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Redistributive Constraints under High Inequality: The Case of Mexico

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Abstract

The paper presents a comprehensive analysis and interpretation of redistributive spending in Mexico. It reviews the evolution over the last two decades of the principal redistributive instruments and the distributive outcomes targeted by these instruments (income, land, education, health, nutrition). Using recent income and expenditure surveys, the paper presents a comparative benefit incidence analysis (BIA) of 25 mayor programs or spending categories covering all public spending on education, health and social security, energy and agricultural subsidies, and the principal targeted anti-poverty programs, globally representing 60% of public spending, 10% of GDP, and 15% of disposable household income. The BIA is extended over the 1992-2008 period for the principal instruments, to evaluate the distributive effects of recent policy reforms. The comparative analysis reveals large contrasts in redistributive performance (concentration coefficients), from the Oportunidades CCT program (-0.53) to agricultural, energy and public sector pension subsidies (0.40-0.80). Overall, the regressive programs cancel out the redistributive effects of the progressive efforts, leading to a regressive absolute distribution of public spending. It identifies the principal factors accounting for these results, focusing on political as well as more general structural constraints on the redistributive capacities of the State under high (pre-transfer) inequality conditions.

Resumen

Este trabajo presenta un análisis e interpretación amplios del gasto redistributivo en México. Se analiza la evolución de los principales instrumentos redistributivos y sus resultados distributivos en las dimensiones relevantes (ingresos, tierras, educación, salud y nutrición). A partir de encuestas de ingresos y gastos de los hogares recientes, se presenta un análisis de incidencia de beneficios (AIB) comparativo para 25 programas o rubros de gasto principales, que cubren el gasto total en educación, salud y seguridad social, subsidios energéticos y agrícolas, y los principales programas de gasto dirigido, y representan en conjunto 60% del gasto público programable, 10% del PIB, y 15% del ingreso disponible de los hogares. El AIB se extiende al periodo 1992-2008 para los principales programas, permitiendo una evaluación de las reformas recientes en estos rubros. Los resultados de este análisis revelan contrastes amplios en el potencial redistributivo del gasto público (coeficientes de concentración), desde los programas de gasto dirigido efectivamente focalizados como

Oportunidades (-0.53), hasta los subsidios agrícolas, energéticos y a los sistemas de seguridad social de los trabajadores del estado (0.40-0.80). En conjunto, los programas regresivos cancelan el efecto progresivo de los programas que favorecen a los estratos de menores ingresos, generando una distribución regresiva en términos absolutos del gasto público. El trabajo identifica los factores principales que explican estos resultados, considerando tanto factores políticos como restricciones estructurales más generales sobre las capacidades redistributivas del Estado en condiciones de alta desigualdad original.

Introduction

The lowest inequality rates in the world are achieved by two very different groups of countries, exemplified by Finland and Taiwan: the mature, massive and highly institutionalized welfare states (Lindert 2004), and Asian and Eastern European economies with dynamic and equitable development paths from initial positions of low asset, human capital and income inequality (Drèze and Sen 1989). What is common between the two groups is that "inclusive growth" is achieved in the context of a virtuous cycle of low or moderate inequality and effective redistributive State action. At the other end of the world inequality ranking, many Latin American countries present a mirror image to these qualities, burdened by both high historic levels of asset and income inequality, and chronic fiscal and institutional limits to redistributive capacities. Breaking this inequality trap and transiting to a path of equitable development requires understanding the constraints on redistribution under high inequality conditions.

The political and economic history of Mexico makes this a unique case to study such constraints. The construction of the modern Mexican State over the last two centuries was shaped by two foundational conflicts associated with extreme concentrations of land and political power: the Independence from Spain in 1821, and the Mexican Revolution a century later. The post-revolutionary regime which emerged from the latter movement achieved legitimacy and maintained itself in power for the rest of the 20th century —in the absence of functional democratic institutions— on the promise of two principal offers: a) an institutional order capable of delivering economic growth with political stability, and b) the implementation of the redistributive ideals inherited from the Mexican Revolution. The long-lasting success of the first component has been extensively studied. Beyond the consistent redistributive rhetoric characteristic of all post-revolutionary administrations in Mexico to the present, however, accountability in the practical achievements of the latter ideal has proved more elusive.

This article presents a comprehensive evaluation and interpretation of redistribution in Mexico. The rest of this section reviews basic conceptual and methodological issues on redistributive instruments and the measurement of their redistributive impact. Section 2 reviews the available evidence on the evolution of distributive outcomes in the dimensions directly relevant to the redistributive instruments to be analyzed, including in particular, in addition to income, health and education outcomes (the distribution of land and nutrition are reviewed in the context of the relevant instruments in section 3). Section 3 presents historical background information and a *benefit incidence analysis* (BIA) covering the evolution of the principal distributive instruments over the last decade (and before), including agrarian reform and

subsidies, education, health and social security, pensions, and food subsidies and anti-poverty programs. Section 4 presents a comprehensive comparative and global BIA using the most recent survey information available (2006), and extending the analysis to the most recent shifts in redistributive spending (2006-2008). This analysis covers all public spending on education, health and social security, energy and agricultural subsidies, and the principal targeted instruments, totaling 25 programs or spending categories, representing 60% of public spending, 10% of GDP, and 15% of disposable household income. This is combined with tax incidence data to obtain estimates of the net, global incidence of public redistributive spending. Both the dynamic (section 3) and comparative and global (section 4) BIA presented here is based mostly on the *Encuesta Nacional de Ingresos y Gastos de los Hogares* (ENIGH), available biannually and fully comparable between 1992 and 2006. Finally, section 5 presents an interpretation of the principal observations obtained in the previous sections, in particular the coexistence of highly regressive instruments along with the more progressive programs, cancelling out the progressive effects of the latter on redistributive public spending globally. This account focuses on constraints on redistributive capacities under conditions of high (pre-transfer) inequality, including political economy accounts (Robinson 2008), but also general structural constraints on the design and implementation of redistributive instruments under such conditions. Capture by specific interest groups may account for some of the most regressive programs in Mexico (public sector pensions, agricultural subsidies), but the regressive distribution of "universal" (tertiary education and health) services, the social security system covering private sector workers (IMSS), and "generalized" consumption subsidies involves a combination of political and structural constraints.

The link between redistributive instruments and redistributive outcomes in modern mixed economies is complex. Governments may affect the distribution of income or other outcomes, including assets, health and education, directly or indirectly. They can modify the distribution of income through two channels (and time horizons): (a) by modifying the relation between market (pre-fisc) income and (current) disposable income, through monetary tax and transfers, and (b) by modifying the determinants of market income, through transfers of productive assets (including investments in human capital) and policies affecting the use of, and returns to, these assets. Considering only fiscal (budgetary) interventions, there are three principal types of redistributive instruments available to governments:

i) progressive taxes on income or assets,
ii) direct monetary transfers, and
iii) transfers "in kind", through the fully or partially subsidized provision of goods and services.

Although monetary transfers and transfers in kind correspond closely with the two noted redistributive options (a and b), the two classifications do not map perfectly. Monetary transfers redistribute current income, while the provision of public health and education services promotes equitable access to human capital and thus future capacity to generate income through the market, in addition to educational and health outcomes valuable for their own sake. However, monetary instruments may also be used to promote equitable access to services and improve future income-generating capacities, if allocated conditionally on relevant investments on the part of households, as in the case of conditional cash transfer (CCT) programs, and even in unconditional form, by providing liquidity in the (ubiquous) context of credit market failures. Conversely, the public provision of education and health services has an impact on the distribution of current disposable income, by liberating private household income otherwise allocated to these services.

Estimating the redistributive impact of monetary transfers and transfers in kind present very different methodological challenges. Most income and expenditure surveys report the former as a component of household income. The contribution of these transfers to overall income inequality can then be estimated through the application of standard decomposition techniques on inequality measures by income source. This is the path followed by most case studies in the present volume, including the companion chapter on Mexico (Esquivel 2008). An important limitation of this method for the present purpose, however, is that this only captures a small part of public transfers. In contrast to mature welfare states, where monetary transfers represent between a third and half of all social spending, and account for reductions in inequality on the order of 20-50%[1] (Ervik 1998, Smeeding and Ross 1999), monetary transfers in the LAC region (as in most middle-income countries) represent a small fraction of social spending. In the case of Mexico, for example, the two principal redistributive cash transfer programs reported in the ENIGH survey (Oportunidades and Procampo) represent just 5% of redistributive spending, as classified in the present study (see table 6), below. The other 95% is thus left out of the Gini decomposition analysis.[2]

To estimate the effect of transfers in kind, this chapter presents a benefit incidence analysis based on the use of public services reported in ENIGH, valued at cost of provision (section 3 and 4). This imputed distribution of transfers received, valued in monetary terms, is then used to obtain an

[1] These reductions are measured in purely accounting terms: pre-transfer Gini - post-transfer Gini.

[2] In addition to *Oportunidades* and *Procampo*, table 6 classifies pension subsidies and energy and agricultural subsidies as "cuasi-monetary" transfers (see definition below, section 4). Of the latter, only pensions are reported in the ENIGH survey, but these cannot be analyzed as public transfers because a) the ENIGH data does not allow public pensions to be identified separately from private ones, nor b) does it allow the identification of the subsidy (vs. saving) component in the public pensions. Pension income is therefore correctly decomposed as a separate income component in Esquivel (2008), where it is found to be unequalizing. The incidence analysis presented below (section 4) includes only the tax-financed subsidies to the public pension systems, and uses information on social security affiliation reported in the ENIGH (for active workers only) to impute these.

estimate of the (monetary and in kind) post-transfer Gini coefficient, and thus (by comparing to the pre-transfer Gini) of the total redistributive impact of all transfers. These imputations augment the concept of non-monetary income reported in ENIGH, and differ from the non-monetary concepts already included in the latter (notably imputed housing rent) not by being imputed (rather than actual monetary quantities), but only by the method of valuation used to obtain the relevant monetary values: cost of provision vs. self-reported valuation. In defense of the inclusion of transfers in kind it should be noted that, while both of these methods are imperfect and imply measurement errors: a) it is not obvious that the former is less accurate than the latter (in the absence of real estate markets and household knowledge of actual market-values), and b) given the order of magnitude of transfers received (thus valued) relative to pre-transfer household income (75% for the poorest decile: see table 7 below), the measurement errors are in any case unlikely to be larger than the non-measurement error: failing to measure this income concept at all.

It would of course be possible to apply a standard decomposition analysis on the (post-transfer) Gini coefficient obtained from this augmented concept of total income, thus allowing in principle a direct and full comparison of the effects on inequality and its evolution of private vs. public income sources. Given the noted measurement issues, however, such a direct comparison would have to be interpreted with care. This would also imply a substantial revision of the (total income) Gini coefficients reported for countries. The present analysis reports the estimated effect of these transfers on the Gini coefficient in purely accounting terms, following common practice in benefit incidence analysis.

Finally, it should also be noted that by considering only the current value of benefits received, the redistributive effect of transfers in kind is valued in terms of current income. This assumes implicitly that the only objective of these transfers is to redistribute current income, which is obviously unwarranted, as this objective would be much more efficiently pursued through direct (and untagged) monetary transfers. Two more relevant objectives of transfers in kind are: a) the reduction of current inequalities in the specific dimensions of these transfers (valued intrinsically), and b) the reduction of future income inequality through a redistribution of productive assets in the relevant dimensions, notably human capital. Both of these are ignored in the incidence analysis below, but the following section reports the evolution of inequalities in the relevant dimensions.

2. Distributive outcomes: multi-dimensional inequality and poverty

The companion chapter on Mexico in this volume (Esquivel 2008) presents a detailed analysis of the evolution of monetary income inequality. This section complements the latter by presenting a broader (and thus more superficial) characterization of distributive outcomes, including the non-monetary dimensions motivating the principal transfers in kind and reporting poverty as well as inequality measures.

A. **Income inequality.** Though income inequality measures are available for Mexico since 1950, these have been fully comparable only since 1992. With this caveat, for most of the second half of the 20th century income inequality in Mexico seems to have cycled within a +/- 10% band of a 0.50 Gini, declining significantly from the mid-sixties to the mid-eighties, growing back in 1984-1994, and declining again in 1994-2006 (Fig. 1 and 2 in Esquivel 2005). Though the latter decline may reflect in part a one-off gain associated with a massive expansion in the coverage of the Oportunidades program (from 2.5 to 5 million families between 2000 and 2004), it is mostly explained by labor income, reflecting declining wage inequality and declining returns to higher education post-NAFTA (López-Acevedo 2006). To the extent that the latter responds to declining schooling inequalities (see table 1), the recent decline in income inequality would represent a structural trend, as the dynamics of expanding educational coverage ensure that educational inequality will continue to decline in the future (see below).

B. **Income poverty.** Again bearing in mind comparability problems,[3] graph 1 suggests that there was no progress in the reduction of extreme ("food") poverty[4] over the last three decades of the 20th century (with the absolute number of poor increasing from 11 to 23 million), followed by a rapid decline in 2000-2006. The 2000-2004 decline may again partly be explained by the expansion of Oportunidades (Székely and Rascón 2004), but the continuing declining trend reflects mostly an increase in labor incomes associated with a 73% gain in average schooling of the poorest population quintile over the last decade (table 1). It is interesting to

[3] Comparability is even more challenging in the case of poverty measurements, as there are significant gaps in the measurement of the absolute level of aggregate income/expenditure in ENIGH in comparison to the closest equivalent concepts in the National Accounts, and these vary between surveys. Despite a well-established tradition of adjusting survey income data with the NA in poverty measurements in Mexico (as in other countries), these adjustments inevitably impute income on the poor originating partly in underreporting at the top of the income distribution. The official measures, reported here, therefore do not apply such adjustments (Leyva-Parra 2005).

[4] "Extreme poverty" in this paper refers to the lowest of three poverty lines currently used in Mexico as official poverty measures, referred to as "food poverty". This is calculated as the cost of a basic food basket, which for 2006 was valued at 1.8 pesos per person per month in rural areas, and 2.5 pesos in urban areas.

compare the evolution of poverty in the 1989-1994 and the 2000-2006 *sexenios*, bracketing out the 1994-2000 period lost in terms of poverty reduction to the 1994/5 crisis (graph 2). Both periods involved important and similar increases in anti-poverty spending and GDP growth was significantly higher in 1989-1994, but the reduction in the extreme poverty rate was almost 7 times higher in 2000-2006. Part of the explanation for this contrast must lie in the effectiveness of anti-poverty spending. The surge in spending in the earlier period was allocated through the *Programa Nacional de Solidaridad* (PRONASOL), a program which allocated resources mostly to basic social infrastructure and did not apply transparent and effective targeting mechanisms. As noted before, the latter period involved a massive expansion of the *Oportunidades* program, an effectively targeted and transparent CCT program introduced in 1997, as the *Programa de Educación, Salud y Alimentación* (PROGRESA).

C. **Regional poverty differences.** Despite the growing urbanization and a significant reallocation of social spending towards rural areas over the last decade (see section 3), extreme poverty is still concentrated in rural areas: between 1992 and 2006 the rural share in national extreme poverty has remained stable at around 65% (graph 3). The extreme poverty rate was 11% in urban areas (more than 15 thousand) but 42% in rural ones (less then 2500) in 2002 (Wold Bank 2005). But the differences in extreme poverty within the rural sector, between northern and southern states, are even wider (graph 4): from 6.5% in Baja California, to close to 60% in Chiapas and Guerrero.[5] The eight poorest states (Chiapas, Guerrero, Oaxaca, SLP, Puebla, Veracruz, Tabasco and Michoacán) account for 64% of the rural poor, but only 18% of agricultural GDP. The same graph illustrates a parallel division in public transfers to the rural sector: anti-poverty spending (illustrated here with *Oportunidades*) is effectively targeted to the poor, thus contributing to narrowing the regional income gap, while agricultural subsidies follow agricultural production rather than a compensatory allocation, thus contributing to widen the gap.

