

REGIONAL INCOME REDISTRIBUTION AND RISK-SHARING: LESSONS FROM ARGENTINA

WALTER CONT

*Fundación de Investigaciones Económicas Latinoamericanas
and Universidad Nacional de La Plata*

ALBERTO PORTO*

Universidad Nacional de La Plata

PEDRO JUARROS

Universidad Nacional de La Plata and Georgetown University

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This paper estimates redistribution and risk-sharing across provinces in Argentina during the 1995-2010 period as a result of the national budget. We find that the aggregate national budget (expenditure, transfers and their corresponding revenues) reduces differences in the per capita provincial Gross Geographic Product by 5% in the long term, and stabilizes such differences by 10%. The redistributive tool is national expenditure, while automatic intergovernmental transfers are almost neutral and tax revenues amplify regional disparities. The quantitative effects are somewhat modest in comparison with those achieved in developed countries. Regressive taxation is the key difference with developed countries.

JEL classification codes: H5, H6, H7

Key words: fiscal policy, redistribution, risk sharing

* Alberto Porto (corresponding author): Emeritus Professor, Universidad Nacional de La Plata, Calle 6 entre 47 y 48, Oficina 519, La Plata, 1900, Argentina; email: porto.alb@gmail.com. Walter Cont: Adjunct Professor, Universidad Nacional de La Plata, Calle 6 entre 47 y 48, Oficina 322, La Plata, 1900, Argentina, and Associate Economist, Fundación de Investigaciones Económicas Latinoamericanas, Córdoba 637, Piso 4, CABA, 1054, Argentina; email: walter@fiel.org.ar. Pedro Juarros: Economist, Universidad Nacional de La Plata and Georgetown University; email: pedro.juarros@gmail.com. This research was funded by the program PICT 2013-1864, FONCYT, Argentina, and the research project "Incentivos a Docentes-Investigadores", Universidad Nacional de La Plata. We are grateful to Jorge Streb, two anonymous referees and seminar participants at the III Seminar in Local Public Finance (iFHC, Brasil) and the 2014 Argentinean Annual Meeting of Political Economy (AAEP).

I. Introduction

During the past 20 years there has been growing interest in understanding whether national fiscal policy redistributes income among provinces and whether it compensates fluctuations in provincial economic activity. However, this analysis has not been extended to developing countries with different institutional arrangements. In this paper we study the case of a developing country, Argentina, characterized by a multi-level government organization with a restricted role of social expenditures at the national level, a complex tax system, high macroeconomic volatility and structural changes in its fiscal policy.

The case of Argentina is different from the extensive literature that analyzes the redistributive and stabilizer role of the national budget across provinces in developed countries for four reasons. First, macroeconomic instability and frequency of crises is greater in developing countries, where the volatility of fiscal policy and its pro-cyclicality makes things worse (Gavin et al. 1996). Countries that are more volatile have greater variability in tax collection and expenditures and, as a consequence, the central government is less likely to correct long term territorial disparities and provide insurance against idiosyncratic shocks within the country (Martner and Aldunate 2006). Argentina is an exemplary case of a large developing country with high output volatility and fiscal procyclicality, going from hyperinflationary episodes to sovereign default crisis and depression. Second, macroeconomic instability has this negative effect through its links with diverse forms of uncertainty, not only economic but political and policy-related (Loayza et al. 2007). At the same time, economic instability can generate an enthusiastic inclination for reform leading to political instability. The institutional structure of Argentina is *de facto* different from similar federal systems in developed countries, in that weak checks and balances among Executive, Legislative and Judicial powers result in political instability.¹ Bercoff and Meloni (2009) characterized the political period under analysis of Argentina as an emerging democracy, where the Executive branch of the government has a predominant policy-making role in the country, and the Congress has a weak role. This hyper-presidentialism is particularly important in the programming and execution of

¹ According to the new institutional view (Acemoglu et al. 2003), distortionary macroeconomic policies are not the causal effect that lead to macro volatility and crises. Rather, weak institutions that do not constrain politicians lead to ineffective enforcement of property rights and high degrees of political instability, being the underlying causes of economic instability.

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