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THE SOURCES AND CONSEQUENCES OF POVERTY AND INEQUALITY IN EASTERN EUROPE AND THE CIS COUNTRIES AT THE BEGINNING OF THE 21ST CENTURY

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1. Introduction

The issues of poverty and inequality which occupied an important place in the development policies of the UN in the 1950s and 1960s have been brought back into the international dialogue on the future of humankind by a great number of changes. These include changes in the distribution in income and wealth associated with globalization and with the restoration of the dominating role of the market system. The causes and consequences of the large and in many cases growing income gap between countries comprise another important justification for the dialogue. The collapse of the communist regimes in Central and Eastern Europe has been not only a new source of the increase of poverty and inequality, but added also a special ideological dimension to the discussions. These changes have been also in the background of the Millennium Program, adopted by the General Assembly of the UN in 2000 which opened a new action oriented dimensions in the debates, related mainly to some of the crucial aspects of the human condition of future global development. The debates have become more and more multi-dimensional. They included issues related to sustainable development, to the process of capital accumulation. One of the important questions which have been “emerging”: is inequality or at least certain level of it a necessary condition of sustainable capital accumulation and hence of economic growth? They were also related to the social aspects development, to the possible “humanization” of the globalization process, the feasibility of the progress toward “ethical markets”. These global debates have many region specific aspects in general and particularly in the former socialist countries. The ongoing process of change from a socio-economic system, the replacement of a centralized, totalitarian, non-market “egalitarian” system with a democratic market economy in this countries influences both of the main dimensions of inequality: the international, and the national, within the countries. The change in the former socialist countries is described either as a ‘transition’ or a ‘transformation’ to a modern, democratic, market-economy. The transition concept is a narrower one, while transformation implies something more comprehensive that embraces political, economic, social, psychological, institutional, national and international changes.

One of the most important issues of the transformation process, how the similar tasks will be implemented in this extremely diverse region between Western Europe and the Pacific Ocean,

divided by ethnic, religious and political conflicts,² cultural traditions, political interests and economic potentials. It is no accident that the two world wars started in the region, which also saw in the 1990s the longest post-war civil conflicts in Europe. The rivalry between great powers for control, furthered by policies of divide and rule, fuelled violent nationalism and chauvinism in some countries, bringing serious conflicts and tragedies.

The 27 countries³ of the region, most of them, new states are extremely diverse in size, development level, historical background, and social and political structure. The étatist-socialist regimes collapsed also in different ways, producing the present spectrum of regimes.

⁴ 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 diversity extended to the degree of progress they made in marketization, liberalization, and economic and social development. At the early stage of the 21st century, the region includes those Central European countries, which are the new members of the European Union, together with the Baltic States. These countries comprise a special case not only

² Cohabiting in the region, often in the same country, are Poles, Slovaks, Czechs, Moravians, Hungarians, Germans, Lithuanians, Ruthenians, Romanians, Bunevać, Sokac, Serbs, Croats, Slovenes, Bosnians, Albanians, Bulgars, Turks, Russians, Ukrainians, Gypsies etc. The cultural divide runs between the Orthodox faith and the Western Christian denominations (Roman Catholic, Reformed, Lutheran and Unitarian). Poland, for instance, has a strong Roman Catholic identity. Other countries in the region, such as Bosnia and Bulgaria, contain Moslem minorities. Hungary is heterogeneous in its religious affiliations. There is a divide between Greek Catholics and Orthodox believers running down Ukraine. A challenge is posed by the region's unresolved ethnic conflicts, which are more divisive than those elsewhere in Europe are. Majority-minority conflicts are constant erupting, causing political unrest and carrying the potential of igniting a social explosion.

³ Albania, Armenia, Azerbaijan, Belarus, Bosnia-Herzegovina, Bulgaria, Croatia, Czech Republic, Estonia, FR Yugoslavia, Macedonia, Georgia, Hungary, Kazakhstan, Kyrgyzstan, Latvia, Lithuania, Moldova, Poland, Romania, Russian Federation, Slovakia, Slovenia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan.

⁴ There were different sources of strength and of fragility and weakness in the various political systems and political structures. The former étatist-socialist regimes of Central and Eastern Europe legitimized their political systems largely by promising economic advances and continual improvements in living standards. It was becoming clear by the 1970s that they could not keep their promises or even sustain the levels achieved. Stagnation and decline in living standards and intensifying domestic political conflicts resulted from the strains of the arms race, external economic difficulties, particularly the oil-price explosion, and deteriorating economic performance. Another factor was change in the Soviet Union. There had been popular uprisings in East Germany in 1953 and Hungary in 1956. The Prague Spring of 1968 was also an effort to introduce systemic changes. These attempts had been crushed by Soviet forces, at times when the domestic political structure of the Soviet Union was still relatively stable. By the end of the 1980s, a major domestic crisis had developed in the Soviet Union, which was neither willing nor able to use its earlier methods of crushing mass movements in the satellite countries. There have been substantial differences in the character of the systemic changes and their consequences. East Germany underwent the unification process. In Hungary, the replacement of the Kádár regime with a more liberal, reform-communist approach ensured a peaceful transition. In Poland, the long struggle of Solidarity culminated in the collapse of the Jaruzelski regime. Czechoslovakia underwent a 'velvet revolution' of mass, peaceful protests. In Romania, a violent revolution erupted against the Ceaușescu regime. Bulgaria had a relatively peaceful transition. In Yugoslavia, the process of disintegration, beginning with the oil crisis of the 1970s, brought decades of political and economic crisis, leading to civil war and the re-emergence of deep-rooted ethnic conflicts. Disintegration and civil war have also resulted from political errors and mismanagement. In the Soviet Union, the disintegration brought major changes and various political structures.

because they are the members of the EU, but they are well ahead in the process of marketization and regained those losses in per capita income that they suffered as the consequence of the transformation crisis. East of this region there are two countries which are the candidates for the next round of admission to the EU, and the member states of the Commonwealth of Independent States. (CIS). They share many similarities with the former members of Yugoslavia and with Albania in the Balkans. Which are outside of this region. ⁵ (Mongolia, which does not belong to any of these groups is a highly special case)

The Russian Federation is still the most important power in the region, occupying 76 per cent of the territory of the former Soviet Union, with over half of its population (80 per cent Russians) and about half its natural endowments. Russia inherited about half the economic capacity and about 80 per cent of the R and D and military potential. It is a major Eurasian power of geo-strategic importance, encompassing 67 regions and 21 national republics.

Some political thinkers saw the collapse of the socialist-étatist system in Central and Eastern Europe as in the former Soviet Union as a global victory for liberal democracy.

⁵ The main cause of the collapse was the historical failure of the Soviet Union and the Central and Eastern European countries to build up efficient and competitive economies. This cannot be understood in isolation from the political factors and forces: a totalitarian bureaucratic state, a one-party system, and politicization and bureaucratization of the economic processes. The 'centrally planned' economies achieved important goals at a relatively early stage of development, later described by Soviet economists as the era of extensive growth, since it was based not on raising productivity and efficiency, but on greater factor inputs. Even then, the gains were costly. The economic issues became acute at a stage when the sources of growth should have been rapid technological change, improving productivity and efficiency, and fast, efficient structural adjustments. The need for reform was recognized at various stages in the Soviet Union and other socialist countries. While all countries introduced some measures to change the functioning of the system, they left the foundations unchanged. In the Soviet Union, reforms were 'aborted' either by a bureaucracy jealous of its privileges or by a partial and irrational nature that brought economic chaos, stagnation and decline. Central and Eastern Europe had specific problems. The political landslide after World War II imposed the Soviet model regardless of historical attributes or national development levels. The political changes also isolated countries from traditional Western trading partners and suppliers of modern technology, tying them to a less developed Soviet economy that could not provide the new technologies and managerial expertise needed for modernization. Countries like Czechoslovakia, East Germany and Hungary were locked into their existing development level, their technological capabilities being downgraded in relative terms in an era of rapid global technological changes elsewhere. The Central and Eastern European countries became dependent on Soviet supplies of raw materials and energy and Soviet markets for their goods. This helped full employment and offered some supply and sale security, but it also furthered relatively obsolete, globally uncompetitive economic structures. Some satellites also experimented with political and economic reforms after the death of Stalin. The most important, far-reaching reforms were made in Hungary, as an indirect outcome of the 1956 Revolution, but even these proved insufficient.

The ideas and preferences of different schools of thoughts also emerged in the *international dialogue* on the concept and content of the transformation.⁶ Many Western scholars tended initially to regard the transformation as a kind of ideological training ground for testing their theories – radical, orthodox, gradualist and evolutionist models alike. Others viewed the post-communist economies as a late and delayed imitation of their own social and economic conditions. In the countries themselves, there were few original ideas raised in the context of the goals and character of the changes. In the academic debates two alternatives arose, with little real influence on the political process: (1) joining the mainstream of the global market system and (2) a ‘third road’ that evades the problems of world capitalism, while leaving the region in the global market system. In reality the domestic and international environment left little or no leeway for countries to choose between alternatives. Also disregarded by pundits was the diversity of the capitalist system, which was to serve as a model. The one projected for the transition was more or less a textbook-capitalism, a liberal, free-market system.⁷

It was anticipated by many experts, politicians and members of the public in the early 1990s that reintegration into global markets and the transformation process would open historic opportunities for the former socialist countries to accelerate their economic modernization, with positive welfare effects. It was generally believed that the richer world, along with the institutions and processes of forms of global cooperation from which they had been excluded or in which they had been marginalized, would help the transition countries to fulfil those expectations.

⁶ An interesting contribution to the debates on the character of the systemic changes in the former socialist countries was made by the well-known sociologist S. N. Eisenstadt. Analysing the character of the ‘velvet revolutions’ in Central and Eastern Europe, he stated, ‘These revolutions were not oriented against “traditional”, pre-modern, or even modernizing regimes. They were not rebellious protests against traditional authoritarian regimes, against a divine right of kings, made in the name of modernity and enlightenment. Rather, they constituted a rebellion and protest against what was increasingly perceived by large sectors of the Eastern European societies as a blockage or distortion of modernity, effected by totalitarian regimes.’ The Hungarian scholar József Bognár, on the other hand, saw in the changes in Central and Eastern Europe ‘a conservative-liberal revolution. It constitutes a revolution because ownership, the economic “sub-system”, power relations and the social structure all undergo deep, rapid and radical changes. The revolution is conservative because it replaces the state-socialist system with a restored national-cum-religious value system, because it strives to establish the predominance of a class of property owners (the bourgeoisie) which already exists or needs to be formed, and because it joins conservative schools of thought on current international developments.’

