

Report No. 15380-BY

Belarus

An Assessment of Poverty and Prospects for Improved Living Standards

June 28, 1996

Country Department IV
Europe and Central Asia Region



CURRENCY EQUIVALENTS

(as of March 1996)

Currency Unit	=	Belarussian rubel (BYR)
US\$1	=	BYR 12,700

AVERAGE EXCHANGE RATES

Rubels per US\$1

1993 January	559
1994 January	6,801
1995 January	11,551
1996 January	11,900
1996 March	12,700

ABBREVIATIONS AND ACRONYMS

BYR	Belarussian rubel
CEE	Central and Eastern Europe
EU	European Union
FAO	Food and Agriculture Organization
FBS	Family Budget Survey
FSU	former Soviet Union
GDP	gross domestic product
MCB	Minimum Consumer Basket
NGO	nongovernmental organization
NHS	New Household Survey
OECD	Organization for Economic Cooperation and Development
PPL	Proposed Poverty Line
UNU	United Nations University
WHO	World Health Organization

GLOSSARY OF TERMS

income	Income can be defined as only cash income, or all forms of income, including in kind income. In this report, income is measured both ways, resulting in a range of estimates of the poverty rate.
oblast	Administrative unit like a U.S. state; the first subdivision below national level.
poverty gap index	A measure of the depth of poverty, calculated as the difference between the poverty line and the mean income of the poor, expressed as a percentage of the poverty line.
poverty headcount	The number of individuals with incomes below the poverty line.
poverty rate or incidence	The percentage of the population below the poverty line.
poverty line	In this report, an absolute level of income required to meet basic food requirements in accordance with international basic nutritional standards, plus an allowance for essential nonfood expenditures.
<i>raion</i>	Administrative unit like a U.S. county; lies between municipality and state.

BELARUS: AN ASSESSMENT OF POVERTY AND PROSPECTS FOR IMPROVED LIVING STANDARDS

CONTENTS

EXECUTIVE SUMMARY	iv
CHAPTER I. ECONOMIC DETERIORATION, INEQUALITY, AND POVERTY	1
A. Shrinking Economy and Falling Living Standards	1
B. Growing Poverty and Inequality	1
CHAPTER II. POVERTY AND CHARACTERISTICS OF THE POOR	4
A. Changes in Inequality and Poverty in a Highly Unstable Environment	6
Incidence of Poverty and Recent Trends	6
B. Poverty Patterns	7
The 1995-Q1 Static Poverty Profile	7
Dynamic Aspects of Poverty: An Analysis over the Course of 1994	10
C. Risk Factors for Poverty	14
CHAPTER III. ATTAINING SUSTAINABLE AND EQUITABLE GROWTH	16
A. Belarus Since Independence: Costs of Maintaining a Decaying and Obsolete System	16
B. Preconditions for Success	16
C. Prospects for Economic Growth	17
D. Reforms Are Key to Economic Growth	17
E. Economic Growth is Key to Reducing Poverty	19
F. Social Sector Reform Is Vital to the Success of Economic Transformation	19
High Tax Levels	20
Distorted Incentives to Work and Save	20
Untargeted Transfers Are Costly and Inefficient	20
CHAPTER IV. SOCIAL POLICY FOR SUSTAINABLE AND EQUITABLE GROWTH	22
A. The Impact of Existing Social Programs and Services	22
Background	22
Human Development Trends Since Independence	22
The Social Policy Challenge	25
B. Cornerstones for the New System	26
C. Policies that Foster Human Capital Development	27
Health	27
Education	28
Labor Market Reform	29
D. Policies that Foster and Protect Lifetime Savings	30
Social Security	30
Housing Ownership	32
E. Policies that Improve Income Sufficiency	32
Social Assistance	32
Social Services	34
Support for Marginalized Areas	35
F. The Balance Between Short-Term and Long-Term Needs and Policy Objectives	36

ANNEX 1. Belarus Poverty Line	37
ANNEX 2. Income Concept and Other Methodological Issues	41
ANNEX 3. Rural-Urban Differentials	46
ANNEX 4. Gender and Poverty	52
ANNEX 5. Determinants of Earnings and Low Pay.....	55
ANNEX 6. Problems with the Existing Social Protection System	57
ANNEX 7. Checklist for the Development of a Means-Tested Program	59
ANNEX 8. Conditions for Good Social Policy: Effective Monitoring of Poverty and Social Welfare.....	61
ANNEX 9. Simulated Impact of the Cost of Possible Variants of a Wage Supplement Program	64
for Poor Families with Children	

