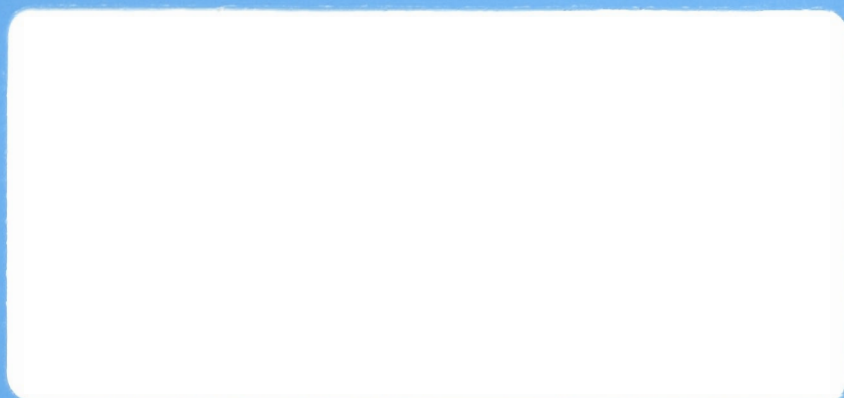




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THE DISTRIBUTIVE IMPACT OF
FISCAL AND LABOUR MARKET POLICIES:
CHILE'S 1990-1 REFORMS

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EXECUTIVE SUMMARY

The evolution of social policy-making in Chile can be divided into three major periods, each notable for a particular theoretical perspective and the manner in which policies were implemented.

The first period extended from 1920 to 1973. It was characterized by significant social development, including the promulgation of the first "social" laws on benefits and the introduction of a modern tax system. Two major problems stand out in the social policy approach of this period. First, there was no coherent long-term financing strategy for social programmes. Second, social policies were carried out primarily through social security programmes, the benefits of which were linked to formal sector incomes, thereby leaving informal sector workers and the poorest segments of the population without adequate social safety nets.

The second period, between 1973 and March 1990, was characterized by the introduction of an extreme version of the neo-liberal model which has dominated the Latin American scene over the last two decades. Such an approach featured in particular a heavy reliance on the principle of "subsidiariedad", by which the Government focused social initiatives only on those areas where the private sector had proved inadequate in providing social services. Also, as the state was thought to be very inefficient in performing redistributive functions, economic growth was viewed as the sole way for generating prosperity for all and for alleviating poverty.

Social assistance was therefore concentrated on those groups which were unable to satisfy their basic needs, while social services for the middle- and high-income groups had to be provided by these groups on their own. Social policy was bolstered also by a profound drop in Government expenditures, by a reduction in the size of Government and by the greater role assigned to the market in providing health care, housing and education services. This neo-liberal approach was taken to the extreme insofar as income transfers were limited almost exclusively to only the poorest of the poor. While the economic achievements of the military regime were appreciable, the shortcomings of cutting social spending became clear, especially in the aftermath of the economic crisis of 1982-3.

The third and final period - the main focus of this paper - covers the first two years of the Concertación Government. This period has been characterized both by a continuity with the previous economic policies and a new emphasis on the need for more social justice and equal opportunity. These goals have been undertaken through an open-market economic approach supplemented by a major effort at expanding social spending within an environment of sustainable economic growth and macroeconomic and budgetary stability. The possibility of achieving these goals all at once has been favoured by the important tax reform initiated in June 1990. This reform generated over \$800 million in resources for additional fiscal spending during 1990 and 1991. Moreover, during 1990 a labour market reform was undertaken in an effort to create more balance of relations between the power of management and that of workers.

Both these reforms have led to improvements in several social areas, including health care, housing, education and social security, as well as in labour and minimum wage policies.

Finally, the Concertación Government has been attempting to confront the problem of poverty in a serious and determined fashion. The importance assigned to macroeconomic and budgetary stability has permitted a significant effort to be undertaken in social spending without belt-tightening in economic growth or investment.

The evolution of social policy-making in Chile can be divided into three periods, each notable for a particular perspective, or lack thereof, and for the way the policies were implemented. The first and longest period lasted from 1920 to 1973. It was characterized by the increasingly important role of the state in the social sector in terms of redistribution and the satisfaction of basic needs.

The second period extended from October 1973 to February 1990. During this period the Government took a "laissez-faire" approach toward economic activity and the social sector, thereby introducing a drastic shift in the theory and practice of social policy.

During the third period, from early 1990 to today, the lessons of the other two periods have been used to formulate a global strategy aimed at overcoming poverty while achieving sustainable long-term development in a context of fiscal and monetary stability.

I. THE EVOLUTION OF GOVERNMENT SOCIAL POLICY, 1920-73

One-half Century of Social Development

Before 1973 no explicit theoretical approach was employed to deal with the problem of poverty. This created a certain amount of incoherence in social policies. Nonetheless, because of a clear policy orientation toward the realization of a more just society, social development progressed steadily during the period. Indeed, Chile became a pioneer in Latin America in the implementation of social policies and the search for greater equality of opportunity. The most important issues were already being considered in 1924.

Keen interest in the "social question" first emerged as a forceful nationwide reaction against the "export-led" development model. Although the opposition of the poorest groups to such a model had already found expression in the reformist movements of the 1920s, the Great Depression of the 1930s strengthened the trend because of the sharp drop in national income. The decline in exports and the heavy restrictions on imports induced structural changes in the productive sector in Chile, as in the rest of Latin America, that raised the significance of import substitution, thereby nurturing infant national industries.

The political and economic strategies which were adopted fostered the appearance of active and powerful labour organizations in the large mining centres, especially among low- and middle-income groups. Meanwhile, the middle class was benefiting from a newfound prominence in the democratic political scheme, the educational opportunities available to it

and the growth of professional, governmental, commercial and intellectual activities. A relatively small upper class, which accounted for most of the wealth of the nation, managed to maintain its position by making minor concessions.

In this context, social policies began to be implemented in the 1930s that aimed at alleviating the most acute social problems resulting from the world economic crisis. The economic model which was followed led to major changes in social structure and permitted the appearance of new pressure groups. These groups began to articulate a series of "social" demands that came to be widely supported in political circles. However, at that time, the available policy instruments were inadequate to cope with these demands.

Although some areas of the social sector were ignored in the development process, the expanding role acquired by social policies during subsequent decades was an important cause of the steady improvements registered in income distribution and welfare.

The role played by the Government in meeting the essential needs of the population centred on two main policy directions: the regulation of labour relations, working conditions and salaries and the satisfaction of basic needs in education, health care, nutrition, housing and social security.

In his analysis of this period Arellano (1985) identifies three key approaches to the social "question" during these years. Neither systematic nor institutionalized, the approach of the Conservative Party was expressed primarily through the charities of the Catholic Church and was undertaken in an effort to justify the party's position as an economically privileged group. The Radicals wanted the state to assume a protective role and provide the tools which would allow the weakest and most destitute to defend their rights. Finally, socialism and anarchism were the most important approaches among workers; both aimed at reducing or eliminating the economic power of management and establishing a just and egalitarian distribution of income.

Social Policy in Practice

The marked contrast among these approaches fuelled a debate over the proper institutional framework required to confront the social question. Thus, in 1917, the first Congreso de Beneficencia Pública (Public Welfare Congress) declared that it was the duty of the state to support the public institutions necessary to care for the aged, the sick and the poor. The contrast was also at the heart of a dispute between Radicals and Conservatives over the need

for compulsory primary education.

The political platform which brought Arturo Alessandri Palma to power (from 1920 to 1924) acknowledged clearly that working conditions had to be improved and workers protected because of their importance as an irreplaceable element in the economic health of the nation. Thus, the moment Alessandri was elected the way was open for a flurry of social legislation. A series of laws was presented in 1921 and finally passed by Congress in 1924. Employment contracts, trade unions, the right to strike and compensation for accidents at work were regulated. The Caja de Seguro Obligatorio (Mandatory Insurance Savings Bank), the Caja de Empleados Particulares (Private Employees Savings Bank), the Caja de Empleados Pública (Public Employees Savings Bank) and the Ministry of Hygiene, Social Assistance and Social Security were created. The general income tax and the personal income tax were introduced in 1924-5. In short, social initiatives were no longer viewed as works of charity but as matters of social justice. This notion prevailed during most of the following decades.

The sharp expansion in fiscal spending generated by the social legislation of the 1920s was halted abruptly by the Depression of the 1930s. The economy was badly damaged due to its dependence on the external sector; this bolstered import substitution, which was favoured by the Government.

The Labour Code became law in 1931. The law integrated existing legislation and new norms on minimum wages and the protection for workers. During the second Alessandri Government (1932-8) a law requiring automatic wage indexation (to compensate for price increases) was approved. In 1936 the Caja de Habitación Popular (Low-Cost Housing Savings Bank) was created using funds contributed by the Government and the Social Security Savings Bank.

Starting in 1938, preventive health care services were established for workers. These services were also made available to the dependants of industrial workers. The National Health Service was created in 1952. New groups of workers came to be integrated in the social security system, and fresh benefits were created, such as the family allowance, the unemployment benefit and the maternity leave benefit. The National Health Service and the new Social Security Service improved social assistance and service coverage substantially. In 1952 a pension system for non-public-sector employees was also instituted; the system covered the aged and the disabled and provided life insurance benefits to the families of deceased employees.

Primary education became compulsory in 1920. The share of the population receiving primary education rose significantly as a result. This led eventually to growing enrolments at other levels of education, particularly postprimary levels. The Junta Nacional de Auxilio Escolar y Becas (JUNAEB, the National Council for Scholarships and Student Financial Assistance) was established in 1953 to help the poorest families meet the incidental costs, including the costs of school meals, of the education of their children.

These measures led to a jump in Government spending. The fiscal expenditure on such social programmes tripled between 1930 and 1955. In order of importance, social security, health care and housing accounted for the largest increases. Spending on education also rose rapidly. Although the majority of the gains in education reached the population at large, the benefits offered to trade unions and other worker organizations were gradually expanded. This eventually translated into a complex set of laws and a very unequal structure of benefits. Thus, some small groups came to be particularly favoured by social spending.

After the Radical Party came to power (1938-52), the Government's role shifted from "protector" to "direct benefactor". This created additional complications mainly since each new benefit had to be financed on an ad hoc basis, thus leading to alterations in the established structure of contracts, other distortions and (unexpected) indirect effects. Because of such problems, severe anti-inflationary measures had to be taken in the mid-1950s to put a brake on the rising expenditure on benefits. From then until 1964 the growth rate of social spending slowed, although it was still higher than the GDP growth rate.

Beginning in 1964, the new Christian Democrat Government considered improvements in income distribution a key goal of economic policy. Once again benefits were expanded. However, segments of the population which had previously been ignored, such as marginalized city dwellers and poor farmers and agricultural labourers, were now targeted. These policies played a major part in the doubling of public expenditure to 20 percent of GDP between 1964 and 1970. Land reform was also undertaken. Fifteen percent of the country's agricultural land was expropriated for this purpose. Farm labourers and poorer urban groups were encouraged to become organized.

Overall, however, the tendency evident in previous decades to favour an increase in the benefits available to urban workers and middle-income groups was maintained. Several attempts to render the distribution of benefits more equitable failed. Thus, for example, Congress in 1965 rejected a proposal of the Administration to peg the family allowance at a fixed level. Meanwhile, as more segments of the population were brought into the system,

Government social expenditure swelled. These trends became even more apparent under the Popular Unity Government of 1970-3.

Two problems stand out in the social policy approach prior to 1973. First, there was no coherent long-term financing strategy to assure that the various programmes could be sustained. Instead, the benefits offered by the state were constantly fluctuating, and the "social effort" was hostage to macroeconomic disequilibriums as periods of economic boom were followed by severe fiscal adjustment. Thus, the goal of an equitable redistribution of income could be reached only partially. Especially the poor suffered from this situation.

Second, social policies were carried out primarily through social security programmes, the benefits of which were linked to formal sector incomes. Here again, the poor, particularly the urban poor who had no regular wages, were at a special disadvantage. Moreover, the Government was inclined to concentrate on its power base among the lower-middle and middle classes rather than on those most in need.

Summary

During the period 1920-73 successive Governments became more and more involved in the social sector, chiefly in the satisfaction of basic needs. An institutional framework gradually emerged to implement programmes and services in health care, education, housing and social security. On the principle that it should safeguard the common good, the state played a key role in expanding these social programmes and services to cover an ever greater portion of the population. Chile thereby became a pioneer in Latin America in the social sector and achieved a relatively high level of social development (Table 1).

However, in the mid-1950s the steady increase in Government social expenditure to satisfy mounting needs, together with a lack of appropriate instruments to generate the necessary fiscal resources, began to erode the effectiveness of social policies. Periodic macroeconomic crises were followed by growing fiscal debt and inflation. As a result of the wideranging economic adjustments which frequently had to be undertaken, the quality of Government investment in the social sector dropped.