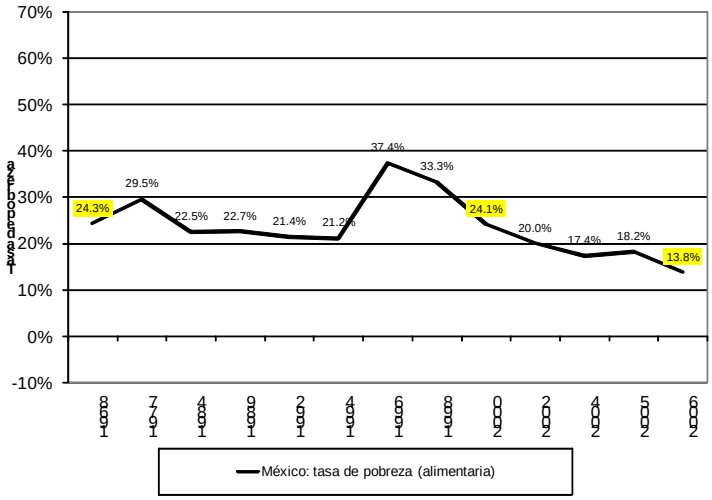
D. **Educational inequalities.** Mexico is not only affected by high levels of income inequality, but also by severe educational and health inequalities. In the case of education, Mexico presents one of the largest absolute schooling gaps between rich and poor in the LAC region (graph 4). Though the gap has actually increased over the last two decades (table 1), this reflects a rapid increase in average schooling achieved in

[5] One important caveat to these measures is that they do not take into account regional price differences, as regional consumer price indexes are not available for rural areas in Mexico. It seems likely that including regional price variations would further increase these poverty differences, as the market isolation of the smaller and more remote localities where the southern poor tend to live are likely to face higher prices.

this period, from 4.9 to 8.3 years. Relative educational inequality, measured through the schooling concentration coefficient, remained broadly flat between 1984 and 1994, but declined rapidly thereafter, following a trajectory similar to that of income inequality (graph 6). This decline is mostly explained by the rapid educational expansion, demographic dynamics and the truncated nature of the indicator, as increasingly educated cohorts enter the adult population, while the older, least educated cohorts exit it. This observation is consistent with the "educational Kuznets curves" observed in other countries as well as cross-sectionally, which tend to peak at around 6-7 years of schooling (Thomas et al. 2000). The decline in schooling inequality will thus continue with growing educational coverage, but will certainly receive a further boost as the *Oportunidades* cohorts enter the labor force over the next years.

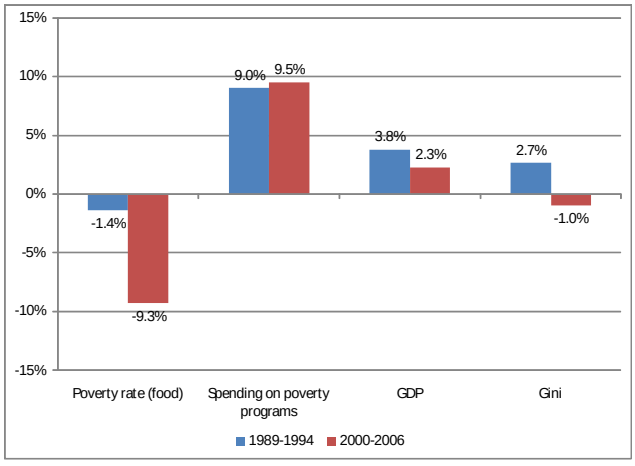
E. **Health inequalities.** Comparable international data on health inequalities are scarce, but the evidence available suggests that Mexico suffers from high inequalities in this dimension as well (Scott 2006). The national infant mortality rate (IMR) is estimated at 15 per thousand live birth in 2008, but municipal IMRs vary widely between municipalities, from 3 infant deaths per thousand live birth to 79 in 2005 (graph 7), a distance comparable to the gaps observed between the richest and poorest countries in the world. Graph 7 also reports the percentage change in IMR between 2000 and 2005. This suggests that IMR inequality has increased significantly in this period, as the rate of declines in IMR is negatively correlated with IMR and poverty. Using the same data, PNUD (2008) reports a 45% increase in municipal health inequality between 2000 and 2005, as measured by the health component of the Human Development Index. This result should be interpreted with some care, however, as the magnitude of the changes observed for the low-IMR municipalities suggests comparability problems between the two years.

GRAPH 1. EVOLUTION OF EXTREME POVERTY ("FOOD POVERTY")



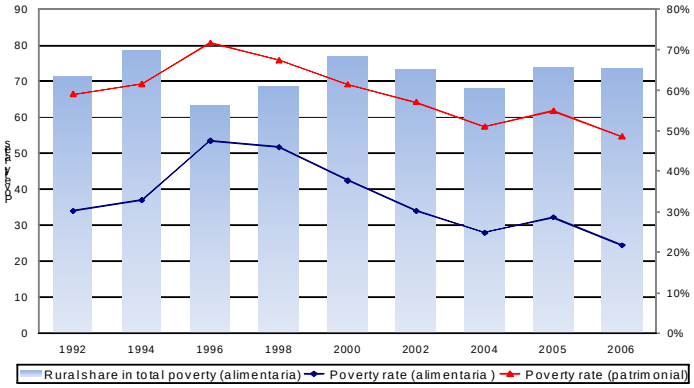
Source: Székely, M. 2003; CONEVAL.

GRAPH 2. EVOLUTION OF EXTREME POVERTY, ANTI-POVERTY SPENDING, GDP AND GINI (AVERAGE ANNUAL CHANGE)



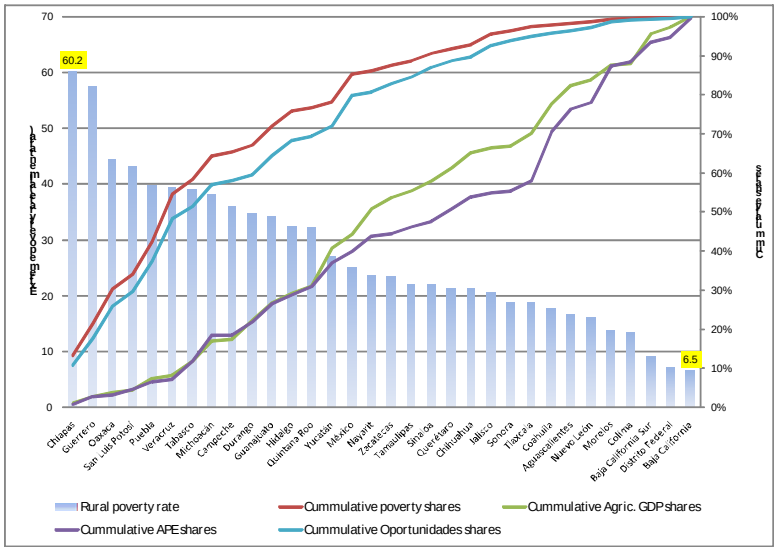
Source: CONEVAL (poverty); Anexo Estadístico del Informe de Gobierno, various years (federal spending on poverty program); INEGI (GDP); Esquivel (2008) (Gini).

GRAPH 3. EXTREME RURAL POVERTY RATES AND SHARE IN NATIONAL POVERTY: 1992-2006



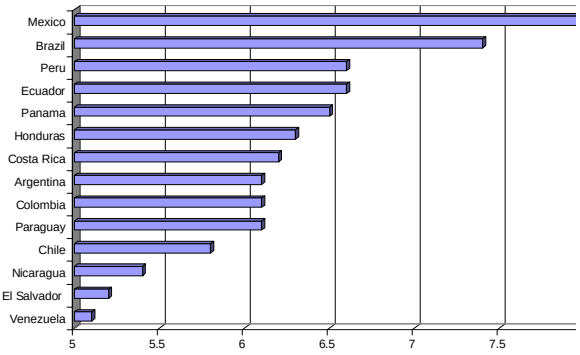
Source: CONEVAL.

GRAPH 4. EXTREME RURAL POVERTY RATES, OPORTUNIDADES, AGRICULTURAL GDP, AND AGRICULTURAL PUBLIC EXPENDITURE (APE): 2005/2006 (STATES ORDERED BY RURAL POVERTY RATE)



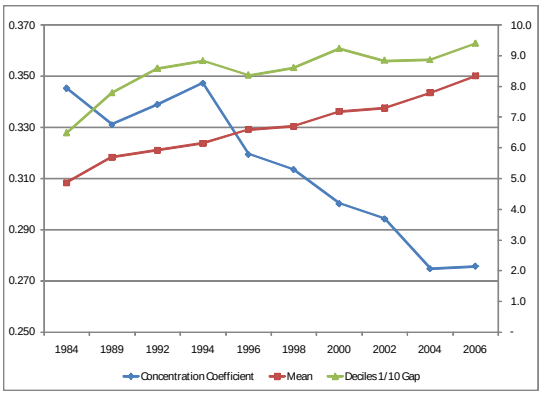
Source: CONEVAL (rural poverty); INEGI (Agricultural GDP); Cuenta Pública (ARD expenditures).

GRAPH 5. SCHOOLING GAP BETWEEN THE POOREST AND RICHEST POPULATION QUINTILE



Source: World Bank, 2003.

GRAPH 6. EVOLUTION OF SCHOOLING INEQUALITY IN MEXICO: 1984-2006



Source: Authors calculations using ENIGH 1984, 1994, 2006, INEGI.

TABLE 1. SCHOOLING INEQUALITY: 1984-2006 (ADULT POPULATION: 25-65)

	AVERAGE SCHOOLING			% CHANGE	
QUINTIL	1984	1994	2006	84-94	94-06
1	2.2	2.8	4.8	27	73
2	3.0	3.9	6.4	30	65
3	3.9	5.1	7.3	32	43
4	5.6	6.7	8.9	19	34
5	7.9	9.9	12.1	25	22
Mean	**4.9**	**6.1**	**8.3**	**27**	**36**
Concentration Coefficient	**0.345**	**0.347**	**0.276**	**1**	**-21**
Gap decile 10-1	**6.5**	**8.8**	**9.4**	**36**	**6**

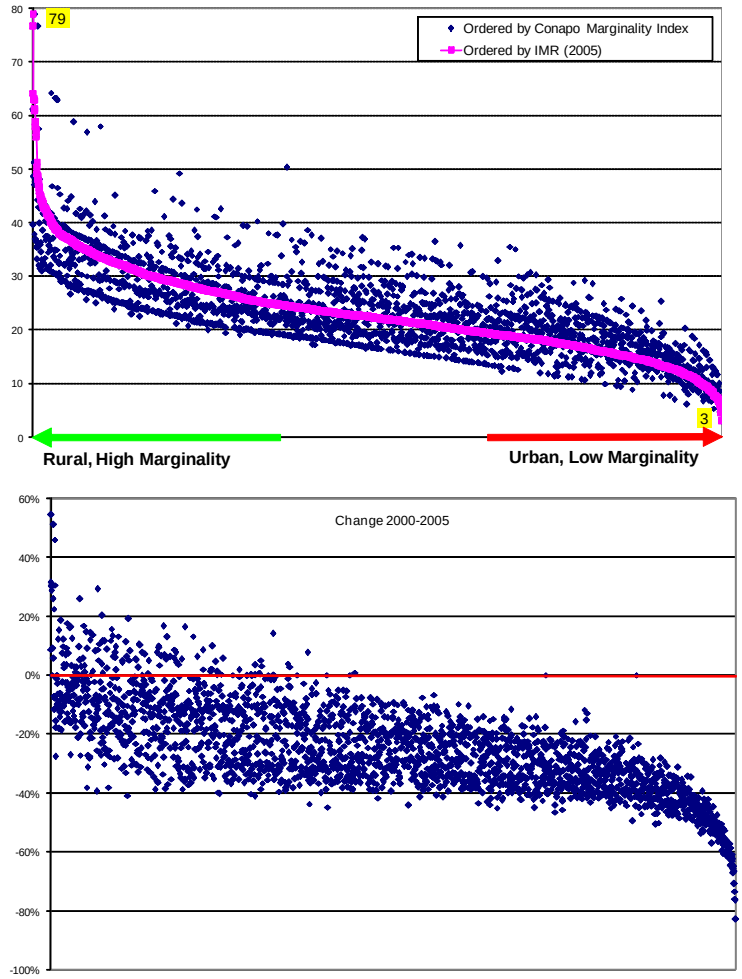
Source: Authors calculations using ENIGH 1984, 1994, 2006, INEGI. Population quintiles.

3. Redistribution: historical background and recent reforms

The (post-revolutionary) history of redistribution in Mexico may be divided into three principal chapters. The first was the agrarian reform process following the Mexican Revolution and prolonged until the early 1990's, complemented by substantial agricultural support policies and subsidies since the 1940. The second was the construction and massive expansion of the public education, health and social security systems over the second half of the 20th century. Finally, a third chapter may be defined by a cumulative series of equity and efficiency reforms on the redistributive instruments over the last two decades, including the creation of innovative targeted cash transfer instruments and increasing spending on basic education services and health services for the uninsured.

This section presents a brief historical background and reviews the recent evolution of the redistributive instruments implemented in Mexico, evaluating the changes in their distributive incidence following the recent reforms. The instruments analyzed include (in this order) agrarian reform and subsidies, education, health and social security, pensions, and food subsidies and anti-poverty programs.

GRAPH 7. INFANT MORTALITY RATES (IMR) BY MUNICIPALITIES ORDERED BY IMR AND CONAPO MARGINALITY INDEX: 2005



Source: CONAPO.

3.1. Land redistribution and agricultural subsidies: from the First to the Second Agrarian Reform

Over its long history the Agrarian Reform redistributed more than 100 million hectares —half of the country's present agricultural land— to 3.8 million producers, in the unique "social" *ejido* property system. The effect on the distribution of agricultural land was truly revolutionary (graph 8). In 1905, when some 70% of the working population was engaged in agriculture, 0.2% of these owned 87% of the land (8,431 *hacendados*), while 91% were landless (3.2 million *peones*). Today, Mexico has the lowest land concentration coefficient

(0.6) in the LAC region, comparable to the land concentration coefficients reported for East and Southeast Asia (Deininger and Olinto 2002). This distribution had been achieved by 1940, and sustained through half a century of continued land redistribution in a context of rapid rural population growth.

The agrarian reform was accompanied since the Cardenas administration, in the 1940's, by two principal forms of agricultural support: input subsidies (mostly irrigation, fertilizers, stockholding) and market price support. Up to the mid-1990s an expensive combination of market price support and general consumption subsidies aimed to support producers through a price floor on basic crops (especially corn and beans), while protecting the purchasing power of urban consumers through subsidies, especially on *tortillas*. The principal instrument for this policy was the *Compañía Nacional de Subsistencias Populares* (CONASUPO), operating between 1965 and 1999, and absorbing on average, over a quarter of a century, half a percentage point of GDP annually.

In contrast to the land redistribution, however, the latter policies where highly inequitable (as well as distorting), failing to reach in particular the millions of subsistence farmers and small-holders created by the agrarian reform. The input subsidies benefited mainly the larger, commercial farmers, while the net incidence of CONASUPO subsidies favored mostly urban consumers in the 1970's and 80´s. The big losers were the poorest of the poor, subsistence farmers and landless rural workers: as net buyers of corn they were taxed by the pricing policies, while consumption subsidies mostly failed to reach rural areas (see below, section 3.6).