Text Tables

2.1 Household Mobility by Quintiles, March–July 1994	4
2.2 Changes in Poverty, 1991–1995	6
2.3 Poverty by Household Type, 1995-Q1	7
2.4 Poverty by Geographic Location, Gender, and Age, 1995-Q1	8
2.5 Poverty by Number of Workers, Education, and Socioeconomic Status, 1995-Q1	9
2.6 Characteristics Affecting the Probability of Poverty, 1995-Q1	14
2.7 Needs-Adjusted Income Components by Poverty Status 1994.....	15
4.1 Individuals Who Could Not Access Health Services Because of Cost, by Type of Service, 1995	22
4.2 The Social Safety Net in Belarus	24
4.3 Needs-Adjusted Government Benefits and Taxes by Poverty Status	25

Annex Tables

A1.1 Impact of Changes in the Value of Poverty Line (PA) upon Poverty Counts (PC).....	40
A2.1 Importance of Different Sources of Income, 1995.....	42
A2.2 Poverty Incidence in Belarus with Different Income Concepts.....	43
A2.3 Impact of Underreporting of Income on Poverty Counts (PC).....	44
A3.1 Comparison of Urban and Rural Private Agricultural Plots	50
A3.2 Comparison of Urban and Rural Housing Conditions	51
A5.1 Determinants of Earnings in Belarus, 1995	55
A5.2 Characteristics Determining Low Pay.....	56
A9.1 An Earned Income Subsidy Program for Belarus	64

Text Figures

1.1 Income Distribution in Belarus: Comparison of 1995 and 1992	2
1.2 Poverty, Pension Benefits, and Family Benefits.....	3
1.3 Simulated Impact of Real Wage Growth on Poverty.....	3
2.1 Percentage Distribution of Poor by Poverty Spells.....	10

2.2 Average Number of Spells by Residence and Household Size.....	11
2.3 Distribution of Individuals According to Poverty Status.....	11
2.4 Individuals' Poverty Status by Gender and Age Groups, 1994	12
2.5 Probability of Poverty According to Previous Month's Poverty Status, Rural vs. Urban.....	13

Annex Figures

A1.1 Trend in the Monthly Amount of the Average Wage, Poverty Line, and Minimum Consumer Basket, 1994–95	37
A1.2 Price Changes by Main Expenditure Categories, January 1994–February 1995.....	39
A1.3 Changes in Urban-Rural Price Differentials in 1994	39
A3.1 Agricultural Average Wage as a Percentage of Industry Average Wage	47

Text Boxes

2.1 Measuring Poverty in Belarus: A Brief Overview of the Proposed Methodology	5
4.1 Antipoverty Means-Tested Programs: Fiscal Cost and Effectiveness	34

Annex Boxes

A1.1 Belarus Poverty Lines	38
A2.1 Unit of Measurement: Income or Expenditure.....	41
A8.1 Some Facts from the Belarussian New Household Survey.....	62

BIBLIOGRAPHY	65
---------------------------	----

EXECUTIVE SUMMARY

i. The standard of living in Belarus has eroded substantially for most people since independence in 1991 from the Soviet Union. The outlook for improvements in the near future is somber. This gives rise to the following three paramount concerns for policymakers in Belarus:

- shrinking economy and falling incomes;
- growing poverty and inequality; and
- ineffective and poorly targeted spending on social protection.

A brief analysis of these issues and policy recommendations for improving the situation provide the central focus of this report.

Shrinking Economy and Falling Incomes

ii. Since independence, the collapse of exports to traditional markets in the former Soviet Union (FSU), the sharply higher energy prices, the inefficiencies of the institutional mechanisms inherited from the collapsing system of the Soviet era, and inappropriate economic policy choices made in response to these problems have caused the per capita gross domestic product (GDP) to fall from US\$3,440 in 1990 to US\$2,160 in 1994.¹ In 1991, per capita GDP was 15 percent of the average for *higher-income countries*, but had fallen to 10 percent by 1994. Similarly, Belarussian per capita income fell from 125 percent to 92 percent of the average for *middle-income countries* in the same period. Moreover, Belarus has experienced fast inflation and growing unemployment. This has been a shock in a country where, until the early 1990s, prices barely changed and no one was officially allowed to go jobless.

iii. Belarus initially avoided the sharp compression in living standards that was experienced in most other countries of the FSU by postponing the inevitable adjustment process and by sustaining consumption at the expense of falling real investment and a buildup of external debt. In the past two years, however, GDP has fallen by over 20 percent, bringing the total decline since 1989 to almost 40 percent. Unlike many faster-reforming Eastern European countries and FSU republics that have halted output decline and are starting to grow again, the Belarussian economy continues to decline. There is little prospect for resumed growth unless the Government reverses the current trend of increasing state control over key areas of the economy, and sharply accelerates the pace of economic reforms. As most of the poverty and hardship today in Belarus can be attributed to economic decline, this poverty assessment devotes significant attention to the actions needed to restore economic growth, and to do so in a way that directly reduces poverty.