Table 1: SELECTED INDICATORS OF SOCIAL DEVELOPMENT
(1920-90)

Year	Government Social Spending		Coverage of Primary Education ^a	Illiteracy Rate ^b	Infant Mortality Rate ^c	Professionally Assisted Childbirths ^d	Coverage of Potable Water Supply		Sewer Coverage
	% of GDP	% of Total Government Spending					Urban	Rural	
1920	1.0	6.6	—	36.7	—	—	—	—	—
1925	2.1	12.1	—	—	—	—	—	—	—
1930	2.7	18.1	—	25.3	—	—	—	—	—
1935	2.8	23.5	56.7	—	—	—	—	—	—
1940	—	—	60.6	27.1	192.8	—	—	—	—
1945	4.4	28.1	59.7	—	164.5	—	—	—	—
1950	—	—	66.0	19.8 ^e	136.2	—	—	—	—
1955	6.0	31.7	71.1	—	116.5	57.8	—	—	—
1960	8.6	39.6	80.2	16.4	120.3	66.9	—	9.5	—
1965	10.0	45.2	93.2	—	95.4	74.3	53.5	12.2	25.4
1970	10.5	42.5	96.5	11.0	79.3	81.1	66.5	34.2	31.1
1975	10.3	36.0	105.3	—	55.4	87.4	77.4	34.8	43.5
1980	10.3	37.1	103.5	8.9 ^f	31.8	91.4	91.4	44.2	67.4
1985 ^g	15.1	57.0	—	—	19.5	97.4	95.2	69.3	75.1
1990	10.7	65.2	—	—	17.1 ^h	98.8 ^h	98.0 ^h	75.0 ^h	80.8 ^h

Sources: Arellano (1985), PIIE (1984), BCCH (1990), MOH (1990) and calculations of the author based on unpublished data of DIPRES, the Budget Directorate of the Ministry of Finance.

^a In percentages. The calculations count pupils who repeat classes; some figures may therefore reach above 100 percent.

^b In percentages. Only persons 15 years of age or older are considered.

^c Per 1,000 live births.

^d In percentages of all childbirths.

^e Data for 1952.

^f Data for 1982.

^g The higher figures in 1985 relative to those for surrounding years were due to the serious economic recession of 1982-3 that led to a more substantial effort in the social sector, as well as to a nearly 15 percent drop in GDP during the recession.

^h Data for 1989.

II. SOCIAL POLICY UNDER THE MILITARY REGIME, 1973-90

Reducing the Scope of the Government's Intervention

According to the neo-liberal model adopted by the authoritarian Government between 1973 and 1989, the state is very inefficient in performing redistributive functions. As growth was viewed as the sole means to achieve prosperity for all and to alleviate poverty, the state came to play only a minor role in fostering the conditions for more equality in opportunity.

Social policy-making during this period focused on the elimination of *extreme* poverty. The state was no longer a "direct benefactor", the universal provider of services and benefits.

Instead, Government social policies were concentrated on those groups which were unable to satisfy their basic needs. Social services for the middle- and high-income groups now had to be provided by these groups on their own. Henceforward, the distribution of social subsidies was to be based on extreme need.

The theoretical approach of the military regime to the social sector relied on the principle of "subsidiariedad", according to which the state was to act only to protect individual freedoms, assure the respect of contracts and equal opportunity and assume responsibility solely for the production of pure "public goods" and for those functions which could not be carried out in an adequate way by individuals or private organizations. Given this "enabling framework", economic growth would by itself lead to a reduction of poverty.

Individual freedom was understood mainly as the power to choose goods and services in the marketplace, including basic social goods and services. "Equal opportunity" in this context was seen as the absence of interference or discrimination on the part of the public authorities in the free play of market forces. Rigidities and distortions in the social structure and the operation of market forces could be easily removed through direct Government subsidies designed to meet the basic needs of vulnerable groups. All other determinants of poverty would then be offset automatically once people reached certain critical minimum levels of well-being in terms of health care, education and housing. Any remaining inequalities would be merely the result of the differing propensity of individuals to save, or their differing natural abilities.

The Neo-liberal Model in Practice

The implementation of the neo-liberal model generated profound economic changes, including a sharp reduction in public spending that had a significant impact on social spending. The drop in Government expenditures was due to both short- and long-run goals. On the one hand, the aggressive anti-inflationary policy of the first years of this period dictated a fall in Government spending. On the other, the private sector became an essential actor in the long-term development strategy, and this required a decline in the size of Government. Moreover, by the mid-1970s the country was suffering from the world economic crisis; this created an intense domestic recession and imposed restrictions on spending. Likewise, the economic and financial crisis generated in Chile in 1982-3 by the serious world

recession of these years forced severe cuts in the level of public spending, along with substantial shifts among the various expenditure items.

Since economic growth was considered the only valid way to eliminate poverty effectively, interventions aimed at the redistribution of income were discarded. The fact that social policy was focused on specific groups whose extreme poverty could not be overcome solely through economic growth meant that objective criteria had to be established for the targeting of benefits. These criteria and the related institutional mechanisms had to be gradually fine-tuned.

The most important tool in the effort to target direct subsidies to alleviate extreme poverty was the "ficha de estratificación social" ("social classification card"), which was used at the municipal level. However, this method involved problems which made it impossible to identify extreme cases of poverty at particular moments. Originally, only access to housing and sanitation were considered in the classification of families. The method was subsequently altered to include other determinants of poverty.

The Two Pillars of Social Policy

The efforts of the Government to alleviate the most acute cases of poverty centred on the distribution of direct subsidies to the "deserving" poor and the eradication of any "leakage" of benefits to groups for which they were not intended. The direct intervention through assistance and non-assistance programmes financed by the public sector and decentralized institutions formed one of the two pillars of the "social safety net". The other pillar was the more active participation of the private sector in the provision of basic social services in education, health care and housing.

1. Two main types of "subsidies" to very poor families can be differentiated: social assistance benefits designed to help those in greatest need and those subsidies and social services offered on a more permanent basis. The family allowance, the "subsídio único familiar" (SUF, the "'unique' family subsidy") and the social assistance pension (PASIS, the *pensión asistencial*) were especially important among the first type.

Established in the 1950s, the family allowance programme provided a monthly sum for each non-working member of the families of poor workers in the formal sector. The amount of the benefit was independent of the income level of the family and was thus

neutral or even slightly regressive in terms of income redistribution since only the families of workers in the formal sector were eligible.

The SUF (unique family subsidy) was first provided in 1981. It was furnished for under-15-year-olds who did not benefit from the family allowance. (Initially, the subsidy was offered only for under-6-year-olds.)

Created in 1975, the PASIS "social assistance" pension was designed as a social security benefit for those over 65, or the handicapped under 18, who lacked resources and were not eligible for other benefits.

The National Supplementary Food Programme (PNAC) and the School Meal Programme (PAE) were also part of the social safety net. Instituted in 1954, the former aimed to assure that all pregnant women and small children received proper nutrition. Originally universal, the programme gradually became more directly focused on children in poor medical condition. It thus lost its preventive nature and became more curative in character (Vergara 1990).

Established in 1964, the School Meal Programme offered free meals at schools for poor pupils between the ages of 6 and 14. As in the case of other similar programmes, the targeted population gradually changed, and by the end of the 1970s the focus was the extremely poor and undernourished.

Apart from these income transfers, the social policy also involved public expenditures in more traditional initiatives in health care, housing and education. These initiatives were typically designed to generate human capital through social investment, as well as to enhance access to opportunities.

2. Seen as the only truly efficient resource allocators, **the private sector and the market** played a particularly vital role in providing health care, housing and education services.

In *education* the role of market forces was emphasized through the decentralization to the municipal level of the management of primary and secondary schools. At universities tuitions were raised and low-interest student loans were created. On the theory that competition among educational institutions would lead to systemwide improvements, a competitive mechanism for the allocation of public funds was established. The role of private schools was also enlarged.

The attempts to hand *health care services* over to the private sector were numerous, but the reforms which were eventually introduced were less significant than those originally proposed. A mechanism was established by which the allocation of resources to the various

health care entities was directly related to the quantity of services provided. Through the ISAPRES (Instituciones de Salud Previsional) scheme, which was created to offer the private sector a greater role, wage earners were allowed to use their mandatory contributions to the health care system to acquire health insurance through private companies.

The reforms undertaken to open *the social security system* to market forces were wideranging. The Administradoras de Fondos de Pensiones (Pension Fund Administration) was instituted in 1981 as part of the privatization of social security funds. This reform involved a shift from a fairly solidaristic pay-as-you-go system to one in which pension benefits were calculated strictly according to personal contributions.

In *the housing sector* the subsidy system was altered to assign a greater role to capital markets as a financing mechanism and to the real estate industry in general. A series of regulations governing urban real estate markets was also eliminated.

The application of excessively liberal *labour policies* led to the loss by workers of some benefits and guarantees they had acquired under previous administrations. Authoritarian rule and the passage of laws designed to restrict the bargaining power of workers generated a climate of instability and insecurity in the labour movement. Meanwhile, the power of employers was increased so much that it became a real obstacle in negotiations with labour and hindered trade union activities. For example, a new labour law was promulgated in 1981 in order to enhance wage flexibility. This further eroded the bargaining power of workers by limiting the right to strike and permitting employers to lay off practically at will.

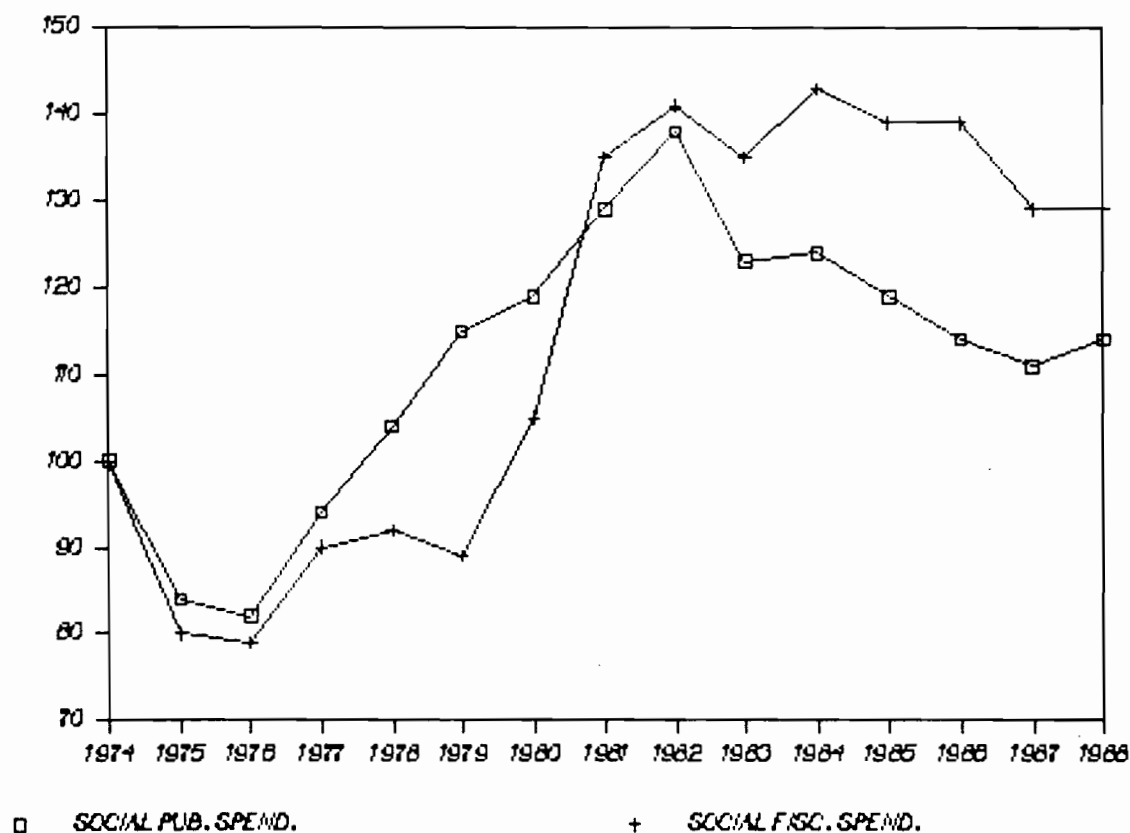
Government Social Expenditure

1. **The Level of Spending.** Two different concepts of Government social expenditure can be considered, i.e. "public" social spending and "fiscal" social spending. While the former covers all Government expenditure related to social initiatives, including all administrative costs associated with the provision of social services, the latter represents those social resources actually received by the population and is therefore a more accurate measure of the real social assistance furnished by the state. Although one might expect both types of spending to behave in a similar fashion over time, the structural reforms of the 1973-89 period altered their relationship. Thus, an initial drop can be observed during the period in both types of social spending (Figure 1). This decline coincided with the implementation of anti-inflationary adjustment measures. During the subsequent recovery both types of

spending rose, so that the cumulative growth for both reached 40 percent between 1974 and 1982. After 1982 "public" social spending fell once more, while "fiscal" social spending was more erratic.