It is was only towards the end of the 20th century, ninety years after the Mexican Revolution, that post-revolutionary governments actually succeeded in reaching their putative target population with direct income support. This was achieved in the context of a broad, market-orientated reform effort to modernize the agricultural sector in the early and middle nineties, which has justly been described as Mexico's "second agrarian reform" (Gordillo et al. 1999). This included, along with the formal end of the Agrarian Reform, the constitutional reform of the *ejido* land tenure system (1992) designed to liberate agricultural land markets, and the opening up of agricultural commodity markets under the *North American Free Trade Agreement* (NAFTA) introduced in 1994, with a long transitional period in the case of agricultural products, culminating with the full liberation of maize, beans, sugar and milk powder in 2008. These market reforms were accompanied by a number of innovative program reforms, introducing more efficient as well as equitable instruments. Farmers were compensated for the reduction of market price support through three principal programs: a) the *Programa de Apoyos a la Comercialización,* an output-based subsidy program introduced in 1991, functioning as a deficiency payment program, *Ingreso Objetivo*, since 2003, b) the *Programa de Apoyos Directos al Campo* (*PROCAMPO)*, a per hectare direct transfer program decoupled from production and commercialization,

introduced in 1994, and c) *Alianza para el Campo,* an investment support program (or family of programs) offering matching grants and support services, introduced in 1996.

The expectation was that these programs would not only play a compensatory role in the face of growing external competition but, in the case of *Procampo* and *Alianza*, would also provide the necessary support for farmers to modernize production and switch to higher value crops in the newly liberalized land and product markets. In the context of Mexico's earlier (and current) agricultural support policies, the decoupled design of *Procampo* made this program highly innovative in terms of efficiency as well as equity. By delinking transfers from production/commercialization, the program was not only expected to minimize distortions in productive decisions, but also to transfer income to subsistence farmers.

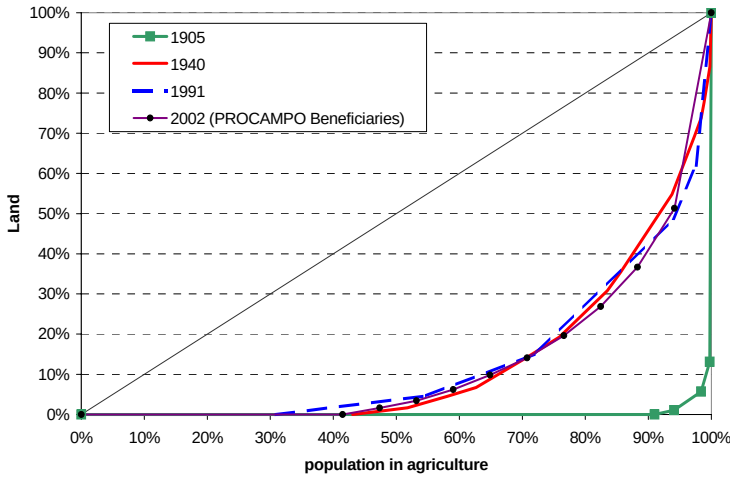
Despite this belated achievement, agricultural subsidies overall are still among the most regressive programs implemented in Mexico. Graph 9 presents concentration curves for the principal agricultural subsidies in 2006, ordering producers by the size of their land-holdings (Scott 2008a). These reveal extreme concentrations of benefits for all programs. The richest 10% of producers (in terms of land) receive the following shares of the principal programs' transfers:

a. 45% of Procampo,
b. 55% of Programa de Desarrollo Rural- Alianza para el Campo,[6]
c. 60% of energy and hydrological subsidies (proxied through the distribution of irrigated land), and
d. 80% of Ingreso Objetivo.

The latter assessment may be generalized to agricultural support spending overall, which represents 11% of all redistributive spending as classified in the present study (see table 6). The concentration curve for agricultural land can reasonably be interpreted as an *upper bound* for the concentration curves of *non-targeted, input- or output-linked support programs,* generally. A large part of the rural population (at least the poorest 50%) is excluded from such programs simply because they are landless or have plots which are too small to be reached by such programs (except for a decoupled program like Procampo), and in the upper half of the land distribution there are probably strong economies of scale in the capacity to attract agricultural support resources (unless some explicit targeting is applied, as in the case of *Alianza's Programa de Desarrollo Rural*).

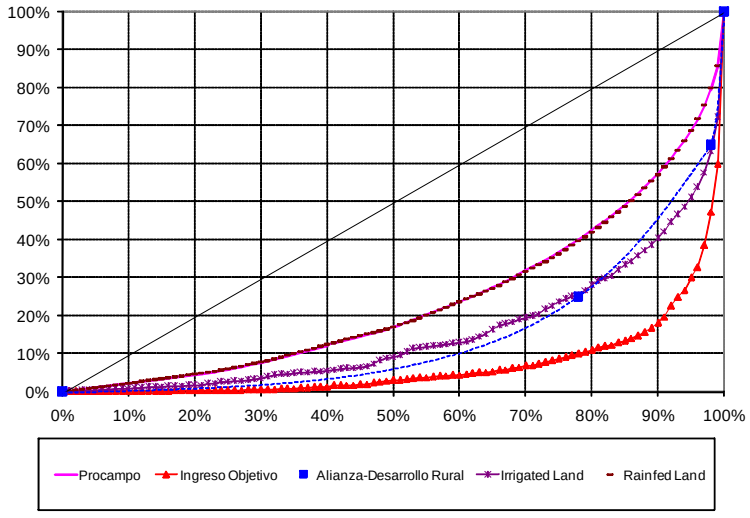
[6] *Alianza para el Campo* was introduced in 1996 as a grouping of the principal productive and investment support programs, through matching grants. The *Programa de Desarrollo Rural* is the only component of the program which is formally targeted to the poor, according to its operation rules, but the evaluation data of the program reveal a failure to reach these groups (Scott 2007).

GRAPH 8. LAND CONCENTRATION CURVES: THE MEXICAN REVOLUTION AND AGRARIAN REFORM



Sources: author's calculations based on tabular results from the 1905, 1940, and 1991 Agricultural Censuses and PROCAMPO's Beneficiary Register (the latter as reported in Székely 2003, table 5).

GRAPH 9. PROCAMPO, INGRESO OBJETIVO, ALIANZA (DESARROLLO RURAL), AND LAND CONCENTRATION CURVES: 2006



Source: Scott (2008a), using the ASERCA beneficiary database, FAO (2005) and World Bank (2006).

3.2. Social spending growth and cycles

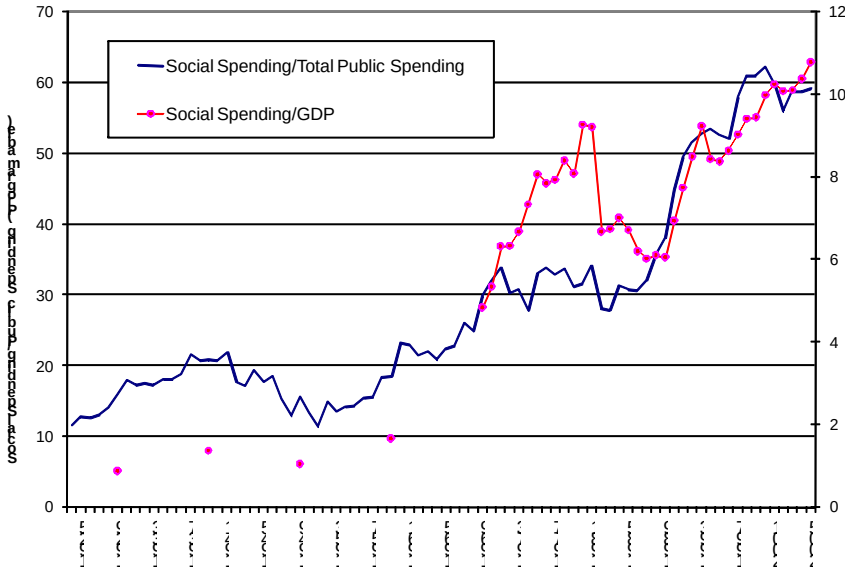
Social spending barely surpassed 1% of GDP in the first half of the 20th century, but surged rapidly in the second with the construction and expansion of the public education, health and social security systems,[7] reaching 9% of GDP by the beginning of the 1980's (graph 10). It then collapsed by 30% in the aftermath of the 1982 debt crisis and ensuing fiscal adjustment process, regaining pre-crisis spending levels only by the turn of the century. The latter recuperation was not achieved through an increase in Mexico's fiscal capacity, as a relevant tax reform has remained elusive up to the present, but through a shift in the allocation of fiscal resources to social programs, doubling their share of the public budget from 30 to 60% in the course of the 1990s.[8] The growth of social spending over the last two decades was interrupted by two further, though milder, economic downturns, caused by the 1995 "tequila" crisis and the 2001-2002 US recession, respectively. A pro-cyclical behavior of social spending is evident in the cuts to social spending even as a share of public spending observed in each of these periods.

In addition to the overall growing trend of social spending over the 1990's, a number of important policy and program reforms were introduced in that decade, achieving significant improvements in the equity and efficiency of this spending. The growth of social spending up to the early eighties was absorbed principally in "universal" education and health services and "generalized" consumption subsidies. However, far from achieving a wide and neutral coverage, as these terms might suggest, the incidence of these programs was highly regressive and urban-biased, as revealed in the following sections.

[7] The two principal institutions of social security, the *Instituto Mexicano del Seguro Social* (IMSS) and the *Instituto de Seguridad y Servicios Sociales de los Trabajadores del Estado* (ISSSTE) were created in 1944 and 1959, respectively.

[8] Here, as elsewhere in this article, "public spending" is used to refer to the concept of *gasto programable*, which is public spending *net of debt payments and mandatory tax shares to the states*, and represents the most relevant measure to compare federal budgetary commitments between programs.

GRAPH 10. EVOLUTION OF SOCIAL SPENDING: 1925-2006



Source: Historical Statistics and National Accounts, INEGI; Public Accounts, SHCP.

3.3. Education

The allocation of public spending in the 1970's and 1980's was heavily biased towards higher education. Following the 1968 student revolt in Mexico City, over the 1970's the share of educational spending allocated to upper-secondary and tertiary education grew from 20 to 42% while the share of spending on basic education contracted by an equivalent amount, despite an expansion in enrollment in public basic education from 9.7 to 16.5 million students. The impact on spending per student in basic education was aggravated in the 1983-1988 adjustment period, as the latter educational level absorbed a disproportionate share of budgetary cuts. This bias was reversed with the change in administration after 1988, with an increasing reallocation of educational spending towards basic education.[9] Between 1992 and 2002 spending per student expanded in real terms by only 7.5% in the case of tertiary education, but by 63% in the case of primary education. The relative ratio of spending per student in tertiary vs. primary education thus declined from a historical maximum factor of 12 times in 1983-1988, to less than 6 in 1994-2000 (for a reference, the OECD average is close to 2).

[9] This policy change may perhaps be explained by the incorporation of Pedro Aspe as Finance Minister in the 1989-1994 (Salinas) administration, co-author of a mayor study identifying inequities in educational spending in the 1970s and early 1980´s, which concludes: "The greatest significance of this study is a negative one: the educational and health policies have not been corrective and have not diminished the disparity in income, but have, on the contrary, confirmed and reaffirmed these conditions." (Aspe and Beristáin 1984, 323).

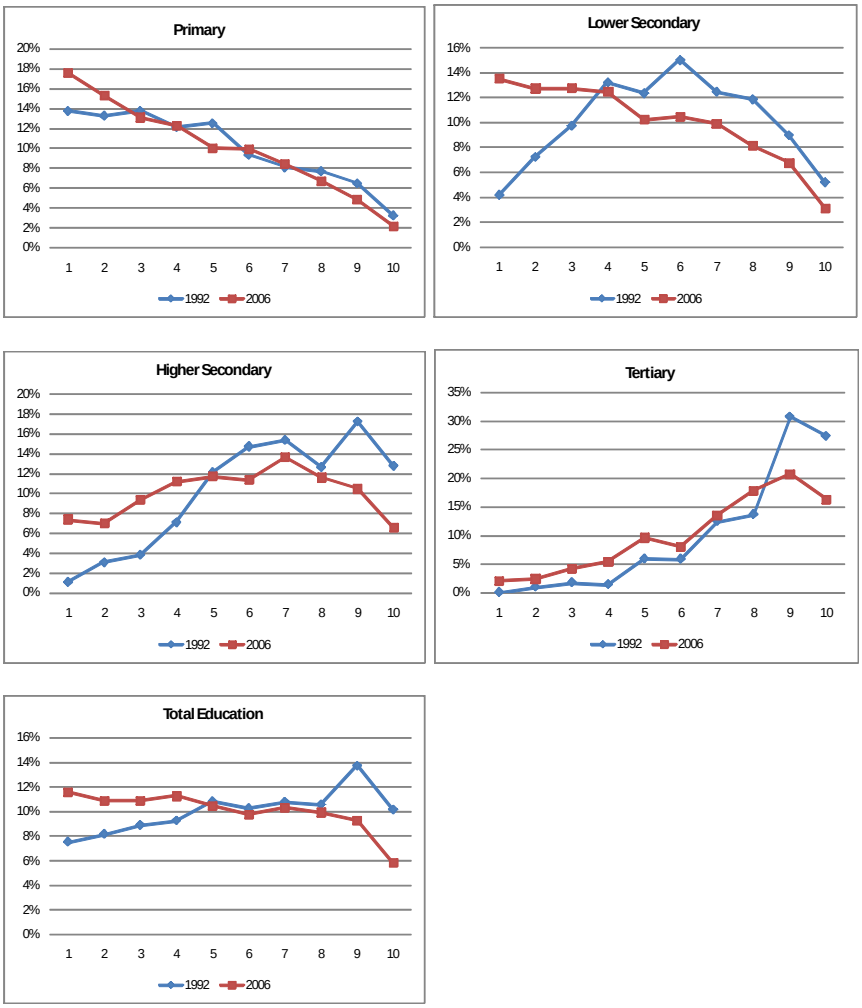
In addition to the budgetary allocation between educational levels, progressivity in educational spending was constrained by the limited use of post-primary public education services by the poor, even when these are fully subsidized. This is explained by supply (limited availability of secondary schools in rural areas) as well as demand constraints (high opportunity cost of even basic education aged children in poor rural households). Both of these factors where addressed in the 1990's through the expansion of basic education facilities and, most notably, PROGRESA's direct monetary transfers to poor rural households conditional on participation in basic education and health services.

The effect of these reforms may be observed in graphs 11 and 12, which presents the participation by income-ordered population deciles in the use of public education services at each level, as well as the implied distribution in total education spending, comparing in each case the distributions for 1992 and 2006. Combining the budgetary and participation effects, the distribution of total public spending on education has changed qualitatively over the decade, from (mildly) regressive to progressive in absolute terms, with the poorest decile obtaining a share of educational spending twice as large as the richest one. All levels have became more progressive (less regressive), but the most important change is observed in the case of lower secondary education. This is explained by at least three factors: a) most importantly, the dynamics of educational expansion: as full coverage of primary education of the relevant age group was achieved by the early 1990s, even among the poor, these cohorts were at least formally qualified to access the next level; b) the conditional scholarships of Progresa/Oportunidades, with increasing payments to lower secondary students and upper secondary education (since 2001); and, less encouragingly, c) public education at the basic level (and higher secondary education from the 7^{th} decile) are progressive in part because higher-income groups opt of private services, because they are perceived to be of better quality (as is confirmed by standardized evaluation surveys). In other words, public spending on basic education is progressive in part because it is self-targeted through low quality. An immediate corollary is that efforts to improve the quality of public education would, if successful, would necessarily be so at the cost of equity, unless accompanied by explicit geographic or administrative targeting.