Growing Poverty and Inequality

iv. Incomes in general have continued to grow in current money terms, partially disguising the sharp reduction in real purchasing power during the past two years. In 1995, the vast majority of families were able to buy significantly less than they could a few years ago. However, not everybody lost from the changes, and—of the losers—not everybody lost an equal amount. Inequality has increased, and the artificially constrained gap of the Soviet era between rich and poor has widened. Belarussian society faces

¹ Data are from the *World Bank Atlas* and are based on purchasing power parity concept.

issues linked to these developments which, for Belarus, are unprecedented. The number of poor people has dramatically increased, and these people are experiencing longer spells of poverty. By the absolute poverty standard used in this report, those most affected by poverty are single parents, one-worker families, and large, less-educated families with children. Large families with children less than 6 years old are particularly at risk. Likewise, the economic position of rural areas has declined relative to cities. This decline would have been more dramatic had agricultural workers not increasingly focused their farming efforts on self-sufficiency. Other segments of the population have also turned to small-scale agriculture and self-employment to satisfy their daily needs. While roughly one quarter to one third of the Belarussian people have become poor, some people are becoming increasingly wealthy. This group includes the new successful entrepreneurs and—disturbingly—people who enjoy the fruits of corruption and other criminal activities.

v. The increase in poverty in Belarus is overwhelmingly due to the drop in overall levels of production and income rather than to an increase in the inequality of income distribution. The incidence of poverty² rose from 5 percent in 1992 to 22 percent in 1995.³ However, in the last quarter of 1994, the incidence of poverty was as high as 33 percent. In the first quarter of 1995 (the period of reference for the poverty profile described in this report), the incidence of poverty was 36 percent. Less than 5 percentage points of the increase in poverty between 1992 and 1995 is due to the less equal distribution of income in 1995; the rest is due to the overall decline in incomes. On average, wage income permits the poor to satisfy only 40 to 60 percent of their “minimum consumption basket” (as measured by the absolute poverty line suggested in this report). About 90 percent of the poor live in households with one or more workers, but they earn wage incomes that are insufficient to support a family. Scarce job opportunities make it difficult, if not impossible, for other adult members to contribute to the well-being of the family. In these circumstances, a policy that promotes real income and employment growth is the best and most effective antipoverty instrument that the Government can use.

vi. About 36 percent of all individuals are considered poor according to the poverty snapshot in the first quarter of 1995. The sizable fall in incomes since independence makes this figure credible. However, the nature and degree of hardship vary widely across groups and over time, and need to be studied carefully. For instance, poverty can be experienced on a recurring basis or as a single incident. It can be temporary or permanent. Only longitudinal data can reveal these aspects of poverty. Fortunately, Belarussian data permit this analysis. For example:

- Over two thirds of all households are poor at some point during the year. However, for almost 50 percent of all families, poverty is a short-term experience that lasts three months or less.

2 In this report, the incidence of poverty or “poverty rate” is defined as the percentage of people with incomes in cash and kind lower than the poverty line, which—taking into consideration factors such as the age of the person and the number and characteristics of the people living in the house—is defined as the minimum income in cash and kind required for decent physical survival based on minimum caloric requirements and other essentials of life. See Annexes 1 and 2 for a more detailed definition of the methodology used.

3 Poverty rates usually drop as the reference period becomes longer because fewer people are poor for long periods than for short periods. Thus, as can be seen in Table 2.2 of the main text, and as is mentioned at various points throughout this report, the average poverty rate in each quarter of 1995 was between 24 percent and 36 percent. However, for the year as a whole, the average dropped to about 22 percent. This happens because, while a family may be poor for the majority of a three month period and thus qualify as poor on a quarterly basis, the same family is unlikely to be poor for more than six months and thus qualify as poor on an annual basis.