A sectoral analysis of social expenditure reveals that the evolution of total "fiscal" social spending depended chiefly on expenditures on social security, including pensions and social assistance (Table 2, Figures 2 and 3). Greater levels of social spending occurred precisely in those years when there was a downturn in economic activity. Indeed, the greater spending was due mainly to the increased expenditure on income transfers. It therefore appears that social expenditure during those years was aimed especially at compensating for the income losses deriving from the drop in the level of economic activity and was thus used principally for assistance purposes.

Figure 1: INDEX OF PER CAPITA GOVERNMENT SOCIAL EXPENDITURE
(1974-88, 1974 = 100)



Sources: Ffrench-Davis and Raczynski (1990), BCCH (1990).

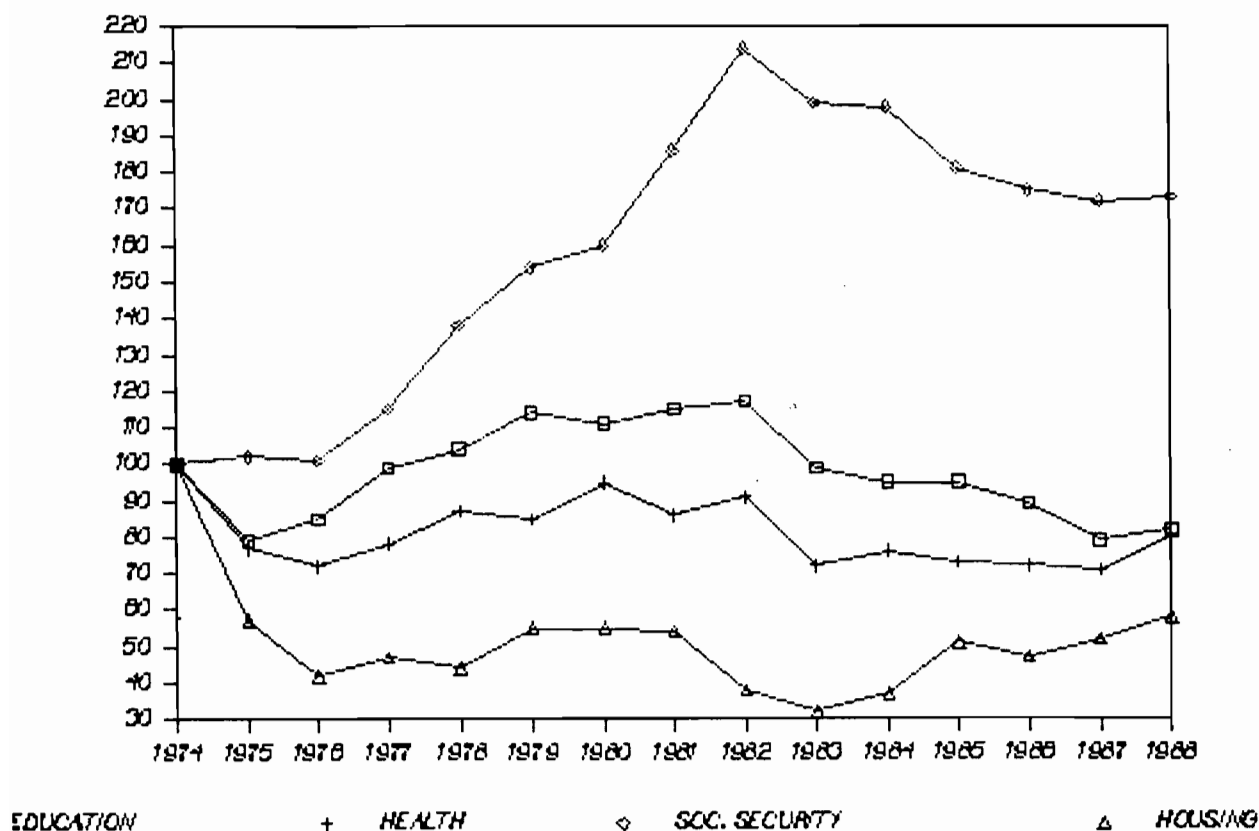
Table 2: INDEX OF PER CAPITA GOVERNMENT SOCIAL SPENDING BY ITEM
(1975-88, 1974 = 100)

Year	Education	Health Care	Social Security	Housing	Other	Total
Panel A: "Public" Social Spending*						
1975	79	77	102	57	31	84
1976	85	72	101	42	80	82
1977	99	78	115	47	158	94
1978	104	87	138	44	135	104
1979	114	85	154	55	164	115
1980	111	95	160	55	166	119
1981	115	86	186	54	137	129
1982	117	91	214	38	106	138
1983	99	72	199	32	162	123
1984	95	76	198	37	142	124
1985	95	73	181	51	136	119
1986	89	72	175	47	142	114
1987	79	71	172	52	138	111
1988	82	80	173	58	144	114
Panel B: "Fiscal" Social Spending*						
1975	74	71	119	40	109	80
1976	74	59	121	35	171	79
1977	88	67	139	37	144	90
1978	88	68	154	28	139	92
1979	90	64	142	31	130	89
1980	94	81	186	34	128	105
1981	111	84	282	32	136	135
1982	111	78	329	11	63	141
1983	94	63	336	21	48	135
1984	95	62	364	33	37	143
1985	91	54	358	36	20	139
1986	90	50	361	36	57	139
1987	81	48	325	42	85	129
1988	75	49	320	58	99	129

Sources: Ffrench-Davis and Raczyński (1990), BCCH (1990).

* "Public social spending" covers all Government expenditure related to social initiatives, including all administrative costs associated with the provision of social services. "Fiscal social spending" covers those social resources actually received by the population.

Figure 2: INDEX OF PER CAPITA GOVERNMENT "PUBLIC" SOCIAL EXPENDITURE
(1974-88, 1974 = 100)



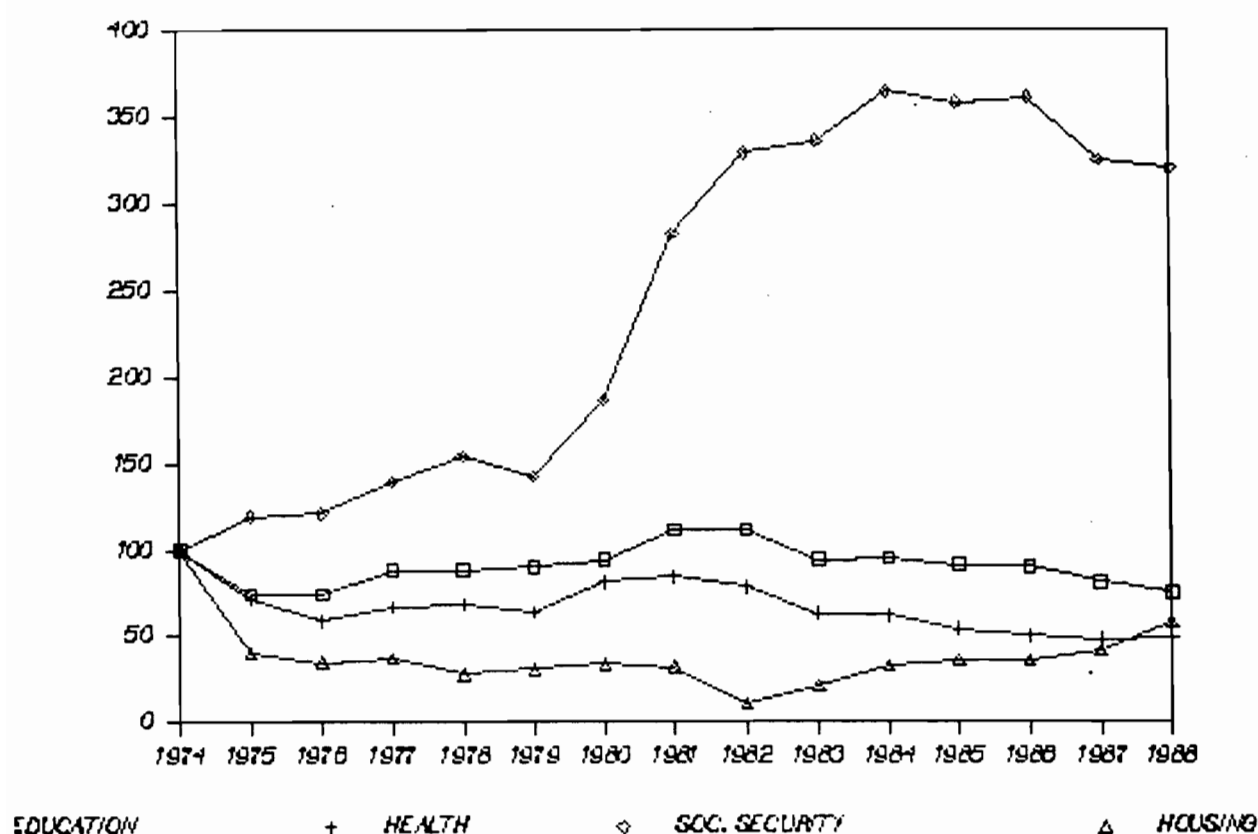
Sources: Ffrench-Davis and Raczynski (1990), BCCH (1990).

2. The greater recourse to **targeting** during this period fostered concrete improvements in the development of the necessary mechanisms to measure objectively the efficiency of social spending. The development of these mechanisms, along with the establishment of the social safety net, assured that most monetary subsidies, as well as some of the non-monetary benefits, reached those sectors of the population that needed them most. Tools such as the social classification card (see earlier) were essential in the effort to direct fiscal resources toward the appropriate segments of the population and thereby offset somewhat the impact on poor families of economic reforms.

Although the number of people receiving benefits fell after 1973, the effectiveness of social policy measures grew insofar as the most vulnerable were being reached. However, the criteria were applied in such a narrow manner that only those identified as being in

extreme need were eligible for the benefits. Moreover, several social programmes suffered as a result of the harshness of the fiscal adjustment measures implemented following the recession of 1982-3. Because their value was set in nominal terms, the purchasing power of many cash subsidies fell. Likewise, many people who still needed Government social assistance lost their eligibility due to the strict nature of the benefit requirements.

Figure 3: INDEX OF PER CAPITA GOVERNMENT "FISCAL" SOCIAL EXPENDITURE
(1974-88, 1974 = 100)



Sources: Ffrench-Davis and Raczyński (1990), BCCH (1990).

A study (Haindl, Budinich and Irrázabal 1989) based on the CASEN survey (ODEPLAN 1987) has shown that, while the distribution of the benefits resulting from public expenditure on health care programmes may be considered to have been appropriate and that of the benefits resulting from public expenditure on housing programmes was relatively

balanced (at least among the poorer half of the population), the distribution of the benefits resulting from public expenditure on education was somewhat skewed toward the upper income deciles (Table 3). However, because the available data do not reflect the fact that some of the public expenditure on higher education is used for research, the "skewedness" of the distribution may have been less marked than appears.

Table 3: THE DISTRIBUTION OF SELECTED GOVERNMENT SOCIAL ASSISTANCE EXPENDITURES*
(In Percentages By Decile, 1987)

Population Decile	Education	Health Care	Housing
1	12.99	22.76	13.51
2	13.24	17.06	10.58
3	10.52	15.59	12.51
4	9.06	11.41	11.68
5	9.16	10.00	10.31
6	8.38	6.97	9.48
7	7.79	5.84	10.00
8	10.43	4.47	9.58
9	11.32	3.95	6.77
10	7.12	1.96	5.58

Source: Haindl, Budinich and Irarrázabal (1989).

* The columns may not sum to 100 percent due to rounding. "1" is the poorest population decile, and "10" is the wealthiest.

The targeting of public social spending was generally enhanced during this period. However, the improvements in the efficiency in public spending due to the better targeting were not enough to offset the effects of the overall decline in public social expenditure. Moreover, the emphasis on the market and the application of the principle of "subsidiariedad" for Government initiatives in areas in which it should not have been applied ended by impairing some social services. The reduced flow of fiscal resources led in many cases to a drop in the quantity and quality of services below optimum levels, and in some extreme cases services could no longer be provided to important segments of the population.

The Impact of the Economic and Social Policy Changes

Primary income distribution (that is, before redistribution through taxation and social expenditure), as well as total per capita Government spending in traditional social sectors, deteriorated during this period (Table 4; see also Table 2, page 12). The adjustments and internal shocks at the beginning of the period, together with the world economic crises of 1975-6 and 1982-3, forced cuts in expenditures on health care, education and housing. Public spending in health care and education dropped from around 45 percent to only 30 percent of total public social spending between 1980 and 1989. Along with a slump in real wages and higher average unemployment rates, this implied a serious erosion in the standard of living of low- and middle-income groups, which lost many of the benefits they had acquired, especially through their participation in the labour force.

Table 4: PRIMARY INCOME DISTRIBUTION AMONG FAMILIES^a
(In Percentages, 1978, 1985 And 1988)

Population Decile ^b	1978	1985	1988
1	0.91	1.06	1.15
2	2.24	2.16	1.99
3	3.22	3.01	2.70
4	4.17	3.91	3.46
5	5.21	4.93	4.34
6	6.59	6.28	5.42
7	8.38	8.13	6.95
8	11.11	10.98	9.82
9	16.46	16.66	14.37
10	41.68	42.88	49.77
Gini coefficient ^c	0.4803	0.4896	0.5387

Source: IDB (1991).