Access to tertiary education, on the other hand, is still highly regressive, only slightly improving since 1992. The participation of the poorest quintile is insignificant, and among the lowest in the region (Scott 2002b). As in the case of secondary education, this is slowly improving and should be expected to increase in the future simply as a consequence of advancing coverage in the earlier cycles. But there are two further constraints explaining the failure to reach the poor which will require decisive policy reforms to make this potential demand effective. First, the high opportunity cost of tertiary

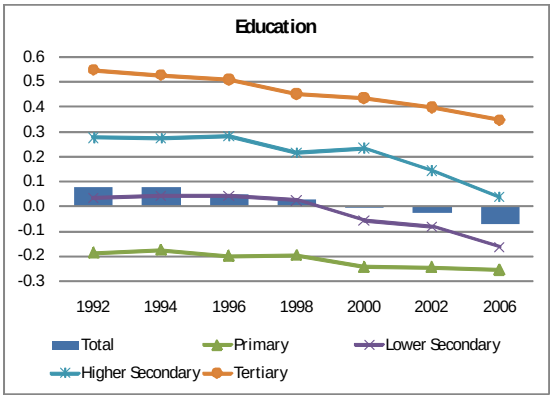
education will require a reform in university financing, targeting public subsidies to the poor through scholarships or educational credits, rather than simply offering free tuition to middle- and upper-income groups. Secondly, however, the poor are also barred from public university through the low quality of their pre-university education, as they have to compete for scarce university places with students from private schools. Increasing the quality in addition to the quantity of upper secondary education opportunities for the poor is therefore also required to improve equity at the tertiary level.

GRAPH 11. DISTRIBUTION OF BENEFITS FROM PUBLIC EDUCATION (POPULATION DECILES ORDERED BY PRE-TRANSFER INCOME PER CAPITA)



Source: author's calculations using ENIGH 1992, 2006.

GRAPH 12. EVOLUTION OF CONCENTRATION COEFFICIENTS EDUCATION: 1992-2006



Source: author's calculations using ENIGH 1992-2006.

3.4. Health and Social Security

Mexico has a highly segmented public health system, with contributive social security serving formal sector workers and non-contributive services provided by the state and federal Health Ministries (SSA) serving the uninsured. Social security is in turn fragmented into three groups of institutions, with sharply differentiated benefits: a) the *Instituto Mexicano del Seguro Social* (IMSS) serving formal sector workers, b) the *Instituto de Seguridad y Servicios Sociales de los Trabajadores del Estado* (ISSSTE), serving public sector workers, and c) a number of specialized systems covering public sector workers in state companies (including PEMEX, the electricity companies, and IMSS) the armed forces, the judiciary, etc.

The principal sources of inequality in public spending on health and social security arise from three historical characteristics of these systems: a) the truncated and regressive coverage of the formal (contributive) social security institutions, b) the gap in total public spending per beneficiary and in tax-financed subsidies, between the formally insured and the uninsured, as well as between the different social security institutions, and c) demand and supply restrictions on the use of public health services for the uninsured.

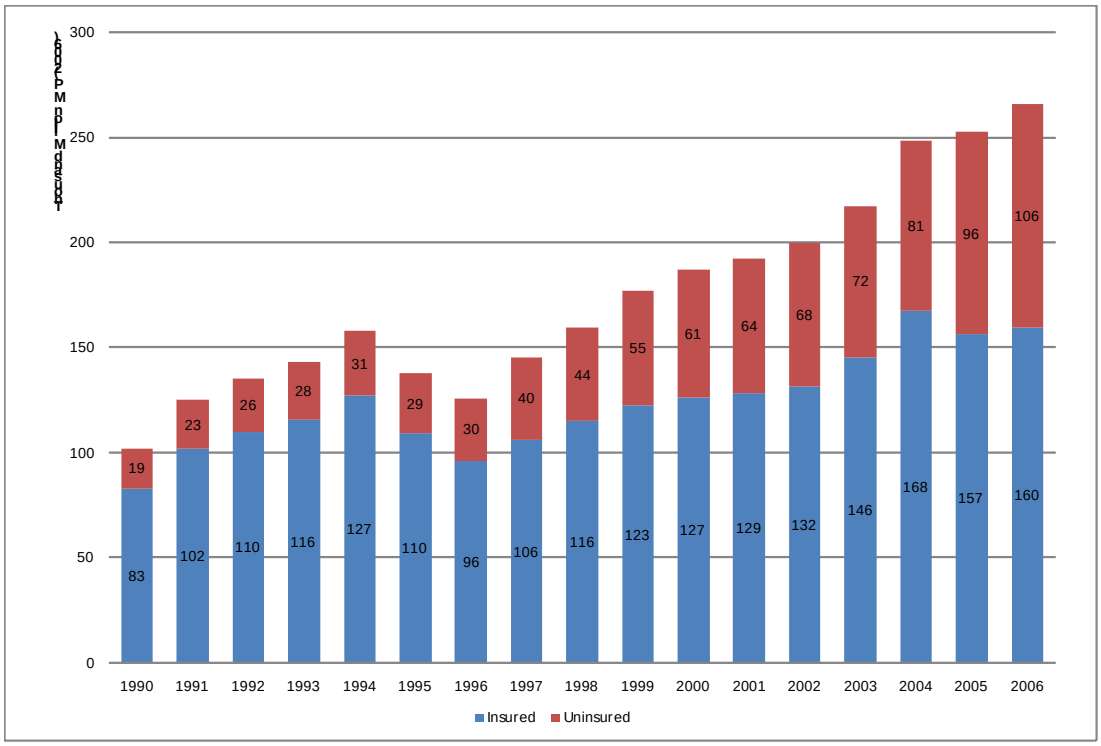
Considering public health and non-health components of social security together, during 1970-2000 total spending by the principal social security institutions (IMSS, ISSSTE) represented on average 87% of total public health and non-health social security spending, and 56% of tax-financed spending. On average, public spending per beneficiary on the insured in 1970-1990 was 11 times higher than on the uninsured, and tax-financed spending allocated per insured was *twice* as high.

Considering health services only, the gap in financing between insured and uninsured narrowed significantly over the last decade (graph 13). Between 1996 and 2006 public health spending by the social security institutions increased by 66% in real terms, but public health spending on the uninsured (federal and state) increased by 257% (SSA, Cuentas Nacionales y Estatales de Salud, 2008). The share of total public health spending allocated to the uninsured, which represent roughly half of the population, has thus doubled over the decade from 20 to 40%. At the same time, the progressivity of health spending on the uninsured has increased significantly, as the poor have dramatically increased their use of these services (graphs 14 and 15). Both of these changes are explained by an ambitious and ongoing effort to expand health coverage for the formally uninsured, through a) an expansion of health facilities in rural areas (*Programa de Ampliación de Cobertura*, PAC, launched in the mid 1990's), b) the health component of the *Progresa/Oportunidades* program (which, as in the case of education, is conditional on the use of health facilities), and finally c) the creation and rapid growth since 2003 of the *Seguro Popular*, a new and ambitious health insurance scheme programmed to achieve universal basic health coverage for the uninsured by 2010.[10]

That the latter developments have nevertheless failed to make total public health spending progressive is explained by the fact that public health spending on the insured is still 50% higher than spending on the uninsured, and social security has failed dismally to penetrate to the rural poor (graph 14).

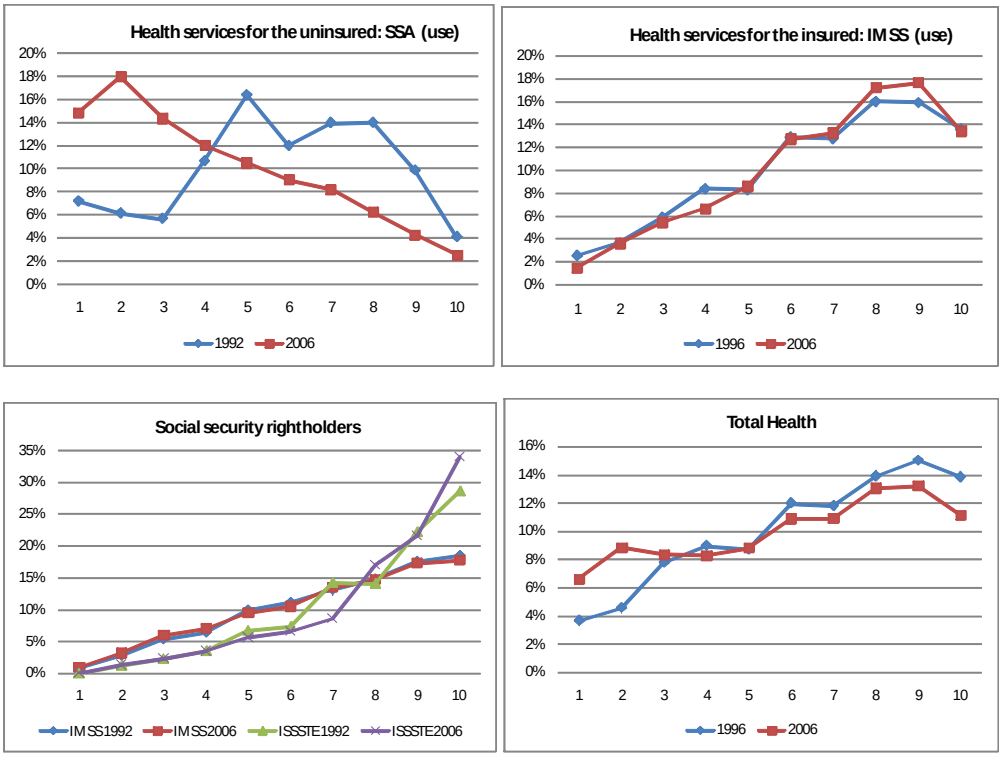
[10] The *Seguro Popular* was launched as a pilot in 2002, but formally established (as the *Sistema de Protección Social en Salud,* SPSS) through the 2003 reform of the *Ley General de Salud* (LGS). The LGS specifies a 14.3% annual coverage growth rate, from 2004 to 2010. As such, the SP represents the most ambitious effort to expand the coverage of basic health protection since the creation of the National Health System in 1943. In 2007 the SPSS spent 34.6 billion MP, 26 from federal resources, 8.4 from state spending, and 0.2 from family contributions. At the end or that year, it had incorporated 7.29 million families (21.9 million persons), more than half of its final coverage target, currently estimated at 12.9 million families (CNPSS 2008). This coverage includes the *Seguro Médico de Nueva Generación*, an initiative introduced by the present administration offering SP access to all families with children born since December 2006.

GRAPH 13. TOTAL FEDERAL AND STATE PUBLIC HEALTH SPENDING IN MEXICO: 1990-2006 (BP 2006)



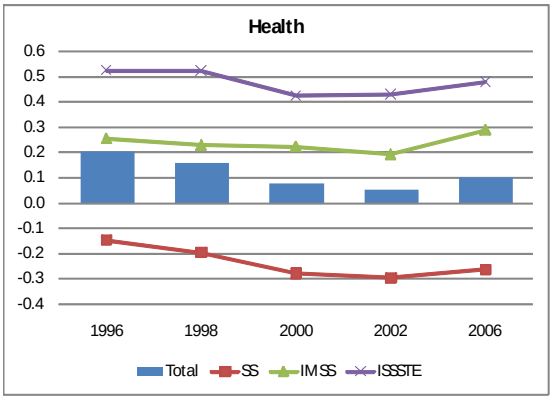
Source: Cuentas Nacionales y Estatales de Salud, Secretaría de Salud.

GRAPH 14. DISTRIBUTION OF BENEFITS FROM PUBLIC HEALTH SPENDING (BASED ON USE OF SERVICES) (POPULATION DECILES ORDERED BY PRE-TRANSFER INCOME PER CAPITA)



Source: author's calculations using ENIGH 1992, 1996, 2006.

GRAPH 15. EVOLUTION OF CONCENTRATION COEFFICIENTS FOR PUBLIC HEALTH SPENDING: 1992-2006



Source: author's calculations using ENIGH 1996, 1998, 2000, 2002, 2006.

3.5. Pensions

The degree of segmentation and inequality is most extreme in the case of pensions. In contrast to what is observed in the mature welfare states, where public pensions tend to be among the most redistributive transfers, pensions in Mexico contribute to increase income inequality: the ratio between the total average per capita income of the richest and poorest decile is 28:1, but if we consider only pension income it is 287:1.[11] The truncated coverage of social security is aggravated in this case by two factors.

First, in contrast to health, where services for the uninsured coexisted with social security for most of the past century, and as just documented are now converging to the latter financial terms, Mexico has until very recently lacked non-contributive old-age pension programs in any form. This has changed only in the last three years, with the introduction of a basic universal old-age (70+) pension in Mexico City in 2005 and the subsequent introduction of federal non-contributive pension programs in rural communities, in 2006 as a modest (US$ 25 per month) targeted program linked to *Oportunidades*, and since 2007 through a more generous (US$ 50 per month) and universal rural pension program (*Atención a los Adultos Mayores en Zonas Rurales*). Despite this rapid expansion from zero, public spending on non-contributive programs still lags well below the average spending levels on such programs observed in the region (table 2).

Secondly, the segmentation of the different pension systems within the insured entails a high degree of vertical and horizontal inequality in the allocation of subsidies to these systems. Total public subsidies to the pension systems in Mexico are in the order of 1.5% of GDP (Scott 2005). A tenth of these resources correspond to government contributions to workers' individual accounts arising from the 1997 reform of the IMSS pension system (from the old PAYG system to a defined contributions system with individualized accounts). The other 90% is divided almost equally between current obligations under the old IMSS regime (which have been completely absorbed by the federal government), and the deficits of the principal public-sector pension systems, ISSSTE and State enterprises (IMSS, PEMEX, electricity utilities, etc.). The first of these components is bounded and represents a transitional cost of the reform, though obligations will keep growing in the medium run. A reform for ISSSTE has recently been approved similar to the IMSS reform, except for more generous terms to ISSSTE right-holders (and thus a higher public subsidy per beneficiary). In the absence of similar reforms, subsidies to the State enterprise pension systems are in increasing and

[11] Scott (2005). The decomposition analysis in Esquivel (2008) shows that pensions are the most unequal component after (but almost equal to) property income, with a Gini of 0.98 in 2006.

unbounded growth trajectories, fiscally unsustainable even in the medium run.

To appreciate the degree of horizontal inequality in the allocation of public subsidies to the different pension systems,[12] table 3 compares the average monthly subsidies per pensioner. Compared with IMSS, even considering the full transitory financing of the pension obligations under the old regime, the subsidies per pensioner are 1.6 times higher in ISSSTE, and between 4 and 8 times higher in the state enterprises. The three state enterprises considered here represent 8% of all pensioners, but absorb almost a third of the total pension subsidies (World Bank 2004). As in the old IMSS regime, these deficits may be due in part to demographic forecasting errors, design errors, or administrative failures. The differences also reflect, in part, higher salaries of public sector workers. But the size of the differences between private and public sector pensioners is largely due to privileged contractual conditions negotiated (captured) opaquely within the old corporative regime. For example, private sector workers in IMSS retire at 65 with average expected replacement rates in the order of 40-50% (in the 1997 regime), while public sector workers can retire, in general, ten years earlier, with replacement rates close to a 90-100%, and even higher in the State enterprises. In the specific case of the workers *hired* by IMSS, these retire on average at 53 (there is no minimum) with an average replacement rate of 130% —generating a financial burden which puts the viability of the health services provided by the institute at risk (IMSS 2007).

To appreciate the full spectrum of public pension subsidies, table 3 also reports the recent non-contributive pension programs, revealing a *hundred-fold* difference between the lowest and highest pension subsidies per beneficiary.

[12] "Public subsidies" here means the costs of the pension obligations *net of contributions* by workers and employers, financed through general tax revenues, and/or in the case of the State companies like IMSS and the electricity utilities, by diverting own resources (from the sale of electricity and private sector worker/employer contributions) from the provision of public services/utilities to the financing of pension deficits (see IMSS 2007).