⁷ Capitalism is not, of course, a closed or homogenous ideological system. Various ideologies exist on its socio-economic foundations, in a broad spectrum embracing libertarians, liberals and right-wing populists. Some, for example, have been unresponsive to basic global problems, while others recognized them early. The system has also accommodated fanatical ideologies such as violent nationalism and fascism, which are now gaining ground again in various parts of the world. Fuelled by socio-economic problems and political impasses, they preach divisive doctrines such as racism, ethnic hatred and religious bigotry. They cannot be expected to support global solutions to poverty, environmental degradation or crime.

It is not easy to gauge what actually happened. The new problems and sources of risk and instability brought about by the transformation have to be weighed against positive aspects of the changes. The qualitative and quantitative aspects of the process and the differences between countries impede such judgements. There are some common characteristics however, related the theme of this paper: in the first decade of the transformation little or no attention was paid to the social implications of the process. At the same time, the social consequences of the transformation recession have been dramatic, particularly in the territory of the former Soviet Union. At this stage, at the early parts of the 21st century it is more or less an academic question whether the countries had a real choice at the beginning of the changes, to introduce a model, facilitating a more equitable market system? It is also an academic issue whether the transformation crisis, the radical increase of poverty, deprivation, deterioration of health, exclusion and inequalities could have been avoided?

This paper is not a comprehensive analysis of the social changes. It is dealing with certain aspects of them, which have a major influence on the human dimension of the transformation process in the Eastern European region and in the CIS, countries (on the east of the frontiers of the European Union). This includes the former Soviet Union and those countries in South Eastern Europe, which may join the European Union after 2007. This is a large region, which is partly Europe, partly Asia.

While the economic performance of these countries has been quite uneven during the past 12-14 years both in time and space, it has been generally recognized that in certain areas much has been accomplished in the process of transformation, also in these countries. Macroeconomic stability has improved, though varying degree, there has been fiscal consolidation, and most of the countries introduced important liberalization measures in their domestic economy and international economic relations. Most of the currencies in the region are convertible. The new institutions, indispensable for a market economy, though functioning with varying efficiency, are in place. Growth has been resumed in most countries. The countries became capitalist, or market economies. Many of them resemble more to the systemic hybrids of the developing countries than to the developed models of the modern market systems. There are important differences in the ownership patterns, particularly in three areas: the size of public ownership (the leftovers of the socialist era) the character of private ownership (institutional, personal, small or large scale) and the proportion and character of foreign ownership of the main assets, firms, bank, *etc.* The development of the

legal framework of the markets, the character of the existing institutions is also quite different. There are also differences in the functioning of the markets, in the degree and character of competition, in the size and role of the informal sector, in those areas which are considered as the "dark side" of the system: crime, corruption etc. and its main role. The degree and character of the integration of these countries into the global markets is also different. All these and other factors have a major influence on the social condition of the given countries, on employment, poverty, and inequalities and on the related policies. The mentality of people and their value system is also quite diverse and mixed. It is interwoven with the ideological heritage of the past and the expectations, related to the future. All these should be taken into account when one tries to evaluate the situation and the main trends.

The countries, the statistical data for which have been selected in this paper are representing also different "types". They differ in their development level, size of economy and population, the degree of marketization and integration with the global markets, the speed of social changes and the social costs of the transformation. The incidence of poverty for example was about 25-30 per cent in the Russian Federation and 70 per cent in the poorest CIS member state, Tajikistan.

Due to the level of development, the character and speed of the institutional reforms, the transition to a market-based system in Central Asian countries over the past decade has been much more difficult than in the European part of the CIS or in Central Europe, Economic contraction and the related growth in poverty and unemployment in those countries were much greater and of longer. During the first half of the 1990s, real GDP of Central Asian countries fell by more than 50 per cent and poverty and inequality increased substantially. In spite of the resumed growth since the later part of the 1990s output of most subregional economies in Central Asia in 2002 remained around 25-30 per cent below the 1989 level, poverty and unemployment remained also a major problem. It has even deteriorated in some countries.

There are five sections of this paper. The first section is an overview of the social consequences of the transformation process. This includes also the social consequences of the disintegration of the Soviet Union, the privatization process and of the liberalization of the external sector. The second section is dealing with the changes in the labor market and the consequences of unemployment. The third section is analyzing the implications of poverty,

the fourth section is dealing with the changing social stratification and the fifth section is looking at certain social policy issues.

2. The social dimensions of the geopolitical, institutional and economic changes

Particularly during the first half of the 1990s there has been a rather simplified approach in most of the international organizations and in social sciences to the process as a “transition”. The international and national debates over-emphasized the policy and the institutional aspects of the changes and practically neglected the welfare effects and the mentality of the people. This had also an adverse influence on the local leadership. Not only some of the neoliberal gurus of the transition, but many other experts assumed that the relatively low level of poverty, inequality and the safety nets of the socialist system will make the social costs of the transition tolerable. They also anticipated that the transition process and reintegration into the global markets would open historically unprecedented opportunities for the transition countries to accelerate their economic modernization, with positive welfare effects. Many western economic advisers to the new regimes have suggested that fast liberalization is the key remedy for curing all the economic ills of the transition countries, including the rapid improvement of their export potential. Their assumptions were based more on mainstream theories than on practical experiences of other changes, like for example the socio-economic implications of the decolonization process. On such foundations, for example, it was thought that, regardless of their structural impediments, the opening of the previously closed economies would result in an increase in exports in exchange for increased imports, as the new exports sectors expanded and, following import competition, certain inefficient sectors disappeared. There would be winners and losers, and due to cost differences between the industrial countries and the former socialist countries, the winners would soon compensate the losers. All these raised unfounded expectations concerning the degree of external assistance and the speedy improvement of the situation.

It was already clear in the mid 1990 that the reality proved to be different. That is why the analysis and the objectives offered by the World Summit for Social Development and the social goals of the Millenium Program concerning for example poverty are also relevant for many of the former socialist countries.

2.1. Some debated issues

The debates in the countries over the social issues of the transformation and the future trends are influenced also by a number of factors. One is the relation to the past. This is much less the nostalgia of the older generation for the great power status and the values reflected in the Marxist ideology communist values. /which also exists/, than the ambiguity about rejecting the collectivist past. Many people insist that the state should provide job security, price stability, full social services, free health and education, and pensions. There are also strong egalitarian and populist pressures in society in practically all the transition countries, rooted in the experiences of the past few decades. These coincide with rapid divergence of incomes and economic polarization. The presence of the two is strongly apparent in political life.

Certain group of people in the light of the growing inequalities, poverty and social marginalization questions the legitimacy of the transformation process. In some countries the neglect of the social. Problems, the tendencies towards paternalism and the use of political power for private gains, the practice of using illegal, often criminal instruments by the new economic elite aggravated the situation.

One of the important Russian economists, a well known advocate of the economic and social reforms, Abel Gezovich Aganbegian, in his new book raised some important critical issues about the situation. He criticised the fact, that the different long term strategic programs for the consolidation of the Russian Federation developed by the Government did not contain a special chapter about the struggle against poverty, about the real incomes and consumption. It is not giving sufficient place or devoting attention to the catastrophic situation in health. It wants to protect the “commodity producers and not the consumers, the people.” He compares the situation with the Soviet years, when in the ideology there have been lip service to human interests, but in practice, everything was concentrated on production goals.⁸

The professional debates about the issues, which are dealt with in this paper are searching answers to such questions, whether poverty can be or will be grown out in the countries as the consequence of economic growth, or the structural transformation, including the deliberate reform measures, privatization and changes in income distribution which led to such deep

⁸ Aganbegian A. G. (2003) *Socialno-ekonomicheskoe razhvitie Rossii* (Social and Economic Development of Russia) Moscow, Delo. 2003. pp. 93-94.

changes in the functioning of the economy and society will perpetuate growing inequality and poverty?

2.2. The level of human development

It is generally understood that the countries of this region were “middle level economies” before the changes. The GDP per head and the standard of living of their population was in general about one third or less than of the developed countries. Due to such characteristics, as the full employment, the provision of the basic health services and social benefits for the population, the social mobility which was based more on education and political affiliation than on private property ownership and wealth, the Human Development Indicator was generally higher than their “grading” according to per capita GDP. The HDI has changed during the past couple of years, due to the growing inequalities, the deterioration of public health and education. Even though the HDI changes are not dramatic in the case of the CIS countries and in Bulgaria and Romania, they reflect the trends. The HDI have also a limited importance. In the countries of the given region for example, mainly the following direct factors have been expressing the human side of the transformation crisis:

- the catastrophic decline in real wages,
- unemployment,
- the increasing poverty and misery of large segments of the population,
- the fast growing polarization of the society,
- deterioration of the health condition of people,
- degradation of the educational system,
- the deterioration of social protection of the needs,
- the degradation of social infrastructure.

Any one of these problems if sustained, may have extremely adverse long term consequences for the society.⁹

⁸ Rimasevskaia N. M. (2003): *Chelovek i Reformi: Secreti Vyzhivania*. Moscow, 2003. Delo. (The People and the Reforms The Secrets of Survival)

Table 1. Human Development trends in selected countries

Ran-king in 2001		1975e	1980e	1985e	1990e	1995e	1997a	1998b	1999c	2000d	2001e
100	Armenia	.	.	.	0,756	0,709	.	0,721	0,745	0,754	0,729
89	Azerbaijan	.	.	.	.	..	..	0,722	0,738	0,741	0,744
53	Belarus	..	..	..	0,806	0,774	0,763	0,781	0,782	0,788	0,804
57	Bulgaria	..	0,769	0,790	0,792	0,784	0,758	0,772	0,772	0,779	0,795
76	Kazakhstan	..	..	..	0,781	0,738	..	0,754	0,742	0,750	0,765
72	Romania	..	..	0,782	0,768	0,765	0,752	0,770	0,772	0,775	0,773
63	Russian Federation	..	0,796	0,811	0,809	0,766	..	0,771	0,775	0,781	0,779
113	Tajikistan	..	..	0,736	0,736	0,665	..	0,663	0,660	0,667	0,677
75	Ukraine	..	..	..	0,797	0,748	..	0,744	0,742	0,748	0,766
101	Uzbekistan	..	..	..	0,728	0,712	..	0,686	0,698	0,727	0,729

HDI change

	1980-1985	1985-1990	1990-1995	1995-2001	1990-2001
Armenia			93, 8%	102, 8%	96, 4%
Azerbaijan					
Belarus			96, 0%	103, 9%	99, 8%
Bulgaria	102, 7%	100, 3%	99, 0%	101, 4%	100, 4%
Kazakhstan			94, 5%	103, 7%	98, 0%
Romania		98, 2%	99, 6%	101, 0%	100, 7%
Russian Federation	101, 9%	99, 8%	94, 7%	101, 7%	96, 3%
Tajikistan		100, 0%	90, 4%	101, 8%	92, 0%
Ukraine			93, 9%	102, 4%	96, 1%
Uzbekistan			97, 8%	102, 4%	100, 1%

a - Source: UNDP Human Development Reports, different years

It is evident from the data, that the countries during the socialist period had a relatively similar HDI and the diversity of the deterioration could be observed during the years of the transformation. Some of the countries the HDI is higher than the per-capita GDP index, but the gaap between the two is getting smaller. Behind the HDI data, there are many tragic changes. In Russia for example life expectancy of the male population fell to 57 years, five years below the Indian level, reflecting the deteriorating human condition.

