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**Poverty and Inequality in Eastern Europe
and the CIS Transition Economies***Mihaly Simai*

Abstract

This paper deals with the causes and consequences of inequality and poverty in the countries east of the new frontiers of the European Union, mainly with the CIS countries. Poverty and inequalities in the former socialist countries were partly mitigated by the social policies of the state. The transition processes, however, have resulted in new distributions of income and wealth. The new structural sources of poverty and inequalities have often been more extreme. Some CIS countries have moderated poverty, which nonetheless persists in most CIS countries, in spite of some economic improvements.

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Poverty and Inequality in Eastern Europe and the CIS Transition Economies

Mihaly Simai

In Eastern Europe, changes in the distribution of income and wealth associated with globalization, the restoration of the market system, the growing income gap in the former Socialist countries, and the rise of the nouveau riche have brought issues of inequality into national politics. The political implications are country specific—as the countries are extremely diverse in terms of size, level of development, historical background, and social and political structure—and are related to the characteristics of the regimes.¹ This paper deals with certain aspects of the transformation.

It has been generally recognized that much has been accomplished in certain areas such as macro-economic stability, fiscal consolidation, currency convertibility, liberalization and international economic relations. Institutions indispensable for a market economy have been put in place and growth has resumed in most of these new market economies, which more closely resemble the systemic hybrids of developing countries than developed market systems. However, there are important differences in ownership patterns, particularly in three areas: the size of public ownership, the character of private ownership, as well as the share and character of foreign ownership of major economic assets. The development of legal frameworks and market institutions are also quite different. Differences also arise in the functioning of markets, the level of integration into global markets, the degree and nature of competition, the size and role of the informal sector, and the level of crime and corruption. These and other factors have a major influence on employment, poverty, inequality and related policies.

The statistical data in this paper cover countries that differ in terms of development level, size of the economy and population, degree of marketization and integration into global markets, and social costs of transformation. Per capita GDP is the most widely-used indicator for showing differences.

Due to the level of development and speed of the institutional reforms in Central Asian countries, transition to a market-based system over the past decade and a half has been much more difficult than in the European part of the CIS or in Central Europe. Economic contraction and related growth in poverty and unemployment have been longer and greater in magnitude. During the first half of the 1990s, real GDP of Central Asian countries fell by more than 50 per cent, while poverty and inequality increased substantially. Although growth resumed after the latter part of the 1990s, output of most economies in Central Asia in 2002 remained around 25-30 per cent below the 1989 level, while poverty and unemployment persisted.

This paper consists of five sections. The first section provides an overview of the social consequences of the transformation process, including the consequences of the disintegration of the Soviet

¹ There are complex interactions between past and present and between the diverse political, economic and social processes, cultural values, national and external factors and institutions. The etatist-socialist regimes collapsed in different ways, creating the present spectrum of regimes with varying levels of progress made in terms of marketization, liberalization, and economic and social development.

Table 1:
Classification of Transition Countries by Income

<i>Low Income</i>	<i>Middle income</i>		<i>High Income</i>
	<i>Lower</i>	<i>Higher</i>	
Armenia	Albania	Croatia	Slovenia
Azerbaijan	Belarus	Czech Republic	
Georgia	Bosnia-Herzegovina	Estonia	
Kyrgyz Republic	Bulgaria	Hungary	
Moldova	Kazakhstan	Poland	
Tajikistan	Latvia	Slovak Republic	
Turkmenistan	Lithuania		
Ukraine	FYR Macedonia		
Uzbekistan	Romania		
	Russian Federation		
	Republic of Yugoslavia		

Source: World Bank (2000: 334-5).

Union, the privatization process and liberalization of the external sector. The second section deals with changes in the labour market and consequences of unemployment, while the third section analyzes the implications of poverty. The fourth section deals with the changing social stratification, and finally, the fifth section reviews certain social policy issues.

Social dimensions of the transitions

Most international organizations and social sciences have taken a rather simplified approach to the process known as ‘transition’, particularly during the first half of the 1990s. While international and national debates have emphasized the policy and institutional aspects of the changes, they have practically neglected the welfare effects and mentality of the people.

Some neoliberal gurus and many experts on transition assumed that the relatively low level of poverty and inequality, and the safety nets of the socialist system would make the social costs of the transition tolerable in the transition economies. They also anticipated that re-integration into global markets would open historically unprecedented opportunities for these countries to accelerate their economic modernization, with positive welfare effects. Many Western economic advisers to the new regimes suggested that rapid liberalization was the remedy for curing all the economic ills of the transition countries, while rapidly increasing their export potential.

These assumptions were based more on mainstream economic theories rather than practical experiences of other changes, e.g. the socio-economic implications of decolonization. Based on such foundations, it was thought that, regardless of structural impediments, the opening of previously closed economies would increase exports and imports, as new export sectors would rapidly expand while certain inefficient sectors would disappear following import competition. Although there would be winners and losers, winners would be able to compensate losers due to the cost differences between the industrial countries and the former socialist countries. Hence, unfounded expectations were raised concerning the degree of external assistance needed and rapid improvement of the situation.

By the mid-1990s, reality proved to be quite different. The analysis and objectives offered by the World Summit for Social Development and the social goals of the Millennium Declaration concerning poverty, among other issues, are relevant for many former socialist countries.

Some debated issues

Debates over the social consequences of the transformation and future trends have been influenced by a number of factors. Firstly, one must look at these countries' relation to the past, where there is much less nostalgia for previous Russian dominance or Marxist ideology than ambiguity about rejecting the statist past. Many people still insist that the state should provide job security, price stability, social services, free health and education, and decent pensions. Strong egalitarian and populist pressures are present in society, rooted in the experience of earlier decades. Coinciding with rising income disparities, these pressures have important political implications. In the light of growing inequalities, poverty and social marginalization, certain segments of the populations have challenged the legitimacy of the transformations. In some countries, the neglect of social problems, tendencies towards paternalism and the use of political power for private gain, as well as illicit practices by the new economic elite have exacerbated the situation.

Debates about these issues ultimately seek answers to questions about whether poverty can be eradicated as economic growth and structural transformation seem to exacerbate inequality and perpetuate poverty. Another debated issue—concerning the interrelations between economic development and inequality—seeks to understand the extent to which inequality may be conducive for achieving greater efficiency.

It has been generally recognized that before the changes, countries in this region were 'middle level economies', with GDP per capita that were generally about one third or less than those of the developed countries. Employment, provision of basic health services and social benefits, social mobility (based more on education and political affiliation than on private property ownership and wealth) and social conditions (as reflected by the human development indicators published in the Human Development Reports of UNDP) were generally higher than those solely based on per capita GDP levels. However, over the past few years, inequalities have risen, as public health and education have deteriorated. While there have been improvements for certain segments of the population, many steps backward have occurred at the same time. For example, the life expectancy of the male population in Russia fell to 57 years, reflecting the deteriorating human condition.

