
3. Other forces

- Informality and minimum wage
- Played a secondary role
- Had a non-negligible impact, but only in some countries
The role of informality and minimum wage

Reduction in informality

- Equalizing in the 2000s in Argentina, Brazil, Mexico and Peru, but not in Chile and Uruguay

Rising Minimum wage

- Reduced inequality in Brazil, but only during the boom
- Not an important factor in Bolivia, Colombia, Mexico, Paraguay, Peru and Uruguay
To summarize

- Economic growth and better access to education were the primary drivers
- Other forces (informality and minimum wage) had a smaller role
Is the economic slowdown increasing wage inequality?
Slowed wage inequality reduction after the mid-2011 slowdown in growth
Because of the economic slowdown, further progress will require extra work.

Reduction in countries in South America now looks very similar to that of Mexico and Central America.
How to prepare for the future?
The future: How will wage inequality drivers evolve?

- Education expanding, fueling equalization
- New pattern of slower growth will slowdown wage inequality reduction
  - Two effects of real exchange rate adjustment
    - Higher demand in the tradable sector
    - New exporting opportunities
- Less space for minimum wage hikes
Towards growth with equity: A two-pillar approach

- **Don’t hinder productivity growth**
  - Remove policies that protect inefficient firms (e.g. corporate subsidies)
  - Reform antitrust and competition policies
  - Don’t fear technological change

- **Continue to expand the coverage and quality of education and training**
  - Improve public schools attended by the poor
  - Enhance quality (not just access)
  - Training
Link to the report:
https://openknowledge.worldbank.org/handle/10986/28682

Thank you!