TABLE 2. PUBLIC SPENDING ON NON CONTRIBUTIVE PENSIONS (% GDP)

MEXICO	
2006	0.03
2007	0.06
2008	0.1
BRAZIL	1.3
BOLIVIA	0.9
CHILE (AFTER 2007; ESTIMATE FOR 2025)	0.8
CHILE (BEFORE 2007)	0.4
URUGUAY	0.6
COSTA RICA	0.3
ARGENTINA	0.2

Sources: Mexico: PEF 2006, 2007; Programa de Atención a los Adultos Mayores de 70 Años y Más en Zonas Rurales, 2º Informe Trimestral 2008. Other countries: Gill et al. 2004.

TABLE 3. AVERAGE MONTHLY PUBLIC PER BENEFICIARY (PENSIONER) (NET OF ACTIVE WORKER CONTRIBUTIONS)

	PESOS	% IMSS
LUZ Y FUERZA (2003)	17,556	834
IMSS-PATRÓN (RÉG. DE JUBILACIONES Y PENSIONES, 2004)	12,552	596
PEMEX (2003)	8,250	393
ISSSTE (2003)	3,281	156
IMSS (PENSIONS DUE UNDER PRE-1997 SYSTEM)	2,105	100
ATENCIÓN A LOS ADULTOS MAYORES EN ZONAS RURALES (2007, 2008)	500	24
APOYOS PARA ADULTOS MAYORES EN OPORTUNIDADES (2006)	250	12
ATENCIÓN A LOS ADULTOS MAYORES EN ZONAS RURALES (2005)	175	8

Source: World Bank (2004b), IMSS (2005), Tercer Informe del Gobierno (2003), Rules of Programs.

3.6. Food subsidies and anti-poverty programs

As reviewed above (section 3.1), the price support policies on basic crops operated in Mexico between the 1940's and the 1990's (through CONASUPO) were complemented on the demand side with generalized subsidies designed to protect the purchasing power of urban consumers. These became unviable in the early 1990s, when the internal price of corn was 70% above international prices, and the *tortilla* subsidy —which had been cut back after the 1983 crisis— was insufficient to compensate urban consumers for this differential. The generalized (urban) consumer subsidy was gradually replaced by targeted tortilla (Tortibonos) and milk (Liconsa) subsidies, but these were

costly to operate, still urban, and not effectively targeted even within the urban sector (table 4). The general *tortilla* subsidy (and CONASUPO) was finally eliminated in 1998, and most food subsidies were reallocated to rural areas through the *PROGRESA/Oportunidades* program, whose food component became the principal food aid program in Mexico.

Table 4 compares the targeting efficiency of the general and targeted tortilla and milk subsidies, with Progresa/Oportunidades and, for reference the *Programa de Empleo Temporal* (a self-targeted rural work-fare program introduced in 1995) and an average for targeted programs in the LAC region (Grosh 1994). Given Mexico's income distribution, the distribution of spending on even basic necessities like tortillas and milk turns out to be regressive in absolute terms. Thus the poorest population quintile obtained just 4 and 12% of the generalized milk and tortilla subsidies, respectively. Targeting efficiency was improved modestly through the Liconsa and Tortibonos programs to 8.5 and 17.3%, respectively, but increased to almost 60% through Progresa.

To appreciate the effect of this reallocation, graph 16 compares the regional distribution of all food aid spending with the distribution of undernourished children (low height/age) before and after the reallocation. In 1988, 70% of food subsidies were concentrated in Mexico City, where only 7% of undernourished children were located, while only 7% of these resources reached the Southern states, which accounted for 50% of undernourished children. By 1999, the distribution of food subsidies was in line with the regional distribution of undernourished children in the country, with remarkable regional targeting accuracy. The effect of these reforms was an increase in the rural share of food subsidies from 31 to 76% by official estimates (1994-2000),[13] or from 40 to 55% using ENIGH (2002).[14]

Graph 17 presents the same comparison considering the distribution at the household level. In just half a decade, the reallocation of food subsidies through *Progresa* transformed a broadly neutral distribution into a highly progressive one, with the share benefiting the poorest decile increasing from 8 to 33%.

In addition to Progresa's direct impact on the allocation of food subsidies and its indirect but no less significant impact on the allocation of education and health services, the introduction of this CCT program represented a mayor innovation in anti-poverty transfers. Together with the self-targeted *Programa de Empleo Temporal* (PET), Progresa was the first (accountably) effectively targeted anti-poverty program implemented in Mexico. The concept of targeting itself, as an explicit category reported separately from "universal" spending, was introduced in official budgetary statements only in the mid 1990's. Table 5 reports the evolution of targeted spending, as

[13] SHCP (2000).
[14] Scott (2004).

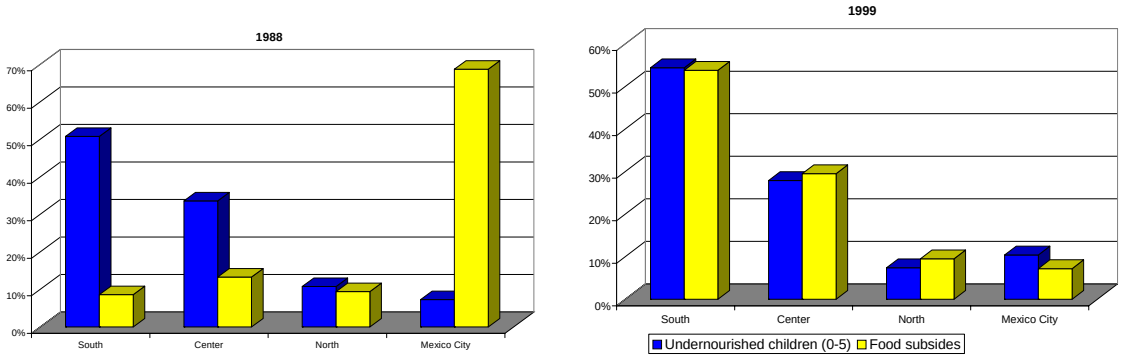
classified in annual government reports. Though this spending has increased over the last two decades, it still represents a relatively small fraction of redistributive spending. More importantly, as shown in the following section, only a fraction of this spending is *effectively* targeted to the poor.

TABLE 4. TARGETING COST-EFFICIENCY OF SELECTED FOOD SUBSIDIES

	Objective Population (OP)	Progresa/ Oportunidades	Milk subsidy		Tortilla subsidy		Programa Empleo Temporal (PET)	Average for targeted programs in LAC[a]
			Targeted (Liconsa)	General	Targeted (Tortibono)	General		
% of transfer received by OP	20%	64.9%	12.2%	4.3%	20.0%	12.3%	65.8%	
	40%	89.0%	35.4%	15.7%	62.4%	33.6%	86.0%	72.0%
Administrative costs		8.2%[b]	28.5%[a]	5%	12%[a]	5%	4%[c]	9.0%
Participation costs		2%[b]	2%	0%	2%	0%	50%[c]	2.0%
Share of spending benefiting OP	20%	58.3%	8.5%	4.1%	17.3%	11.7%	31.6%	
	40%	80.1%	24.8%	14.9%	53.8%	31.9%	41.3%	64.2%
Cost per transfered peso ($)	20%	1.7$	11.7$	24.5$	5.8$	8.6$	3.2$	
	40%	1.2$	4.0$	6.7$	1.9$	3.1$	2.4$	1.6$

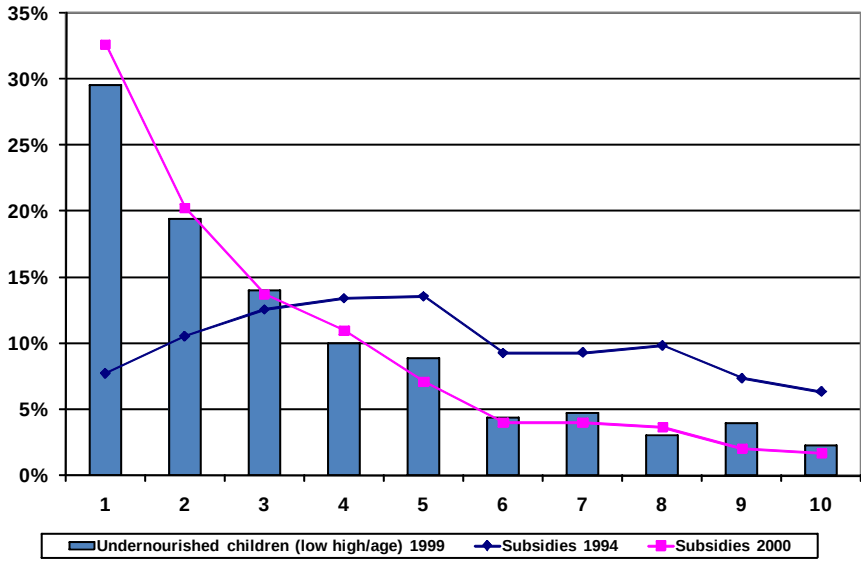
Sources: own calculations based on Módulo Social ENIGH 2002, and data form [a]Grosh (1994), [b]Coady (2000), and [c]Scott (2004). Numbers in italics are assumed.

GRAPH 16. REGIONAL DISTRIBUTION OF FOOD AID AND UNDERNOURISHED CHILDREN (LOW HEIGHT / AGE)



Source: Scott (2002a), using the 1988 and 1999 EncuestaNacional de Nutrición.

GRAPH 17. DISTRIBUTION OF FOOD SUBSIDIES AND UNDERNOURISHED CHILDREN (LOW HEIGHT / AGE) BY PER CAPITA INCOME-ORDERED POPULATION DECILES (% SHARES IN TOTAL SUBSIDY)



Source: Scott (2004), using the 1988 and 1999 Encuesta Nacional de Nutrición.

TABLE 5. SPENDING ON TARGETED PROGRAMS

YEAR	% GDP, BASE:		% PUBLIC SPENDING
	1993	2003	
1990	0.7		4.6
1995	1.1		6.2
2000	1.2	1.1	6
2005	1.5	1.3	8.4
2006	1.5	1.4	8.5
2007	1.6	1.4	8.3
2008		1.8	10.9

Source: Segundo Informe de Gobierno, Presidencia de la República (2008).

4. Redistribution: comparative and global incidence of current redistributive public spending: 2006-2008

This section presents a comprehensive comparative and global benefit incidence analysis for the principal redistributive instruments implemented in Mexico at present using the most recent survey information available (2006), but extended to the most recent changes in redistributive spending (2006-2008). These instruments include all public education and health spending, including state as well as federal spending, and all public spending on social security, and energy and agricultural subsidies, as well as the principal targeted programs (table 6), a total of 25 programs or specific spending categories. The public expenditures covered represents close to US$ 100 billion, 10% of GDP, 15% of disposable household income, 60% of total public spending, and 80% of social spending. The analysis focuses on federal spending, except in the case of education and health, where state spending is included as well (including state spending financed through tagged federal transfers, untagged federal revenue shares, and own fiscal revenue).

The distribution of each instrument is grouped in population deciles ordered by total current income per capita before taxes and transfers (pre-fiscal), and the degree of absolute progressivity is measured with concentration coefficients (CC). The principal data source for the analysis is the 2006 ENIGH household income and expenditure survey. In addition to being the most detailed source for household income available in Mexico at present (September 2008), this survey reports the principal monetary public transfers, the use of public education and health services, right holders to social security, and spending on electricity. With the exception of *Oportunidades*, the targeted programs included in the analysis are obtained from a special module on social programs commissioned by the Social Development Ministry as part of the 2004 ENIGH. The distribution of agricultural public expenditures, and in particular *Procampo* and *Ingreso*

Objetivo, are obtained from the administrative beneficiary data base, and reported as producer deciles ordered by the extension of land holdings.[15]

Public spending data is obtained from the *Public Accounts of the Federation* for the relevant years, and in the case of health the *National and State Health Accounts* published by the Health Ministry (education state spending is estimated from federal per student spending rates and the coverage of state financed schools reported by the Education Ministry). As is common in household income surveys, total household income in ENIGH tends to be underreported by a large margin (a factor of 1.87 in 2006) when compared to the closest equivalent concept in the *National Accounts*. To estimate the incidence and redistributive effect of public transfers it is necessary to ensure comparability between public transfers obtained from the Public Accounts and private income reported in ENIGH, so the latter data is adjusted to ensure consistency with the National Accounts, and both adjusted and unadjusted incidence estimates are reported.

Finally, though this study did not include a tax incidence analysis, tax incidence estimates by the Finance Ministry (SHCP, 2008) are used to obtain net benefits. The latter uses the same data base (ENIGH) and applies the same methodology as the spending incidence analysis reported here, so the tax and transfer incidence estimates are comparable.

Table 6 presents the total magnitudes for public transfers, taxes and household income. The present analysis distinguishes between transfers in kind and monetary or cuasi-monetary transfers, where the latter are tagged to consumption of basic goods, but close substitutes of beneficiaries' spending commitments, thus allowing households to free up general purchasing power of a value approximately equivalent the subsidized good. These include food and energy subsidies, as well as input subsidies to agricultural producers. Transfers in kind, on the other hand, which include mainly education and health services, may be highly valued by some (though not all) beneficiaries, but are non-tradable, highly labor-intensive, depend for access on locally available infrastructure, and are thus highly variable in quality. One implication relevant for the present analysis is that the gap between the public cost of the transfer, and the monetary benefits to recipients, is likely to be larger in latter than in the former case. Another is that the low quality of services may act as an implicit, but effective, self-selection targeting mechanism.

[15] The inclusion of the latter results with the ENIGH-based estimates is justified on the assumption that the size of land-holdings is positively correlated with income. The only agricultural subsidy reported in ENIGH is Procampo, but the survey is not designed to report the distribution of this program accurately: a large fraction of Procampo's benefits are concentrated on a small group of producers at the top end of the land and income distribution. The ENIGH survey is particularly poor at capturing income at the top end of the distribution, for well-known reasons of small samples and problems of underreporting (see footnote 4, above) and therefore significantly underestimates the concentration of Procampo transfers.

Transfers in kind, in this narrow definition, represent 69% of transfers, of which 40 and 25 percentage points correspond to education and health services, respectively, and the rest to agricultural services. After these the largest category are generalized consumer subsidies (energy subsidies and VAT exemptions principally on food and medicines[16]), followed by agricultural and pension subsidies. The targeted programs analyzed here represent just 4% of total transfers (5% including *Seguro Popular*).

Comparing the concentration coefficients for all programs (graph 18) reveals a wide range of coefficients, from *Oportunidades* (-0.53) to *Ingreso Objetivo* (0.81). On the progressive (pro-poor) side, we find most of the targeted programs, the recently introduced health insurance program, *Seguro Popular* (SP, which is in principle universally accessible to all the uninsured, but has been targeted to poor rural areas in its initial phase), health services for the formally uninsured, and basic education. On the regressive side, we find agricultural subsidies, energy and other generalized consumption subsidies (gasoline, LP gas, residential electricity, VAT exemptions), social security benefits, and tertiary education.

Considering the share of benefits received by the poorest quintile (graph 19), only 11 programs manage to transfer to this group at least a share proportional to their population weight, while another 11 allocate to this group a share which is even lower than their share in pre-transfer income. These transfers are effectively out of reach from the poor. Of the 9 targeted programs reported in ENIGH's Modulo Social (graph 20), only four are effectively targeted to the poor, and only two (Oportunidades and PET) allocate more than 50% of their transfers to the first population quintile. The rest are either neutral (Microregiones), or favor middle-income groups over the poor (Liconsa, *Vivienda, Crédito a la Palabra, Habitat*).