Social dimensions of the transformation

The transformation process has included three types of changes, each with profound social consequences. The first was the disintegration of the Soviet Union. States formed on the ruins of the Union had new economic boundaries, institutions and government bureaucracies, which implied new currency, tax, price and market systems. The second was the collapse of the statist/socialist regime, resulting in new institutions with market economy characteristics such as unsubsidized market prices and employment insecurity. The third transformation was the change in social structure, with the old structure replaced by one increasingly similar to middle or low income capitalist societies. In many ways, these changes were interrelated and reinforced each other.

Disintegration of the Soviet Union had significant economic implications for former members of the Soviet Union. The division of labour was drastically changed, which deprived some republics, like

Ukraine and Belarus, of oil and other sources of energy. The republics no longer supplied manufacturing in Russia with raw materials or semi-finished products. Some Central Asian republics lost subsidies they had received from Moscow, while most non-Soviet Central and Eastern European countries lost their markets, as the Russian military industry collapsed. All these resulted in substantial economic decline, hyperinflation, unemployment and government budget collapses.

Independence left many CIS countries bereft of resource transfers, external markets, and many of the institutions necessary for running a modern economy. Tax and fiscal administrations are particularly relevant examples. In addition, as in all transition countries, many state-owned enterprises collapsed when they were cut off from their traditional markets and had to confront world energy prices. To prevent public enterprises and public services from failing, governments borrowed heavily, thereby reducing some of the initial social costs associated with the transition. Much of the subsequent external debt crisis developed from these early borrowings. In many cases, the economic disruptions created by the break-up of the former Soviet Union were compounded by shocks, including armed conflicts and massive terms-of-trade changes. Adjustment to world prices has been estimated to be equivalent to terms-of-trade shocks of up to 15 per cent of GDP. Large fiscal deficits emerged, which initially could only be met by nonpayment of existing obligations and external borrowing.

The collapse of the Soviet market had an adverse economic effect on the countries in the bloc, particularly the former members of the Soviet Union. National economies emerged, and many industries lost their markets. Trade within the old Soviet Union became foreign trade with many new impediments. GDP declined on a scale unprecedented during peacetime. The cumulative loss of output and incomes during 1991-2001 was equivalent to about three years of GDP of the former Soviet Union, although the distribution of these losses among the affected countries and social groups was, of course, different.²

Analysis of the factors responsible for the diversity in GDP decline lies beyond this paper. However, it is necessary to highlight two factors that influenced the social situation, namely the impact of the decline on different sectors and on national policies. Industrial and agricultural output declined very rapidly, due to the collapse of the Eastern markets, the unavailability or loss of means which made important inputs unaffordable, the crowding-out effects of imports and shrinking domestic purchasing power. Output and income losses were much greater and more sustained than those in the USA and Germany during the Great Depression of the thirties. Although there was an initial belief that the richer countries and their institutions would help moderate the social consequences of the transformation, this only happened on a very small scale.

The social consequences of economic decline were aggravated by the well-known 'conditionalities' demanded by the Washington Consensus policies shared by the World Bank, the IMF and Western-educated advisers. These policies included fiscal and monetary austerity measures, trade liberalization, free capital movements, exchange rate unification and devaluation, increased interest rates, removal of subsidies on food and other prices, large scale privatization, tax reforms and other measures. While some countries tried the gradual approach, others introduced radical 'shock treatment'. In certain cases, these policies had favourable effects, resulting in macroeconomic stability, fiscal consolidation, new economic activities, and the development of basic institutions required for the efficient functioning of market economies. However, the human consequences of the transition process were generally neglected.

2 Calculated by the author on the basis of World Bank statistics.

Global market integration

The reintegration of the countries with global markets exposed them to the forces of globalization, which included the different forces of global competition. This integration implied three major changes. Firstly, it led to the development or the reform of institutions, which paved the way for the new regulation of external economic relations, and the establishment of tariffs and other instruments of market oriented trade policy. The main trend was the liberalization of factor movements, the dismantling of the foreign trade monopoly of the state and the privatization of the foreign trade system, the establishment of convertible currency, and the introduction of the new migration regime. The second was the countries' participation in the multilateral trading system and the financial institutions, resulting in the need to fulfil certain conditions required by those institutions. The third change related to the disintegration of the Soviet Union and the dissolution of the Council for Mutual Economic Assistance (COMECON). Relations with new external partners, both countries and transnational corporations, had an important influence on the process, speed and character of reintegration.

The processes have been difficult and unequal, often with painful economic and social consequences. The patterns and forms of competition and the institutions of the global market system, shaped mostly by strong corporations and developed industrial countries, have also made the reintegration process more difficult for the transition economies. The degree of liberalization of the external sector is greatest in Armenia, Azerbaijan, Georgia, the Kyrgyz Republic and Moldova from among the CIS countries. The least liberal economies are those of Turkmenistan, Belarus and Uzbekistan. Countries on the lower level of development with few export industries, e.g. Kyrgyz Republic, Georgia and Moldova, have liberalized their trade more than those that wanted to protect their industries. There are also differences between raw material exporters and the rest. All the countries have different non-tariff barriers. The liberalization of the capital account and particularly foreign direct investment (FDI) flows have developed with varying degrees of intensity.

There have been economic and social benefits and costs of the reintegration. Even though it is practically impossible to quantify its effects on income distribution, one may arrive at certain conclusions. The growing and practically uncontrolled exports of oil, diamonds and different raw materials facilitated capital flight, which provided enormous benefits to the new business elite in the resource rich countries. The growth of FDI had a positive effect on the income of those working in the foreign owned firms. The fast indebtedness of a number of countries in the region increased the burden of debt servicing and constrained public expenditure for health and education.

On the macro level, due to the absence of data, it is impossible to isolate the implications of domestic marketization and the reintegration with the global markets. The two are, in many ways, interrelated and interconnected. The influence of trade on income and employment is more direct in the case of raw material and semi-finished product exporters and this has a positive regional effect in Russia and Kazakhstan, as unemployment in import substituting and inter-industry trade sectors were high (Yudaeva 2002). Foreign direct investments so far have had little impact on employment in general, but regions in the CIS countries, particularly Russia, have attracted far more foreign investments than others; such regions have also attracted mostly skilled labour from other regions. However, their effect on social institutions cannot be judged on the basis of existing data.

The marketization process and the reintegration with the global markets have necessitated the restructuring of the uncompetitive industries. Some of these changes have been taking place with the help of

FDI, which implies lay-offs and repatriated profits. The restructuring process with national capital is still at a relatively early stage in most countries such as the Russian Federation, Ukraine, Kazakhstan, Romania and Bulgaria. Available facilities for the support of dismissed workers and their families remain limited.

The integration of the CIS countries into the global information system has important implications, as it can reduce the information gap between different groups of the society, thus contributing to the reduction of inequality. The use of Internet is spreading very fast in the Russian Federation and has been growing by 20-25 per cent annually since 2001. However, Russia is still among the countries at the lower middle level of Internet users. Other CIS countries also still lag behind.