- The group of permanent poor is quite small—less than 7 percent of all individuals, and only one in six families is poor for five months or more.
- The probability of remaining in or falling into poverty is *ten times greater* for the lowest-income households and five times greater for middle-income households than for the top-income households.

vii. When movements in and out of poverty are followed over a full year, the policy conclusions suggested by dynamic poverty profiles are remarkably different from those arising from a snapshot of poverty from a single point in time. Because of the short average duration of poverty and the small number of permanently poor people, savings and support from family and friends may be able to provide much of the necessary safety net as they move in and out of short-term poverty episodes. This raises important policy issues, for example: Who should be eligible for Government-financed social assistance? For how long should benefits be paid? Should benefits be tailored to the severity of poverty? Answers to questions like these will depend in part on fiscal constraints, for tighter fiscal constraints will force the Government to reduce the generosity of the safety net. Fiscal constraints will make it impossible to supply adequate social assistance for groups who are not classified as hard-core, long-term poor. It will not be possible for the Government to avoid discriminating between the short-term and the long-term poor. This report discusses ways in which this can be done to maximize efficiency and equity.

viii. The dynamic nature of most poverty in Belarus also underscores the importance of pursuing policies that create new job opportunities. The experience in other countries indicates that policies which foster the growth of small-scale enterprises are the best way to create new job opportunities, which in turn help people avoid long-term poverty during the transition process. Policies that stimulate investment, enterprise development, and employment are needed, especially as an increasing number of old, large-scale enterprises undergo major restructuring.

Ineffective and Poorly Targeted Social Protection Spending

ix. The existing social safety net in Belarus encompasses an extensive system of cash and in-kind benefits. The Government spends large amounts of money on social programs (13 percent of GDP and 36 percent of total public spending), yet given their size, these programs appear to do little to reduce poverty, because only a fraction of income support is targeted to the poor. Some programs, such as family benefits, are reasonably well targeted to households that are likely to be poor—for example, families with large numbers of children, especially those headed by single women. Overall, however, the non-poor receive 1.5 times more benefits than the poor. This is partly due to the fact that “social protection” includes not only social assistance programs such as means-tested housing support for low income families, but also social insurance programs such as pensions, which by design are not specifically targeted to help those who are already poor, but are instead designed to reduce the risk that people will become poor. Falling productivity and an aging population are placing the social protection systems, particularly the pension program, under severe and increasing strain. Moreover, eligibility control is lax, and many benefits are largely unrelated to previous contributions. A crumbling tax base must struggle to support a growing number of beneficiaries at higher benefit levels. Without repair, the pension system and other programs face the risk of insolvency. The Government urgently needs to begin implementing both short-term and long-term reforms of the social protection programs in Belarus. Changes such as tighter eligibility requirements for disability pensions are needed in the short term to prevent bankruptcy of the system. To help assure longer term effectiveness and efficiency, the Government needs to begin initiating reforms that will create a clear distinction between social insurance and social assistance programs. Social insurance programs for old age and disability should be based on mandated savings, and should be self-financing on

an actuarial basis. Social assistance programs, such as family benefits and housing support payments, should be designed explicitly to transfer income from richer to poorer people. These programs should have tight, means-tested eligibility criteria to maximize their effectiveness and efficiency. And to avoid disincentives to the creation of new employment opportunities, these programs should be financed out of general budgetary revenues rather than out of payroll taxes

x. Emphasizing fiscal sustainability and the separation of social insurance and social assistance functions would help shelter the social security system from political demands for benefits that are not supported by contributions paid during working life. Any such excess of pension benefits over payments is effectively a form of social assistance—a transfer from one group of people (workers) to another group (pensioners). To maximize the efficiency and effectiveness of such programs, any transfer of income should be targeted to the poor. A complementary effort is required to modernize and improve the efficiency of administration for social protection programs.

Policy Recommendations

xi. **Growth is key.** Limited earnings capacity is the main cause of poverty in Belarus. Consequently, growth is the first pillar of higher living standards for all. *More and better job opportunities and higher real wages require economic growth.* Attaining growth depends on an improved institutional environment and on greatly increased levels of investment. So far, the Government has concentrated on macroeconomic stability, but this is not enough. Good macroeconomic policies need to be reinforced by a credible and determined effort to create a legal and administrative environment that encourages business development and physical investments. Otherwise, growth will continue to lag.

xii. Growth requires a fundamental restructuring of the economy and a redefinition of the role of the state in the economy. Instead of remaining directly involved in business, the Government needs to focus on creating an environment that is favorable to the development of private business, one that is characterized by clear and well-enforced “rules of the game.” Reform is also needed to develop economically efficient incentive structures, a competitive environment, an efficient financial system, and conditions conducive to the development of new enterprises that can then compete in the FSU, Central and Eastern Europe, and world markets.