^a Based on absolute values in constant 1988 pesos and per capita terms. Columns may not sum to 100 percent due to rounding.

^b "1" is the poorest population decile, and "10" the wealthiest.

^c The Gini coefficient is a measure of dispersion that varies between 0 and 1. A value of 0 would indicate a perfectly egalitarian distribution, while a value of 1 would indicate that all incomes accrue only to one person.

1. Public expenditure on **education** declined from about 4.3 percent to 2.7 percent of GDP between 1970 and 1988. Moreover, the municipal administration of educational institutions was facing serious problems, particularly in the poorest areas, due to the growth in enrolments in private subsidized schools and the consequent reductions in enrolments and Government financial support at municipal establishments. The quality of education also deteriorated, and teacher salaries lost ground in real terms. Although it had been expected to contribute to efficiency, the decentralization in school administration was generating an overall bias against the poorest communities, which were unable to supplement the scarce resources coming from the Government.

Meanwhile, the number of breakfasts and dinners provided to pupils through the School Meal Programme dropped from 1.4 million to 480,000 and the number of lunches from 674,300 to 497,500 between 1973 and 1988.

Although the coverage of the education system at the preschool level rose from 6.1 percent to 21.3 percent between 1973 and 1989, the coverage of primary education suffered a downturn. Thus, over 200,000 children between 6 and 13 years of age remained outside the school system in 1987. Of these children, who represented 10.7 percent of the age group, 49.8 percent came from the poorest 30 percent of households. While the coverage of the primary school system overall was 90 percent, the year-end scores of pupils in low-income schools, as measured through the SIMCE (System of Measurement of the Quality of Education) tests, were about 50 percent lower than those of pupils in wealthier schools (ODEPLAN 1987).

Substantial problems of quality and orientation were also experienced in secondary education. Students leaving secondary schools were all too often poorly prepared to enter the labour market or university. Whereas secondary school enrolments increased appreciably, the CASEN survey (ODEPLAN 1987) found that 53.9 percent of those young people who had not been brought into the secondary system belonged to the poorest 30 percent of the population.

At the same time, technical schools faced serious infrastructural problems and lacked modern equipment, which meant that the system was unable to respond to the country's needs in terms of well-trained manpower.

In higher education the process of restructuring that was undertaken in 1973 actually undermined the standing of the universities. Along with the constant cuts in Government financial support, this caused a decline in university enrolments among 20-to-24-year-olds between 1973 and 1989. Nonetheless, new professional institutes helped fill the gap, and total

enrolments among this age group in all types of educational establishments grew between 1973 and 1989.

The number of adults enrolled in special education courses decreased from 148,410 in 1980 to only 72,974 in 1988. There were two causes for this downturn: the curriculums and course programmes had not been adapted to the requirements of the population, and the municipal education system allocated funds per student that were only about one-fifth to one-third of the corresponding funds allocated for other forms of education, creating a bias against teachers in adult education programmes.

2. **The housing sector** was strongly affected by the economic crises of the mid-1970s and early 1980s. The slash in Government expenditures in this sector, together with structural changes in the way policies were implemented, created a growing housing shortage. By the end of 1989 around 800,000 families were estimated to be without a home, and the number of homes without basic sanitation or of substandard quality had reached 300,000.

While annual public sector investment in housing had stood at an average 2.6 percent of GDP during 1953-73, it fell to under 2 percent on average in 1974-89, when it even went below 1 percent of GDP in some years.

3. As Government spending on **health care** diminished, structural and operational deficiencies began to emerge. The creation of ISAPRES, the privatized health insurance scheme (see earlier), generated problems of equity in health insurance coverage. Although a redistribution of resources within the health care system was undertaken to compensate for some of these problems, it appears not to have been sufficient, and the flight of people with higher incomes (and paying higher contributions) from the system led to a financing crisis.

There were two major consequences of this situation. First, since the health care system was essentially being financed by middle-income groups, cross-subsidies were necessary to support the access of those at lower incomes. Second, only about 20 percent of the population could afford to participate in the ISAPRES plan, which relied heavily on more advanced medical technologies. Thus, the scheme in no way helped to offset the deficiencies of the overall health care network.

Especially during the years following the economic crises of 1975-6 and 1982-3 public spending on health care contracted sharply. Thus, in real terms the amount spent in 1987 was 8 percent lower than that spent in 1974 and 23 percent lower than that spent in 1982. Despite a recovery after 1987, expenditure did not regain the 1982 levels, although GDP was 49

percent higher in 1989 than it had been in 1982. Likewise, the expenditure per beneficiary fell by 13 percent between 1974 and 1987.

The financing structure of the health care system changed significantly during the period. Between 1974 and 1987 the contribution per beneficiary fell by 38 percent. This was partially overcome by an increase in the mandatory contribution rate from 4 percent to 6 percent in December 1982 and to 7 percent in December 1985. Between 1974 and 1987 the share of social security contributions in the income of the sector grew from 14.5 percent to 45 percent.

The overall drop in the financial resources available for the health care system eroded service quality, damaged infrastructure and maintenance and reduced the scope for hiring and retraining personnel. Moreover, the number of those who could be served decreased. The lower-income groups suffered the most from these changes.

Poverty, Unemployment and Income Distribution

Under the military regime poverty levels rose and income became even more concentrated among the higher socioeconomic strata (see Table 4, page 16). By 1987 households considered poor accounted for over 38 percent of all households in the country (ECLAC 1990). Likewise, between 1978 and 1987 the real level of consumption of households belonging to the highest income quintile increased, while that of the other four quintiles fell (INE 1978a, 1988). Even in 1990, 34.5 percent of all households were living in poverty.

One of the major reasons for this rise in poverty was the jump in unemployment generated by structural reforms and stabilization programmes. During the 1974-83 period average annual levels of unemployment reached 14.3 percent, while rates had previously been closer to 6 percent (Mujica and Larrañaga 1992). The surge in unemployment led to a significant use of resources on special counter-cyclical employment programmes such as the Occupational Programme for Heads-of-Household (POJH) and the Minimum Employment Programme (PEM). These programmes reached a peak in 1983 (Table 5).

Another cause of the growth in poverty was the fact that changes in real wages were severely affected by stabilization programmes and shifts in the economy. Thus, the strongly deflationary policies introduced between 1973 and 1976 for stabilizing inflation generated a major drop in real wages between 1973 and 1976. Although wages subsequently began to rise again, they fell once more, by 13 percent, during the 1982-7 period as a result of the economic

Table 5: MEMBERSHIP IN THE PEM AND POJH EMPLOYMENT PROGRAMMES
(December 1979-June 1989)

Date	PEM ^a		POJH ^b	
	Total Members	% Change	Total Members	% Change
December 1979	161,476	--	--	--
June 1980	187,867	16.3	--	--
December 1980	203,141	8.1	--	--
June 1981	171,186	-15.7	--	--
December 1981	168,149	-1.8	--	--
June 1982	190,161	13.1	--	--
December 1982	336,469	76.9	102,772	--
June 1983	391,564	16.4	137,792	34.1
December 1983	263,763	-32.6	221,944	61.1
June 1984	152,695	-42.1	139,448	-37.2
December 1984	170,915	11.9	207,639	48.9
June 1985	143,066	-16.3	190,219	-8.4
December 1985	105,646	-26.2	171,360	-9.9
June 1986	84,486	-20.0	142,939	-16.6
December 1986	61,410	-27.3	122,812	-14.1
June 1987	36,169	-41.1	85,623	-30.3
December 1987	22,245	-38.5	64,201	-25.0
June 1988	8,344	-62.5	23,087	-64.0
December 1988	3,521	-57.8	5,345	-76.8
June 1989	--	-100.0	--	-100.0

Sources: BCCH (1990), *Boletín Mensual* (various).

^a The Minimum Employment Programme.

^b The Occupational Programme for Heads-of-Household was first undertaken in 1982.

adjustment programme implemented following the 1982-3 crisis. The decline in the minimum wage and in the wages of the less qualified informal sector workers was much higher than that for average wages (Mujica and Larrañaga 1992).

A comparison of data for 1978, 1985 and 1988 reveals that, while the second through ninth income deciles of all families experienced a decrease in their share in national income,

the share of the poorest decile rose slightly, presumably because of the effect of the more efficient targeting of social spending. Nonetheless, the share of the wealthiest income decile soared (see Table 4, page 16). Indeed, the Gini coefficient climbed from 0.4803 in 1978 to 0.5387 in 1988.

Moreover, the increase in income concentration was not as pronounced between 1978 and 1985 as it was between 1985 and 1988, when the share in national income of the wealthiest decile exhibited its most substantial expansion. During the first period the increase in income inequality may have been due to a deterioration in primary income distribution because of the financial and economic crisis of 1982-3, while during the second period it may have been due to the adjustments following the crisis and the resulting cuts in social spending starting in 1984.

Likewise, the share in overall consumption of the four less well-off quintiles of all households fell between 1978 and 1988 (Table 6). Moreover, the household spending on various major items of consumption shifted as well. Thus, while the spending on food shrank in relative importance, that on education, health care and housing rose, probably as a result of Government expenditure support in these areas.

Table 6: OVERALL HOUSEHOLD SPENDING BY INCOME QUINTILE
(In Percentages, 1978 And 1988)

Income Quintile	1978	1988
1. Low	5.2	4.4
2. Low to middle	9.3	8.2
3. Middle	13.6	12.6
4. Middle to high	21.0	20.0
5. High	51.0	54.9

Source: INE (1978a), (1988).

Summary

The development model followed by the military regime from 1973 to 1989 relied on market forces and the individual consumer to boost the economic and social development of the

country. The role of society at large in decision-making and in the direct provision of social services was considerably reduced. Social policy was understood merely as a tool to counteract the negative effects of economic crisis or social problems, but not as an instrument of social development.

The Government attempted to adhere to the principle of "subsidiariedad" by focusing social initiatives only on those areas where its neo-liberal approach proved inadequate to enhance social progress. The neo-liberal approach was taken to the extreme insofar as Government social assistance was limited almost exclusively to only the poorest of the poor. This meant that a large portion of low- and middle-income families lost the benefits which they had acquired during the previous period. This approach represented an important break from the ideals which had motivated social policies since the 1920s.

While the economic achievements of the military regime were appreciable (Tables 7-9), the shortcomings of the policy of cutting Government social spending eventually became clear, especially in the aftermath of the economic crisis of 1982-3. Although steps were taken to alleviate the problems, they were insufficient to offset the damage to the social service system, which had lost the capacity to respond to the growing needs of the population.

Table 7: GOVERNMENT EXPENDITURE AND REVENUE
(In Percentages Of GDP, 1970-88)

	1970	1980	1985	1986	1987	1988
Expenditure	26.4	23.1	32.5	30.0	28.3	30.7
Debt payments	3.5	2.7	6.5	4.3	4.3	7.2
Other	22.9	20.4	26.0	25.7	24.0	23.5
Revenue	23.7	26.2	26.2	27.2	28.2	29.0
Direct taxes	4.8	6.2	4.2	4.1	3.7	3.0
Indirect taxes	10.6	14.3	19.4	19.8	20.2	18.3
Nontax income	1.1	1.9	1.4	2.0	2.7	3.7
Copper income	4.8	3.8	1.2	1.3	1.6	4.0
Other	2.4	--	--	--	--	--
Surplus/Deficit	2.7	-3.1	6.3	2.8	0.1	1.7

Sources: BCCH (1990), *Boletín Mensual* (various).

Table 8: GDP AND THE BALANCE OF PAYMENTS
(1975-91)

Year	GDP			Balance of Payments (\$, millions)					
				Current Account		Capital Account		Errors and Omissions	Total
	In Millions of Constant 1977 Pesos	Growth Rate (%)	Inflation Rate (%)	Balance	Merchandise Exports (f.o.b.)	Merchandise Imports (f.o.b.)	Capital	Reserves	Balance
1975	253,043	-	340.7	-491	1,590	1,520	373	211	584
1976	261,945	3.5	174.3	148	2,116	1,473	66	-281	-215
1977	287,770	9.9	63.5	-551	2,185	2,151	577	-118	459
1978	311,417	8.2	30.3	-1,088	2,460	2,886	1,946	-712	1,234
1979	337,207	8.3	38.9	-1,189	3,835	4,190	2,247	-1,047	1,200
1980	363,446	7.8	31.2	-1,971	4,705	5,469	3,165	-1,244	1,921
1981	383,551	5.5	9.5	-4,733	3,836	6,513	4,698	-67	4,631
1982	329,523	-14.1	20.7	-2,304	3,706	3,643	1,215	1,165	2,380
1983	327,180	-0.7	23.1	-1,117	3,831	2,845	508	541	1,049
1984	347,926	6.3	23.0	-2,111	3,651	3,288	1,940	-17	1,923
1985	356,447	2.4	26.4	-1,329	3,804	2,955	1,384	99	1,483
1986	376,627	5.7	17.4	-1,137	4,199	3,099	741	228	969
1987	398,230	5.7	21.5	-808	5,223	3,994	944	-45	899
1988	427,530	7.4	12.7	-167	7,052	4,833	1,009	-732	277
1989	470,243	10.0	21.4	-767	8,080	6,502	1,278	-437	841
1990	480,323	2.1	27.3	-824	8,310	7,037	3,356	-2,368	988
1991	509,153	6.0	18.7	93	8,929	7,353	860	-1,238	-378

Sources: BCCH (1990), *Boletín Mensual* (various).