The UN, particularly the UN Economic Commission for Europe and the UNDP, has been dealing with the social consequences of the transformation. The Social Summit in Copenhagen in 1995 drew attention to the social problems of the former socialist countries. A publication of the World Bank in 1996 raised the question of the responsibility of the policies advocated by the Bretton Woods institutions, though there was little immediate influence on policies. It is important to mention that not one of the countries in the region has fulfilled the targets of the Copenhagen Summit or the Millennium Declaration.

The erosion of human capital and social support systems

CIS countries and other countries like Bulgaria and Romania inherited a relatively large human capital stock from the socialist period, due to the relatively large investments in education, and the relatively well-developed and comprehensive system of pre-primary, primary, secondary and university education. They also established research infrastructure that was more developed and sophisticated than those of market economies on similar development levels. After the changes, the quality of state financed education deteriorated quickly and a large number of research institutes ceased to exist, as tens of thousand of scientists, researchers and engineers emigrated.

The introduction of market institutions from 1991 onward, and the transformation recession also seriously undermined the social support system of the socialist period (based on low, administered prices for food, rent, household utilities and other basic goods and services, along with the virtual guarantee of a job). Expenditure on health and education amounted to around 5 per cent of GDP each before the changes in the former Soviet Union. By the end of the 1990s, expenditure on education declined to 4.2 per cent of GDP, and in the low income CIS countries, to 3.8 per cent. Health expenditure went down to 3.4 per cent of GDP, and in the low income CIS countries, to 2.7 per cent (UNDP 2003).

Before the transition, education used to be basically free for all. Enrollment ratios for girls at all levels were high and the quality of education was relatively high. Over the years, the situation began to deteriorate. By the beginning of the new millennium, the school system in general deteriorated due to budgetary constraints and neglect. While the share of public education expenditure averaged around 5 per cent of GDP in CIS countries at the beginning of the 1990s, it declined to around 4.0 to 4.2 per cent of a smaller GDP by the end of the decade. According to a UNICEF-Innocenti report, the average share of education in terms of GDP in the low income CIS countries is still higher than the world average of low income states, but with much greater dispersion. In Armenia, Georgia and Tajikistan, it was below 2 per cent of GDP (UNICEF, Innocenti Research Center 2002: 14). There is an increasing social stratification of the educational system, resulting in a deteriorating prospect for low income people that will contribute to inferior employment opportunities and marginalization.

The health situation has deteriorated in all the CIS countries, with unequal access to services. In some of the CIS countries, mortality is rising or has ceased to decline, the incidence of serious diseases (e.g. tuberculosis) has increased, and some infectious diseases (e.g. malaria) have reappeared. In the Russian Federation, the accumulation of unfavourable changes in the population's health, the unsatisfactory development of basic medicine, and the inaccessibility of highly-effective treatment methods have further aggravated the dynamics of morbidity and resulted in a rise in the disablement level among the population. The deterioration can be viewed through the fast spread of 'social diseases' Since 1992, the annual increment in the number of people suffering from tuberculosis has been 10 to 15 per cent. Among those registered for the first time, there was an increase in the share of people with neglected or destructive forms of tuberculosis. The incidence of syphilis registered in 2000 was 31 times higher than that in 1990. The rise in the HIV morbidity also testifies to the rapid spread of the HIV epidemic in the country. With the emergence of privately financed (out-of-pocket) and unregulated health care, access to health care services by the poor has diminished.

The inherited structure of social benefits, comprising both social insurance (pensions and unemployment benefits) and social assistance programs (including family allowances), is inadequate to deal with the needs created by the transition. Social insurance is largely financed through payroll taxation and federal budgetary funds, whereas social assistance is largely the responsibility of local authorities, who also finance and deliver the bulk of education and health services and subsidize housing and domestic utilities. Enterprises still provide a wide array of social benefits for their workers and local communities, encompassing housing, health care and child care. A more profound analysis shows not only the gap between expectation and reality, but also an increasingly unequal distribution of economic gains and losses, both within countries and between them.

New growth path

Since the late 1990s, GDP has been growing in nearly all 14 countries in the CIS region and also in Bulgaria and Romania, for reasons which go beyond the scope of this paper. Although economic growth in these countries cannot compensate for the losses suffered during the 1990s, it at least contributes to some improvements in the standard of living of a large segment of the population, particularly for those in some of the oil producing countries of the region. In 2003 and in 2004, the upturn in the largest countries—the Russian Federation, Ukraine and Kazakhstan—benefited the whole region. Growth was driven by the expansion of private consumption, investments and oil exports. While there was some improvement, mainly in the capital cities and larger towns, most of the adverse social consequences of the changes remained, with high incidences of poverty and unemployment in the small towns, one-industry towns and villages.

The following reviews the factors and processes related to some fundamental social problems, particularly those which contributed to increasing inequality—including the labour market situation, the sources and consequences of poverty, the new social stratification, as well as other outcomes of the changes. Some aspects of social policies and their effectiveness will also be discussed.

The evolving labour market

The labour market has been the most sensitive and difficult of the three main markets (the market for goods, capital and labour) in the transformation process. It has been most directly connected with political and institutional changes. In the Russian Federation, Ukraine and Kazakhstan, it has been international-

ized and de-internationalized simultaneously, and has been influenced by ethnic diversity, exclusion and discrimination. The economic consequences of the transformation include unemployment, de-skilling, privatization and job insecurity. The relationship between urban and rural areas and the increase of regional differences also influence the evolving structure and institutions of the labour market.

Social implications of the labour market

The establishment of labour markets in the former socialist countries had limited success in reducing poverty, providing employment, increasing labour mobility, and facilitating market oriented wage determination. Most of these countries built up institutions for handling both active and passive labour market policies and introduced some unemployment benefits, retraining institutions and job counseling. The labour markets are interrelated with all the other major markets and also with important demographic and social processes like the age structure of the population, health and education.

Historically, markets in different countries have been the result of organic development, rooted in exchange and influenced by the socio-economic systems. These systems also created the legal framework and other institutions indispensable for its functioning. As the result of the character of the systemic changes, there was an important contradiction from the beginning between the ideological assumptions related to the tasks of market building and the practical measures. Both the domestic and external ideological advocates of the free market system demanded the downsizing of governments in the former socialist countries.

The experts, advocating liberal or neo-liberal theories in the CIS countries, particularly in the Russian Federation, recommended 'de-etatisation' in the labour market. The tasks, however, could not be implemented without the active involvement of the governments that had limited experiences dealing with 'market failures'. Also, while there had been some form of market for goods and capital in the socialist countries before the changes were made, there was no labour market since labour was not considered as a commodity.

