

The Evolution of the Middle Class in Latin America

By Leopoldo Tornarolli

I. Introduction

Latin American countries have always been characterised by relatively high levels of income inequality, even taking into account their degree of economic development. If such 'excess inequality' is combined with the fact that these are mostly middle-income and low-income countries, it can be understood that, in general, the middle class has not historically represented a significant proportion of the population in many countries in the region.

However, since the beginning of the 21st century, most countries in the region have enjoyed a relatively stable process of economic growth, accompanied by decreases in income inequality. This has resulted in a reduction of poverty in the region and an increase in the size of the middle class.

This situation has spawned a literature covering the potentially beneficial social effects of the expansion in the size of the middle class in the region. In particular, some authors stress that the potential growth of the middle class would imply a reduction of the 'excess inequality' in the region.

However, that literature has not reached consensus on the empirical definition of the concept of the middle class. The applied literature on the middle class is characterised by a diversity of definitions which may complement or contradict each other. In this study a particular definition of middle class is applied. This definition is based on absolute income thresholds, a relatively standard approach in the literature. Using that definition, this work traces the evolution of the middle class in 16 Latin American countries during the period 2001–2011.

II. The data

The empirical evidence presented in this study is based on microdata from more than 150 household surveys from 16 Latin American countries (Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Honduras, Mexico, Panama, Paraguay, Peru, Uruguay and Venezuela) covering the period 2001–2011.

The whole set of surveys belongs to a large database of household surveys from Latin American and the Caribbean: the Socio-Economic Database for Latin America and the Caribbean (SEDLAC), assembled by the Centro de Estudios Distributivos Laborales y Sociales (CEDLAS) of the Universidad Nacional de La Plata (Argentina) and The World Bank's Latin America poverty group (LCSPP).

Databases in SEDLAC have been constructed from national household surveys, which are not uniform across countries. The main contribution of the project is to homogenise the original data using the same criteria and procedures, making statistics comparable across countries and over time. This is particularly important for the case of the main variable of interest in this work: per capita household income.

As mentioned above, the report includes information for 16 countries over a period of 11 years, which means that 176 combinations of country/year were used. For 149 of these 176 combinations the information presented comes from estimates obtained directly from household surveys from the SEDLAC project. In the remaining 27 cases statistics were not estimated directly from household surveys due to various reasons: (i) some countries do not perform household surveys every year (for example, Chile's household survey is conducted every three years); (ii) at the time of this report SEDLAC did not yet have access to some surveys (for example, the 2011 household survey for El Salvador); and (iii) it was decided not to use the data for some combinations of country/year where the household survey had significant methodological changes, to preserve comparability.

For the cases in which statistics were not obtained from household surveys combining country/year, the information was completed using simple projections drawn from the closest available survey and data from the World Development Indicators (WDI) on per capita GDP growth (World Bank, 2013a). The following examples illustrate how the missing information was estimated:

- Chile 2004 and 2005: Chile carries out its household survey every three years. The Encuesta de Caracterización Socioeconómica Nacional (CASEN) was carried out in 2003 and then in 2006, so there are no surveys for 2004 and 2005. In this study, the estimations for 2004 were obtained from CASEN 2003 by adjusting per capita household income by a factor that takes into account the growth of GDP per capita between 2003 and 2004. Similarly, the statistics for 2005 were estimated from CASEN 2006, adjusting per capita household income by the growth rate of GDP per capita between 2005 and 2006.
- Brazil 2010: Brazil did not carry out the Pesquisa Nacional por Amostra de Domicílios (PNAD) in 2010. In this particular case there is a survey for 2009 and another one for 2011. Two alternative estimations were obtained for 2010. The first one was based on PNAD 2009 and adjusted by the growth rate of GDP per capita between 2009 and 2010. The second one was obtained using PNAD 2011 and adjusted to take into account the growth rate of GDP per capita between 2010 and 2011. The statistics reported in this study are an average between these two alternatives.

III. The definition of middle class

This study analyses the evolution of the middle class in Latin America over the last decade, adopting the definition of middle class proposed by the Secretaria de Assuntos Estratégicos (SAE) da Presidência da República Federativa do Brasil in its publication *Vozes da Classe Média* (2012). In that report, Brazil's population is broken down into three groups (lower, middle and upper classes), according to the level of per capita household income. It is worth noting that defining the middle class using absolute income thresholds is a conceptually similar exercise to the measurement of poverty using an absolute poverty line. Several economic studies on the middle class follow this approach, including a recent book by The World Bank (2013b).

In the case of the SAE's publication, the income thresholds defining the three classes were chosen after a detailed analysis of different alternatives. SAE defines a household as belonging to the **lower class** if it has a high probability of remaining or becoming poor in the near future.