2.3. The main areas of transformation and the social dimension

The transformation process included three types of profound changes.

The first change was the disintegration of the Soviet State. The states, which have been formed on the ruins of the Union, had not only new economic boundaries but also new institutions and government bureaucracies. This implied a new system of currency, taxes, prices, and markets. The second was the collapse of the etatist/socialist regime. The non-

market command economy has been replaced by new institutions, with characteristics of a market economy such as unsubsidized market prices and employment insecurity. The third transformation is the change in the social structure. The old structure which has been replaced by a social structure increasingly similar to the middle level or low income capitalist societies. The consequences of these changes were manifold. They were in many ways also interrelated and intensified each other.

From among the POLITICAL factors, the disintegration of the Soviet Union had a very important economic influence first of all on the republics, which were the members of the Soviet Union. The division of labor which characterized relations within that state was drastically cut, depriving some republics, like Ukraine, Belorus from oil and other sources of energy. The Russian Republic concentrated most of the manufacturing activities, and other supplied it with raw materials or semi-finished products. These ties were cut. Some of the Central Asian republics lost the subsidies what they got from Moscow. Most of the non-Soviet CEE countries lost their markets. The Russian military industry collapsed. All these resulted in economic decline, hyperinflation, unemployment, the collapse of the government budget. Independence left many CIS countries bereft not only of resource transfers and markets, but also of 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 faced collapse when they were cut adrift from their traditional markets and confronted with world prices for energy consumption. Rather than allow public enterprises and public services to fail, governments borrowed heavily. They thereby reduced some of the initial social costs associated with the transition. It is from this early borrowing that much of the current external debt crisis developed. In many cases, the economic disruptions created by the break-up of the former Soviet Union were compounded by diverse shocks, including armed conflicts and massive changes in the terms of trade. The adjustment to world prices has been estimated by Russian economists to be equivalent to terms-of-trade shocks of up to 15 percent of GDP. Large fiscal deficits emerged that initially could only be financed by nonpayment of some obligations and external borrowing. (In the case of CIS countries from Russia and different institutional, state and other external creditors.)

The ECONOMIC factors of the changes have been of course related to the dismembering of the Soviet Union in the former republics. The collapse of the Soviet market had an adverse

economic effect on all the countries of the former bloc but particularly on the former members of the Soviet Union. The division of labor within the Soviet state disintegrated. National economies emerged, and many industries lost their market and justification. The trade which was domestic in the Soviet Union became foreign trade influenced by many new regulations. . The economic decline, or as it has been characterized by some analysts, the „transition crisis” had of course structural and institutional roots as well. The economic decline was substantial and had profound social effects.¹⁰

Table 2. The decline and growth of GDP in the region

Real GDP Growth (1989=100)													
	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2003
Armenia	100,0	92,6	81,8	47,6	43,4	45,7	48,9	51,8	53,5	57,4	59,3	62,9	89,6
Georgia	100,0	89,9	67,0	36,9	26,1	23,4	24,0	26,7	29,5	30,4	31,3	31,8	38,2
Tajikistan	100,0	96,0	91,7	62,1	52,0	40,9	35,8	29,8	30,3	32,0	33,1	35,9	47,7
Uzbekistan	100,0	99,0	98,7	87,7	85,7	81,2	80,5	81,9	86,1	89,9	93,9	97,6	111,0
Kazakhstan	100,0	99,6	88,6	83,9	76,1	66,5	61,1	61,4	62,4	61,3	62,9	69,1	93,3
Azerbaijan	100,0	88,3	87,7	67,9	52,2	41,9	37,0	37,4	39,6	43,6	46,8	52,0	70,2
Russian Federation	100,0	100,0	94,5	76,9	66,9	57,9	55,5	53,6	54,1	51,5	54,2	58,7	77,0
Ukraine	100,0	96,0	85,8	77,5	66,5	51,3	45,0	40,5	39,3	38,5	38,5	40,7	51,9
Belarus	100,0	98,0	96,7	87,4	80,8	71,4	63,9	65,7	73,2	79,4	82,1	86,8	102,0
CIS	100	98,0	91,0	78,3	70,7	60,5	57,1	55,1	55,9	54,1	56,9	62,0	74,4
Bulgaria	100,0	90,9	80,3	74,4	73,3	74,6	76,8	69,6	65,7	68,3	69,9	73,6	87,3
Romania	100,0	94,4	82,2	75,0	76,1	79,1	84,7	88,0	82,6	78,2	75,7	77,0	92,4

Sources: Interstate Statistical Committee of CIS. UNICEF Innocenti Research Center. Economic Survey of Europe, 2004

The analysis of the factors responsible for the diversity of the GDP decline is beyond the tasks of this paper. It is necessary to underline however that the degree of influence on the social situation depended on two main factors: the incidence of the decline on the different sectors and on the character of the national policies.

The losses of the countries were very high. During 1990-98, the total value of GDP loss in the former Soviet Union calculated on the basis of potential and real GDP data by the author of

¹⁰ Decline as a concept means the slope downward, to decrease, to loose strength or vigor. (Oxford Dictionary) It could be a gradual process (regression) or a sudden change (collapse). In a complex system, like countries or societies, the processes of growth and decline may be present simultaneously. It may characterise certain components of the society (or economy) only, (agriculture as a declining sector, the declining rural population) or the system as a whole. In the case of systemic decline, the question is when and how the process becomes predominant, influencing the fundamental components of the system. In the case of socio-economic systems, empires or countries, decline could be understood in relative terms (loss of international competitiveness, slower economic growth, diminishing military power, as compared to others) or in absolute terms (shrinking population, contraction of the economy, diminishing incomes *etc.*)

this paper was about 1500 billion dollars. Industrial and agricultural output declined very fast, due to the collapse of the eastern markets, the unavailability or the loss of means which made important inputs unaffordable, the crowding out effect of imports and shrinking domestic purchasing power. The output and income loss was much greater, and proved to be more long term, than in the USA and Germany during the great depression of the thirties. At the beginning of the changes there was a general belief in the population of the countries that the richer part of the world, the institutions and processes of global cooperation from which they were either excluded or were only marginal participants will help the catching up process and the moderation of the social consequences of the transformation. This happened only at a very small scale.

One may add here that while the decline of GDP has been indeed dramatic, the decline of consumption was smaller. This can be explained either by the liquidation of personal assets of the people or by the role of the grey economy in supplementing incomes.

The social consequences of economic decline have been aggravated by the well known “conditionalities” those macro-economic policies, the introduction of which has been suggested and often directly requested by the World Bank, IMF and advisers from who were hired from the Western academia. These policies have been basically identical with the conditionality formulated by the Washington Consensus. They included fiscal and monetary austerity measures, the liberalization of trade, capital movements and prices, the unification and devaluation of exchange rates, the increase of interest rates, the removal of subsidies on food and other prices, large scale privatization, tax reforms and other measures. Some countries tried the gradual approach, others introduced radical “shock treatment” In certain cases these policies had also favorable effects, resulting in macroeconomic stability, fiscal consolidation, new economic activities, and development of the basic institutions required for the efficient functioning of market economies. There was however a more or less common problem: the human consequences of the transition process have been by and large neglected.

2.4. Integration with the global markets

The integration, or reintegration of the countries in the region with the global markets had also deep impact on the society this opened the road to the forces of globalization to countries,

which have been isolated from the global market forces for decades. This included also the different forces of global competition. Integration into the global markets implied three major changes. The first has been the development or the reform of institutions: new regulation of external economic relations, the establishment of tariffs and other instrument of market conform 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 also the introduction of new migration regime. The second was the joining the multilateral trading system and the financial institutions. This included the fulfillment of certain conditions, required by those institutions. The third change has been related to the disintegration of the Soviet Union and the dissolution of COMECON and resulted in changes in partners. The relations with the new external partners, who included both countries and transnational corporations, had also an important influence on the process, speed and character of reintegration. This processes have been difficult, unequal, often with painful economic an social consequences. Regulations vary significantly in the different countries. The degree of liberalization of the external sector are the greatest in Armenia, Azerbaijan, Georgia, the Kyrgyz Republic and Moldova from among the CIS countries. The least liberals are Turkmenistan, Belarus and Uzbekistan. Some of the countries on the lower level of development, with little export industries, like Kyrgyzistaan, Georgia and Moldova /which are members of WTO/liberalized their trade more, than those which wanted to protect their industries. There were also differences between the raw material exporters and the rest. In general the trading system of most of the CIS countries on the lower level of development is quite open. All the countries have different non tariff barriers. The liberalization of the capital account and particularly FDI flows developed also with different intensity and degree. The reintegration process has been also influenced by the weak competitive position of the former socialist countries. The patterns and forms of competition and the institutions of the global market system are shaped mostly by strong corporations and powerful, developed industrial countries.

There have been economic and social benefits and costs of the reintegration. Even though it is practically impossible to quantify its effects on the incomes and on income distribution, one may arrive to certain conclusions. The growing and practically uncontrolled exports of oil, diamonds and different raw materials facilitated capital flights which provided enormous benefits to the new business elite. This was the case of course in the resource rich countries. The growth of FDI had certainly 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 the public expenditures for health and education.

On macro level, due to the absence of data it is impossible to isolate the implications of the social consequences of domestic marketization and the reintegration with the global markets. The two are many ways interrelated, interconnected. The influence of trade on income and employment is more direct in the case of the raw material and semi-finished products exporters and this has a positive regional effect in Russia, Kazakhstan. Unemployment in import substituting and inter-industry trade sectors had been higher and longer, than in export industries.¹¹ Foreign direct investments so far had little impact on employment in general, but for example those regions in the CIS countries and particularly in Russia which had foreign investments grew faster than others and they attracted mostly skilled labor from other regions. Their effect on the social institutions cannot be judged on the basis of the existing data.