xiii. **Protecting the vulnerable is also important.** The benefits of growth will have to be shared by all citizens to assure a reasonable degree of equity and social harmony. The demand for the social protection programs needed to attain these objectives is large and growing, and the necessary resources are scarce. Moreover, existing social programs distort market incentives and penalize economic activity. They need to be reformed, but no clear vision exists on how this should be done. Similarly, no consensus exists on needed institutional reforms and economic restructuring. Without a vision of the future, the way ahead remains paved with uncertainty.

xiv. Good social programs assist in building a social consensus, reducing uncertainties and risks, and improving human capital. In addition, social programs are needed to protect the most vulnerable groups and to spread the benefits of growth more evenly. Poverty must be prevented through a market-based growth strategy where possible, and where poverty occurs, assistance should be provided in ways that do not encourage dependency. To this end, *the existing social programs in Belarus need to evolve toward a set of integrated universal and categorized programs that are tailored to meet the needs of specific segments of the population.* From an economic perspective, these programs should be based on the principles of (a) fiscal sustainability, (b) incentive neutrality, (c) support for human capital

formation and capital accumulation, and (d) cost effectiveness. From a social perspective, they should be based on the following cornerstones: (a) ample opportunities for earning adequate wage incomes, which will depend on good education, health, and labor market policies; (b) promotion of self-reliance and rehabilitation rather than dependency for all working-age citizens; (c) a clear distinction between social insurance and social assistance; (d) a preference for targeted social services rather than cash redistribution to help handicapped people; and (e) categorized social programs of last resort to help those who fall through the safety net of universal social programs.

xv. Since permanent or core poverty is still confined to a small group, and as family and community support systems remain important, fighting poverty and reducing its incidence are manageable undertakings. Two factors make the task challenging, however. First, careful targeting of social protection benefits is urgently needed to alleviate the existing poverty with the scarce resources that are available. However, Belarus has practically no antipoverty policies or experience with targeting. Whatever exists (e.g. social pensions and aid to families with rent-income ratios above 15 percent) is far from being cost-effective. Second, Belarus does not have readily accessible income information, and this makes the administration of means testing problematic, but not impossible. This report argues that Belarus has the capacity to administer a simple means-tested system of social assistance if it focuses its means testing efforts on three core at-risk groups:

- *Low-income families with children*—a group including less than 1 million households who should be given means-tested family benefits, scaled on the gap between earnings and the poverty line. (Total cost:⁴ about one percent of GDP.)
- *Poor pensioners living alone or as couples*—a group of about 200,000–250,000 households for whom means-tested cash supplements should be granted (possibly in the form of coupons or vouchers), to help meet housing, mobility, and other special needs. These benefits would be granted in addition and/or parallel with other in-kind benefits. They would be calculated on the basis of pension income and paid by social protection offices. (Total cost: about 0.2 percent of GDP.)
- *People in other low-income groups*—a set of about 30,000–40,000 households who would be eligible for means-tested assistance from local raion offices, after passing a comprehensive means test. (Total cost: about 0.1 percent of GDP.)

xvi. This system would be based primarily in the Ministry of Social Protection, and would be supported by local administrative units and by information from other offices such as the Ministries of Finance, Housing and Labor. It would allow the Government to tailor means-testing procedures to the specific circumstances of each group, thereby minimizing errors and fraud. It would also permit maximization of cost-effectiveness and targeting efficiency. Top down fiscal constraints should be used to control total social benefit expenditures. This global constraint would in turn help determine the level of benefits, the phase-in and phase-out rates, and more generally, eligibility conditions such as the severity and the duration of poverty. The three types of social assistance (antipoverty) programs listed above would complement the existing social insurance programs. For its implementation, many models can be used. This report outlines one possible model and proposes a variant that is fiscally neutral and cost effective (see Chapter IV). The impact of such a program on poverty incidence would be significant.

4 Total cost is sensitive to eligibility conditions and, in particular the income reference period used to determine poverty or non-poverty status.

CHAPTER I

ECONOMIC DETERIORATION, INEQUALITY, AND POVERTY

A. Shrinking Economy and Falling Living Standards

1.1 Almost all socioeconomic indicators show that the standard of living in Belarus has eroded substantially since independence from the Soviet Union. The outlook is somber, and many developments are cause for growing concern:

- shrinking economy and falling incomes
- growing poverty and inequality; and
- ineffective and poorly targeted spending on social protection.

This chapter addresses the first two issues; the third will be examined in Chapter IV after the nature and sources of poverty have been examined in Chapters II and III.