Given the share of fiscal resources allocated to regressive programs, the latter effectively cancel out the pro-poor impact of the progressive ones, producing a slightly regressive global distribution of public spending. Transfers in kind are broadly neutral (graph 21), while (cuasi) monetary transfers are regressive, despite the fact that they include Oportunidades and the other targeted programs considered here, because their main components are the generalized consumer subsidies and social security transfers. Despite the large difference between targeted and untargeted programs in degree of progressivity, given the marginal resources allocated to the former, their capacity to affect the overall regressivity of spending is minimal (though not of course in terms of poverty alleviation).

A similar neutralization effect can be observed within the rural sector (graphs 22), where agricultural subsidies effectively cancel out the

[16] VAT exemptions are reported for reference in table 6 and graphs 18 and 19, but are not added in the total transfer estimates, as they represent revenue lost rather than actual subsidies.

redistributive effect of targeted rural programs, measured in terms of the Gini coefficient.

Finally, table 7 presents the global distribution and incidence of taxes and transfers in 2006. The top decile's share of total transfers is almost twice that of the poorest decile, and taxes are only mildly progressive in their incidence: the average tax rate in the richest decile is only 7% higher than in the poorest one. The effect of (cuasi) monetary transfers is modest, reducing the pre-fisc Gini by just 1.7%, as is the effect of taxes, which reduces it by 2.8%. Adding transfers in kind increases this effect to 9.3% (only transfers), and 12.7% (transfers & taxes). Unlike monetary and cuasi-monetary transfers, however, this estimate would have to be adjusted downwards to the extent that the value of services received is less than the cost of provision.

Despite their absolute regressivity, the incidence of transfers on household incomes is highly progressive, reflecting the high level of inequality of pre-fisc income. Transfers represent 75% of income for the poorest decile, but only 5% for the richest. Only the richest 20% are net contributors to the fiscal system, but these account for 57% of pre-fisc income.

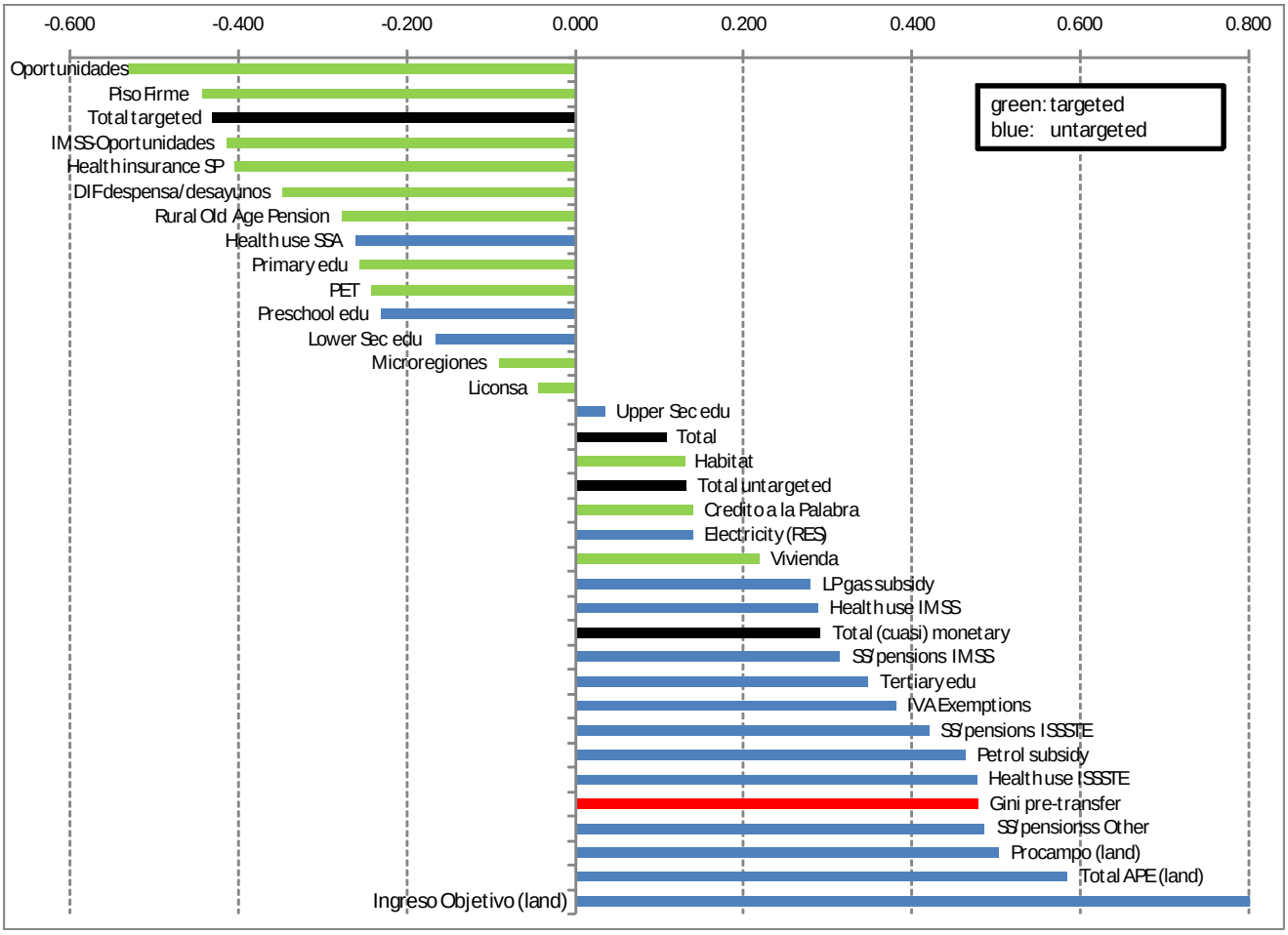
TABLE 6. TOTAL PUBLIC TRANSFERS, TAXES AND HH INCOME: MILLION MP OF 2006

CONCEPT	MILLION MP	% TOTAL TRANSFERS
ADJUSTED		
Y POST TRANSFER & TAXES	7,681,023	
Y POST TRANSFER (CUASI-MONETARY) & TAXES	6,987,414	
Y POST TAX	6,683,020	
Y POST TRANSFER	8,519,612	
Y POST TRANSFER (CUASI-MONETARY)	7,826,003	
Y PRE-TRANSFER & TAX	7,521,608	
UNADJUSTED		
Y POST TRANSFER & TAXES	4,180,691	
Y POST TRANSFER (CUASI-MONETARY) & TAXES	3,487,082	
Y POST TAX	3,182,688	
Y POST TRANSFER	5,019,280	
Y POST TRANSFER (CUASI-MONETARY)	4,325,671	
Y PRE-TRANSFER & TAX	4,021,276	
TOTAL TRANSFERS	**998,003**	**100**
TOTAL TAXES	**838,589**	**84**
TRANSFERS IN KIND	**693,609**	**69**
TRANSFERS (CUASI) MONETARY	**304,395**	**31**
TOTAL UNTARGETED	**955,629**	**96**
TOTAL TARGETED	**42,374**	**4**
EDUCATION	**402,385**	**40**
PRESCHOOL	44,583	4
PRIMARY	135,352	14
LOWER SECONDARY	86,817	9
UPPER SECONDARY	52,932	5
TERTIARY	82,701	8
HEALTH	**252,290**	**25**
SSA	92,304	9
IMSS	128,716	13
ISSSTE	22,948	2
PEMEX	8,322	1
SEGURO POPULAR	11,700	1
IMSS-OPORTUNIDADES	5,716	1
SS PENSIONS	**85,230**	**9**
IMSS	50,004	5
ISSSTE	35,226	4

CONCEPT	MILLION MP	% TOTAL TRANSFERS
GENERALIZED CONSUMER SUBSIDIES	**270,102**	**27**
ELECTRICITY SUBSIDY (RESIDENTIAL)	64,935	7
PETROL SUBSIDY (IEPS)	42,218	4
VAT EXEMPTIONS	162,949	16
AGRICULTURAL SUBSIDIES	**108,572**	**11**
PROCAMPO	15,025	2
TARGETED	**42,374**	**4**
OPORTUNIDADES	33,526	3
VIVIENDA	3,652	0
LICONSA	1,300	0
DIF DESAYUNOS	2,806	0
PROGRAMA DE EMPLEO TEMPORAL	1,090	0

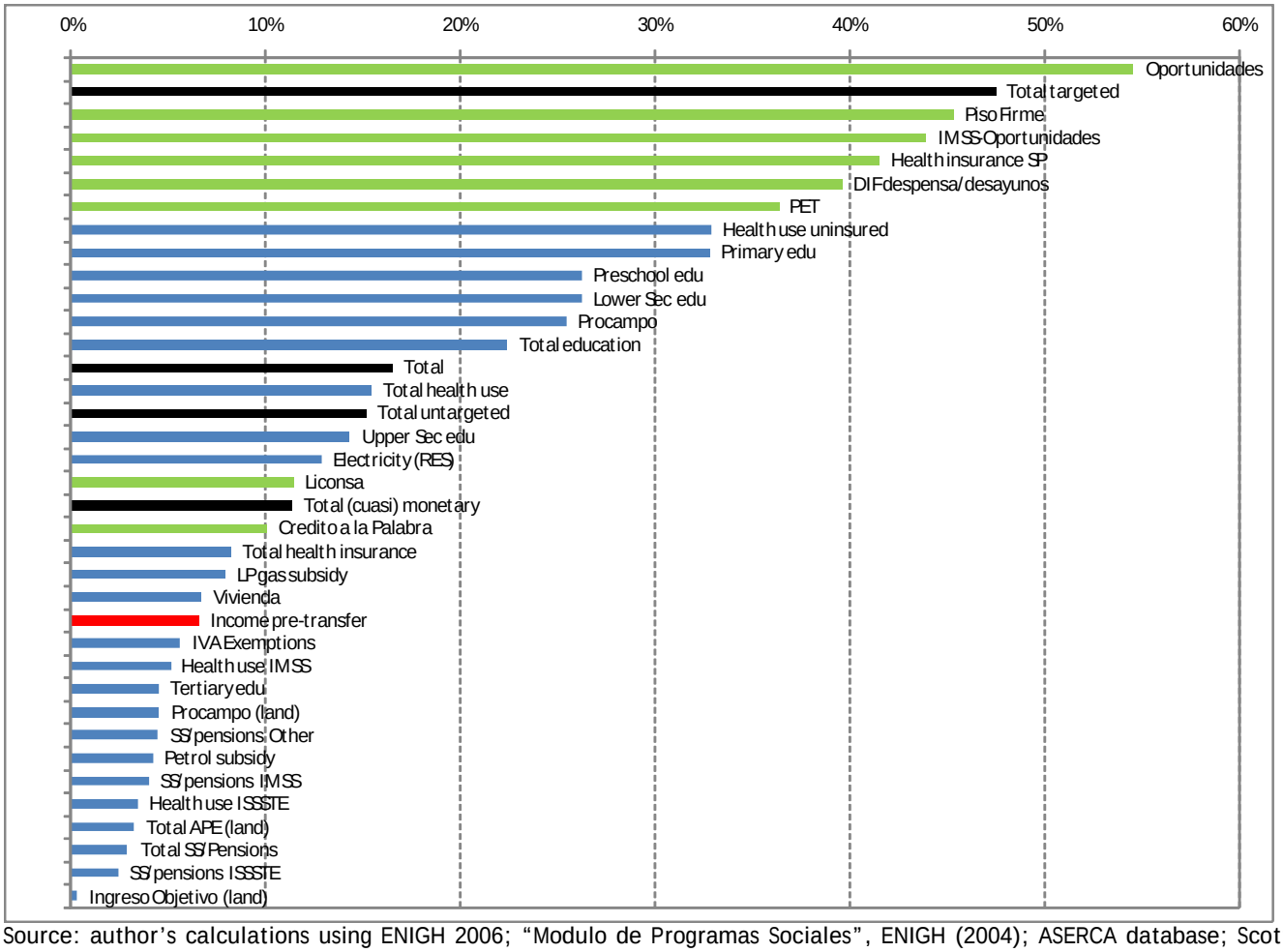
Sources: Cuenta Pública, 2006; Primer Informe de Gobierno, 2007; CFE; Presupuesto de gastos fiscales, 2007, SHCP; Cuentas Nacioanles y Estatales de Salud, SS; SEP; ENIGH 2006; Sistema de Cuentas Nacionales, INEGI.

GRAPH 18. CONCENTRATION COEFFICIENTS FOR REDISTRIBUTIVE PUBLIC EXPENDITURE: 2006



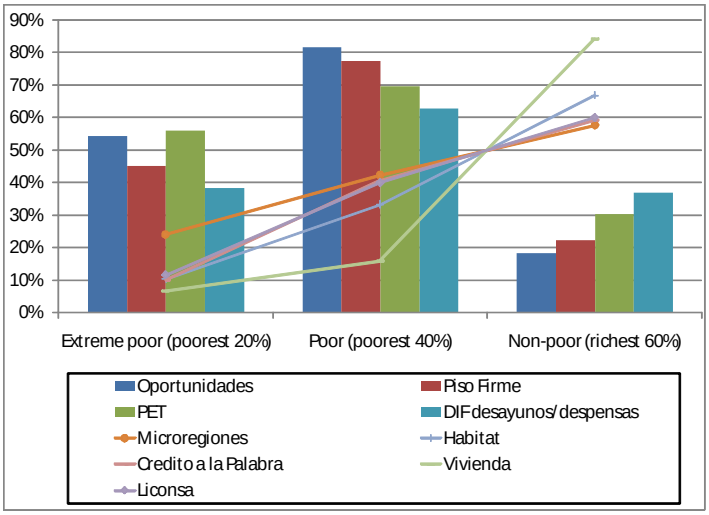
Source: author's calculations using ENIGH 2006; "Modulo de Programas Sociales", ENIGH (2004); Scott (2008b); Table 6, above.

GRAPH 19. SHARE OF BENEFITS FROM PUBLIC EXPENDITURE RECEIVED BY 20% POOREST: 2006



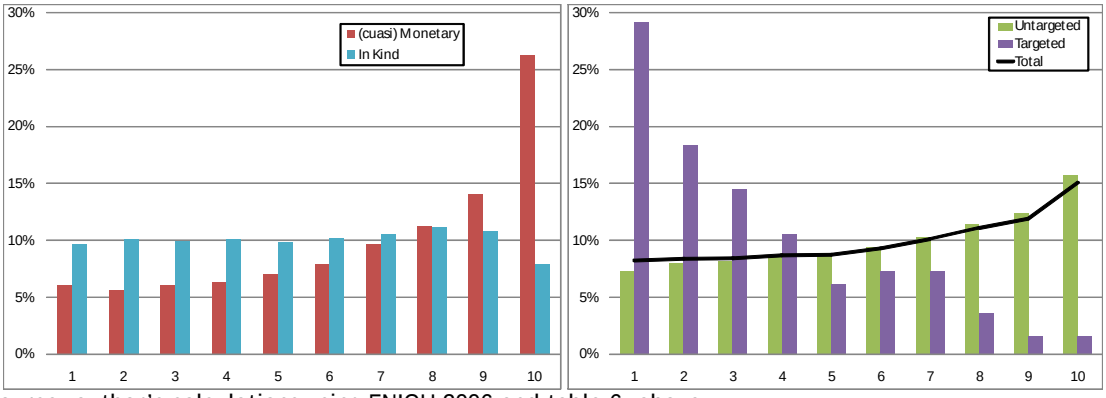
Source: author's calculations using ENIGH 2006; "Modulo de Programas Sociales", ENIGH (2004); ASERCA database; Scott (2008b); Table 6, above.