Central planning offered job security, guaranteed benefits, employment, and high labour force participation (Barr, 1994: 122-123). While the central allocation of labour was abolished in most countries even before the systemic changes began, certain elements survived in the form of wage rigidities, allowing narrow differentials and little open unemployment. Labour hoarding that was encouraged by the system resulted in a highly inefficient use of labour. In a number of countries, skilled workers earned more than engineers, and in a number of cases, semi-skilled workers earned more than skilled workers. Labour mobility was restricted by legal measures and socio-economic outcomes of the functioning of the system.

The development of labour market institutions in the Western region of Central and Eastern Europe was relatively fast. However, it was slower and more difficult in the CIS countries, where specific problems emerged. The full employment commitment of the socialist governments—achieved by huge state-financed investments in labour intensive sectors of the economy—came to an end. Unemployment grew in open and hidden forms because of the obsolescence of skills. The decline in employment however was much smaller than the decline of output, as firms adapted to the problems with lower or unpaid wages than with unemployment. As a result, there was an increase in the number of low paid jobs, which was a factor of growing inequalities among the working population.

Persistent structural unemployment or temporary lay-offs?

Unemployment statistics do not reflect the actual situation very well since many of the unemployed (according to statistics in the CIS countries, between 50-80 per cent) do not register in the labour offices, given the lack of benefits and services provided. In Russia and Ukraine, where output declined during 1990-94 by 50 per cent, registered unemployment remained below 5 per cent even. By 1997, when statistical data became more reliable, the figure rose to 11.8 per cent but employment started growing again a few years later.

Some experts considered unemployment as a positive factor in promoting structural transformation (Jackman 1999). This was not the case. Transnational corporations investing in the region and the new private firms mainly recruited from among those employed in the state sector or in other private firms. This was probably due to the fact, that most of those unemployed had lower skill or educational levels, or that they were older people over 45. There has been a decline in the participation rate, partly because of shrinking employment opportunities for women, not well reflected in the statistics on unemployment.

Small entrepreneurs, the informal sector and rural problems

The rapid increase in the number of small entrepreneurs was another important indicator for the changing patterns in the labour markets. Beyond the fact that a great number of people became self employed after losing their jobs, the increase of the number of small firms failed to create more employment opportunities.

A very important area in absorbing unemployed people has been the growing informal or parallel sector of economy, which has created new jobs and absorbed part of the displaced labour force. Although many job seekers find this source of income degrading since informal activities do not correspond to their education or income expectations, they turn to it for part time work to supplement their incomes. Unfortunately, there is little information on the employment and incomes earned in this sector, and therefore it is difficult to objectively evaluate the role of the growing informal sector in increasing wage inequality.

Another source of new employment opportunities is the service sector, which was previously undersized, except for social services, health care, education, science, and culture. As the statistics for these occupations were missing or included in the former labour statistics under other economic activities, they were heavily underestimated. The previously poorly developed trade, catering, banking and insurance, communications, and real estate activities have boomed since transition in all the former socialist countries. Wages, of course, differ according to the type of services.

Employment in agriculture fell faster than total employment. Large-scale agriculture in the form of collective or state farms and agro-industrial complexes used to be one of the major employers in central and Eastern Europe, particularly for the unskilled rural labour. The transformation from collective farming into private farming, the loss of state subsidies and guaranteed markets, and falling domestic demand significantly reduced labour demand and employment in this sector. According to many analysts, the rural population, comprising the largest group of the poor in certain regions of the Russian Republic, in the Caucasus and Central Asia, were disproportionately affected by the hardships of the transformation (Mikhalev, 2000: 40). The number of small farmers however increased substantially, and this may become an important problem in the future, due to the low level of competitiveness of small-scale farming. The agricultural population has been one of the main losers in the transformation process. The large state and

collective farms have either been dissolved or have gone bankrupt. In most cases, they have been replaced by subsistence farming, similar to those in developing countries.

The increase in unemployment not only resulted in the loss of income but also in the deterioration of the social status of the individuals and their families, as well as growing job insecurity. The trends of unemployment depend not only on the prospects of economic growth but also on structural changes and the demand for skills. The Ministry of Labour in the Russian Federation projects a considerable growth of unemployment in the near future. Power industry, public utilities, railway and metallurgy sector reforms will deprive hundreds of thousands (if not millions) of Russian people of their jobs. "It goes without saying that no population employment departments (not to mention small business or shadow economy) will be able to cope with such a huge mass of people. All these things will eventually result in the fact that the human labour price will drop considerably in Russia as a whole. The supply will exceed the unbalanced employment demand by several fold. Hundreds of thousands of people will remain unemployed" (*Pravda*, 18 February 2003).

Problems of youth and women

One of the most difficult problems in the former Soviet republics and in the region in general is youth unemployment. Unemployment rates for those under twenty five are almost twice as high as the general unemployment rate. Some documents of international organizations emphasise that one of the problems for young people is their lack of work experience. Another problem is the inferior education of these young people due to the fact that they were educated at the time when the transformation resulted in greater differentiation and, in many cases, the deterioration in the quality of education.

Neglect and homelessness among children and young people have become alarming characteristics of Russian society. This social phenomenon is a consequence of the current socio-economic and moral situation in Russia, engendered by a whole complex of factors behind the fall in living standards of a substantial part of the population, a deterioration in the mental health of the adult population, the spread of child abuse both in the family and in orphanages, a distancing of the school from children in difficulties, destruction of the traditional system of child upbringing, a fall in the moral standards of the population, and the growth of crime.³

Unemployment among women and youth is a particularly difficult issue in Central Asian republics. In Tajikistan for example, from the total number of women and young people aged 15-29 years in the labour force in 2002, some 53 per cent and 66 per cent respectively were unemployed.

3 The current generation of young people has lived through a period of extraordinary change and uncertainty. The availability of age-appropriate services and information and any real understanding of their needs both remain very limited. Risky behaviour, reflecting the stresses they are under, leads to very high rates of accidental death, suicide, and alcohol and drug abuse. Trafficking of young women is a serious problem in all three countries. Rates of sexually transmitted infections (STIs) among young people in the Russian Federation and Belarus have doubled in the last decade. Closely connected with risky behaviour, the rapid growth of HIV is concentrated among young people. Currently, Ukraine and the Russian Federation have the fastest-growing epidemics in the world; in the Russian Federation, the number of officially-registered HIV cases doubled during 2001. Over 70 per cent of new infections are among young people aged between 15 and 29 years. While the epidemic began among intravenous drug users, its spread into the mainstream population is already apparent. The transmission of HIV from mother to child is a new and growing phenomenon in the three countries. At least 20 per cent of children born to HIV-infected mothers are abandoned, and many spend extended periods in maternity hospitals because of the lack of alternative solutions.

The disintegration of many families and the breakdown of family ties are closely interrelated with the problems of young people. This problem is also related to the increase of poverty in the region, particularly the urban areas of the Russian Federation, Ukraine and Belarus. There has been a growth in the divorce rate, a decline in marriages and an increase in the number of children born out of wedlock. The growth in the number of teenage mothers has also become an acute problem.