The marketization process and the integration with the global markets necessitated also the tasks of restructuring of the uncompetitive industries. Some of these changes have been taking place with the help of FDI, which implied also lay-offs and the growth of repatriated profits. The restructuring process with national capital is still at a relatively early stage in most countries in the region. It is under way in the Russian Federation, Ukraine, Kazakhstan, Romania and Bulgaria. In most of the countries the available facilities for the support of the dismissed workers and their families are rather limited.

The integration of the CIS countries into the global information system has also important implications for their integration with the global markets and at the same time it has fundamentally important social and economic consequences. It can reduce the information gap between different groups of the society, so it may contribute to the reduction of inequality. The use of Internet is spreading very fast in the Russian Federation it is growing by 20-25 per cent annually since 2001. Russia is still among the countries at the lower middle level of Internet users. The other CIS countries are lagging behind. There is however a very fast spread of mobile phones in these countries.

¹¹ Ksenia Yudaeva: Globalization and inequality in CIS countries: the Role of Institutions. CEFIR, Moscow, 2002

The social influence of the participation in multilateral organizations and agreements would require further research. It was the UN and particularly the UN Economic Commission for Europe and the UNDP which raised the social consequences of the transformation, more or less from the beginnings of the changes. The Social Summit in Copenhagen in 1995 drew already the attention of the world to the social problems of the former socialist countries, the loss of employment and the increase of poverty. A publication of the World Bank, in 1996 raised the question of responsibility of policies advocated by the Bretton Woods institutions, in the transition countries. It had however 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 of the Millennium Assembly. There are also other issues. In the context of the labor market for example, it would be important to study such aspects of the role of ILO in gender equity, labor standards, the minimum working age requirements, safe working conditions, collective bargaining and minimum wages etc.

2.5. The market, the erosion of human capital and the social support systems

CIS countries and also Bulgaria and Romania inherited a relatively large human capital stock from the socialist period, due to the relatively large investments in education, the relatively well developed and comprehensive system of pre-primary, primary, secondary and university education. They also established a research infrastructure, more developed and sophisticated, than the market economies on similar development level. The direct and indirect consequences of the changes resulted in a fast deterioration in the quality of state financed education. A large number of research institutes ceased to exist and tens of thousand of scientists, researchers and engineers emigrated.

The introduction of market institutions from 1991 onward, and the transformation recession have 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 have been around 5 per cent of the GDP each before the changes in the former Soviet Union. By the end of the 1990s, the expenditure on education declined to 4,2 per cent and in the low income CIS countries to 3,8 per cent of the

GDP, on health it went down to 3,4 per cent and in the low income CIS countries to 2,7 per cent. 5 The figures, based on IMF statistics offer further details. The three columns contain the percentage of health, education and defense expenditures in budget as the average for the years 1992-2001 in the respective countries

Table 3
Central Government Expenditure on Health and Education in Selected Countries

Countries	% of health	% of education	% of defense
Bulgaria	5	4	8
Romania	14	10	5
Azerbaijan	1	3	11
Belarus	4	4	4
Georgia	3	4	4
Kazakhstan	2	4	4
Kyrgyzstan	11	20	10
Moldova	3	4	1
Russian Federation	1	2	12
Tajikistan	2	3	10
Ukrain	2	6	5
World	10	6	10
Developing	3	11	10
Industrial	12	14	10

As it has been already mentioned, before the changes the educational system of the countries has been more developed than of the other countries with similar development level. First of all, it was basically free for all. Second, the enrollment ratio was high also for girls at all levels: primary, secondary and tertiary. Third, the quality of education was relatively good and helped the participants to develop different skills.

The situation deteriorated during the past couple of years. By the beginning of the 2000s, it is not only the poor families which have more limited access to quality education. Due to budgetary constraints and neglect, the school system in general deteriorated. The share of public education expenditure averaged around 5 per cent of the GDP in CIS countries at the beginning of the 1990. By the end of the 1990s in went down to around 4-4,2 per cent of a smaller GDP. According to a UNICEF-Innocenti report, the average share of education in GDP in the low income CIS countries has been still higher that of the world average of the low income states, but with much greater dispersion. (In Armenia, Georgia and Tajikistan it

was below 2 per cent of GDP).¹² Under these circumstances, there is a great probability that without deliberate policies and increase in the share of educational expenditure, the differences in the educational system between rural and urban areas, between the more and less developed regions of the countries are going to increase. There is also an increasing social stratification of the educational system. This is already resulting in a deteriorating prospect for the low income people and will contribute to inferior employment opportunities and marginalization. This system may not only reproduce but increase inequalities. One example is the Russian Federation. From the beginning of the 1990s, measures have been taken in the Russian Federation to reform the education system. These reforms are being implemented under the conditions of the transition period, with a cut in financing, deterioration in the conditions under which educational institutions are operating and delays in salary payments to the teaching staff. The share of the education expenditure out of the consolidated budget declined during the 1990s. It started growing during the later years of the decade but it remained lower than it was during the Soviet years. The private sector in education, providing for diversity of the educational services offered, has been developed, and the role of paid education is increasing. At the end of the decade, paid educational services accounted for about 20 per cent of the total expenditure of this branch, compared to 5% in 1995. At the same time, the problem of providing educational institutions with personnel became an important problem there is a stable tendency towards an aging of the staff of educational institutions of all types. The salaries of teachers are still low and this sometimes results in social tension. In 2000, 5.9 million people were employed in education (9.2% of the total workforce) in the Russian Federation. Many schools are experiencing certain difficulties in finding qualified teaching staff. The teaching aids and material facilities of general schools are becoming worn out and obsolete. The rate at which the buildings are wearing out is substantially faster than the rate at which they are being renovated and built. There is an other serious problem. In recent years, primary professional education, which is important for the poorer segments of the population in training their children has been diminishing, mainly due to the a drop in investment by enterprises in teaching aids and material facilities of educational institutions, a lack of work places for undergoing production practice and poor participation by employers in resolving the problems of institutions.

¹² Poverty in the Transition: Social Expenditures and the Working – Age Poor. Innocenti Working Papers No. 91. March 2002. p. 14.

The health situation has deteriorated also in all the CIS countries and its services are available in an extremely unequal way. 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 exterminated decades ago (*e.g.* malaria) have reappeared. In the Russian Federation the healthcare system was not too good even before the changes, but deteriorated rapidly. The long-term accumulation of unfavorable changes in the population's health, the unsatisfactory development of the social sphere and the state of basic medicine, and the inaccessibility of highly effective treatment methods for the majority of the country's population have further aggravated the dynamics of morbidity and resulted in a rise in the disablement level among the population – all this still further exacerbated the mortality situation. An important proof of the deterioration has been the fast spread of "social diseases" Since 1992, the annual increment in the number of people suffering from tuberculosis has been 10-15%. 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 sexually transmitted diseases has grown many times over. The incidence of syphilis registered in 2000 was 31 times higher than that in 1990 and the age of those infected fell substantially, owing to congenital forms. The rise in the HIV morbidity testifies to the rapid spread of HIV epidemic in the country.

Table 4. People living with HIV/Aids

	2001		
	Adults (% age 15-49)	Women (age 15-49)	Children (age 0-14)
Armenia	0.15	480	<100
Azerbaijan	<0.10	280	..
Belarus	0.27	3700	..
Bulgaria (1999)	<0.10	..	..
Kazakhstan	0.07	1200	<100
Romania	<0.10	..	4000
Russian Federation	0.90	180000	..
Tajikistan	<0.10	<100	..
Ukraine	0.99	76000	..
Uzbekistan	<0.10	150	<100

Source: UNDP Human Development Report 2003

As privately financed (out-of-pocket) and unregulated health care has emerged – even for basic care – access to health care services by the poor has diminished. Overall government spending in most countries has declined on a per capita basis to very low levels.

The inherited structure of social benefits, comprising both social insurance (pensions and unemployment benefits) and social assistance programs (including family allowances), is not adequate to deal with the needs created by the transition. Social insurance is largely financed through payroll taxation and federal extra budgetary funds, whereas social assistance is largely the responsibility of local authorities. Local authorities 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 expectations and realities, but also the fact, that both within the countries and between them the direct economic gains and losses have been distributed at an unequal rate.

2.6. On a new growth path

For reasons, the analysis of which go beyond the scope of this paper, since the late 1990s, GDP has been growing in nearly all the 14 countries of the CIS region and also in Bulgaria and Romania. While the transformation crisis is not yet over, the favorable international economic situation is helping the rebound of economic growth, particularly for some of the oil producing countries of the region. In 2003 there was a strong growth in all the CIS countries and also in Bulgaria and Romania. 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 and investments and also of oil exports. There was some improvement also in social field. This was more conspicuous in the capital cities and in the larger towns. Most of the adverse social consequences of the changes however remained. The small towns, the one-industry towns and the villages are still in very difficult situation, with high incidence of poverty and unemployment.

The following sections of this paper are focusing on the factors and processes related to some of the fundamental social problems of these countries, particularly on those which contributed to the increase of inequality in the given societies, the labor market situation, the sources and consequences of poverty, and on the new social stratification, as an outcome of the changes. Some aspects of social policies and their effectiveness will be also discussed.

3. Labor Market, Unemployment and Inequalities

From the three main markets which had to be "created" and developed, the market for goods, capital and labor, the labor market has been the most sensitive and difficult area in the transformation process. It has been most directly connected with the political and institutional changes. In the Russian Federation, Ukraine and Kazakhstan for example it has been internationalized and de-internationalized simultaneously. It has been influenced by the ethnic diversity exclusion and discrimination. The economic consequences of the transformation: unemployment, de-skilling and privatization, the growing job insecurity have been felt in the labor market of the countries by many people. The new relationship between the urban and rural areas and the increase of regional differences had also major influence on the evolving structure and institutions of the labor market.

3.1. Building a labor market

The establishment of a labor market which could help the reduction of poverty, in the provision of employment and social inclusion, support sophisticated employment services, increases the mobility of labor, facilitates a market oriented wage determination, and was an important task in all the former socialist countries. These goals had been achieved with limited success and with great differences between the countries. Most of these countries built up institutions for both the active and passive labor market policies, like job offices, institutions for the management of the unemployment problem, introduced some forms of unemployment benefits, retraining institutions, job counseling.