Table 9: TRANSFERS AND EXTERNAL DEBT
(In Millions Of Dollars, 1975-91)

Year	Balance of Trade	Unilateral Transfers	External Debt		
			Public	Private	Total
1975	70	10	3,597	670	4,267
1976	643	28	3,475	799	4,274
1977	34	75	3,520	990	4,510
1978	-426	70	4,353	1,570	5,923
1979	-355	80	4,771	2,736	7,507
1980	-764	113	4,720	4,693	9,413
1981	-2,677	108	4,415	8,138	12,553
1982	63	109	5,157	8,658	13,815
1983	986	97	8,090	6,742	14,832
1984	363	107	10,601	6,362	16,963
1985	849	147	12,515	5,135	17,650
1986	1,100	85	14,379	3,435	17,814
1987	1,229	126	14,725	2,466	17,191
1988	2,219	177	13,091	2,361	15,452
1989	1,578	215	10,131	3,148	13,279
1990	1,273	199	9,808	4,234	14,043
1991	1,576	232	9,489	4,705	14,194

Sources: BCCH (1990), *Boletín Mensual* (various).

III. THE SOCIAL POLICIES OF THE "CONCERTACION" GOVERNMENT

The New Principles of Policy-making

The Government of the Concertación de los Partidos por la Democracia, an alliance of 17 parties under Patricio Aylwin Azócar that came to power in early 1990 following elections the previous December, has sought to pursue a development model which maintains continuity with previous policies, but which emphasizes in radical fashion the need for more social justice and equal opportunity. The increase in poverty and the erosion in basic social

services during the 1970s and 80s, along with the macroeconomic problems generated by the reliance on a social policy framework which was unsustainable over the medium and long run, have encouraged the Aylwin Administration to adopt a development strategy which is different in important respects from that undertaken by previous administrations.

Social development has become a fundamental goal of the Government's programme, which is based on the proposition that the quality of life of all citizens can be improved, while policies are identified and carried out that are sustainable and do not hamper the growth process nor the economic and political stability of democratic institutions. The development strategy is focused on keeping the nation's economy open and competitive and achieving social goals within the context of rigorous macroeconomic management. Striving to round out the efforts of the private sector to promote growth, the new Government is investing especially in those areas where the social benefits exceed the private ones and is seeking to foster mutual reinforcement between the market and Government initiatives. This requires the more active participation of the public, compromise among the interests of the various social and political groups in order to concentrate on common goals, and more extensive decentralization of Government institutions and the decision-making process.

In the belief that economic growth alone will not necessarily enhance social justice and equality, one of the first major steps of the Aylwin Administration in economic and social affairs was the launch of the Programa de Integración al Desarrollo (the Programme for Integration in the Development Process), which is aimed at improving the lot of the poorest segments of the population (MIDEPLAN 1991). Unlike the military regime, the new Government clearly views the social initiatives of the state and government investment in people as part and parcel of the development process. The programme has been assigned top priority and includes projects in health care, housing and education and training.

Decentralization is considered essential in the attempt to boost economic and social development. The goal is to strengthen local and regional governments, thereby encouraging greater efficiency in public sector investment and resource allocation, opening up the political and economic life of the country and reducing regional poverty and unemployment. The decentralization of policy-making and administration is closely allied with the open and export-oriented development model which the Government is following.

"Solidarity" and "equity" are keywords in the current economic and social approach. They reflect two of the chief principles of the new Government: the access to opportunities must be based on fairness, and helping the poor must be a priority in resource allocation. The

financing of initiatives targeted at the poorest segments of the population and at resolving some of the difficulties of the middle class must come mainly from the higher income groups.

The scarcity of resources in the social sector means that *efficiency* in resource allocation must be emphasized. The need for efficiency signifies that social policy must be selective in some areas; specific programmes may have to be designed for specific groups. *Targeting* the poor may sometimes mean that programmes will have to be aimed at aiding small- and medium-size businesses or at training and retraining people who are not necessarily among the poorest so that these businesses and people are in turn empowered to help the poorest.

Social measures must be *integrated* into a consistent policy framework. Initiatives in one area must complement those in other areas. Thus, social assistance programmes should share goals with programmes focused on human capital investment. A good example is offered by the dual aim of the School Meal Programme: to improve the diets of young people and to encourage pupils to remain in school.

The integration of social policy measures should be achieved through programme coordination at the local, regional and national levels. This highlights another basic element in the approach to social policy of the new Government: *participation*. Greater participation means bringing the needs of the state and the needs of the people into harmony.

These fresh policy guidelines have clearly fostered consensus in political and economic matters. Major economic and social reforms have been introduced successfully. Two of these stand out: the tax reform and the labour reform. The tax reform has been designed to improve Government revenue and help finance greater social expenditure. The aim of the labour reform has been to restore the rights of workers and redress the balance of power between labour and management.

The Tax Reform

A tax reform bill was approved by a wide majority in Parliament on 20 June 1990 and went into effect at the beginning of July. The additional resources generated by the reform have allowed the Government to restructure some existing social programmes and to finance new ones. The surge in resources has been particularly important in high priority programmes in health care, education and housing.

The reform package involved the following changes.

- The value added tax, which had been cut in 1989 from 20 to 16 percent, was raised

back to 18 percent.

- Businesses, which had previously been required to pay income taxes only on profits which were not reinvested in their operations, are now taxed on the basis of all profits. The tax rate was maintained at the former level of 10 percent until the end of 1990 and then raised to 15 percent for 1991-3. It is to be reduced once more to 10 percent thereafter.

- The degree of "progressivity" of personal income taxes was increased for individual incomes above 300,000 pesos per month (around \$1,000 in 1990 based on a nominal exchange rate of 305 pesos per dollar). This was achieved by lowering the income brackets on which marginal tax rates are applied.

- Businesses in agricultural, mining and transportation, which had previously been subject only to taxation on the basis of a fixed minimum assessment, are now taxed according to their actual profits.

All these changes led to a substantial boost in public sector income and an important rise in the social programmes of the Government. However, because of agreements with the opposition, in 1994 the Government must bring tax rates back down to the levels of the beginning of 1990. Current social policies would be unsustainable if this reduction takes place. Discussions have therefore been undertaken to reach fresh agreements in order to maintain the new tax rates for a longer period.

Tax revenue for 1990, excluding that from the copper industry, was approximately \$4.4 billion, or around 15.7 percent of GDP. Of this amount, the revenue attributable to the tax reform has been estimated at between \$400 million and \$450 million, or about 1.5 percent of GDP. Excluding that from the copper industry, tax revenue for 1991 has been estimated at around 18.7 percent of GDP, compared to the 17.4 percent that had been expected. Tax revenue was thus about \$1.5 billion more in 1991 than it had been in 1990 (assuming a nominal exchange rate of 350 pesos per dollar in 1991).

The political consensus over the tax reform was made possible by the obvious need to raise more resources to confront the serious social problems which had emerged following the economic crisis of the early 1980s and which had mounted throughout the decade.

The 1990 budget was drafted in 1989 by the previous Government on the basis of criteria different from those of the present Government, especially in terms of the role of the state in the social sector. Thus, public expenditure on social sector activities in the 1990 budget represented 7.8 percent less than the amount spent in 1989. Spending in those areas which were to be given higher priority by the new administration were particularly affected.

Projected expenditures in health care, education and housing in 1990 were less than the real spending in 1989 by 0.5 percent, 14.7 percent and 20.6 percent, respectively (Table 10). Tax reform was therefore important not only to allow greater spending in the provision of social goods and services in 1990 and 1991, but also to supplement the original 1990 fiscal budget.

Thus, in 1990 the tax reform contributed to a considerable boost, about 17.4 percent, in effective public spending on social programmes relative to the sums originally budgeted. In absolute terms this represented a gain of approximately \$440 million over the original 1990 budget and about \$220 million more than the spending on social programmes in 1989. The rise was especially important in high priority areas. In 1990 fiscal spending was raised in health care by 7.5 percent relative to the amount in the original budget item for that year; in housing, by 39.4 percent, and in education, by 23.3 percent. In absolute terms this meant additional resources of around 4.7 billion pesos (about \$15.4 million) for health care, 16.9 billion pesos (\$55.5 million) for housing and 43.2 billion pesos (\$141.5 million) for education. The greater resources also permitted a 10.6 percent increase in minimum pensions and PASIS social assistance pensions (provided to certain people who are not otherwise eligible for formal pension benefits; see earlier). This increase and a rise in the family allowance produced a 60.1 billion peso (\$197 million) jump in social security expenditures, equivalent to a 14.4 percent rise in relation to the original 1990 budget. Between 1989 and 1990 social spending grew from 60.1 percent to 65.2 percent of total public spending.

Meanwhile, although the new Government has been bolstering investment in people, the economic difficulties of the poorest families have forced it to boost pure social assistance as well. Thus, a potable water subsidy has been established, and the resources available for the "unique" family subsidy (SUF) and the unemployment subsidy have been raised. These steps have accounted for a climb of about 14.3 billion pesos (\$46.9 million), or 32.7 percent, in relation to the "subsidy" item in the original 1990 budget.

The 1991 contribution of the tax reform is estimated to have significantly surpassed the initial projections of about \$600 million. This allowed social investment, chiefly the expenditure on health care, education and housing, to grow by at least \$365 million, or 12.2 percent, in real terms relative to the sums spent in 1990 and over and above the additional amount required because of higher wages in health care and education. Thus, relative to the effective social spending in 1990, the spending during 1991 is estimated to have risen by \$46.7 million, or 21.1 percent, for health care, \$45.1 million, or 23 percent, for housing, and \$51.4

Table 10: "FISCAL" SOCIAL SPENDING^a
(In Millions Of Constant 1990 Pesos And In Percentages Of GDP, 1985-91)

Year	Health Care ^b		Housing ^c		Social Security ^d		Education ^e		Subsidies ^f		Other ^g		A: Total Social Spending		B: Total Spending ^h		A/B
	Total	% GDP	Total	% GDP	Total	% GDP	Total	% GDP	Total	% GDP	Total	% GDP	Total	% GDP	Total	% GDP	
1985	67,867	1.19	42,120	0.74	392,159	6.85	260,044	4.55	145,913	2.55	42,932	0.75	951,035	16.62	1,407,635	24.66	67.6
1986	63,957	1.06	42,641	0.71	436,936	7.23	259,948	4.30	113,289	1.87	36,512	0.60	953,283	15.77	1,430,808	24.66	66.6
1987	64,844	1.01	50,393	0.79	425,431	6.66	242,335	3.79	95,158	1.49	51,164	0.80	929,325	14.54	1,418,023	24.65	65.5
1988	73,673	1.07	76,284	1.11	466,335	6.80	242,080	3.53	79,053	1.15	21,354	0.31	958,779	13.97	1,546,007	24.60	62.0
1989	63,097	0.84	50,342	0.67	415,564	5.51	233,503	3.09	56,786	0.75	22,291	0.30	841,583	11.15	1,399,728	24.61	60.1
1990 ⁱ	62,777	-	42,916	-	417,880	-	185,386	-	43,636	-	23,318	-	775,913	-	-	-	-
1990	67,463	0.88	59,844	0.78	477,987	6.20	228,573	2.96	57,928	0.75	19,025	0.25	910,820	11.81	1,396,479	24.62	65.2
1991 ^j	81,697	-	73,595	-	512,145	-	244,260	-	60,563	-	49,895	-	1,022,155	-	-	-	-

Sources: MIDEPLAN (1991) and calculations of the author based on unpublished data of the Ministry of Finance.

^a "Fiscal" social spending represents the fiscal contributions and programmes of the Public Treasury. The "totals" have been adjusted for inflation according to the annual average consumer price index. The data published by the Banco Central de Chile before 1985 are not comparable due to changes in the method of adjusting for inflation and in expenditure items and subitems. These changes also account for the differences between this table and Table 1 (page 6) in the "% GDP" figures for social spending in 1985 and 1990. (Also see footnote "g" for Table 1.)

^b Outlays of the Ministry of Health, minus the maternal leave subsidy and the health care resources of the National Fund for Regional Development.

^c Outlays of the Ministry of Housing and Urban Development and the Ministry of the Interior, along with the Basic Sanitation Services Programme (Ministry of Housing and Urban Development), which is designed to assist poor families in building their own kitchens and bathrooms.

^d Social security benefits paid out through various entities within the Ministry of Labour and Social Security, as well as the social security benefits paid out through the Supplementary Operations Programme of the Public Treasury, less the layoff payments for public sector employees and some other early layoff payments.