Poverty and inequality

While unemployment, changes in the labour markets and poverty are in many ways interrelated, poverty should be dealt with as a separate issue since it is an indicator and a major factor of growing inequality. The reduction of poverty is a major condition of the economic and social consolidation of the region.

Who are the poor?

Poverty in this region is not new and has existed even before the transformation. Most of the countries began their transformation with extensive hidden unemployment and at least one-tenth of its population below the then subsistence level (based on a 'social minimum' consumption basket). The growth of poverty has not been a consequence of the transition crisis, as it has been growing since the early 1980 due to economic difficulties, external indebtedness and mismanagement.

Poverty statistics are seldom exact or reliable. They depend on the concept and the method of measurement. One common approach in poverty measurement is to define the 'poor' as those persons living in households with income or expenditure significantly below the average in their country. The rationale for this definition of relative poverty is that people whose living standards (as measured by their income or expenditure) fall far below the average are at risk of being excluded from the advantages and benefits considered normal in society. Where poverty is measured according to a relative criterion, a rise in inequality will cause the number of people in relative poverty to increase. When inequality declines, the number of relatively poor people will drop. An alternative approach to poverty measurement involves calculating the cost of a minimum 'basket' of goods that people would need to survive. Globally, the absolute poverty threshold has been defined as two dollars income per day. According to the two dollars threshold, there were about 50 million people living in poor families in the former socialist countries at the end of the 1990s, mostly in the CIS countries.

Since then, however, the number of poor households has risen. By 1993, some 32 per cent of the population in Russia was living below the revised official poverty line. At that time, some 12 per cent of the Russian population was very poor (below 50 per cent of the poverty line). In early 1994, an estimated 26.8 per cent were poor, and 10.4 per cent were very poor. Real earnings have halved since their end-1991 peak and remain somewhat lower than the 1987 level. Reductions in work hours have been widespread; workers have been placed on short-time work status or had to fake involuntary leave.

In the Russian Federation during 1993 and 1994, only 40 per cent of the workforce was paid fully and on time. High inflation has adversely affected the poor, especially those who rely on modest pensions and unemployment benefits. Earlier poverty indicators were based on income data, which are problematic (especially during high inflation), and rely on unrepresentative survey sources.

Table 2.
Trends in real wages in the region, 1989-2001

Countries	1989	1995	2001
Bulgaria	100	60	51
Romania	100	74	71
Armenia	100	5	11
Azerbaijan	100	14	50
Georgia	100	12	40
Kazakhstan	100	23	36
Kyrgyzstan	100	21	26
Moldova	100	25	32
Russian Federation	100	36	52
Tajikistan	100	5	7
Ukraine	100	44	46

Source: UN Economic Commission for Europe (2002: 167).

A two-year analytical work by Russian and international experts on ‘enhancing the measurement, monitoring and analysis of poverty’⁴ is probably the most comprehensive work on the problems of poverty in Russia. According to the Report (World Bank 2005), the national incidence of poverty is close to 20 per cent. The rural population has the highest rates of poverty (30.4 per cent), while the urban population has a poverty rate of 15.7 per cent. The majority of the poor, close to 60 per cent, live in urban areas. The poverty rate is high in small and remote towns, particularly in depressed regions. The unemployed and many of the 30 million pensioners belong in the poor category. A large group of impoverished Russians is made up of able-bodied women and men with primary education, in their 30s and 40s, who are marginalized in the market economy and hence operate in the urban black or informal economy. Millions of others in this group are trapped in remote industrial small towns where manufacturing has collapsed. Many of them live in the far north where job opportunities have dried up. The situation of those who have some jobs is often aggravated by the fact that wages in the unregulated labour market are often far less than the subsistence minimum and are sometimes withheld for months.

In Russia and other CIS countries, the working poor predominate. About half of the poor live in households where the head of household is employed. The largest subgroup is composed of households with children, including single-parent and young households. Generally, the younger and more numerous the children, the more likely that the family is poor. Nearly 62 per cent of families with three or more children fewer than six years are poor. Single-parent households are much more likely to be poor compared to other types of families. More than 90 per cent of such households are headed by women.

Poverty among some of the ethnic minorities, particularly the Roma (gypsy) population, is one of the acute problems in some of the CIS countries, Bulgaria and Romania. The Roma population in these countries represents the real ‘underclass’ who are excluded from the mainstream of society because of their ethnicity and status.

4 This has been a collaborative project by the World Bank, the United Kingdom Department for International Development, the Russian Ministry of Labour and Social Development, the ‘Goskomstat’, the Russian Statistical Office, the Ministry of Labour and Social Development and Trade and the Ministry of Finance.

The poor is not a stagnant group of people. Some of the poor households rose above the poverty level during 1992-93, even while poverty was increasing as a whole. Nearly one-half of Russian households that were very poor in 1992 were not considered as such a year later, while a quarter of nonporous households became poor over the same period. Regional differentiation of welfare indicators dramatically increased during the period. One must, of course, differentiate between countries at the middle level and low level of economic development. Russia, Romania and Ukraine are generally considered middle level countries. Poverty is more widespread in some CIS countries, which are classified as low income countries.⁵ These poorest CIS countries show many characteristics of developing nations and need substantial international assistance to foster economic and human development. The external sources of funds have been relatively small, compared with the losses in GDP and the burden of debt service. During the 1990s, poverty and income inequality increased to very high levels in Central Asian republics.

Physical indicators of poverty have steadily worsened and social safety nets have deteriorated greatly, mainly owing to the limited resources available for poverty reduction and the absence of income and employment generation programs. For example, about 50 per cent of the population in Kyrgyzstan lived below the poverty line in 2002. During the 1990s the population of Tajikistan increased by 14 per cent, reaching 6.5 million in 2002, while GDP fell by 64 per cent, resulting in growing poverty. The majority of the 7.6 million people of Azerbaijan, 3 million of who are children live in poverty, (an estimated 60 per cent of the population) in spite of the rich oil resources of the country. Although privatization of collective farms and state-owned enterprises and the development of the petroleum industry are expected to have positive social implications, they have yet to benefit vulnerable population groups. Poverty is also a grave problem in Bulgaria, especially among rural households and families with children. The Roma community, which comprises around 7 per cent of the population, is reported to be 10 times poorer than other groups (World Bank 2001).

Since the mid-1990s, there has been some improvement in most of the CIS countries and also in Bulgaria and Romania in poverty reduction, mainly due to economic growth. Reforms in the social sector are well under way in practically all these countries, although they may not yet provide equal access to all groups or offer the range of services previously provided. The decentralization of most social services to local governments is not yet matched by the availability of skilled personnel and financial resources; the proportion of people in absolute poverty has fallen even in some of the poorest countries. However, the number of people living in poverty remains substantial. In 2001, half the population in Armenia, Georgia, Kyrgyzstan and Moldova was living below national subsistence levels. In the Russian Republic, real wages were only 53 per cent of those in 1989 (Innocenti Research Center estimates). Unemployment, lower average income and the growing inequality in the distribution of national income and wealth are the most important factors in the growth of poverty in the region. The Gini coefficient for household income per capita rose from 0.26 to 0.43 in the CIS countries between the late 1980s and 1990s.