GRAPH 20. DISTRIBUTION OF BENEFITS FROM TARGETED PROGRAMS: 2004 (POPULATION DECILES ORDERED BY PRE-TRANSFER INCOME PER CAPITA)



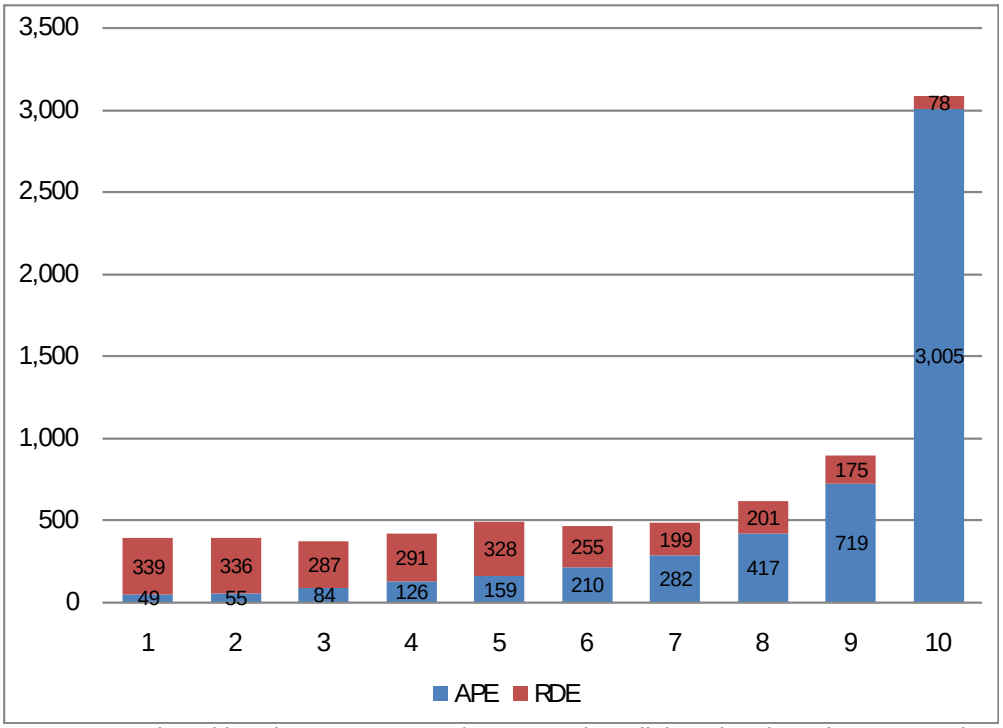
Source: author's calculations using the "Módulo de Programas Sociales", ENIGH (2004), Sedesol.

GRAPH 21. DISTRIBUTION OF TRANSFERS BY BROAD CATEGORIES: IN KIND, (CUASI) MONETARY, TARGETED, AND UNTARGETED: 2006



Source: author's calculations using ENIGH 2006 and table 6, above.

GRAPH 22. ESTIMATED AVERAGE MONTHLY TRANSFERS PER CAPITA TO RURAL HOUSEHOLDS FROM AGRICULTURAL PUBLIC EXPENDITURES (APE) AND RURAL DEVELOPMENT PUBLIC EXPENDITURES (RDE)
(RURAL HOUSEHOLD DECILES ORDERED BY INCOME PER CAPITA BEFORE TRANSFERS)



Source: Scott (2008b), using ENIGH 2006, the ASERCA beneficiary data base for 2006, and Cuenta Pública 2006.

TABLE 7. DISTRIBUTION, INCIDENCE AND REDISTRIBUTIVE IMPACT OF TRANSFERS AND TAXES: 2006

	Distribution								Incidence		
			Income								
Deciles	Transfers	Taxes	Pre-transfer & tax	Post-transfer (cuasi-monetary)	Post-transfer	Post-tax	Post transfer (cuasi-monetary) & taxes	Post transfer & taxes	Transfers	Tax	Net
	adjusted										
1	8.2%	0.9%	1.5%	1.6%	2.3%	1.5%	1.7%	2.4%	74.7%	-6.7%	68.0%
2	8.4%	1.3%	2.5%	2.7%	3.2%	2.7%	2.8%	3.4%	43.7%	-5.9%	37.8%
3	8.4%	2.1%	3.4%	3.5%	4.0%	3.6%	3.7%	4.2%	32.5%	-6.9%	25.6%
4	8.7%	3.0%	4.3%	4.4%	4.9%	4.5%	4.6%	5.1%	26.6%	-7.6%	19.0%
5	8.7%	3.5%	5.3%	5.4%	5.7%	5.5%	5.6%	5.9%	21.9%	-7.5%	14.4%
6	9.3%	5.2%	6.7%	6.7%	7.0%	6.8%	6.9%	7.2%	18.5%	-8.7%	9.8%
7	10.1%	6.2%	8.2%	8.2%	8.4%	8.4%	8.5%	8.7%	16.4%	-8.5%	7.9%
8	11.1%	9.9%	10.8%	10.8%	10.8%	10.9%	10.9%	11.0%	13.6%	-10.2%	3.4%
9	11.9%	16.4%	15.8%	15.8%	15.4%	15.8%	15.7%	15.3%	10.0%	-11.5%	-1.6%
10	15.1%	51.6%	41.4%	40.8%	38.3%	40.1%	39.5%	36.9%	4.8%	-13.9%	-9.0%
Total									**13.3%**	**-11.1%**	
CC/G	**0.1047**	**0.6132**	**0.5024**	**0.4937**	**0.4558**	**0.4885**	**0.4794**	**0.4387**			
Change in G	**16.6%**	**2.2%**		**-1.7%**	**-9.3%**	**-2.8%**	**-4.6%**	**-12.6%**			
	unadjusted										
Total									**24.8%**	**-20.9%**	
CC/G				**0.4867**	**0.4233**	**0.4733**	**0.4562**	**0.3853**			
Change in G				**-3.1%**	**-15.7%**	**-5.8%**	**-9.2%**	**-23.3%**			

Source: author's calculations using ENIGH 2006; SHCP (2008); and table 6, above.

4.1. Recent developments: 2006-2008

Since 2006 two contrasting policy developments have affected the impact of redistributive spending in Mexico (table 8). First, targeted spending on the rural poor has continued to increase, in part through the introduction of new energy (Oportunidades Energéticas: 55 pesos per month per household) and food (Apoyo Alimentario: 120 pesos per month per household) targeted through Oportunidades, but especially through the expansion of social protection spending through the *Seguro Popular* (from 11.7 to 37 billion pesos in these two years) and the introduction (2007) and rapid expansion (2008) of a basic rural universal pension (*Programa de Atención a los Adultos Mayores de 70 Años y Más en Zonas Rurales*).

Secondly, generalized consumption subsidies have grown exponentially, as the federal government has aimed to protect consumers from increasing energy prices (and broader inflationary pressures). There are four principal subsidies of this kind implemented in Mexico at present: a) the residential

electricity subsidy, b) a subsidy on LP gas, c) a subsidy on petrol and diesel,[17] and d) an implicit subsidy, or "fiscal expenditure", associated with VAT exemptions on specific goods and services (principally foods and medicines). In 2006 these subsidies amounted to 270 billion MP (table 6), representing more than total public health spending, and more than six times the spending on all targeted programs. By 2008, these subsidies are estimated to reach 518 billion MP (table 8), following recent decisions by the government to freeze electricity prices and to adjust domestic petrol prices below the trend of international costs. To put this budgetary commitment in perspective, note that it represents more than six times the total spending allocated to Oportunidades, Seguro Popular and Adultos Mayores, together.

To appreciate the distributive contradiction between these two policy strands, graph 24 compares the distribution of the corresponding instruments, revealing an almost exact mirror image between the pro-poor and pro-rich concentrations of targeted vs. generalized subsidies. Despite this, the Petrol subsidy and the Apoyo Alimentario where announced by President Calderón on national TV as part of the same policy package to "protect the income of the poorest families…".[18]

Given the relative magnitudes of the resources committed to these two sets of instruments, their combined effect is highly regressive in absolute terms: households in the poorest 20% obtain an average yearly combined benefit of some MP $3,500 (approx. US $350) *per person*, while households in the top decile obtain almost five times more, $16,000 MP ($1,600 US) *per person.*

To get a sense of the redistributive opportunity cost of the recent rise in generalized consumer subsidies, table 9 shows the redistributive impact resulting from including the 2008 subsidies in the global redistributive estimates presented above (table 7, repeated for reference in the first line of table 9), under four alternative scenarios. Scenarios A-C include only the petrol subsidy, in its current allocation, and simulations of a neutral (equal per capita) allocation and a targeted one assumed to shadow *Oportunidades*. Under the current distribution (A) the petrol subsidy has practically no redistributive impact. If its budget had been allocated neutrally (targeted), the post-fiscal Gini coefficient would have been reduced by 15.2% (18.8%) instead of 12.6%, while the income of the average household in the poorest quintile (Q1) would have increased by 63% (93.5%) instead of 51%. Finally, if all the generalized subsidies reported in table 8 had been effectively targeted, the Gini would have been cut by 25% while the income of the poor would have been increased by 140%.

[17] The distribution of the petrol subsidy is estimated using ENIGH information on household spending on petrol and diesel, and on public and commercial transport, and on the distribution of the subsidy shares between public/commercial vs. private transport reported in SHCP (2008).

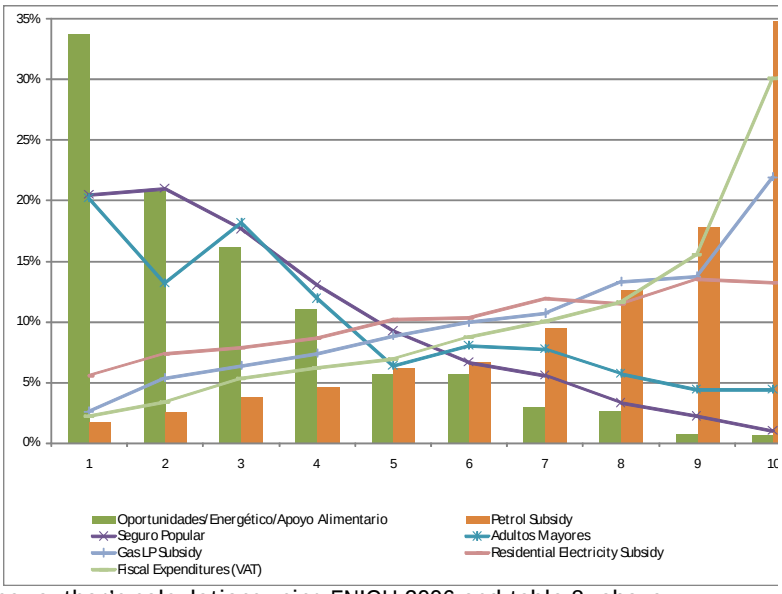
[18] "Acciones en Apoyo a la Economía Familiar", May 25, 2008.

TABLE 8. PUBLIC SPENDING ON TARGETED PROGRAMS AND GENERALIZED SUBSIDIES: 2008 (MILLION MP, APPROVED OR ESTIMATED)

Targeted (approved)	**89,706**
Apoyo Alimentario "Vivir Mejor"	4,500
Oportunidades	38,082
Seguro Popular	37,355
Adultos Mayores	9,769
Generalized (estimated)	**517,998**
Petrol Subsidies	200,000
Gas LP Subsidy	37,000
Residential Electricity Subsidy	70,000
Fiscal expenditures (VAT exemptions)	210,998

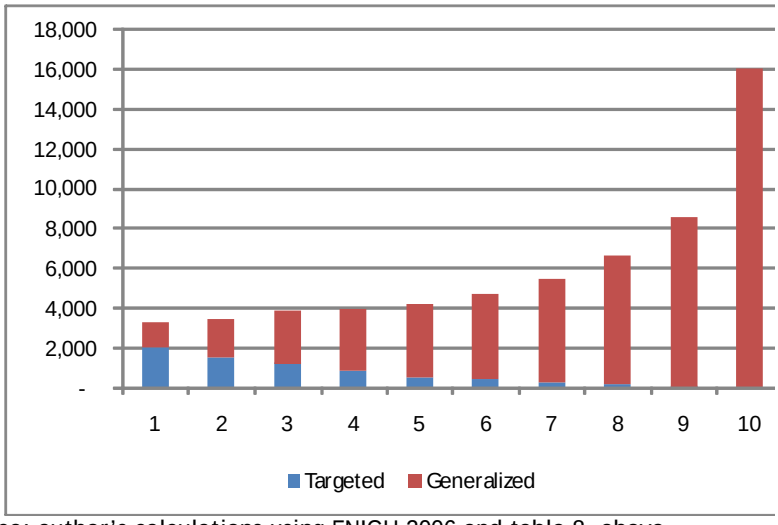
Sources: Segundo Informe de Gobierno, 2008; CFE; Presupuesto de gastos fiscales, 2008, SHCP; Presupuesto de Egresos de la Federación 2008.

GRAPH 24. DISTRIBUTION OF TARGETED PROGRAMS AND GENERALIZED SUBSIDIES: 2008 (PERCENTAGE SHARES)



Source: author's calculations using ENIGH 2006 and table 8, above.

GRAPH 25. AVERAGE TRANSFERS TO HOUSEHOLDS FROM TARGETED AND GENERALIZED SUBSIDIES BY POPULATION DECILES: 2008 (MP PER CAPITA PER YEAR)



Source: author's calculations using ENIGH 2006 and table 8, above.

TABLE 9. REDISTRIBUTIVE IMPACT OF THE 2008 GENERALIZED SUBSIDIES UNDER ALTERNATIVE SCENARIOS

SCENARIOS	FISCAL RESOURCES	ALLOCATION RULES	INCOME POST MONETARY TRANSFERS			INCOME POST TOTAL TRANSFERS AND TAXES		
			G	CHANGE G*	INCIDENCE ON INCOME OF Q1	G	CHANGE G*	INCIDENCE ON INCOME OF Q1
	2006	CURRENT DISTRIBUTION	0.494	-1.7%	11.7%	0.439	-12.6%	49.7%
A	+ 2008 PETROL SUBSIDY	CURRENT DISTRIBUTION	0.493	-1.9%	13.9%	0.439	-12.6%	51.1%
B		NEUTRAL DISTRIBUTION	0.480	-4.4%	25.9%	0.426	-15.2%	63.1%
C		TARGETED OPORTUNIDADES	0.463	-7.9%	56.4%	0.408	-18.8%	93.5%
D	+ ALL 2008 GENERALIZED SUBSIDIES	TARGETED OPORTUNIDADES	0.432	-14.0%	102.3%	0.379	-24.6%	139.4%

*Change in Gini with respect to pre-transfer/taxes. Source: author's calculations using ENIGH 2006 and table 8, above.

5. Accounting for Redistributive Performance

The last two sections revealed significant advances in the progressivity of social spending over the last two decades, most notably in the case of food subsides, anti-poverty programs, and education and health services. On the other hand, the analysis also documented the persistence of regressive allocations for the majority of the programs analyzed, cancelling out the pro-poor effect of the progressive programs in the overall allocation of redistributive spending in Mexico. At the extreme, some programs are more regressive than the distribution of private pre-transfer income, and thus inequality-increasing. Despite the fact that this study has focused exclusively on programs or spending categories motivated principally as redistributive instruments, these programs have been found to be distributed over a wide range of concentration coefficients, [-0.53, 0.81]. This section presents a preliminary account for these contrasting distributive results.