^e The Ministry of Education, the National Council for Kindergartens (UNJI), the National Council for Scholarships and Student Financial Assistance (JUNAEB), the President of the Republic Scholarship Fund and the education resources of the National Fund for Regional Development (FNDR).

^f The Minimum Employment Programme (PEM), the Occupational Programme for Heads-of-Household (POJH), Public Treasury subsidies, the "unique" family subsidy (SUF), unemployment subsidies, the maternal leave subsidy, public sector unemployment subsidies and the potable water subsidy.

^g Various other outlays of the Ministry of Labour and Social Security, the National Service for Minors (SENAME), contributions for firemen, the National Office for Emergency Situations (ONEMI), the Social Fund, the Foundation for Community Assistance (FUNACO), the General Directorate of Sports and Recreation (INDAP) and the National Institute for the Development of Agronomy and Animal Husbandry (DIGEDER).

^h Total Public Treasury spending, less public debt payments, less tax returns.

ⁱ The 1990 budget as prepared by the outgoing administration.

^j Estimated.

million, or 6.9 percent, for education. Fiscal spending on housing in 1991 climbed \$100 million, or 71.5 percent, over the amount set out in the original 1990 budget. The corresponding growth in fiscal spending on health care and education has been estimated at \$62 million, or 30.1 percent, and \$193 million, or 31.7 percent, respectively. Overall "fiscal" social spending gained about \$800 million, or 31.7 percent, in real terms with respect to the sums assigned in the original 1990 budget.

During 1991 cash benefits were also adjusted in order to keep their purchasing power intact. The adjustment in family allowances was designed to help only those with the lowest incomes. Thus, an effort was undertaken to freeze the nominal value of the allowances for those households with higher incomes. Adjustments were introduced as well in the "unique" family subsidy (SUF) and the PASIS social assistance pension to compensate for inflation.

1. **The Improvement in Social Services.** The greater spending on health care meant that service coverage and quality could be enhanced. Although an important rise in the levels of sectoral investment in health care was not possible in 1990, this investment rose during 1991 from \$7.5 million to more than \$58 million. A substantial portion of these resources was used to improve primary health care centres. The opening hours of these centres were expanded, and programmes were created to benefit specific groups like women or the elderly. While a real overall increase of about \$20 million, or 10 percent, is expected in 1992 to finance higher wages, the principal investments in health care in 1992 have also been aimed chiefly at boosting the quality of primary health care.

A programme to raise the quality of the poorest primary schools was initiated in 1990. The programme was designed to help close the gaps in quality that had emerged among primary schools under the previous Government because of the drop in public expenditure in this area. Programmes were also undertaken to modernize technical schools. A plan has been drawn up to transform some educational institutions specialized in science and the humanities into technical schools. The plan is part of joint training initiatives of the Instituto Nacional de la Juventud (the National Youth Institute) and the Ministry of Labour and Social Security. The success of this and similar programmes is felt to depend in large measure on the participation of the private sector through both actual training and the provision of jobs.

The trend of housing shortages during earlier years has finally been arrested through annual housing starts sufficient to cover new needs. Qualitative improvements have been introduced in housing construction, and new criteria have been added within the system of

allocation priorities in order to deal with such household categories as female-headed families and families who must cohabit with others because of housing shortages. A programme has been implemented as well to allow those who are to be allotted new housing some say in housing design. An extra \$38 million, a real increase of 18 percent, have been budgeted for 1992 for basic housing projects and low-income housing programmes. The housing subsidy programme has grown by around \$22 million, or 13 percent, in real terms.

In many cases the additional resources coming from the tax reform have been used to finance expansions in the social sector, such as the creation of new jobs. This means that the pressures on spending will continue in the future. This should be taken into account, and an effort must be made to maintain fiscal balance over the medium run, especially if income tax rates are indeed brought back down in 1994. Moreover, the generation of extra revenue from the tax reform reached full potential during 1991, and it was possible to raise public social expenditure substantially only that year. As of 1992, additional spending on social programmes is possible only through fresh resources resulting from growth or reallocation within the Government budget. (Other new resources could be obtained by boosting the public debt. However, this option necessarily means that fewer resources will be available to future generations.)

In this regard, the budget bill proposed to Parliament in 1992 estimated that tax revenue, excluding that due to the copper industry, would have reached 18.2 percent of GDP. This represented a small drop in relation to the 18.7 recorded in 1991. In view of the fact that GDP growth for 1992 has exceeded 10 percent, the total budgetary expenditure of the various "social" ministries grew in real terms by about 7.5 percent. In absolute terms this is around \$443 million (assuming a nominal exchange rate of 400 pesos per dollar). Overall revenue is estimated to have risen in 1992 by 10.2 percent in real terms and to have become one of the principal sources of financing for the additional public spending on all social programmes except for education programmes, which are being financed to a large degree by loans from foreign institutions for specific projects. (Final tax and expenditure data on 1992 were not available at the time of the final editing of this paper in early 1993.)

Among high priority areas in the social sector, the greatest expansion in 1992 has been in investment spending, which has jumped 18.3 percent in real terms. In contrast, current expenditure has climbed only by about 5.3 percent in real terms. An increase in investment spending on education was expected during 1992, mainly through the Quality Improvement Programme in Education (MECE). The aim of the programme is to improve preprimary and

primary education. The cost of the programme is estimated at around \$38 million, 84 percent of which is being financed through a long-term World Bank loan. Another key component of the higher spending in education is the "Estatuto Docente" (the "Teacher Statute"), which has required an additional \$18 million over the amount spent in 1991.

2. Around 63 percent of the **additional resources generated by the tax reform** actually reached the poorest 40 percent of the population in 1990. Although a praiseworthy outcome, this did not mean that there had been improvements to correct the inefficient targeting of overall public social expenditure, mainly because the additional spending was only a fraction of the total social spending inherited from the previous Government (Table 11).

Several conclusions about the scope and impact of the greater social spending in 1990 can be drawn from the data. First, around 79 percent of the extra resources made available by the tax reform for social security, including family allowances, the "unique" family subsidy (SUF), PASIS social assistance pensions and pension adjustment and indexation, went to the poorest 40 percent of the population. Insofar as social spending through these monetary benefits is targeted at those families which are unable to satisfy their basic needs, this is a positive outcome. While 82 percent of the additional social outlays for minimum pensions went to the two lowest income quintiles, the effect of this increase did not really solve the overall problem of targeting among poor pensioners.

Second, 60 percent of the resources from the tax reform allocated to primary and secondary education reached the poorest 40 percent of the population. Likewise, 79 percent of the new resources allotted to those special assistance programmes aimed at pupils in preprimary schools (JUNJI and CADEL) and 59 percent of the corresponding resources for primary education (JUNAEB) reached the poorest 40 percent of the population. On the other hand, the distribution of the new resources in higher education was regressive, since about 43 percent benefited the highest income quintile, and nearly 70 percent the two wealthiest quintiles. However, this is rather understandable given that expenditure on this subitem, in keeping with the goals of the country, must focus on the development of research and high level teaching no matter which segment of the population happens to enter more readily, for whatever reasons, into institutions of higher learning.

Third, nearly 58 percent of the additional resources due to the tax reform assigned to health care reached the poorest 40 percent of the population. Only the new outlays for the maternity subsidy, which is designed to cover the wages of economically active women during work leaves related to childbirth, showed a regressive tendency. This results from the

Table 11: THE ALLOCATION OF THE ADDITIONAL REVENUE FROM TAX REFORM
BY SOCIAL PROGRAMME AND INCOME QUINTILE, 1990^a
(In Rounded Percentages)

Programme	Share by Item	Share by Income Quintile ^b				
		1	2	3	4	5
Social security	100.0	57.0	21.8	14.2	6.5	0.5
Universal family allowance	49.0	30.7	34.9	23.3	11.1	0.0
Targeted family allowance	--	--	--	--	--	--
Pension levelling and indexation	31.0	100.0	0.0	0.0	0.0	0.0
"Unique" family subsidy (SUF)	11.0	57.0	25.0	12.0	4.0	2.0
"Social assistance" pension (PASIS)	9.0	50.0	23.0	17.0	7.0	3.0
Education	100.0	32.1	21.5	16.1	15.3	15.1
Subsidies ^c	40.0	35.0	25.0	18.0	14.0	8.0
JUNAEB ^d	18.0	53.0	26.0	12.0	6.0	3.0
JUNJI and CADEL ^e	2.0	36.0	23.0	19.0	13.0	9.0
Higher education	23.0	8.0	9.0	14.0	26.0	43.0
Transfers to municipalities	15.0	35.0	25.0	18.0	14.0	8.0
FUNACO ^f	2.0	36.0	23.0	19.0	13.0	9.0
Health care	100.0	34.3	23.6	16.0	11.6	14.6
Wages	21.0	40.0	27.0	17.0	10.0	6.0
Consumables and services	42.0	40.0	27.0	17.0	10.0	6.0
Maternal leave subsidy	15.0	1.7	4.3	10.1	20.6	63.3
Investment in infrastructure	8.0	40.0	27.0	17.0	10.0	6.0
Primary care	14.0	40.0	27.0	17.0	10.0	6.0
Housing	100.0	32.6	26.9	22.4	12.3	5.8
Basic housing ^g	15.0	28.0	22.0	20.0	18.0	12.0
Rural and unified subsidy ^h	12.0	25.0	25.0	20.0	19.0	11.0
Special subsidy ⁱ	13.0	25.0	25.0	20.0	19.0	11.0
Basic services ^j	26.0	37.0	29.0	24.0	8.0	2.0
Urban improvement	12.0	37.0	29.0	24.0	8.0	2.0
Interest rate differential	22.0	37.0	29.0	24.0	8.0	2.0
Total	100.0	39.9	23.6	17.5	11.3	7.9

Sources: ODEPLAN (1987) and calculations of the author based on unpublished data of the Ministry of Finance.

^a Constructed on the basis of planned sectoral expenditures (Ministry of Finance) and the quintile shares calculated in ODEPLAN (1987), the table assumes that the distribution of social spending among the quintiles has not changed since 1987. It has been possible to determine the allocation of only 58.7 percent of the total 115 billion pesos in 1990 social expenditures attributable to the tax reform.

^b "1" is the lowest income quintile, and "5" the highest.

^c Grants and per child assistance to non-private-sector establishments.

^d JUNAEB = the National Council for Scholarships and Student Financial Assistance.

^e JUNJI = the National Council for Kindergartens. CADEL = Centros de Atención y Desarrollo del Lenguaje.

^f FUNACO = the Foundation for Community Assistance.

^g A programme involving subsidized credit for the purchase of low-cost housing.

^h Similar to the "basic housing" programme above but confined to rural areas.

ⁱ Similar to the "basic housing" programme above but confined to particular groups, such as municipal workers.

^j The Basic Sanitation Services Programme (Ministry of Housing and Urban Development), which is designed to assist poor families in building their own kitchens and bathrooms.

fact that women who have jobs in the formal sector tend to belong to higher income groups.

Finally, in housing, the other major area which benefited from tax reform, nearly 60 percent of the new spending reached the two lowest income quintiles.

Labour Market Reform

The labour regulations in force up to March 1990 were characterized by a lack of balance between the power of employers and that of workers. They limited collective bargaining and permitted arbitrary layoffs without the possibility of appeal. Trade unions suffered because of these restrictions, and the workplace was a highly unstable and insecure environment.

The new Government's labour policies are intended to reduce unemployment, create higher quality jobs and modify regulations in order to foster an equitable balance of power in labour relations and encourage honest and forthright negotiations to resolve differences between labour and management whenever they arise.

A major condition of the success of the Government's approach is the maintenance of a rate of economic development that will allow the expansion in the number and quality of jobs on the labour market to keep pace with the growth in the size and skill of the workforce. Wage increases will be possible if productivity rises, thus permitting improvement in the living standards of workers, as well as greater competitive capacity in industry, especially among smaller enterprises.

At the same time, efforts must be undertaken to develop the skills and the productive capacity of the workforce, particularly the poorest segments of the population, including workers in the informal sector and the unemployed. Assistance must be made available to small urban and rural businesses so that they can join in these efforts and play a key role.

Institutional reform to support these policies represents another challenge. The Ministry of Labour and Social Security took an important step in this direction by calling together the most representative labour and management organizations to discuss with the Government the basic groundwork for the new labour policy framework. As a consequence a general labour policy agreement was signed on 27 April 1990. This was a momentous covenant. For the first time workers, management and Government found a joint vision of the country's social, economic and political development and became committed to the idea of realizing a common path to the solution of potentially confrontational issues. Many of the subsequent advances in labour-management relations have been due to this agreement.

1. **Wage Accords.** An agreement has been reached by the Government and important worker and employee organizations to raise the legal minimum wage and adjust salaries upward among certain types of employees, including public sector workers. Likewise, an agreement has been reached to continue to adjust pensions automatically whenever cumulative inflation increases by 15 percent since the last previous adjustment. A major reason for these steps was the desire to avoid any substantial erosion in the buying power of consumers.