1.2 Since the breakup of the USSR, the Belarussian economy has deteriorated at an accelerating rate, affecting all aspects of economic, social, and family life. The loss of traditional markets in the former Soviet Union (FSU), sharp energy price increases, a lack of competitiveness with industrial countries, and resistance to adjustment have caused a collapse in production. Resources have continued to flow into activities with little or no real value added. The results have been quite negative. Between 1991 and 1994, industrial production fell by 30 percent and agricultural production by 20 percent. Per capita gross domestic product (GDP) collapsed from US\$3,440 to US\$2,160.¹ Traditional ways of life have been abandoned, and there is growing insecurity at work and in everyday life.

B. Growing Poverty and Inequality

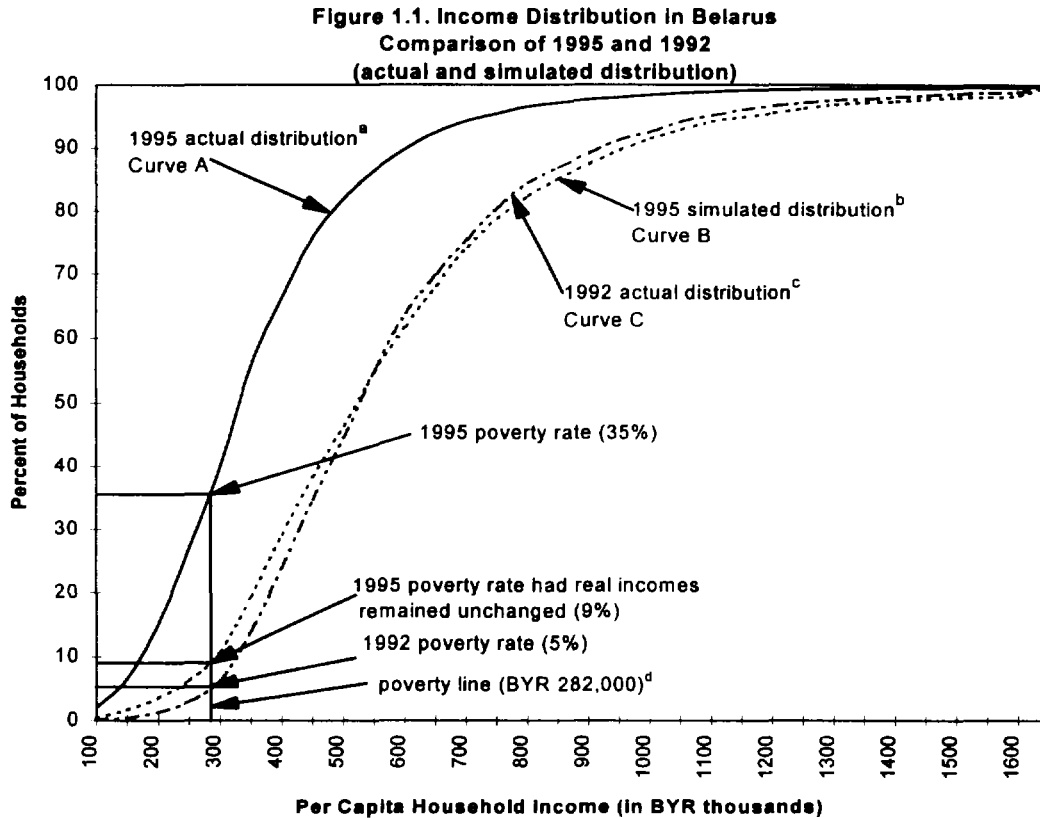
1.3 For the first time, Belarussian society faces two unprecedented developments. The first is the number of poor, which is increasing dramatically, and the duration of poverty spells, which are lengthening.² The second development concerns those who are becoming increasingly wealthy at a time when the rest of the population is encountering great difficulties. As a result, inequality is not only growing, but is becoming increasingly conspicuous. The gap between the rich and the poor—the ratio between the income of the 90th and 10th percentiles—has widened by almost three times in the same period.³

1.4 As shown by Figure 1.1, the principal cause of this increase in poverty has been falling real incomes. Had all households maintained the relative purchasing power they had in 1992, poverty would have stayed below 10 percent instead of rising to 36 percent (compare curves A and B). In contrast, rising inequality, an expected feature of the transition as dispersion of incomes rises to reflect market demands for different skills, has added fewer than 5 percentage points to poverty (compare curves B and C).

1 As measured by the *World Bank Atlas* method.

2 The percentage of households living in poverty has grown from about 5 percent in 1992 to about 30 percent in early 1995.