The labor markets are interrelated with all the other main markets and also with important demographic and social processes, like the growth and the changes in the age structure of the population, health and education. The labor market of the Russian Federation for example is and will be influenced to a great extent by the fact that a process of the depopulation of Russia began in 1992, when for the first time since the end of World War II, the country's population started to fall. From 1992 to 2000 it dropped by 3.5 million people or 2.4% and, as of January 1, 2001, it numbered 144.8 million. Migration has become the only source of population

increase. Without it, the numerical losses would be almost double. There are also important regional losses over the past eight years; the number of inhabitants has fallen in 60 of the 89 constituent entities of the Russian Federation.¹³ The demographic trends are also important indications for the working age population in the other countries of the region. From the following data one can see the main trends and also the differences between the respective countries.

Table 5 Demographic trends in the region

Countries	Population in 2003 (millions)	Projected population 2050 (millions)	Population under 18 (millions)	Population over 65 (%)
Bulgaria	7,9	5,3	1,5	17
Romania	22,3	18,1	4,9	13,7
Armenia	3,1	2,3	1,1	8,8
Azerbaijan	8,4	10,9	2,8	5,8
Belarus	9,9	7,5	2,3	13,9
Georgia	5,1	3,5	1,3	13,3
Kazakhstan	15,4	13,9	5,2	7,1
Kyrgyzstan	5,1	7,2	2,0	6,1
Moldova	4,3	3,6	1,2	9,6
Russian Federation	143,2	101,5	32,2	12,8
Tajikistan	6,2	9,6	2,8	4,7
Turkmenistan	4,9	7,5	2,1	4,4
Ukraine	48,5	31,7	13,5	14,2
Uzbekistan	26,1	37,8	10,7	4,8

Sources: UNFPA: State of World Population, 2003. UNICEF State of the World Children, 2003.

The population of the CIS amounted to 279m people at the beginning of 2004, the CIS statistics committee reported. The population density is from 5 to 10 people per square kilometer of area in Kazakhstan, Russia and Turkmenistan and up to about 95 to 126 in Azerbaijan, Armenia and Moldova. Over 50 percent of the people in Azerbaijan, Georgia and Kazakhstan live in urban areas, while in Armenia, Belarus, Russia and Ukraine their share is over 60 percent. The share of people living in rural areas is almost 60 percent in Moldova and Turkmenistan, while in Kyrgyzstan, Tajikistan and Uzbekistan it is about 63 to 70 percent. The number of employable people was 3.8m in Azerbaijan, 1.2m in Armenia, 4.5m in Belarus, 7.6m in Kazakhstan, 2m in Kyrgyzstan, 1.5m in Moldova, 71.4m in Russia, 1.9m in Tajikistan and 23.5m in Ukraine in 2003.¹⁴

¹³ Goskomstat of the Russian Federation, 2002

¹⁴ Pravda 2004, 02. 09.

The labor markets of the different countries are also influenced by the political system and the values advocated by it. This influence has its historical roots. Historically, markets in the different countries have been the results of an organic development, rooted in their exchange dimensions and influenced by the characteristics of the given socio-economic systems. These created also the legal framework and the different organizations indispensable for its appropriate functioning. As the result of the character of the systemic changes there was a very important contradiction-from the very beginning between the ideological assumptions related to the tasks of market building, and the practical measures. In the development of the markets of the former socialist countries in general, there have been also external influences. Both the domestic and the external ideological advocates of the free market system demanded the fast downsizing of the governments in the former socialist countries. For those, familiar with the great global debates on development this approach was of course not unknown.

The different experts, advocating liberal or neo-liberal theories in all the CIS countries, but particularly in the Russian Federation recommended "de-etatization" also in the labor market. The tasks of labor market building however could not be implemented without the active involvement of the governments. It is important to note at the same time that in economic and social field the state in the former socialist countries and particularly the CIS countries is much more powerless, it has much more limited instruments than the key industrial countries. It has very limited instruments to deal with the internal social consequences of the changes or the social implications of external shocks. They have also more limited experiences to deal with the "market failures" than the states of the developed Western countries. One should add here another problem. While there has been some form of market for goods and even for capital before the beginning of the changes, in socialist countries, there was no labor market. The socialist ideology did not consider labor as a commodity in the system. In the earlier years of central planning, the plan dealing with human resources included the allocation of labor, the patterns of education, the number of participants in the educational system, wages, etc. It offered job security, essential benefits were guaranteed through employment, workers were involved in enterprise matters, and labor force participation was high.¹⁵ While the central allocation of labor was abolished in most countries even before the systemic changes, but important consequences of it survived in the rigidities of wage policies, allowing narrow differentials and little open unemployment. Labour hoarding was encouraged by the system,

resulting in a highly inefficient use of labor. 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. Employment offices have existed mainly for the distribution of labor among enterprises.

The development of the labor market institutions in the Western region of Central and Eastern Europe has been relatively fast. It has been slower and more difficult in the CIS countries and the tasks are far from being accomplished. The system is carrying still many of the characteristics of the past: little differentiation according to skill level, very weak incentives, limited mobility, little difference between unemployment benefits and the low wages.

The changes resulted in many similar problems in most of the CIS countries. Full employment commitment which was artificially maintained by huge state financed investments in the labor extensive sectors of the economy has come to an end. In industry, one of the main problem for the CIS countries has been the collapse of the Soviet market, the decline in defense industries and the shrinking domestic demand. Unemployment was growing in its open and hidden forms also because of the obsolescence of skills. The decline in employment however was much smaller than the decline of output. In Russia and in Ukraine, where output declined during 1990-94 by 50 per cent, registered unemployment remained below 5 per cent even during the peak. The firms adapted more to the problems with lower or unpaid wages than with unemployment. The result has been the fast increase of low paid jobs which was a factor of growing inequalities among the working population.

3.2. Persistent structural unemployment or temporary lay-offs?

Unemployment statistics do not reflect too well the actual situation since many of the unemployed (according to statistics in the CIS countries, between 50-80 per cent) do not register in the labor offices, because the weakness of the incentives to do so. The benefits have been very low and the services offered very limited. Total expenditure on both active and passive labor market policy measures have been just 0, 3 per cent of the GDP in the

¹⁵ Nicholas Barr (ed) *Labour Markets and Social Policy in Central and Eastern Europe. The transition and Beyond.* pp. 122-123. Oxford University Press, 1994.

Russian Federation, 0,4 per cent in Ukraine (The EU average is close to 3 per cent) It is necessary to add however that in Russia and in Ukraine, where output declined during 1990-94 by 50 per cent, registered unemployment remained below 5 per cent even during the peak. The decline in employment is a more reliable indicator. Between 1989 and 1999 in the CIS countries the decline in industrial employment was 38,5 per cent, the largest was in Georgia, close to 80 per cent.¹⁶ It started growing again at the beginning of the 21 century. Some experts considered unemployment as a positive factor in promoting structural transformation.¹⁷ It was not the case transnational corporations, investing in the region and the new private firms recruited mainly 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 level, or that they were older people, over 45. There has been a decline also of the participation rate, partially because of the shrinking employment facilities for women. This is not reflected in the statistics on unemployment.

3.3. The small entrepreneurs, the informal sector and rural problems

The increase and the importance of small entrepreneurs is an other important indicator for the changing patterns in the labor markets. The process of the growth of small enterprises has been rather slow in the Russian Federation At the beginning of 2003 there were 882 000 small enterprises in the Russian Federation. About half of them has been in commerce. The progress of the SME sector has been somewhat faster in the Central Asian republics and in Bulgaria and Romania.

Beyond the fact, that a great number of people moved to the self employed position more as the result of losing their jobs, the increase of the number of small firms failed to create more or better productive employment opportunities so far Wages are low, there are often less incentives than in the sector of large scale firms.

A very important area of absorbing unemployed people has been the growing informal or parallel sector of economy. This has created new jobs and absorbed part of the displaced labor

¹⁶ Interstate Statistical Committee of CIS

¹⁷ R. Jackman "Unemployment and Restructuring" in P. Boone, S. Gomulka and R Layard (eds) Emerging from Communism Cambridge MA MIT Press

force. For many job seekers, this was a source of degradation. They found informal activities which did not correspond to their wishes, education, or income expectations. This sector became at the same time an additional source of income for some of those who have a job in the formal sector, because it has offered part time work. Unfortunately, there is little information on the employment and incomes earned in this sector, and therefore it is complicated to evaluate objectively the role of the growing informal sector to the increase of wage inequality.

The service sector was an other source of new employment opportunities. The tertiary or service sector was formerly undersized, except for the social services, health care, education, science, and culture. But, as the statistics for these occupations were missing or included in the former labor statistics for other economic activities they were heavily underestimated. Trade, catering, banking and insurance, communications, and real estate activities were poorly developed but have boomed since transition in all the former socialist countries. Wages in the service sector of course differ, according to the type of services. In some of the services however in the CIS countries there are very low wages.

Employment in agriculture fell faster than total employment. Large-scale agriculture in the form of collective or state farms and agro-industrial complexes were one of the major employers in central and Eastern Europe, particularly for the unskilled rural labour. Many workers in the rural areas were employed in other supporting occupations, or in the industrial or service sector of the collective and state farms. The transformation of collective into private farming, the loss of state subsidies and guaranteed markets, falling domestic demand had significantly reduced labor demand and employment in this sector. According to many analysts the rural population has been disproportionately affected by the hardships of the transformation. They comprise the largest group of the poor in certain regions of the Russian Republic, in the Caucasus and Central Asia.¹⁸ The number of small farmers however increased substantially. This fact may become an important problem in the future, due to the low level of competitiveness of small scale farming. Agriculture is a specific problem also for the labor markets. The era, when industry and services absorbed the out flowing labor force from agriculture is practically over in all the CIS countries, particularly in Russia and Ukraine. Agricultural population has been one of the main losers in the transformation

¹⁸ V. Mikhalev: *Inequality and Transformation*. UNU/WIDER, Research for Action Series No. 52, p. 40. Helsinki 2000.

process. The large state and collective farms have been either dissolved or went bankrupt and disintegrated. In most cases they have been replaced by subsistence farming, similar to the developing countries. These poor farmers comprise a large group among the impoverished people. Due to their age, the lacks of the necessary equipment they have little or no hope to improve their situation. There are very few commercially viable agricultural establishment and they provide employment for a much smaller number of people than the former state farms. The wages in these farms are very low.

Increase in unemployment resulted in not only a loss of income but also a deterioration of the social status of the individuals and of their families and contributed to the growth of job insecurity. The trends of unemployment depend not only on the perspectives of economic growth but also on the structural changes and the demand for skills. The Ministry for Labor in the Russian Federation for example projects a considerable growth of unemployment in the nearest future. Power industry reforms, public utilities reforms, railway and metallurgy 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 those things will eventually result in the fact that the human labor price will drop considerably in Russia as a whole. The supply will exceed the unbalanced employment demand several times. Hundreds of thousands of people will remain unemployed"¹⁹

3.4. The special problems of youth and women

The unemployed in Russia have a younger age composition than the employed population. The most frequently encountered age among the unemployed is 22 years. The biggest group among the unemployed consists of people between the age of 20 and 24, making up 17% of the total number. All in all, people under the age of 30 account for 38% of the unemployed. The share of people under the age of 30 among the employed population is considerably less 23.6%.