In 1990 the Labour Directorate of the Ministry of Labour and Social Security began publishing statistics on wage changes resulting from collective bargaining. These statistics are especially interesting because they offer an indication of the way wage levels respond to changes in the economy. Thus, for example, as measured by the wage index of the National Statistics Institute, the average wage among formal sector enterprises has changed only gradually as a result of economic factors, due to the large proportion of workers in these enterprises who have nominal wages which are fixed over specified time periods (Table 12). In contrast, the wage shifts following wage negotiations tend to be more obvious and thus more indicative of the reaction of wages to the economic situation, since standard overall wage increases and the wage indexes to be applied in the future are determined then at the negotiating table.

2. **Changes in Labour Laws.** Various labour bills recently passed by Congress deal with work contracts, trade unions, collective bargaining and trade union federations. A chief purpose of the legislation has been to enhance the job security of workers, while allowing management the flexibility to adapt businesses to meet the challenges of a competitive and open economy. Although some statutes contained in earlier laws have been eliminated, the freedom of management has not been altered appreciably, assuring that management can make decisions on worker-related matters based on objective business needs.

One of the key labour laws has been Law 19.010, which was passed on 29 November 1990. It contains the following important regulations.

- There must be a basic legal reason for any layoff. Among the practical motivations recognized as "legal" are restructuring, modernization, changes in market conditions and a worker's lack of technical adaptability. A worker who has been laid off has the right of appeal in court. A worker who successfully appeals remains laid off but is entitled to a severance compensation which is 20 percent higher than the one which he or she would normally have received.

Table 12: INDEX OF REAL WAGES
(1985 Through 1991, December 1982 = 100)

Year	Period	Index	Change (%)	
			Cumulative Average over Previous Period ^a	Previous 12 Months
1985	Average	92.7	--	1.9 ^b
1986	Average	94.6	2.0	2.1 ^b
1987	Average	94.4	-0.2	0.5 ^b
1988	Average	100.6	6.6	4.3 ^b
1989	Average	102.5	1.9	3.1 ^b
1990	March	103.7	--	1.5
	June	104.6	--	1.8
	September	101.6	--	-0.6
	December	108.9	--	5.0
1991	Average	104.5	2.0	5.0 ^b
	January	111.4	6.6	6.7
	February	111.5	6.7	6.8
	March	111.2	6.9	7.2
	April	110.6	6.6	5.8
	May	109.5	6.1	4.1
	June	108.9	5.8	4.1
	July	107.5	5.2	1.8
	August	106.5	4.7	1.1
	September	108.4	4.9	6.7
	October	108.0	5.1	6.5
	November	109.1	5.1	5.8
	December	111.8	4.9	2.7
	Average	108.5	3.8	0.3 ^b

Source: INE (1992).

^a A change in the cumulative average relative to the cumulative average up to the corresponding moment of the previous year.

^b December to December.

- A worker laid off by a company with which he or she had been employed since before August 14, 1981, is entitled to receive as severance pay an amount equivalent to one month's wages per year of employment. The compensation to which any other worker is entitled was raised from the equivalent of 150 days' wages to 330 days' wages, that is, one month's wages per year employed up to 11 years at the company laying the worker off.

These indemnities are designed to assist workers who have been laid off while they look for new employment.

- A worker who has been employed for at least seven years by the same company is free to enter into an agreement with management that will allow the worker to receive a compensation "for any occurrence", whether layoff, resignation or retirement. This type of compensation is equivalent to one-half of one month's wages per year worked.

- A compensation "for any occurrence" has also been created for employees in private households. For this purpose, every month and at their own expence, the employers must deposit a sum equivalent to 4.11 percent of the employee's wages in a special Pension Fund Administration account. The accumulated sum, including interest and any extra amounts due to indexing, can be retrieved by the worker when the employment is terminated, no matter what the reason.

3. **Labour Organizations and Collective Bargaining.** In general, the Government is attempting to expand and improve the bargaining power of the more than one million workers in small- and medium-size businesses by favouring the establishment of appropriate organizational mechanisms and procedures.

4. **The Implementation of the New Labour Regulations.** While the planned institutional restructuring represents a key focus of the activities of the Ministry of Labour and Social Security, the ministry has also assumed special responsibility for the implementation and enforcement of the new labour regulations. Within the limits of the available resources, a series of major initiatives have been developed to fulfil this task.

- The number of responses to complaints and visits by ministry inspectors to enterprises increased by approximately 11 percent during the first six months of 1991 with respect to the number over the same period the previous year.

- The ministry has instituted an inspection policy for specific industries, including commerce, textiles and metallurgy. The number of workers benefiting from this policy has been substantial in these industries, and the increase in social security payments which are made in a timely and correct fashion has been significant.

- The ministry's Labour Directorate has taken an active role in mediating labour disputes and reconciling the various sides in order to foster fair and reasonable compromises.

- A collective bargaining unit has been established within the Labour Directorate. The unit maintains a constant watch on labour disputes in order to promote the success of collective bargaining.

- The Department of Labour Organizations within the Labour Directorate has developed a training programme for trade union leaders. The leaders of over 200 labour organizations took part in this programme during the first six months of 1990.

5. **Professional Training.** Enhancing the productivity of enterprises and businesses and improving the technical and professional skills of the workforce, particularly younger people and women, are important goals in the new labour policy. With the support of the Servicio Nacional de Capacitación y Empleo (SENCE, the National Employment and Training Service) and the Inter-American Development Bank, the Job Training Development Programme has been created to meet these goals. The various programme initiatives are expected to benefit around 100,000 young people over the next few years. This is to be accomplished through:

- The development of job training programmes through financial credits and capital investment for construction and new equipment at vocational schools and technical institutes.
- The establishment of an on-the-job youth training programme mainly through the employment of apprentices.
- The creation of innovative projects for employment and training among young people who have become marginalized.
- The provision of support for appropriate governmental and non-governmental organizations that is designed to bolster the role of these institutions in job training or in research aimed at determining the training needs of the country.

Summary

The new Government is pursuing economic and social development policies which maintain continuity but are nonetheless radically different in important respects from those undertaken by previous administrations. Striving to complement the efforts of the private sector to promote growth, the Government is encouraging the more active participation of the public, compromises among the interests of the various social and political groups in order to focus on common goals, and greater decentralization of the decision-making process.

One of the first major steps in this direction was the launch of the Programa de Integración al Desarrollo (the Programme for Integration in the Development Process), which is aimed at improving the lot of the poorest segments of the population and has been given high priority. It includes projects in health care, housing and education and training.

The policy guidelines of the Government have clearly nourished consensus in political

and economic matters. Major economic and social reforms have been introduced successfully. Two of these stand out: a tax reform and a labour reform. The tax reform has been designed to change the dynamics of Government revenue and expenditure and help finance greater social spending. The aim of the labour reform has been to restore the rights of workers and redress the balance of power between labour and management.

IV. THE DISTRIBUTIVE IMPACT OF SOCIAL POLICY, 1990-1

To achieve economic and social growth with equity, the Government has been attempting to improve income distribution. However, although the policies it has explicitly adopted in this effort have clearly had redistributive effects, adjustments and shocks in the market and other macroeconomic policies have also had indirect impacts.

Thus, for example, while fiscal policy, notably the expansion of social spending, became an important engine of income redistribution during 1990, the tax reform of that year did not immediately translate into a more progressive tax system. Moreover, persistently high inflation led to the application of strict adjustment measures which were designed to slow the growth in prices, but which also dampened the growth in output and employment. Finally, a series of internal and external price shocks and the high level of inflation had an uneven impact on the purchasing power of the various income groups within the population. For instance, whereas some of the negative effects of inflation were muted by labour law reform, an increase in the minimum wage and the greater Government support for the bargaining power of worker organizations, inflation was especially high on the goods in the typical consumption basket of the poorest groups.

Adjustment succeeded in bringing inflation under some semblance of control in 1991. The economy recovered its dynamism, and all economic growth projections, which had stood at around 4 or 5 percent, were surpassed. Preliminary data for 1992 indicate that growth has exceeded 10 percent. Employment also showed a positive trend, which became more evident near the end of 1991. Nonetheless, although the unemployment rate fell, total unemployment rose because of a significant expansion in the size of the labour force. Lastly, while the extra tax revenue in 1990 had been produced mainly as a result of the higher value-added tax, the direct taxation system took hold in 1991, thus making the tax system more progressive.

The principal redistributive tools employed in 1990-1 were tax reform and the targeted

increase in social spending. Additional tools were the labour market reform and the adjustment of the minimum wage.

Tax Reform

In terms of the incidence of the tax burden, tax reform on the whole has been progressive. Because indirect taxes, such as the value-added tax, depend on consumption levels, their application is slightly regressive. Nonetheless, the introduction of higher income tax rates has likely led to greater progressivity in the tax system. Other reforms undertaken by the Government such as the establishment of taxation based on actual, rather than on a fixed level of "presumed" profits, also tend to promote equity in the tax system.

In terms of the tax reform, 1990 was a transition year, during which most of the increase in tax revenue was due to the higher yields of the value-added tax. Much of the rest came from additional taxes paid by businesses and a work-related tax (the "impuesto único al trabajo"). It seems reasonable therefore to assume that the redistributive effect of tax reform was generally neutral during 1990.

On the other hand, assuming that the higher business taxes were not eventually passed on to consumers through higher product prices in 1991, then approximately one-third of the extra revenue due to tax reform during that year had slightly regressive distributive implications, while the remaining two-thirds was levied in a fairly progressive manner.

The Increase in Social Spending

In 1990 the additional social spending due to increased tax revenue was clearly distributed among the various deciles of the population in a progressive fashion. Social expenditures were raised, especially in health care, education, housing and social security. The efficient allocation of this greater spending in terms of the targeting on low-income groups should be emphasized. Around 63 percent of the new resources generated during 1990 were spent for the benefit of the poorest 40 percent of the population (see Table 11, page 33).

In 1991, health care, education and housing programmes were not only maintained, but they were also reinforced significantly. Public investment rose considerably, while the real value of subsidies and social security benefits were kept stable. The more substantial redistributive effects in 1991 were undoubtedly due to the higher social spending and the

more efficient targeting of this spending. Thus, for example, around 58 percent of the added social spending attributable to the extra revenue available because of the tax reform was used for the two lowest income quintiles in the population (Table 13). Although this represents a decline from the 63 percent share of the extra social spending that had been allocated to the poorest two income quintiles in 1990 (see Table 11, page 33), the net redistributive effect of the combined 1991 tax and expenditure policy was very likely greater than it had been during the previous year in view of the more progressive distribution of the additional tax burden achieved in 1991, thanks to the increased reliance on direct taxes on the incomes of individuals and the business sector.

Macroeconomic Policy and Labour Market Reform

Adjustment measures, in conjunction with the changes in the minimum wage and in labour regulations, had important but contradictory distributive effects which are evident in data on the share of wages in national income, the behavior of wages and the shifts in the levels of employment and unemployment.

Wages rose an annual average 5.3 percent in 1990 and 1991, while GDP growth was an average 4 percent per year over the same period. This implies that the share of wages in GDP climbed from the 37 percent of 1989 to over 38 percent in 1991.

Consumption originating from "private" income grew 5.1 percent in 1990-1, or around 2.5 percent per year, as a result of the impact of policies and reform on economic activity, employment and real wages. Between 1989 and 1991 the rise in wages spurred a 6 percent increase in this consumption indicator among the lower-income groups and a 8.3 percent increase among the middle-income groups.

During 1990 the share of wages in gross disposable income reached slightly more than 50 percent, reflecting an improvement over 1989, when the corresponding share stood at 46.9 percent. Nonetheless, the figure for 1990 is below the annual average 52.8 percent of the first three years of the 1980s. The difference was probably a consequence of the recession which occurred after 1982 and which greatly reduced the primary incomes of the working class, especially among the poorest segments of the population. A recovery to the levels attained before the onset of that recession has likely been complicated by two factors. First, the levels at the beginning of the 1980s may have been excessively high because of a significant influx of capital and the development of the non-tradable sector, as opposed to the tradable sector.

