

## Effects of Subsidy Reform on Consumption and Income Inequalities in Iran

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**Abstract :** In this paper, we use data on Household Income and Expenditure survey of Statistics Centre of Iran, conducted from 2005-2014, to calculate several inequality measures and to estimate the effects of Iran's targeted subsidy reform act on consumption and income inequality. We first calculate Gini coefficients for income and consumption in order to study the relation between the two and also the effects of subsidy reform. Results show that consumption inequality has not been always mirroring changes in income inequality. However, both Gini coefficients indicate that subsidy reform caused improvement in inequality. Then we calculate Generalized Entropy Index based on consumption and income for years before and after the Subsidy Reform Act of 2010 in order to have a closer look into the changes in internal structure of inequality after subsidy reforms. We find that the improvement in income inequality is mostly caused by the decrease in inequality of lower income individuals. At the same time consumption inequality has been decreased as a result of more equal consumption in both lower and higher income groups. Moreover, the increase in Engle coefficient after the subsidy reform shows that a bigger portion of income is allocated to consumption on food which is a sign of lower living standard in general. This increase in Engle coefficient is due to rise in inflation rate and relative increase in price of food which partially is another consequence of subsidy reform. We have conducted some experiments on effect of subsidy payments and possible effects of change on distribution pattern and amount of cash subsidy payments on income inequality. Result of the effect of cash payments on income inequality shows that it leads to a definite decrease in income inequality and had a bigger share in improvement of rural areas compared to those of urban households. We also examine the possible effect of constant payments on the increasing income inequality for years after 2011. We conclude that reduction in value of payments as a result of inflation plays an important role regardless of the fact that there may be other reasons. We finally experiment with alternative allocations of transfers while keeping the total amount of cash transfers constant or make it smaller through eliminating three higher deciles from the cash payment program, the result shows that income equality would be improved significantly.

**Keywords :** consumption inequality, generalized entropy index, income inequality, Irans subsidy reform

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