One of the most difficult problem in the former Soviet republics and in the region in general is youth unemployment. Unemployment rates under 25 are almost twice as high as the general

14. On the Edge of Unemployment Disaster Pravda. February 18, 2003

unemployment rate. Some documents of the international organizations emphasize that for the young people, one of the main problems is, that they do not have work experience. There is however another, an even greater problem. The educational level of these young people is often more inferior, due to the fact, that they have been educated at the time, when the transformation resulted in a greater differentiation and in many cases a deterioration in the quality of education. There is another more serious problem. Neglect and homelessness among children and young people has become one of the alarming characteristics of the Russian society. This social phenomenon is a consequence of the current socio-economic and spiritual-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, reflecting directly on the children; the spread of child abuse both in the family and in orphanages and children's homes, accompanied by a drop in responsibility for their fate; 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, criminalization of society and a growth of crime.²⁰

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

The disintegration of many families and the breakdown of the family ties have been closely interrelated with the problems of young people. This problem, related also to the increase of poverty in the region, particularly large scale in the urban areas of the Russian Federation, Ukraine and Belarus. There has been a growth of the divorce rate, a decline in marriages and

²⁰ 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 by them, and many spend extended periods in maternity hospitals because of the lack of alternative solutions.

an increase in the number of children born out of wedlock. The growth in the number of teenage mothers became also an acute problem.

4. Poverty and inequality

While unemployment, the changes in the labor markets and poverty are in many ways interrelated, poverty should be dealt with as a separate problem in the region, 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.

4.1. Who are the poor?

In the introduction of this paper, it has been mentioned that the former Socialist countries, on the basis of their GDP per capita, belonged into the group of the middle income countries. Some of them have been in the higher, others in the lower middle income group. Their per capita income declined further since 1989. The following table contains the changes in real per capita GDP between 1989 and 2002, and the relative per capita income level of 12 CIS countries, plus Bulgaria and Romania in 2002.

Table 6. The relative per capita income level of the region in 2002

Countries	GDP/head of the Russian Federation = 100	Real per capita GDP 1989 = 100
Armenia	25	71,0
Azerbaijan	31	54,7
Belarus	60	97,6
Georgia	33	44,2
Kazakhstan	68	93,6
Kyrgyzstan	13	63,4
Moldova	19	46,4
Russian Federation	100	72,9
Tajikistan	8	34,7
Turkmenistan	88	60,9
Ukraine	36	51,2
Uzbekistan	16	84,4
Bulgaria		95,2
Romania		91,3

Sources: calculated from national statistics, in commercial exchange rates

Poverty in this region is not new it 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 only. It has been growing since the early 1980 as the consequence of 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 the one or two dollars income per day. According to UNICEF data²¹ there have been about 50 million people, living in poor families in the former socialist countries at the end of the 1990s, about 43 million of them in the CIS countries. The figure has been much larger at the end of the 1990s, if calculated on the basis of those people who have been living below the nationally defined subsistence level. While there are great differences between the data published by the statistical offices and other sources (national or international) the following table still offers some indication for the extent of poverty in the region.

²¹ UNICEF 2001, A Decade of Transition. Regional Monitoring Report, No. 8 Florence, Innocenti Research Centre.

Table 7. The population living in poverty at the end of 1990s

Country	Date	Total poor* (thousands)	Percent of the population
Bulgaria	1995	1503	18,2
Romania	1998	10016	44,5
Armenia	1999	3271	86,2
Azerbaijan	1999	5080	64,2
Georgia	1999	2926	54,2
Kazakhstan	1996	4664	30,9
Kyrgyzstan	1998	3925	84,1
Tajikistan	1999	5798	95,8
Turkmenistan	1998	1620	34,4
Uzbekistan	2000	11977	43,1
Belarus	1999	1060	10,4
Moldova	1999	3088	84,6
Russian Federation	1998	73706	50,3
Ukraine	1999	14714	29,4

Sources: Poverty in Eastern Europe and the CIS. UNECE Economic Survey of Europe 2004 page 169. Based on the Table 7.2.4.

* 4,30 dollar in PPP per day.

According to the data, the total number of people living in poverty in those countries was about 150 million. From among the poor, the proportion of very poor, living in extreme poverty (2,15 dollars per day in PPP terms) was 47,5 million, about one third of the total. Real wages have dramatically declined, since 1989. Reductions in work hours have been widespread; workers have been placed on short-time work status or had to fake involuntary leave. In many cases they were not paid at all or have been paid in kind.

Table 8. Trends in real wages in the region

Countries	1989	1995	2001	2003
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 Fed.	100	36	52	
Tajikistan	100	5	7	
Ukraine	100	44	46	

Source: UN. Economic Commission for Europe: Poverty in Eastern Europe and the CIS. 2002. p. 167

In the Russian Federation during 1993 and 1994 only 40 percent of the workforce was being paid fully and on time. High inflation has adversely affected the poor, especially those whose administered income, such as minimum pensions and unemployment benefits.

Poverty indicators focused earlier on income data, which are problematic, especially during high inflation, and relied on unrepresentative survey sources.

The Russian Longitudinal Monitoring Survey (RLMS), an initiative jointly financed by Russian's Goskomstat, the World Bank, USAID, and the University of North Carolina, created a nationally representative data set that allows investigation of trends in household welfare. Individual and household expenditures are measured against the Russian government's official poverty line. According to this data about 25 per cent of the households are poor. Many of the poor belong to the 30 million pensioners. The poor pensioners receive pensions that are far below the state designated "subsistence minimum" of 2,143 rubles (about \$75 US) per month. Even from among those, who are in this category, few of them become real paupers; because the state indexes their incomes and most have family and community support networks. During the past 3-5 years under the indexation system, pensions have doubled. The single largest group of impoverished Russians is able-bodied men in their 30s and 40s, who are in the urban black or informal economy, who have moved to big cities without police permission, or have criminal records. They also include people whose Soviet-era education did not prepare them for jobs in the new market economy. Millions of other people in this group are trapped in remote industrial small towns created by the Soviet system, where manufacturing collapsed. Many of them 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 in the unregulated labor market wages are often far less than the subsistence minimum and are sometimes withheld for months. Poverty is also very high in the countryside, but at least in agricultural villages but in many of those places people are able to feed themselves.

It follows from the above data that Russia, (as in 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 in particular single-parent and young households: generally, the younger and more numerous the children, the more likely that the family is poor. Nearly 62 percent of families with three or more children fewer than six years are poor. Single-parent households are much more likely

to be poor than other types of families. More than 90 percent of such households are headed by women. In Armenia is an another special case. There a modest overall stabilization was achieved and some of the social indicators improved still serious social and economic problems of a transitional nature persist. National reforms that focus on improving the quality of social services and establishing cost-effective health and education systems have produced limited results. Families with children comprise 82 per cent of the poor. The educational system is in a particularly difficult situation. Chronic under-funding, low teacher salaries, severe shortages of educational materials, inadequate training of teachers and physical deterioration of schools further exacerbate the situation.

The poverty among some of the ethnic minorities, and particularly of the Roma population is one of the acute problems in some of the CIS countries, in Bulgaria and Romania. The Roma in this countries represent the real "underclass". They are excluded from the mainstream of the society, because of their ethnicity, because they are poor, mostly unemployed. Even in the informal sector they can find only inferior, low paid work.

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 overall. Nearly one-half of households that were very poor in summer 1992 in Russia were not considered as such a year later, while one-quarter of nonpoor households became poor over the same period. Regional differentiation of welfare indicators dramatically increased in the period. One must of course differentiate between countries on the middle level and the low level of economic development. Poverty is more widespread in some of those CIS countries, which are classified as low income countries.²²

During the 1990s, poverty and income inequality increased to very high levels in Central Asian republics. A relatively large proportion of the population in the region lives in poverty. 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 to the absence of income and employment generation programs in most of the Central Asian countries. For example, about 50 per cent of the population in Kyrgyzstan still lived below the poverty line in 2002. During the 1990s the population of Tajikistan increased by 14 per cent,

²² 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.

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 whom are children live in poverty, (still an estimated 60 per cent of the population) in spite of the rich oil resources of the country. Privatization of collective farms and state-owned enterprises and the development of the petroleum industry are expected to have positive social implications in the future, but have not yet benefited vulnerable population groups

Poverty is also a grave problem in Bulgaria. Rural households and families with children are among the most vulnerable. The Roma (gypsy) community, which comprises around 7 per cent of the population, is reported to be 10 times poorer than other groups.²³

The poorest CIS countries are showing many characteristics of the developing nations and, for a longer time than was originally thought, they might need substantial international assistance to foster economic and human development. The external sources of funds have been relatively small in the region, particularly comparing them with the losses in the GDP and the burdens of debt service. This is shown in Table 9

Table 9. Flow of aid, private capital and the growth of debt service

	Official development assistance (ODA) received (net disbursements)				Net FDI inflows (as % of GDP)		Other private flows (as % of GDP)		Total debt service			
	Total (US\$ millions)		Per capita (US\$)						As % of GDP		As % of GDP		As % of exports of goods and services
	2001	2001	1990	2001	1990	2001	1990	2001	1990	2001	1990	2001
Armenia	212, 2	68, 7	..	10, 0	..	3, 3	..	0, 2	..	2, 6	..	8, 1
Azerbaijan	226, 2	27, 5	..	4, 1	..	4, 1	..	-0, 2	..	2, 4	..	4, 7
Belarus	39, 2	3, 9	..	0, 3	..	0, 8	..	-0, 1	..	1, 9	..	2, 7
Bulgaria	346, 0	43, 1	..	0, 1	(.)	5, 1	-0, 2	2, 6	6, 6	10, 1	18, 6	15, 5
Kazakhstan	148, 0	9, 5	..	0, 7	..	12, 3	..	9, 8	..	14, 9	..	4, 7
Romania	647, 0	28, 9	0, 6	1, 7	0, 0	3, 0	(.)	3, 8	(.)	6, 7	0, 0	13, 7
Russian Federation	1109, 8	7, 7	(.)	0, 4	0, 0	0, 8	1, 0	-0, 3	2, 0	5, 6	..	12, 0
Tajikistan	159, 2	25, 9	..	15, 1	..	2, 1	..	1, 6	..	7, 6	0, 0	6, 3
Ukraine	519, 2	10, 5	0, 3	1, 4	..	2, 1	..	-1, 0	..	6, 0	..	6, 5
Uzbekistan	153, 2	6, 1	..	1, 4	..	0, 6	..	-0, 2	..	7, 4	..	20, 6

Source: UNDP Human Development Report 2003

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 the rebounded economic growth in almost every country in the region. Reforms in the social sector are well under way in

practically all those countries, although these may not yet provide equal access to all groups or 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 remained substantial. In Armenia, Georgia, Kyrgyzstan and Moldova in 2001, half the population was living below national subsistence levels. In the Russian Republic, real wages were only 53 per cent of that of 1989.²⁴ 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 example 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 created particularly grave social problems also in other low income countries of CIS. Socio-economic hardships are weakening the health and educational system. Drop out rates increased. The poor quality of education, low morale among teachers, and chronic under-funding of schools are particularly grave problems of the rural areas. In many cities drug abuse, prostitution and juvenile delinquency are increasing rapidly, as are the numbers of children living or working on the street. Education authorities have reported increasing absence among children who are peddling goods and offering other services on the streets. In addition the growing social inequity facing women in many places of these countries may deteriorate and create additional problems.