Table 13: THE ALLOCATION OF THE ADDITIONAL REVENUE FROM TAX REFORM
BY SOCIAL PROGRAMME AND INCOME QUINTILE, 1991^a
(In Rounded Percentages)

Programme	Share by Item	Share by Income Quintile ^b				
		1	2	3	4	5
Social security	100.0	38.3	25.4	18.9	11.1	6.4
Family allowance	48.3	23.9	27.4	22.2	16.2	10.4
Universal	28.1	19.0	22.1	21.3	19.8	17.8
Targeted	20.2	30.7	34.9	23.3	11.1	0.0
"Unique" family subsidy (SUF)	12.4	57.0	25.0	12.0	4.0	2.0
"Social assistance" pension (PASIS)	39.3	50.0	23.0	17.0	7.0	3.0
Education	100.0	30.9	21.2	16.4	15.9	15.6
Subsidies ^c	62.8	35.0	25.0	18.0	14.0	8.0
JUNAEB ^c	9.3	53.0	26.0	12.0	6.0	3.0
JUNJI and CADEL ^c	3.9	36.0	23.0	19.0	13.0	9.0
Higher education	23.1	8.0	9.0	14.0	26.0	43.0
Textbooks	0.3	35.0	25.0	18.0	14.0	8.0
"900 schools" programme ^d	0.6	100.0	0.0	0.0	0.0	0.0
Health care	100.0	39.7	26.9	17.0	10.1	6.3
Wages	31.9	40.0	27.0	17.0	10.0	6.0
Consumables and services	19.4	40.0	27.0	17.0	10.0	6.0
Maternal leave subsidy	1.1	1.7	4.3	10.1	20.6	63.3
Investment in infrastructure	10.4	40.0	27.0	17.0	10.0	6.0
Primary care	10.9	40.0	27.0	17.0	10.0	6.0
Free choice health service ^e	15.7	40.0	27.0	17.0	10.0	6.0
PNAC ^f	10.7	41.0	28.0	18.0	10.0	3.0
Housing	100.0	29.1	24.7	20.9	16.0	9.3
Basic and "two-stage" housing ^g	41.8	28.0	22.0	20.0	18.0	12.0
Rural and unified subsidy ^c	28.9	25.0	25.0	20.0	19.0	11.0
Special subsidy ^c	6.0	25.0	25.0	20.0	19.0	11.0
Basic services ^c	8.4	37.0	29.0	24.0	8.0	2.0
Urban improvement	14.9	37.0	29.0	24.0	8.0	2.0
Total	100.0	34.1	23.9	17.6	13.4	11.0

Sources: ODEPLAN (1987) and calculations of the author based on unpublished data of the Ministry of Finance.

^a Constructed on the basis of planned sectoral expenditures (Ministry of Finance) and the quintile shares calculated in ODEPLAN (1987), the table assumes that the distribution of social spending among the quintiles has not changed since 1987.

^b "1" is the lowest income quintile, and "5" the highest.

^c See the notes to Table 11, page 33.

^d Additional tutoring services and other support for schools where students are doing relatively poorly.

^e Essentially, the ISAPRES scheme (see earlier).

^f The National Supplementary Food Programme.

^g "Two-stage housing" is a new programme which provides additional housing construction subsidies to families who have already benefited from the Basic Sanitation Services Programme (see footnote "j", Table 11, page 33).

Second, the severe adjustment measures implemented in 1990 acted as a brake on job creation and therefore also on the share of the labour force in national income. Overall, in 1990 the increase in wages generated a rising trend in the proportion represented by labour in total revenue, while macroeconomic adjustment measures opposed this trend somewhat.

The most important single event in labour-management relations in 1990 was the general agreement between labour and employer associations that was favoured by the Government and that permitted a jump in the nominal minimum wage from 18,000 pesos to 26,000 pesos per month (\$57 to \$85). Along with an adjustment in public sector wages during December, this helped boost the growth in real wages by 1.8 percent during 1990. However, the impact of both the higher minimum wage and the pay raise in the public sector was sharply offset by a rather significant inflation rate and the price shocks caused by a drought in Chile and the oil crisis associated with the troubles in the Persian Gulf. Moreover, despite the 1.8 percent increase in wages in 1990, a few occupational categories, especially some related to lower-income groups, experienced a drop in real wages.

Albeit only by 2 percent, the number of jobs rose during 1990, despite the fall in the GDP growth rate to just 2.1 percent and the simultaneous implementation of tax and labour reforms. The unemployment rate dropped to 6 percent from 6.3 percent in 1989, although the main reason for this was the dip in the growth rate of the labour force (Table 14).

From a macroeconomic perspective, the application of adjustment measures has now been terminated and the rising trend in prices has been brought under control. This has had a positive effect not only on the economy in general because of the recovery in the GDP growth rate to around 5 percent in 1991 and to around 10 percent in 1992, but also on the poorer segments of the population because of the upturn in the generation of employment and the wage increases associated with greater productivity. Moreover, due to fresh agreements, the minimum wage has been readjusted so as to maintain its purchasing power at a constant level. This has also bolstered the growth in real wages.

The Differential Impact of Inflation

Changes in external conditions can have a very substantial influence on internal prices and the cost structure of an economy, such as that of Chile, which is "open" to international trade and which relies heavily on price and wage indexing. Thus, the world oil crisis and the local drought strongly affected prices in Chile in September and October 1990. Because of the use

Table 14: THE EVOLUTION OF THE LABOUR MARKET^a
(In Thousands Of Individuals, 1986-90)

	1986	1987	1988	1989	1990
Working-age population	8,389	8,525	8,668	8,814	8,963
Economically active population	4,269	4,355	4,552	4,675	4,728
Unemployment	373	344	286	250	269
Employment	3,896	4,011	4,266	4,425	4,459
Agriculture	802	838	865	857	859
Formal	474	508	521	508	509
Employers	31	31	34	34	35
Employees	443	477	487	474	474
Traditional	328	330	344	349	350
Non-agricultural	3,094	3,173	3,401	3,568	3,600
Formal	1,914	2,067	2,257	2,410	2,454
Employers	91	105	111	144	147
Employees	1,823	1,962	2,146	2,266	2,307
Special employment programmes ^b	191	93	16	0	0
Informal ^c	727	747	832	879	864
Domestic service	262	266	296	279	282

Source: Calculations of the author based on *Encuesta de Hogares* (various).

^a The table reflects October-December "moving" quarter data.

^b Includes those in the Minimum Employment Programme (PEM) and the Occupational Programme for Heads-of-Household (POJH).

^c Includes the self-employed and those who work for relatives.

of the "unidad de fomento", an indexing tool extensively applied in Chile, the increase in the prices of some major goods had important distributive consequences.

Thus, the official consumer price index may not reflect very accurately the real rise in the cost of living of the two lowest income quintiles. Moreover, data indicate that the impact of the oil shock on prices affected these poorest segments of the population the most. Between January and May 1990 the change in the quintile-specific CPI for the poorest 20 percent of the population was about 75 percent of that of the official overall CPI. On the other hand, between June and December of that year, a period during which inflation

accelerated, the quintile-specific CPI for the poorest 20 percent of the population rose 18 percent more than the official overall CPI.

This clearly demonstrates the risk involved for the poor if inflation is allowed to climb rapidly. Likewise, it shows the need for mechanisms to protect an economy from the impact of abrupt changes in the international prices of tradable goods. Indeed, following the Gulf crisis, an oil stabilization fund was established in Chile for use in case of extremely sharp variations in the price of oil on the world market.

In 1991 the control of inflation became a major goal in the Government's efforts to alleviate poverty. Obviously, the Government had understood that rising prices were having a particularly harsh impact on the poor, because the poor lacked the means to offset the inflation. This was especially true since the most important increase in the overall escalation in prices was associated with the rise in food prices, which were affecting poor families the most even though the inflation rate fell from 27.3 percent to 18.7 percent between 1990 and 1991 (Table 15).

Table 15: INFLATION RATES BY INCOME QUINTILE
(In Percentages, 1990-1)

Period	Income Quintile*					Average
	1	2	3	4	5	
1990	28.0	27.5	27.0	27.2	27.3	27.3
January-March	4.0	4.2	4.3	5.0	5.9	5.3
April-June	5.3	5.3	5.4	5.4	5.8	5.6
July-September	11.7	10.9	10.2	9.2	7.7	8.8
October-December	4.6	4.8	4.8	5.2	5.5	5.3
1991	14.6	18.1	19.0	18.9	18.7	18.7
January-March	-1.1	0.3	0.6	1.3	2.6	1.7
April-June	5.5	6.4	6.8	6.5	6.1	6.3
July-September	5.1	4.8	5.0	4.8	3.9	4.4
October-December	4.7	5.7	5.5	5.2	4.8	5.1

Source: *Indicadores de Precios al Consumidor* (various).

* "1" is the lowest income quintile, and "5" the highest.

Overall, while 1990 was a year of economic adjustment and slow GDP growth, an improvement in income distribution that favoured the poorest 20 to 40 percent of the population was evident. Thus, the share in national income of the two lowest income quintiles in the population rose from 12.6 percent to 13.3 percent between September-November 1989 and September-November 1990. By late 1991 it had grown to 14.7 percent (Table 16). Thus, during 1990 and 1991 the new Government's macroeconomic policies had gone a long way toward meeting the challenge of stabilizing prices through severe adjustment measures while taking the steps necessary to correct distributive disequilibriums.

Table 16: THE SHARE IN NATIONAL INCOME BY QUINTILE^a
(In Rounded Percentages, 1978 And 1989-91)

Income Quintile ^b	1978 ^c	1989	1990	1991
1	5.2	4.6	4.9	5.5
2	9.3	8.0	8.4	9.2
3	13.6	11.3	11.5	12.4
4	21.0	16.6	17.2	18.2
5	51.0	59.5	58.0	54.7

Source: INE (1978b), (1989), (1990), (1991).

^a Includes wages, salaries, the income of the self-employed and other income.

^b "1" is the lowest income quintile, and "5" the highest.

^c The data for 1978 refer only to the Greater Santiago area.

The overall distributive impact of Government fiscal, labour and macroeconomic stabilization policies can be analysed through a comparison of the distribution by quintile of private consumption before transfers and the distribution by quintile of total consumption, both in 1991 (Table 17). "Total" consumption in this case includes not only the consumption originating from private incomes, but also that originating from cash subsidies, social security transfers and the estimated value of the benefits due to public social expenditure on health care, education and housing. It also includes an estimate of the gains due to the reduction in inflation (that has benefited more than proportionately the low-income groups). It appears that, while the poorest quintile accounted for only 3.3 percent of private consumption in 1991, its share in total consumption was almost double that level, reaching 6.4 percent of total consumption. Smaller but still significant gains were realized by the second and third lowest

Table 17: PRIVATE CONSUMPTION BY QUINTILE BEFORE AND AFTER TRANSFERS
(In Billions Of 1990 Pesos, 1991)

Item	Income Quintile					Total
	1	2	3	4	5	
A. Private consumption (before transfers) ^a	185.1	466.1	727.5	1,092.1	3,125.3	5,596.0
Share (%)	3.3	8.3	13.0	19.5	55.8	100.0
B. Public expenditures on subsidies ^b	14.1	11.3	10.0	10.8	14.3	60.6
C. Public expenditure on social security & other ^c	113.7	76.4	53.2	40.9	26.4	310.6
D. Total (A + B + C)	312.8	553.8	790.7	1,143.9	3,166.0	5,967.3
Share (%)	5.2	9.3	13.3	19.2	53.1	100.0
E. Quintile-specific CPI ^d	0.969	0.990	0.997	1.000	1.004	1.000
F. Total (D adjusted by E)	321.4	558.1	791.8	1,143.9	3,152.1	5,967.3
Share (%)	5.4	9.4	13.3	19.2	52.8	100.0
G. In-kind benefits in education, health & housing	75.2	48.4	33.7	25.9	16.7	199.9
H. Total consumption after transfers (F + G) ^e	396.6	606.5	825.5	1,169.8	3,168.8	6,167.1
Share (%)	6.4	9.8	13.4	19.0	51.4	100.0

Source: MIDEPLAN (1990).

^a Differential income growth added to the private consumption before transfers in 1990. For the two lowest income quintiles ("1" and "2"), income growth during 1991 has been estimated at 3.5 percent, consisting of a 3 percent wage increase and a 0.5 percent rise in informal sector employment. The corresponding estimate for the next two income quintiles ("3" and "4") is 4 percent, consisting of a 3 percent rise in wages and a 1.5 percent rise in formal sector employment and assuming that these quintiles save 10 percent of their incomes. The estimated income growth for the highest income quintile ("5") is 4 percent.

^b Monetary subsidies such as SUF, PASIS and the family allowance.

^c That portion of social security and other benefits that is estimated to be spent by private consumers directly on goods and services.

^d The consumer price index for each quintile divided by the total CPI, which has been calculated assuming a rise of 18 percent during 1991.

^e The consumption spending of households and non-profit organizations after transfers and corrected by the CPI.

income quintiles. Altogether, after transfers and the provision of services in kind, the share in consumption of the poorest 40 percent of the population rose by one-half, while that of the two wealthiest quintiles increased only marginally. This underscores very clearly the important redistributive role which fiscal policy has played in the new development model being followed in Chile since early 1990.

Summary

The Concertación Government is attempting to confront the problem of poverty in a serious and determined manner. The general consensus among political leaders regarding the

severity of the problem and the important role the Government must play in redressing social imbalances has permitted major reforms to be implemented that are aimed at achieving greater equity while assuring smooth and sustainable economic growth and macroeconomic and budgetary stability. Moreover, the social role of the Government does not end with the satisfaction of the basic needs of the poorest segments of the population, but must also secure the economic and social well-being of workers and the middle class.

The Government has assigned particular importance to the identification of those groups or areas which require some sort of special support in order to develop their full potential so that they will no longer need to rely on the state in the future. It has therefore considered investment in people as one of its most essential tasks. This means particular attention in the social sector, especially health care, housing and education. New reforms and innovative social programmes, as well as a clearer identification of priority areas and the groups at risk, can be expected in the future as the Government strives to deal with all dimensions of poverty.

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