3 This ratio was equal to 3.4 in 1991 and 8.3 in 1995.



a/ Curve A is the actual 1995 monthly per capita income distribution for the first quarter in March 1995 prices.

b/ Curve B applies the 1995 income distribution to the 1992 real income level.

c/ Curve C is the actual 1992 monthly per capita income distribution (corrected to take into account differences in some design features).

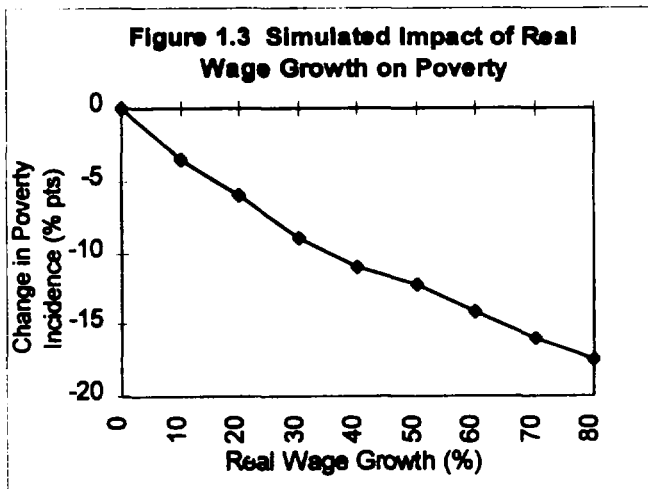
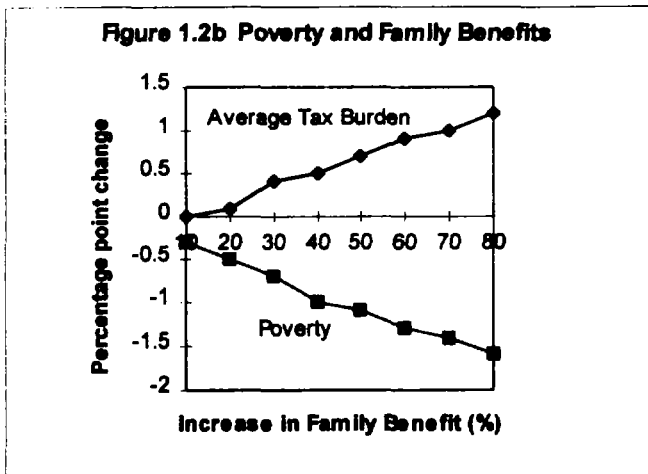
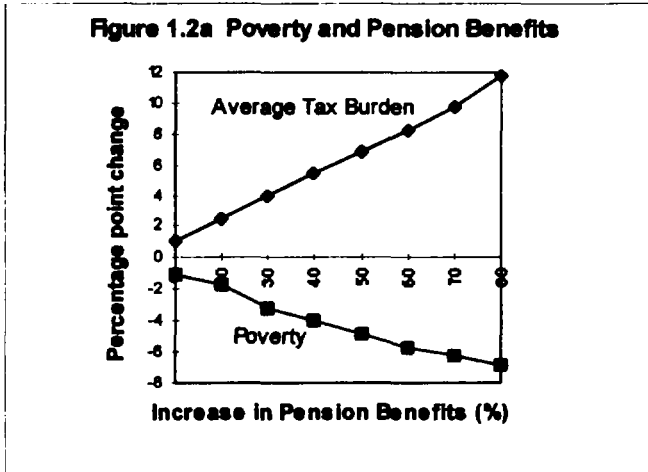
d/ Average value of poverty line for all household types.

1.5 A clear lesson emerges from this simple analysis: Without reversing the real income decline, no significant progress in the fight against poverty is possible. But what about redistributive policies? Can they help fight poverty if incomes continue to drop? The answer to this question can be seen in Figure 1.2, which portrays changes in the incidence of poverty resulting from given increases in pensions (see Figure 1.2a) and family benefits (see Figure 1.2b). This figure suggests that the Government of Belarus could not shelter many people from poverty even if it were to grant benefit increases of 50 percent or more. Simulations show that the number of poor falls by only 5 percentage points when pensions are increased by 50 percent, and by about 1 percentage point when the same increase occurs in family benefits. Moreover, to finance these policies, the Government would have to increase taxes by about 7 percent in the case of pensions, and by 0.5 percent for family benefits. Such increases would reduce real take-home wages even further, with possible negative effects on output and employment. Consequently, redistributive policies by themselves are likely to fail in an economy that is declining. They would only churn more resources, not add to those available to the poor. Eventually, redistribution would occur only by means of the inflation tax.