The lack of resources, unemployment and income inequality have created particularly grave social problems in other low income countries of CIS. Socio-economic hardships have weakened the health and educational system while drop out rates have increased. The poor quality of education, low morale among teachers, and chronic under-funding of schools pose many problems for the rural areas. In many cities, drug abuse, prostitution and juvenile delinquency are increasing rapidly, as are the numbers of

5 Armenia, Azerbaijan, Georgia, the Kyrgyz Republic, Moldova, Tajikistan and Uzbekistan are the poorest countries in the CIS, and their transition to market-based economies over the past decade has been extremely difficult.

children living or working on the street. In addition, the growing social inequity facing women in many of these countries may deteriorate and create additional problems.

Growing inequality and the new social stratification

Clearly, the transformation process and its main factors increased inequality in all the former socialist countries, particularly those in the former Soviet Union.

The social system in these countries was not egalitarian. Instead, it was the kind of society characterized as meritocratic in the West. Even within the group characterized as the ‘nomenclature’, there were differences, according to their role in the party or state hierarchy, and the degree of their control over the allocation of resources and in decision making. These differences were not only ‘status differences’ but were expressed in their standard of living and access to certain goods and services. The top political elite, the leading echelon of the technocrats, and the top managers of the state owned enterprises belonging to the ‘nomenclature’ controlled the allocation and distribution of resources. Professionals enjoyed a higher status in society. The blue-collar workers, particularly the skilled workers, had job security and more privileges compared to the peasantry.

The winners and the losers

The transformation process had a profound effect on the structure of the society. In every society there are winners and losers. The normal functioning of a market system results in some people climbing up the ladder of income and wealth, while others lose their former economic and social position. Similarly, the transformation process in the former socialist countries brought about radical and unprecedented social changes. The winners were the young, well educated, well-connected and entrepreneurial, especially those privileged enough to grasp the assets of the state owned firms. On the other hand, the losers were more numerous and diverse and comprised the old, the pensioners in general, the less educated, women, those with little or no skill, rural people living in remote regions or in small towns, and those belonging to certain ethnic groups. The decline of GDP, the ‘informalization’, liberalization (which included the cessation of the subsidized price system), inflation and unemployment hit all the wage earners. Those with little or no savings have to sell their assets in order to survive.

Income disparities in the Russian Federation between rich and poor during the years of the transformation are reflected in Table 3.

It may be evident from this ‘social balance sheet’ that the concept of inequality must be understood from a multi-dimensional perspective. In addition to the same factors as in other transformation countries, the increase in inequality in Russia has an important territorial dimension, due to its size, geography and heterogeneity. The Russian Federation with its climatic, ethnic and economic variety had a relatively higher level of inequality right from the beginning. The regions, even during the pre-transition era, have been diverse in their level of economic development, the density of transport, and consequently in mean real incomes. Although there was convergence during the Soviet period, this could not eliminate the differences in income levels. Political and socio-economic changes further increased divergence across regions. The income distribution between population groups and regions has also widened in other republics. The following quote by the President of Kazakhstan is relevant also for the majority of the Central Asian CIS countries:

Table 3.
Income shares in the Russian Federation by quintiles, 1975-2001

Years	Poorest 20%	Second	Third	Fourth	Richest 20%	Total
1975	9.5	14.8	18.6	23.3	33.8	100
1980	10.1	14.8	18.6	23.1	33.4	100
1985	10.0	14.6	18.3	23.1	34.0	100
1990	9.8	14.9	18.8	23.8	32.7	100
1991	11.9	15.8	18.8	22.8	30.7	100
1992	6.0	11.6	17.6	26.5	38.3	100
1993	5.8	11.1	16.7	24.8	41.6	100
1994	5.3	10.2	15.2	23.0	46.3	100
1995	5.5	10.2	15.0	22.4	46.9	100
1996	6.2	10.7	15.2	21.5	46.4	100
1997	6.0	10.2	14.8	21.6	47.4	100
1998	6.1	10.4	14.8	21.1	47.6	100
1999	6.1	10.5	14.8	20.8	47.8	100
2000	6.1	10.6	14.9	21.2	47.2	100
2001	5.9	10.1	14.6	21.1	48.3	100

Source: GOSKOMSTAT of the Russian Federation 2002.

“The society is fully aware that the above gap exceeds the admissible limits. If Kazakhstan is a state of a thin layer of the well-off, then, by virtue of too low vitality, instability both within and without, it will be doomed to vegetative existence at best. We have already been a state of the poor though not in its pure form... Domestic political stability and development would rest on all the three classes: the rich, the middle and the poor. The society needs all of them, though naturally—in a normal civilized proportion.

“Polarization acquired a graphic manifestation in the relations established between the city and the countryside. In both cases we witness a global process of social differentiation with the gap there between growing steadily. Within the nearest decade the country-side must become a priority area from the point of view of giving an additional impetus to market transformations, to emphatic settlement of social problems and development of infrastructure.

“We are to expect considerable rejection of a free labour force in the country-side, significant migration to the city from the country-side and ever developing processes of urbanization. The country-side of today has become an epitome of major social problems: nonpayment of wages and pensions, backwardness, poverty and unemployment, poor ecology, poor infrastructure, education and health care. Meanwhile the country-side manifests the highest demographic potential” (Embassy of Kazakhstan document, Feb. 2005).

The new middle class and the new rich

Almost all the protagonists of the changes underlined the necessity of developing a new ‘middle class’ as the new owners of the privatized state property, necessary for the creation of a well functioning economy. In the economic history of the Western world, the development of property owners, or a capitalist class was a long-term process. This was also the case in the pre-socialist period of the Central and Eastern European countries as well as Russia.

Privatization was considered as the main instrument for the development of the new middle class. It had two dimensions: the ‘organic development’ of private ownership and the transfer of wealth from state ownership into the hands of domestic or foreign individuals or firms. The latter has resulted in radical shift in income distribution and has become the most important source of income inequalities. One of the consequences of restitution, voucher privatization, public auctions or direct sales of state property has been the increasing importance of capital income, related to ownership, among the sources of income. Of course, this is received by a small minority of the population. The idea of worker privatization, a popular concept during the early stages of the changes, as a more egalitarian form of private ownership has been more or less forgotten in the process.

There are significant differences among the respective countries concerning the relative importance of the different forms of capital income. The role of dividends is relatively small, while the concentration of larger assets and corresponding larger capital income in the hand of the few is greater in countries where the legal framework is less developed.