5. The growing inequality and the new social stratification

As one could already see from the previous sections of this paper, the transformation process and its main factors, increased inequality in all the former socialist countries, particularly in the area which was the Soviet Union.

The social system in these countries was not egalitarian. It was a kind of a society which has been often characterized as meritocracy in the West. Even within that group which has been characterized as the „nomenclature” there were differences, according to their role in the party

²³ 2001 World Bank Poverty Assessment Report

²⁴ Innocenti research Center estimates.

or state hierarchy, the degree of their control over the allocation of resources, and in decision making. These differences were not only “status differences” but have been expressed in their standard of living and access to certain goods and services. The top political elite, the leading echelon of the technocrats the top managers of the state owned enterprises etc. belonging to the “nomenclature” controlled the allocation and distribution of resources. Professionals enjoyed also a higher status in the society. The blue collar workers, particularly the skilled workers, had job security and as the base of the society, they also had privileges as compared with the peasantry. Poverty as such was not recognized officially. There have been of course many poor people in larger families with the low paid jobs, among the pensioners, among the disabled people.

5.1. The winners and the losers

The transformation process already in its rather early stage 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 is resulting in constantly people, who are climbing up on the ladder of income and wealth and those who are losing their former economic and social position. The transformation process in the former socialist countries, the transition to a market system, brought about much more radical social changes, in many ways unprecedented in the history of the given countries in peaceful times. The winners of the process of transformation are the younger, healthy, well educated, flexible and mobile people in general. Those, who had a privileged position in grasping the assets of the state owned firms, who have been entrepreneurial, and have been well connected at home and abroad, are in the forefront of the winners. The group of the losers are more numerous and diverse. The old people, the pensioners in general, the less educated, women, with little or no skill, most of the rural people, many people living in remote regions or in small towns or belonging into certain ethnic groups, *etc.* The impact of the decline of GDP, the “informalization” the liberalization, which included the cessation of the subsidized price system, inflation and unemployment hit all the wage earners. For some, the problems were more short term; others had to face long term degradation. Most of the people had very little or no savings or assets to sell in order to survive.

The income disparities in the Russian Federation between rich and poor during the years of the transformation are reflected in table 10:

Table 10. Percentage share of income in the Russian Federation

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

It may be evident from this “social balance sheet” that the concept of inequality must be understood in a multi-dimensional perspective. The inequality increase in Russia for example has an important territorial dimension, in addition to the same factors as in the other transformation countries, due to its size, geography and heterogeneity. The Russian Federation with its climatic, ethnic and economic variety had a higher underlying level of inequality than the other states, right from the beginning of the changes. The regions even during the pre-transition era have been diverse in their level of economic development, the density of transport, railways, roads, in economic structures, potentials and consequently in mean real incomes. During the Soviet period, there was convergence, but this could not eliminate the differences in income levels. The political and socio economic changes increased divergence across regions, with the poor regions staying poor or getting even poorer, and the rich regions getting richer. The income distribution between population groups and regions has widened, Regional disparities, inherited from the Soviet period, have become more pronounced and widened. Industrial districts with high concentrations of military firms and light industry, primarily in central Russia and the North Caucasus, were especially hard hit, whereas major cities and resource-rich regions in the East and major cities suffered relatively less.

5.2. The new middle class and the new rich

From among the goals related to the creation of a well functioning market economy, practically all the protagonists of the changes underlined the necessity of developing a new “middle class” as the new owners of the privatized state property. In the economic history of the Western World the development of the property owners (middle class, or capitalist class), was a long term process. This was also the case in the pre-socialist period of the Central and Eastern European countries and in Russia through centuries of accumulation of capital and the development of firms and entrepreneurship.

Privatization was considered as the main instrument for the development of the new middle class. Privatization was also an important part of the liberalization package. It had two dimensions one of it has been the process of the “organic development” of private ownership, the other was in essence the transfer of wealth from state ownership into the hands of national or foreign individuals or firms. This latter resulted in more radical shift in income distribution. It has become the most important source of income inequalities. The degree and the concrete models of privatization were of course not identical. One of the common 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. This is of course received by a small minority of the population. The idea of workers privatization which was a popular concept at the early stages of the changes in some countries, as a more egalitarian form of introducing private ownership has been more or less forgotten in the process. The value of assets owned by individual workers is extremely small for facilitating any control of as a source of income.

There are also great differences between the respective countries concerning the relative importance of the different forms of capital income. The role of dividends for example is relatively small. The concentration of larger assets and correspondingly larger capital income in the hand of the few is greater in those countries, where the legal framework has been less developed or strict.

The process of privatization included also the establishment of small and medium size enterprises. The organic development of capitalists from the grassroots resulted in more the

small and medium size enterprises, the small capitalists, which comprise about 90 per cent of the entrepreneurial middle class. Some of this people, about half of them were those, who lost their jobs and starting some business was the only area which was open to them for making their living. The small entrepreneurs include the 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, in handicrafts and in services. Their total number is relatively large, but they get a rather small proportion of capital incomes. (In Russia their share is around 15-18 per cent).

The most important ways for becoming very rich within a relatively short period of time, might have been often immoral, but were basically legal in some countries, and mixed with illegal activities in others. The following main general patterns could be observed (with different specific importance in the individual states):

1. The understanding and grasping of those opportunities, in trade which were offered by the evolving market in certain new segments or niches of it, as the results of liberalization and opening(banks, foreign exchange business, information technology, imports of cars and industrial consumer goods *etc.*). The large fortunes were obtained through the trading system.
2. Insiders privatization, or buying out: (using the privileged position of being a top manager) pushing the state owned production firms into bankruptcy and purchasing it for a low price, often by borrowed money, restructuring it, selling parts of it for much higher price, than the original purchase was, and investing in other branches or keeping a part of the originally purchased firm and modernize it. This method was often combined with the active participation in the stock and currency exchanges, and using inside information.
3. In Russia and in some of the other CIS countries, which have important raw materials or oil, a certain number of people in the political or government hierarchy have been able to gain control over these resources and their domestic and export sales. This resulted in large monopolies particularly in the extracting industries. The external revenues facilitated large foreign investments and different other legal or illegal operations abroad.
4. Obtaining and commercializing an important invention or patent or defense related technology which was not properly valued and utilized in the state owned enterprises, mainly through finding a foreign partner with whom joint ventures could be established.
5. Utilizing the loss of government control or special position in the administration. This form has opened the door to criminal elements at a scale, probably unprecedented in the history

of Capitalism These elements gained access to important assets in a several sectors of the economy, particularly in hotels, restaurants, commerce and banking. They developed the most greedy and lawless systems that country has ever experienced, often characterized as “cleptocracy”. Only during the last couple of years, since the end of the 1990s could the government achieve success in the struggle against the lawless system.²⁵

The upper class in the CIS countries includes also the political elite, the top bureaucrats in the government, in the army and in most of the political parties. In the leadership in Russia, the most recent changes in the political power structure include many people from the middle echelon of the former party, state and army bureaucracy. These people have a nickname, called "silniki", meaning "power-people". In the new elite, those top managers, working for national or foreign firms occupies a special place. Some of them, still working for the state owned firms had a more favorable position in the past, as leading technocrats. They shared many privileges with the leading officials of the ruling party and the government. The top managers in the foreign owned and the large private firms enjoy high salaries and they represent the most "globalized" part of the elite.

There is an evolving middle class also in this region, which includes the small businessmen, the professionals, the people in science, education, the middle and lower level people in the public administration in the middle income level.

According to some estimates about two third of the population in Russia, (and a much greater proportion of the other CIS countries belongs to the lower income group.

The following table reflects the degree of inequalities in the respective countries:

²⁵ Transition: The Newsletter about Reforming Economies, The World Bank, April 1994, Vol. 5, No. 4, p. 6.

Table 11. Inequality in income or consumption

		Share of income or consumption (%)				Inequality measures		
		Poorest 10%	Poorest 20%	Richest 20%	Richest 10%	Richest 10% to poorest 10%	Richest 20% to poorest 20%	Gini index
u Armenia	1998	2, 6	6, 7	45, 1	29, 7	11, 5	6, 8	37, 9
u Azerbaijan	2001	3, 1	7, 4	44, 5	29, 5	9, 7	6, 0	36, 5
u Belarus	2000	3, 5	8, 4	39, 1	24, 1	6, 9	4, 6	30, 4
u Bulgaria	2001	2, 4	6, 7	38, 9	23, 7	9, 9	5, 8	31, 9
u Kazakhstan	2001	3, 4	8, 2	39, 6	24, 2	7, 1	4, 8	31, 2
u Romania	2000	3, 3	8, 2	38, 4	23, 6	7, 2	4, 7	30, 3
u Russian Federation	2000	1, 8	4, 9	51, 3	36, 0	20, 3	10, 5	45, 6
u Tajikistan	1998	3, 2	8, 0	40, 0	25, 2	8, 0	5, 0	34, 7
u Ukraine	1999	3, 7	8, 8	37, 8	23, 2	6, 4	4, 3	29, 0
u Uzbekistan	2000	3, 6	9, 2	36, 3	22, 0	6, 1	4, 0	26, 8

Source: UNDP Human Development Report 2003

u – Data refers to urban area

As far as the occupational status and the sectoral characteristics are concerned, this income group is extremely diverse in all the countries of Eastern Europe and the CIS. The transformation process had an adverse effect on their status and material situation. The decline of their real income had been quite substantial in all the countries. They have become more vulnerable and exposed to the different adverse effects of the changes, while enjoying much less the positive effects than the middle class or the new political and economic elite. The majority of peasants also belong into this group. They represent a relatively large proportion in some of the CIS countries and in Bulgaria and Romania.