Empirically, a household is part of the lower class if its per capita household income is lower than USD5.5 a day, at purchasing power parity (PPP) exchange rate. A household is considered **middle class** if it has a low probability of becoming poor in the near future. In terms of per capita income, these are households with income levels between USD5.5 and USD19.2 a day at PPP. Finally, the **upper class** comprises households with an extremely low probability of becoming poor in the near future—that is, those with per capita household income higher than USD19.2 a day at PPP.

Even though this definition was specifically constructed for Brazil, it is interesting to use it to compare countries in Latin America, since Brazil's GDP per capita is relatively close to the average GDP per capita of the 16 countries in the sample. According to the WDI, the GDP per capita of Brazil was USD10,264 (PPP) in 2011, while the population-weighted average of the sample was USD10,755.

IV. The evolution of the middle class in Latin America

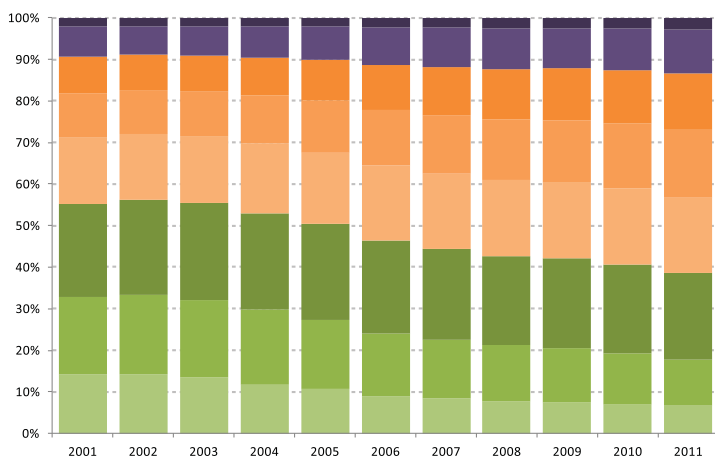
The evolution of the middle class in Latin America as a whole between 2001 and 2011 is presented in Figure 1. This was constructed as a weighted average of the 16 countries included in the sample used in this study. The graph shows the percentage of the total Latin American population represented by each class: lower in green, middle in orange and upper in purple. The different shades of each colour indicate a subsequent division within each class: the lower class is divided into extremely poor, poor and vulnerable; the middle class into lower, middle and upper middle class; and the upper class into lower and upper upper class.

The results confirm what other authors have found, even using different methodologies: the region's middle class has experienced a significant increase in the last few years. While Latin America's middle class accounted for 35.3 per cent of the population of the region at the beginning of the century (2001), by 2011 that share had risen to 48.0 per cent.

The size of the upper class also increased, from 9.5 per cent in 2001 to 13.3 per cent in 2011. Obviously, these results imply that there was a significant decrease in the proportion of the population represented by the lower class, from 55.2 per cent in 2001 to 38.6 per cent in 2011. This result coincides with one of the main findings of the empirical literature on poverty in Latin America: in recent years the incidence of poverty has fallen sharply in the countries of the region.

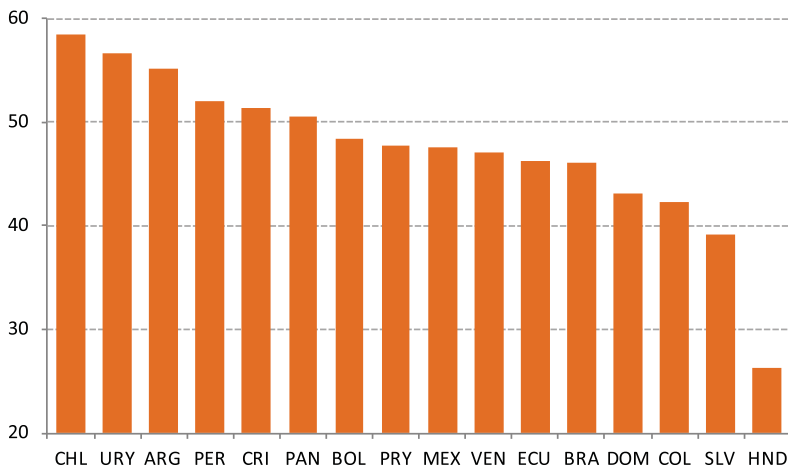
One aspect of interest in Figure 1 is the year-on-year change in the relative size of the middle class. The results show that the trend mentioned above was not consistent throughout the period. At the beginning, between 2001 and 2003, the size of the middle class remained virtually unchanged in the region due to a combination of economic crisis in some countries (including Argentina, Uruguay and Venezuela), stagnation in others (such as Brazil, Colombia and Mexico) and low growth rates in the remainder (Chile, Costa Rica and Peru, among others).

Figure 1
The Evolution of the Middle Class in Latin America



Source: Author's calculations based on SEDLAC.