Privatization has also involved small and medium size enterprises. Capitalists in these small and medium size enterprises comprise about 90 per cent of the entrepreneurial middle class. More than half of them lost their jobs and starting some business became the only means of making a living. These small entrepreneurs include micro-entrepreneurs of the informal sector, who are similar to the ‘barefoot-capitalists’ of the developing countries. Most of the small entrepreneurs are in commerce, handicrafts and services. While their total number is relatively large, they get a rather small proportion of capital incomes. In Russia, their share is around 15-18 per cent.

Although ways of becoming very rich within a relatively short period of time might have been often immoral in some countries, they were legal and mixed with illegal activities in others. The following patterns could be observed (with varying levels of importance in individual states):

- *Trade opportunities*—the market evolved in certain new segments or niches (banks, foreign exchange, information technology, car imports, industrial consumer goods etc) as a result of liberalization, and large fortunes were obtained through the trading system.
- *Insider privatization or buying out (using the privileged position of being a top manager)*—state owned production firms were pushed into bankruptcy and purchased for low prices, often by borrowed money, restructuring, or the sale of parts for much higher prices. Sometimes, investments in other branches were made, or parts of the originally purchased firms were modernized. This method was often combined with the active participation in the stock and currency exchanges, often using insider information.
- *Control over resources*—In Russia and some of the CIS countries with important raw materials or oil, certain political or government elites gained control over these resources, resulting in large monopolies, particularly in the extracting industries. The number of billionaires in the Russian Federation is only second to the United States. The largest private owners account for 42 per cent of employment and 39 per cent of sales (*Beyond Transition: 3*). The external revenues facilitated large foreign investments and other operations abroad.
- *Patent technology*—Important inventions or patent or defense related technology which were not properly valued and utilized in the state owned enterprises were obtained and commercialized, mainly through finding a foreign partner with whom joint ventures could be established.

- *Exploiting the system*—This form opened the door to criminal elements at an unprecedented scale in the history of capitalism. Exploiting the loss of government control or special positions in the administration, some gained access to important assets in several sectors of the economy, particularly in hotels, restaurants, commerce and banking. The lawless system, often characterized as ‘cleptocracy’, was clamped down only during the last couple of years, since the end of the 1990s (*Beyond Transition*: 6).

The upper class in the CIS countries includes the political elite, top bureaucrats, and army leaders. The most recent changes in the political power structure have involved many from the middle echelon of the former party, state and army bureaucracy, who are called ‘silniki’, meaning ‘power-people’. Top managers in foreign owned and large private firms enjoy high salaries and represent the most ‘globalized’ part of the elite. The evolving middle class includes the small businessmen, professionals, those in science and education, and the middle and lower level staff in the public administration.

According to some estimates, about two thirds of the population in Russia (and a much greater proportion in the other CIS countries) belong to the lower income group. Table 4 reflects the degree of inequality in the respective countries. As far as occupational status and sectoral characteristics are concerned, the lower income group is extremely diverse in the countries of Eastern Europe and the CIS. The transformation process has had an adverse effect on their status and material situation. The decline of their real income has been quite substantial, and they have become vulnerable and exposed to the adverse effects of the changes, while enjoying few positive effects compared to the middle class or the new political and economic elite. The majority of the peasantry belongs to this group and constitute a relatively large share of the population in some CIS countries, Bulgaria and Romania.

The lower income groups are quite heterogeneous, divided by gender, skill levels, sectors, geography and ethnicity. Many of them belong to the category of the working poor. About one third of all the workers in the Russian Federation belong in the low paid category, receiving less

Table 4.
Inequality in income or consumption around 2000

	Year	Share of income or consumption (percentage)				Inequality measures		
		Poorest 20%	Poorest 20%	Richest 20%	Richest 10%	Richest 10% to poorest 10%	Richest 20% to poorest 20%	Gini index
Armenia	1998	2.6	6.7	45.1	29.7	11.5	6.8	37.9
Azerbaijan	2001	3.1	7.4	44.5	29.5	9.7	6.0	36.5
Belarus	2000	3.5	8.4	39.1	24.1	6.9	4.6	30.4
Bulgaria	2001	2.4	6.7	38.9	23.7	9.9	5.8	31.9
Kazakhstan	2001	3.4	8.2	39.6	24.2	7.1	4.8	31.2
Romania	2000	3.3	8.2	38.4	23.6	7.2	4.7	30.3
Russian Federation	2000	1.8	4.9	51.3	36.0	20.3	10.5	45.6
Tajikistan	1998	3.2	8.0	40.0	25.2	8.0	5.0	34.7
Ukraine(*)	1999	3.7	8.8	37.8	23.2	6.4	4.3	29.0
Uzbekistan	2000	3.6	9.2	36.3	22.0	6.1	4.0	26.8

Source: UNDP (2003).

(*) Data refers to urban areas only

Table 5.
Gender income differentials, 2001

	<i>Estimated earned income</i>		
	<i>(PPP US\$)</i>		
	<i>Female</i>	<i>Male</i>	<i>Female to Male (%)</i>
Armenia	2 175	3 152	69.0
Bulgaria	5 484	8 378	65.5
Kazakhstan	5 039	8 077	62.4
Romania	4 313	7 416	58.2
Russian Federation	5 609	8 795	63.8
Tajikistan	891	1 451	61.4
Ukraine	3 071	5 826	52.7
Uzbekistan	1 951	2 976	65.6

Source: UNDP (2003).

than two thirds of the median earnings) About 12 per cent belong to the ‘very low paid’ category, earning less than one third of the median earning (Russian Longitudinal Monitoring Survey, 2000).

In view of the sources and consequences of the changes and growing inequality, government policies—which can moderate the adverse social effects and consequences of unemployment, de-skilling and other forms of degradation—have special importance in these countries. The necessity of policies for poverty alleviation is also unquestionable. The increasing inequalities, the impoverishment of large number of people, the conspicuous gap between the rich and poor may create social tensions that may even explode in violence. To what extent are these policies already at place? Are the governments able or ready to reduce the adverse effects of the transformation? What should be the priorities of these policies? The answers to these questions require a much more thorough and detailed analysis of the economic conditions and the new political and economic power structure, which goes beyond the scope of this paper.

Challenges for national social governance

Most of the international organizations are recommending the ‘standard trio’ to the transformation countries as priorities for their social policies: social protection (safety net), health and education. The national and international programs for good governance include growth and employment oriented national policies, and democratic participation.⁶ Major investments in education and health, and policies to provide people (especially the young) with skills are probably the most important long term goals in all the countries.

Practically all the countries in the region have some form of social safety net, like unemployment benefits which, in principle, should provide some support to the most needy and most vulnerable citizens. In practice, these benefits are very small (e.g. around 20 per cent of the average wage in Russia) and very few unemployed receive them.

⁶ President Putin identified among his second-term priorities (after winning re-election on March 14, 2004) stepped-up social programs and mechanisms to sustain intensive economic growth, which will boost the country’s GDP and sharply cut poverty.