The lower income groups are also quite heterogeneous, divided by gender, skill levels, sectors and locations and ethnicity. Many of them belong to the category of the working poor. About one third of all the workers in the Russian Federation belongs into the low paid category. (These people get less than two third of the median earnings.) About 12 per cent belong to the "very low paid" category, who earn less than one third of the median earning.²⁶

²⁶ Russian Longitudinal Monitoring Survey, Microdata. 2000

Table 12. Gender related development

	Estimated earned income		
	(PPP US\$)		Female related to Male (%)
	2001		
Female	Male		
Armenia	2175	3152	69,0
Azerbaijan	..	..	..
Belarus	..	..	..
Bulgaria	5484	8378	65,5
Kazakhstan	5039	8077	62,4
Romania	4313	7416	58,2
Russian Federation	5609	8795	63,8
Tajikistan	891	1451	61,4
Ukraine	3071	5826	52,7
Uzbekistan	1951	2976	65,6

Source: UNDP Human Development Report 2003

In the view of the sources and consequences of the changes and the growing inequality, government policies, which could moderate the adverse social effects, the consequences of unemployment, de-skilling and other forms of degradation gained 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 and may even explode in violence. To what extent these policies are already at place or what would be required from the governments? Are the governments able or ready to reduce the adverse effects of the transformation? What should be the priorities of these policies? The answer to these questions would 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.

6. Tasks 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 different national and international programs for good governance include also growth and employment oriented national policies, and democratic participation.²⁷ Major investment in the development of education and health, policies which

²⁷ President Putin was identifying among his second-term priorities after winning re-election on March 14 2004 for example among the poverty-fighting goals an extra \$2 billion US in taxes to pay for stepped-up social

could train people for skills, corresponding to the needs of the new era, which would also "empower" the unskilled young people are probably the most important longer term tasks in all the countries. The national problems, related to poverty and unemployment resulted in mainly shorter term measures so far. Most of the poorest part of the population gets social transfers in the form of pension or special support to the disabled and to families with large number of children. The real value of these transfers' eroded. Family allowances cover in Russia for example about 20 per cent of the subsistence minimum for a child. In most of the countries assistance to the poor is the task of the local authorities and it depends very much on the possibilities and policies of the regions.

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 neediest and most vulnerable citizens. In practice these benefits are very small (in Russia for example around 20 per cent of the average wage) it is paid for short duration, and very few unemployed gets it.

The rise in poverty levels and the initiatives of some intergovernmental organizations, has led the countries in the region to critically re-examine their policies and to adopt some form of Poverty Reduction Strategy as a new and more efficient way to mobilize domestic ownership and external resources for poverty reduction. They started or improved the poverty monitoring procedures, by investigating the incidence of poverty by gender, region and ethnic group. On the basis of available – admittedly weak – 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 also to the reforms in the labor markets which included the development or improvement of the labor legislation and the creation of new employment opportunities. Azerbaijan for example adopted an employment generation program based on the new business environment and self-employment opportunities. There are programs for training and retraining employees and on the establishment of an information system on labor markets. A similar information system was developed in Tajikistan to monitor labor markets and to improve systems for job search, particularly in the private

programs, and mechanisms to sustain intensive quality economic growth, which will allow to radically boost gross domestic product and sharply cut poverty.

sector. New economic conditions in labor markets in Kazakhstan have enabled unemployment rates to be reduced with a high level of self-employment and increased labor mobility. Nevertheless, total employment in Central Asia in 2001 was still some 15-25 per cent below the 1989 level. The Governments of Central Asian countries introduced reforms of income generation policies aimed at increasing the general wage level as well as improving payment systems to stimulate employment. Azerbaijan adopted a law on the minimum budget needed by consumers, which identified the subsistence consumption basket for the population based on the minimum wage and the most important goods and services needed by households.

In Uzbekistan the social support system for the most vulnerable groups of the population has now been reformed. The main reform measures included direct social transfers to poor families, targeted social benefits and privileges, as well as other incentives and payments.

Anti-poverty policy initiative in the seven low income countries of the region: 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 it has been indicated 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 the countries spend on education or health care which have declined to historically low levels. This puts the long-term well-being of a whole generation of children and young people at risk.

The national strategies have been helped and stimulated by some international initiatives. In 2002, the World Bank and other international financial institutions launched the CIS-7 Initiative with the governments of seven of the poorest countries in the region.

These recommendations contain strategies which go much beyond the social sphere. It has been realized for some time, that the reduction of poverty cannot be achieved only by social transfers. It requires sustained economic growth, employment friendly economic policies, a high level and sustained public expenditure in health and education and structural reforms in

taxation. These measures together could moderate also the adverse social consequences of inequality in income and wealth and promote social mobility.

In conclusion

This paper has been dealing mainly with the problems of inequality and poverty within the countries, East of the new frontiers of the European Union. In these countries poverty emerged often in its extreme form as an adverse consequences of the transformation process. Inequality is the consequence of the new distribution of income and wealth and also of certain policies. They tend to persist in most of the CIS countries, in spite of the economic improvements.

The different dimensions of the transformation process, including the integration with the global market and the spillovers of the globalization process in most of the countries in the region resulted in growing international inequality, de-industrialization, de-modernization, and widespread impoverishment. This paper did not analyse in depth the implications of the globalization process for the transformation and for the countries concerned. The pattern of changes in these countries indicate, that globalization, rather, than uniformly integrating them into the global system results in new global and regional exclusions as well as novel inclusions, new winners and new losers. The way, globalization is reconstituting the role and place of these countries depends on their geostrategic and economic importance for the main actors in the system and also on their relative position in the global power structure. All these reflect the new geography of power and privilege which transcends political borders. and regions, reconfiguring established international and transnational hierarchies of social power and wealth.

The evolving capitalist economy which in many CIS countries is dominated by a few politically connected financial-industrial groups (oligarchs) centered on the exploitation of raw materials; a relatively small, poorly paying, and non-dynamic small and medium-sized enterprise sector. Some authors called the process a “great leap backward”.

As the result of the adverse consequences of the changes some of the countries of the region are closer to the developing world than to the economically advanced regions. The upper class

and particularly the new grand bourgeoisie in Russia and other CIS countries seems to be resembling more to the rent seeking parasitic capitalists of the past than to the modern entrepreneurial class of the market system. Without major changes in economic and social policies inequality and the erosion of human capital tends to get worse in most of these countries. In order for such a change to happen, there must be a radical change with the current structuring of power. There is a need for a new middle class capable of initiate positive developments. The progress toward this goal is slow uncertain and full of conflicting problems.

The main causes of poverty and of increased inequality included temporary factors, like the decline of output, hyperinflation, unemployment, certain consequences of macro-economic stabilization, like the abolition of subsidies devaluation, banking crises. They included also long term changes, like the economic consequences of the disintegration of the Soviet Union, the redistribution of productive assets in favor of a minority in the society Employment creation, poverty reduction; social consolidation became vitally important tasks in this difficult and heterogeneous region. These tasks are formally similar to those in other, mainly semi-developed regions of the world. The content of the required policies however must take into account the specific characteristics of the countries, which are on various stages of climbing out from the transition crisis. There are differences between the poor in the developing countries and even in the lower income countries of CIS. The poor people in the CIS countries still have higher educational level. Their dwelling conditions are still better. They still have access to some form of social services There are however a number of factors which may reduce the difference. Many of the labor market problems are increasingly of long term, structural nature. It is not any more just the decline of income and the loss of jobs but de-skilling, changing ownership patterns and new relations with the global market place.²⁸ The perpetualization of the growing inequalities in incomes, consumption and wealth will have long term influence not only on the poor adult people, but also on the future of their children. More and more families are belonging to the marginalized, deprived groups of the society. The process of social degradation, without effective countervailing social and educational policies may become an irreversible thing for their children. In this paper the interrelations between inequality and economic growth, which has been a debated issue also in economic theories in the past, was not discussed. From social perspective it is however an extremely important question, what degree of poverty and inequality is sustainable or tolerable in the countries where egalitarian values had deep roots.

²⁸ De-skilling means that their earlier skills are less and less required.

One important experience may be from other countries and regions of the world that the degree of tolerance depends on the growth of the “national cake”.

In most of the Central and Eastern Europe and the Commonwealth of Independent States, there have been three or more consecutive years of positive economic growth and the pre 1989 level of GDP has been achieved in the most important countries of the Central European region, but not yet in most of the countries, further in the East. Neither did the social situation of the population follow the rebound of the economy in the majority of the countries at the same rate. The improvements in social field have been much slower and unequal. In some countries living standards are rising and poverty is falling. Even in these countries however there are great differences behind the national averages. In other countries, particularly in some of the poorer CIS countries the turnaround from the difficulties that people faced in the 1990s. Is still far away. A relatively high level of poverty remained particularly in areas outside the capital cities. This is partially due to the structural and institutional problems, partially to the fact, that the social transfer which constituted over 25 per cent of the income of the population were not and most probably will not be restored, due to the changes in the system. The inequality which is based on the new distribution of wealth will not disappear either. There are different recommendations and promises for reforms, which could moderate inequalities and lead to higher tax revenues, to the increase of higher public expenditure in the field of health, education, unemployment benefits and other efficient active labor market measures, like retraining and subsidized job creation. The introduction of those reforms is of course not easy but not beyond their reach. There are also different warnings concerning the potential political consequences of the increasing inequality. The source of these warnings are mainly the academia, the political opposition and some NGOs. They emphasize that the future peace and security of the region depends to a large extent on the appropriate management of the social problems. The Millennium program of the UN and the resolutions of the different Summits are also calling for similar actions. Overcoming the consequences of the unprecedented destruction of the economy, science and culture reducing the big gap between the very few rich and the majority of the population, eliminate corruption, violence and criminality, moderating the impoverishment of the population would require of course much more than to implement the limited goals of the different programs, adopted by UN Summits. Still these summits and their resolutions underline also the international responsibilities of the political leaders of the region for commitments which they also shared. One can also share the conclusions of the chapter of the 2004 Economic Survey

of Europe dealing with poverty in Easter Europe:”Stimulating growth that will benefit the poor and reduce income inequalities will require confronting the vested interests that are holding back restructuring, stifling small scale private enterprise and frustrating efforts to improve public expenditure management”²⁹

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²⁹ UNECE: *Economic Survey of Europe* 2004 No. 1 p. 176.

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