Figure 2
The Size of the Middle Class in 2011, by Country



Source: Author's calculations based on SEDLAC.

From 2003 to 2008 there was strong growth in the percentage of Latin American households that had moved from the lower class to the middle class—a process that took place in all the countries of the sample. This explains about 75 per cent of the growth in the middle class in the region over the period. Between 2008 and 2009, due to the international financial crisis, the growth of the middle class in the region stagnated, but between 2009 and 2011 the share of this group in the total population grew at a rate similar to that observed between 2003 and 2008.

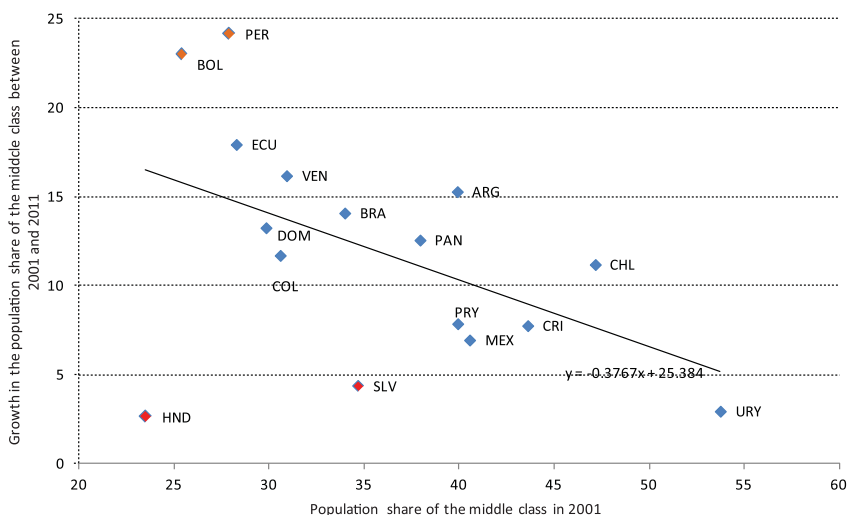
Although the relative size of the middle class increased in all countries of the region in the period under analysis, there were marked differences in the size of that particular socio-economic group between countries in 2011, as seen in Figure 2. In six countries (Chile, Uruguay, Argentina, Peru, Costa Rica and Panama) the middle class accounted for more than half of the population, while in eight other countries (Bolivia, Paraguay, Mexico, Venezuela, Ecuador, Brazil, Dominican Republic and Colombia) the middle class

represented between 40 per cent and 50 per cent of the population. El Salvador, with 39.1 per cent, and Honduras, with less than 30 per cent, are the two countries with the lowest proportion of the population in the middle class.

However, there appears to be some convergence in the proportion of the population that represents the middle class in different countries, to the extent that the average growth of the group seems to have been, on average, higher in countries in which the middle class represented a smaller proportion of the population in 2001, as shown in Figure 3.

This graph shows the increase in percentage points of the size of the middle class as a proportion of the population of each country between 2001 and 2011. As can be seen, there is a clear negative relationship between the relative size of the middle class in 2001 and the growth in percentage points between 2001 and 2011. Even though most of the countries are located around the trend line, the situation of some particular countries is worth mentioning in further detail.

Figure 3
Convergence between Countries in Terms of the Relative Size of the Middle Class?



Source: Author's calculations based on SEDLAC.

Honduras and El Salvador, along with Uruguay, are the only countries in the region where the middle class has experienced a slower growth in percentage points. However, in Uruguay over half of the population already belonged to the middle class in 2001, which was not the case in the other two countries. By contrast, in 2001, Honduras and El Salvador had relatively small middle classes as a proportion of the total population. In that sense, we can say that these two countries seem to be the exception to a possible convergence in the relative size of the middle class among Latin American countries.

For their part, Peru and Bolivia, two countries where the share of the middle class in the total population was relatively low in 2001, experienced the greatest growth in the relative size of the group, with growth above 20 percentage points in the period under analysis. The case of Peru is not surprising given that this is the country with the highest rates of economic growth in the region over the period of analysis. The case of Bolivia is more striking, as the country did not show very promising economic performance. As data from the household survey of the country have only recently been released, estimations for this document are preliminary, so these numbers should not be considered definitive.

V. Conclusions

The results presented in this work confirm the findings of other authors: the middle class has increased its share of the total population in all Latin American countries in recent years. As we have seen, this process has not followed a consistent pattern but shows different rates of growth across countries and over time.

However, there is a pattern worth noting from the statistics shown in this study: there seems to be convergence in the relative size of the middle class across countries, to the extent that (with the clear exception of Honduras and El Salvador) countries where the middle class represented a lower proportion of the population in 2001 are, in general, those which experienced the highest growth in the relative size of this socio-economic group over the last 10 years. ■

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