The rise in poverty levels and the initiatives of some intergovernmental organizations have led the countries to critically re-examine their policies and to adopt some form of poverty reduction measures. Poverty monitoring procedures by investigating the incidence of poverty by gender, region and ethnic group have improved. Using available data and monitoring systems, the countries have begun to analyze the poverty impact of their policies and of exogenous shocks, and to formulate approaches to increase the pro-poor focus of these policies. The poverty reduction strategies are closely related to reforms in the labour markets which include the development or improvement of labour legislation and the creation of new employment opportunities. For example, Azerbaijan adopted programs for training and retraining employees and established an information system for labour markets. A similar information system was developed in Tajikistan to monitor labour markets and to improve systems for job search, particularly in the private sector. The governments of Central Asian countries have also introduced reforms of income generation policies aimed at increasing the general wage level as well as improving payment systems.

Anti-poverty initiatives in low income countries like Armenia, Azerbaijan, Georgia, the Kyrgyz Republic, Moldova, Tajikistan and Uzbekistan are particularly important due to the high incidence of poverty and deprivation in these countries, aggravated by a large debt. Much of the public debt, which accumulated during the early 1990s in the poorest CIS countries, was taken on to bolster day-to-day government spending after the breakup of the Soviet Union. As mentioned earlier, some of these poorest countries are paying a considerable sum – 2 to 4 per cent of their national incomes – to service external public debt. In certain cases, this is more than what they spend on education or health care, which have declined to historically low levels, putting the long-term well-being of an entire generation of children at risk.

National strategies have been stimulated by some international initiatives. In 2002, the World Bank and other international financial institutions launched the CIS-7 Initiative with governments of seven of the poorest countries in the region. These recommendations contain strategies that go much beyond the social sphere. It has become increasingly clear that the reduction of poverty cannot be achieved only through social transfers, as it also requires sustained economic growth, employment-friendly economic

Table 6.
Public Spending Priorities, 1990-2000

	Public expenditure on education (as % of GDP)		Public expenditure on health (as % of GDP)		Military expenditure (as % of GDP)		Total debt service (as % of GDP)	
	1990	2000	1990	2000	1990	2001	1990	2001
Armenia	7.0	2.9	..	3.2	..	3.1	..	2.6
Azerbaijan	..	4.2	2.7	0.6	..	2.6	..	2.4
Belarus	4.9	6.0	2.5	4.7	..	1.4	..	1.9
Bulgaria	5.2	3.4	4.1	3	3.5	2.7	6.6	10.1
Kazakhstan	3.2	..	3.2	2.7	..	1.0	..	14.9
Romania	2.8	3.5	2.8	1.9	4.6	2.5	(.)	6.7
Russian Federation	3.5	4.4	2.5	3.8	12.3	3.8	2	5.6
Tajikistan	9.7	2.1	4.9	0.9	..	1.2	..	7.6
Ukraine	5.2	4.4	3.0	2.9	..	2.7	..	6.0
Uzbekistan	4.6	2.6	..	1.1	..	7.4

Source: UNDP Human Development Report, various years.

policies, a high and sustained level of public expenditure in health and education and structural reforms in taxation. Together, these measures will be able to moderate the adverse social consequences of inequality in income and wealth and promote social mobility.

Conclusion

This paper has dealt mainly with the problems of inequality and poverty within the countries east of the European Union frontiers. Poverty emerged as an adverse consequence of the transformation process, while inequality was the consequence of the new distribution of income and wealth as well as other policies. In spite of economic improvements, these problems persist in most CIS countries.

Different dimensions of the transformation process, including integration with global markets and the spillover effects of the globalization process, have resulted in growing inequality, de-industrialization, de-modernization, and widespread impoverishment. The evolving capitalist economy remains dominated by a few politically-connected financial-industrial groups (oligarchs) centered on the exploitation of raw materials and the relatively small and non-dynamic small and medium-sized enterprise sector, that some authors term a 'great leap backward'.

As a result of the adverse consequences of the changes, some of the countries are now closer to the developing world than to the economically advanced regions. The upper class, particularly the new bourgeoisie in Russia and the other CIS countries, seems to more closely resemble the rent seeking parasitic capitalists of the past than a modern entrepreneurial class. Without major changes in economic and social policies, inequality and the erosion of human capital will get worse in most of these countries. In order for such a change to happen, there must be a radical change in the current power structure. In spite of the uncertain and problematic path to progress, there is a need for a new middle class capable of initiating positive developments.

The main causes of poverty and inequality in these countries include the decline of output, hyperinflation, unemployment and macro-economic stabilization policies. They also include other factors such as the disintegration of the Soviet Union and the redistribution of productive assets in favour of a select minority. Employment creation, poverty reduction and social consolidation have been important tasks in this difficult and heterogeneous region. Although these tasks are formally similar to those in other, mainly semi-developed, regions of the world, the required policies must take into account the specific characteristics of the countries, which are at various stages of climbing out from the transition crisis. Many labour market problems are increasingly of a long term, structural nature, involving de-skilling, changing ownership patterns and new relations with the global marketplace.⁷

The level of inequalities in incomes, wealth and consumption will have a long term impact, especially on the marginalized groups, and government intervention is necessary to avoid tension and conflict. The process of social degradation, without effective countervailing social and educational policies, may become irreversible. From the ongoing trends, it is evident that economic growth without redistribution is not enough to moderate the impact of inequality of ownership patterns. The degree of poverty and inequality that is sustainable or tolerable in these countries, with deeply-rooted egalitarian values, is an important issue.

7 De-skilling implies that existing skills are less required.

In most Central and Eastern European and CIS countries, there have been three or more consecutive years of positive economic growth and the pre-1989 level of GDP has been recently restored in most countries. However, social improvements have been much slower and more uneven, due to the increasing inequality of income distribution and structural problems of poverty. In some countries, living standards are rising and poverty levels are falling. In others, particularly the poorer CIS countries, the turnaround from the difficulties of the 1990s is still far away. A relatively high level of poverty remains in areas outside the capital cities, partly due to structural and institutional problems.

There are different recommendations and promises for reforms which could lead to higher tax revenues, increase public expenditure for health and education, and provide unemployment benefits and other efficient active labour market measures such as retraining and subsidized job creation. Although the introduction of these reforms is not easy, they are not beyond reach. Warnings about the potential political consequences of increasing inequality are increasingly voiced by academics, political opposition leaders and some NGOs, who emphasise the importance of appropriate measures to maintain the peace and security of the region.

The Millennium Declaration of the UN and the resolutions of the different Summits, especially the Copenhagen Summit of 1995, also call for similar actions. Reducing the gap between the rich minority and the majority of the population, eliminating corruption, violence and crime, and moderating the impoverishment of the population would, of course, require much more than merely implementing the limited goals of the various programs adopted by UN Summits. However, these summits and their resolutions underline the responsibilities of leaders in the region in meeting these shared commitments.

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