The noted (absolute) regressive distribution of a large proportion of public spending, in the context of the low (relative) level of progressivity of the tax system (table 7, above), is consistent with a well-established principle in the tax incidence literature: the benefits principle. This postulates that the distribution of tax burdens should be congruent with the distribution of benefits, so that those groups who contribute most should also be those who obtain more benefits. This principle represents the cancellation of the redistributive role of the State, and has therefore been rejected as a relevant norm in the tax literature at least since John Stuart Mill. However, the principle is still useful in accounting for actual tax/spending allocations in many contexts. For example, a recent survey of the distribution of public health spending and financing finds that in contrast to high-income countries, "in low-income countries, the better-off tend to pay more for health care, both absolutely and in relative terms. But they also consume more health care. Health care is financed largely according to the benefit principle." (van Doorslaer and O'Donnell, 2008). This interpretation does not suggest, of course, that the benefit principle is explicitly adopted by the governments in these countries as a norm for the fair allocation of burdens and benefits, only that the revealed allocations are consistent with the principle. Methodologically, to account for the latter it is not the redistributive intentions of governments which are of interest, but the constraints faced by governments in the realization of these intentions.

Most attention in this context has focused on political constraints, but there are also more fundamental constraints to redistribution under high-inequality conditions, as described below. There is a large theoretical and empirical literature on the political economy of redistribution, though most of this literature refers to the context of industrialized countries. Robinson (2008, this volume) presents a comprehensive reviews of the literature and its

relevance to recent LAC history. As will be seen below, the Mexican redistributive experience, as documented above, provides a rich illustration of some of the principal findings in this literature. However, the present account adopts a more eclectic perspective, including but not limited to political constraints. A very general constraint of the former kind, at the center of modern welfare economics (e.g. optimal tax theory) as well as liberal political philosophy (e.g. Rawls), is the idea of incentive-compatibility constraints on optimal redistribution. The constraints to be considered here are specifically associated with high inequality conditions.

The following subsection (5.1) presents a typology of constraints to redistribution and classifies the principal regressive public expenditures in Mexico in these terms. Conversely, the conditions explaining recent reforms in pro-poor spending are then analyzed as a guide to future reform opportunities (5.2).

5.1. Redistributive Constraints under High Inequality

This section focuses on three general types of constraints on redistribution associated with conditions of high income inequality: a) truncated state coverage, b) consumption inequality, and c) political constraints. These constraints do not apply in isolation, but are mutually reinforcing and account jointly for the noted "benefit principle" allocations.

5.1.1. Truncated State

The most fundamental form of constraint on the redistributive capacities of the state is the failure of state actions to reach a fraction of its subjects. At the extreme form of state failure, states may lack the capacity to extend even their most basic function of public security and protection beyond specific enclaves within the national territory. More commonly in the LAC region, as exemplified by the Mexican case, states may be heavily truncated in their fiscal capacity, social security and (post-basic) educational coverage: small states, and smaller welfare states. "Universal" public spending on education, health and social security subsidies represent 75% of redistributive spending in Mexico.

Consistently with the benefit principle, only a fraction of the population pays direct (income and social security) taxes, but only this same fraction benefits from social security. It may be argued that *contributive* social security is based on the benefit principle *by design*. But first, this is just the point: a contributive social security system which might at least be neutral under conditions of low (ex ante) income inequality, necessarily entails a truncated, and thus regressive, coverage under conditions of high inequality. But secondly, social security need not be constrained by the benefit principle: its broad design parameters (nominal progressivity of contribution/benefits schedules), its homogeneity or fragmentation into "privileged" systems, and

the weight of complementary *non-contributive* social protection systems, entails a wide range of redistributive performances, from the highly progressive systems of the European welfare states, to Mexico's highly regressive system. While inequality represents a basic constraint on the redistributive performance of social security in the former sense, the inequitable bias in the design of this system in the latter sense, is best explained in the political arena and will be considered below.

Why has social security for private sector workers (IMSS) failed to increase coverage at the lower end of the income distribution? The social security system was adopted from similar systems in the emerging industrialized welfares states, designed for less unequal societies, and in the case of Mexico, for a small, organized and relatively privileged fraction of the labor force within the corporatist structure of the old regime. It was thus designed to offer relatively generous replacement rates at high costs, and thus necessarily, low coverage. Sixty years after its introduction (1943), coverage of the rural population was just 14% in 2000, *declining* to 11% in 2005 according to Census data, and just 4% of rural workers according to IMSS own data. Coverage of the old-aged population, at 4.8%, was among the lowest in LA (Rofman 2005). As noted above (section 3), despite such a dramatic coverage failure of the contributive systems, non-contributive pensions did not exist in Mexico until very recently.

In 1997 the IMSS pension system was reformed from a PAYG to a personal account fully funded system, in part to make participation more attractive by transforming the perception of contributions from wage taxes to savings. However, the reform failed to reduce the contributive cost of social security to workers and employers, which for low wage workers represents on average some 35% of salary (Levy 2008). Forced savings and insurance premiums of this magnitude are obviously beyond the reach of the poor in Mexico.

Another possible explanation for the coverage failure of IMSS has been strongly advocated by Levy (2008) (see also World Bank 2007). This suggests that the limited coverage is the effect, rather than the cause, of the noted increase in spending on the uninsured, and in particular the creation of insurance and pension programs aimed at the formally uninsured, like the Seguro Popular and the nascent non-contributive pensions, which compete directly with IMSS' offer, at no direct cost to the worker. The merit of this hypothesis is to draw attention to the labor-market distortions associated with the current social security system, which are growth-constraining as well as inequitable, and the intensification of these distortions implied by the recent rapid expansion of spending on the uninsured. But as we have seen, this expansion is recent, from 2006 in the case of pensions, and a decade earlier in the case of health, while IMSS coverage has expanded slowly for 65 years, and stagnated since the 1980's. In any case, the correct implication to be drawn from this analysis is that the current dual social security/social protection

system is unsustainable in the long term, and must be transformed into an integral system with a non-contributive, universal basic health insurance and pension package at its core.

The truncated coverage of "universal" education services can be similarly explained by the combination of inequality constraints, design failures and political capture. The principal constraints on the access of the poor to post-basic public education is the prohibitive opportunity cost of education, geographic access to the required facilities, and the quality of basic public educational services available to the poor. The first condition is a direct consequence of high income inequality, the second follows from the geographic dispersion of the poor, and the third may be accounted largely in political terms (capture by the providers of these services). As in the case of social security, bad design is aggravated here by its implementation in unfavorable distributive conditions. Comparing Mexico and the LAC region with high-income countries, the allocation of public education resources is biased towards the supply side (especially teacher salaries) and higher education services. These differences, which would imply a more regressive allocation under any distributive conditions, represent the opposite design bias required under conditions of high income inequality: demand finance through scholarships to compensate the poor for their high opportunity costs, and high quality basic education services for the poor. These design biases may again be largely accounted for in political terms.

5.1.2. Consumption Inequality

After "universal" services and social security, the second most important type of redistributive instrument implemented in Mexico at present (in budgetary terms) are generalized consumption subsidies. These provide a further, more obvious, example of redistributive constraints under conditions of high income, and thus high consumption inequality. Under these conditions, as shown above (sections 3 and 4), generalized subsidies are regressive even if aimed at basic necessities, like food, household energy, or public transport, and even when combined with progressive tariff blocks (increasing tariffs with increasing consumption), as in the case of water and electricity pricing in most countries, including Mexico. Again, the introduction and persistence of these instruments despite their redistributive inefficiency (high inclusion errors), and their specific design features, can largely be explained in political terms.

5.1.3. Political Economy

While high inequality conditions directly constrain the redistributive effectiveness of social services and social security and generalized subsidies in Mexico, political economy factors (in turn associated with high economic inequality), play an important role in accounting for the regressive biases in

the introduction and design of these instruments under these conditions. Beyond the "universal" spending categories considered above, political factors are central in accounting for the most regressive instruments analyzed in the present study, which are directed at specific interest groups: pensions and other employment benefits for public sector workers, and agricultural subsidies.

A. Social security and other employment benefits

As we have seen in section 3, the social security in Mexico is fractioned between different sub-systems and highly polarized vertically as well as horizontally, in the (net) benefits offered to workers (table 3). Established and evolved over the 70-year long post-revolutionary, single-party, corporatist period in Mexico's history, this system can be read as a fossilized record of the distribution of political power in Mexico's labor market over that period, with public sector workers, especially in state enterprises and other highly privileged public sector enclaves (armed forces, judges, upper trenches of bureaucracy), at one extreme, and rural workers, at the other, mostly lacking access to formal social security in any form before the 21st century. The present study has only considered the most visible differences in pension and health benefits between these groups of workers, explicitly accounted in the public budget. To these we must add the more obscure, but perhaps even more important in monetary terms, rents extracted by public sector workers through salaries and other employment benefits during the long corporatist history. Though some attempts have been made to estimate salary rents (Guerrero et al. 2008), these are largely unquantified.[19] The position of public sector workers in the national income distribution (see "ISSSTE pensions" in graphs 18 and 19 above) reveals how regressive the distribution of these rents and employment benefits is.

B. Public education

With the capture of rents by basic education teachers, the organized power of public teacher unions in Mexico is the principal constraint for improving performance accountability and thus educational quality at this level. The accumulated evidence of the low quality of public basic education in Mexico by international standards, with the largest gaps in rural public schools serving the poorest students (Alvarez et al. 2007, Mancera 2008), associated with the lack of teacher accountability, has two important distributive consequences: it implies that the progressivity of basic education benefits

[19] An illustration of these more obscure benefits is provided by the virulence of current (October 2008) teacher protests against a recent government program to increase accountability in teacher performance, in which teacher union leaders have openly defended their established right to inherit public sector posts to their offspring as personal assets. In the latest national congress of the principal teacher union, each of the 59 sectional leaders was presented with a luxury Hummer SUV.

presented in sections 3 and 4 above may be significantly overestimated, and it accounts in part for the failure of the poor to access post-basic public education. The capture of public basic education services by the teacher unions has an additional effect on the equity and efficiency of public education spending in Mexico, by diverting resources away from more efficient and equitable supply (libraries, school infrastructure, etc.) and especially demand side interventions (scholarships).

Finally, as noted in section 3, the historic spending bias towards higher education in Mexico reflects the political empowerment of a very different group following the 1968 student revolts: "middle-class" urban university students (in the upper-half of the income distribution, especially the richest quintile).

C. Generalized consumer subsidies

The political economy of generalized consumer subsidies may be illustrated by considering the case of VAT exemptions on food and medicines and energy subsidies (table 8, above). At the risk of simplification, the evolution of these subsidies may be summarized in the following stages:

a) introduced to protect consumption of basic necessities, especially of the poor,

b) gradual expansion of the amount and coverage of the subsidy, becoming increasingly regressive,

c) reform efforts to eliminate or reduce it become increasingly costly politically.

When VAT was increased to 15% in 1995, a basic food basket and medicines where exempted. These represented some 15% of goods and services at the time, but had expanded to almost 50% of goods by 1998 (CIDE-ITAM 2004). This expansion was the result of successful judicial demands of equal treatment on the part of producers of goods not originally covered (processed food, candies, etc.), with the result of undermining the tax efficiency as well as equity of the instrument. A reform effort to eliminate all exemptions in 2001 failed because it was perceived to be regressive and blocked by party opposition from the left, despite the fact that the exemptions in fact fall in the more regressive group of instruments evaluated here (graphs 18 and 19).

Residential electricity subsidies present a similar history. They were introduced in the early 1970s as the authorities failed to fully adjust the price to inflation, and were only formally introduced as a policy instrument in 1974 (World Bank 2008). The average subsidy has grown significantly with the introduction and gradual expansion of additional "summer" subsidies in warmer areas. A reform effort to increase tariffs in 2002 faced intensive

political opposition, and failed to do so significantly as localities reclassified into lower tariff areas and a sixth summer tariff was introduced (1F).[20]

5.2. The possibility of pro-poor reforms: the political economy of Progresa/Oportunidades

As documented in section 3, the creation and rapid expansion of the Progresa/Oportunidades CCT anti-poverty program represented significant progress in social spending on the poor, in multiple domains: direct monetary transfers, food subsides, and education and health services. There are two questions to consider in accounting for this remarkable reform. First, why were food subsidies so inequitably allocated in the past, targeted almost in *inverse* proportion to the distribution of the needs they were supposed to address? That is, why was a reallocation of this kind only achieved by the end of the 20th century, with introduction of Progresa. Secondly, how was it possible, against the standard predictions of the political economy of targeting (Sen 1995), to implement a reallocation of food subsidies from urban centers to remote and dispersed rural communities, and from the federal capital to the rural South?

The answer to the first question must certainly refer to political factors, including the capacity of urban populations to mobilize politically, in contrast to the highly dispersed rural poor, and the authoritarian-corporatist structures ensuring (or pre-empting) the "green vote" to the party in power (PRI). But again, there were more fundamental constraints associated with existing distributive conditions. Before Progresa, it was widely assumed that food subsidies targeted to poor families in remote rural localities were operationally unfeasible, whether in kind or in monetary form. The concentration of the targeted *tortilla* and milk subsidies (Liconsa) in urban areas, and especially in Mexico City, thus responded at least in part to the logistic challenges of delivering these in dispersed rural localities. An early antecedent to Progresa was conceived and piloted in an urban setting (Campeche), with the use electronic debit cards. A mayor contribution of the final Progresa design was to show that effectively targeted and efficiently delivered direct monetary transfers to highly dispersed rural households were possible.

There are various factors which may account for the success of this reform. First, because of the particular circumstances of the selection procedure of the PRI presidential candidate (following the political assassination of its original candidate), the last administration of the single-party era (Zedillo, 1994-2000) was exceptionally free from corporatist ties to the old regime. While the democratic transition process may also have played

[20] The story has threatened to repeat itself once more with the recent decision by the government to freeze petrol prices, apparently responding to political pressure in the media, thus introducing a large subsidy, though this will contract with the current (October 2008) decline in oil prices.

a part in accounting for this reform, by empowering rural voters (Robinson 2008), the fact that the rural vote was still largely loyal to the PRI, and that Zedillo was apparently prepared give up electoral support in Mexico City,[21] suggests that this administration was also largely free from electoral concerns, unlike the following administrations. In contrast to the intensive government media campaigns accompanying the flagship poverty program of the previous administration (Pronasol), as well as the Oportunidades program in the following administrations, such as the Zedillo administration refrained from such a campaign in the case of Progresa, thus facilitating its political survival beyond the administration and PRI regime.

Second, in contrast to education and health service provision, the reallocation of food subsidies is not constrained by labor or physical infrastructure. It is this also unconstrained by the powerful public sector unions which have successfully blocked significant allocation reforms in the case of education and health services. Third, the rapid expansion of the program, with 2.5 million direct beneficiary households by the end of the Zedillo administration, ensured a large constituency in its favor. Forth, just as importantly, the decision to make the program transparent and invest in an ambitious and highly credible external impact evaluation from the very start, also contributed significantly to its political survival.

Finally, it should be noted that the evolution of the program after 2000 might indeed be interpreted in terms of the political economy of targeting. In 2001, when it was rebranded as *Oportunidades*, the program was expanded to urban areas and upper-secondary education, inevitably reducing its targeting efficiency: from 71% of its resources benefiting the poorest quintile in 2000, to 55% in 2006.[22]

Unfortunately, as has been documented here, the redistributive efficiency of the *Oportunidades* program represents an isolated case among the redistributive instruments currently operated in Mexico, and despite its expansion the program still represents a relatively small drop in the ocean of social spending. More importantly, it is not clear that the program could or should be further expanded, or become the backbone for a wider reform of social policy in Mexico. The program was originally conceived and designed to provide a minimum package of human capital and monetary transfers to the extreme poor. Its efficient administrative targeting mechanisms and package of fixed benefits is well designed for this purpose, but not as a platform to construct a truly universal welfare state. This would require effective mechanisms to ensure the quality of social services for the poor, and the integration of the fractured contributive social security system with the non-contributive social protection programs into a single system of universal protection.

[21] The PRI lost Mexico City to the leftist PRD party, and has failed to gain significant presence to the present day.
[22] Authors calculations using the 2000 and 2006 ENIGH.

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