1.6 The poor are not the only group at risk; the futures of many middle-income and upper middle-income families also hang in the balance. Those who have so far managed to stay out of poverty will fall into the ranks of the poor unless real income growth resumes.

1.7 Appropriate macro-economic policies must be put in place to reduce poverty. Restoring efficient growth in the economy, and thus growth in employment, productivity and income, can do far more to reduce absolute poverty than any program of income redistribution. The simulations in Figure 1.3 clearly shows this: a 20 percent growth in real wages would reduce poverty by more than an 80 percent increase in pensions, and an 80 percent increase in average real wages cuts the incidence of poverty in half. Similarly, employment growth can significantly reduce poverty, even if real wages do not increase. If policies were put in place to restore efficient growth sufficient to restore the 1990 level of employment, just over 500,000 new jobs would be generated. This would reduce poverty significantly, even if wages were to remain unchanged.

1.8 Promoting income and employment growth is thus the best policy that the Government has to fight poverty. This does not imply that good social policies are not needed. Indeed cost-effective social policy can—and should—supplement economic policies in achieving income and employment growth through efficient targeting and cost-effective programs. By focusing on growth and supporting this with fiscally sustainable social insurance and assistance programs, the Government of Belarus would best foster conditions which ensure that the transition to a market economy is characterized by both growth and equity.



CHAPTER II

POVERTY AND CHARACTERISTICS OF THE POOR

2.1 Deteriorating living conditions in Belarus reflect a host of socioeconomic factors and developments. In 1990, poverty was almost unknown, accounting for less than 1 percent of the population. By early 1995, nearly 36 percent of the population lived in poverty. Two intertwined developments have had a major influence on these changes. The first is *falling real income*, which intensifies resource scarcity for all. The second is *increasing inequality* and the widening division of society into economic winners and losers. Economic winners are not only moving upward along the income curve, but also receive incomes that are increasingly far above the average. Since 1993, the eighth and ninth percentile ratios¹ increased by roughly 30 and 50 percent, respectively. Moreover, Belarussian households now find themselves in an increasingly volatile socioeconomic environment that reflects changes in the real economy and persistent efforts to maintain administrative control over key economic variables, such as wages. For instance, out of the households in the middle quintile at any point in time, fewer than a third are likely to remain in the same quintile after three months; one tenth will migrate to the bottom or top quintiles, one fifth to the second, and one fourth to the fourth quintile (see Table 2.1).²

2.2 Increased income volatility and mobility are not necessarily bad. Indeed, in many instances they are part of a necessary and unavoidable transformation process that is gaining momentum. For many, however, the high risk of moving from high- to low-income positions in a short period, together with deteriorating health and other conditions, only exacerbates the

Table 2.1: Household Mobility by Quintiles, March-July 1994
Probability of Migrating to Other Quintiles

		July				
	Lowest	Second	Middle	Fourth	Upper	
March	52.7	23.4	12.0	6.8	5.2	
Lowest	24.6	34.1	20.3	12.2	8.9	
Second	12.5	21.9	28.3	23.9	13.1	
Middle	5.2	13.2	25.8	30.0	25.8	
Fourth	5.0	7.4	13.6	27.1	47.0	
Upper						

Source: Estimated from the 1994 Family Budget Survey. Probabilities are calculated on the basis of cash income only.

problems and growing insecurity that many have had to endure since independence. For them, independence and the related changes have not delivered the expected benefits, and past achievements have lost their luster. Moreover, for many families and individuals, problems have formed a vicious circle, wherein less income is accompanied by less of everything else, including health, leading to further declines in income.

2.3 An escape from this vicious cycle is not yet discernible, and to varying degrees, poverty has become part of daily life for many Belarussians. With poverty now affecting the lives of more than one third of the Belarussian people, the risk of poverty has reached levels more common in lower-income countries than in developed nations. By failing to take decisive steps toward economic reform, Belarus risks not only moving closer to the less developed economies,³ but also having its economy become one in which falling per capita GDP is accompanied by growing inequality.

¹ The percentile ratio is equal to the ratio between a decile's income and the median income.

² In 1995 probability values are not very different than in 1994. However, 1995 values suggest that positions along the income curve may be turning to greater stability, with the rich more likely to stay rich, the poor less likely to move out of poverty, and middle-income earners less likely to move either into poverty or to become rich.

³ In 1985, the poverty (head counter) rate was 31 percent for the Middle East and North Africa, 19 percent for Latin America and the Caribbean, and 33 percent for all developing countries. (See World Bank, *Poverty: World Development*)

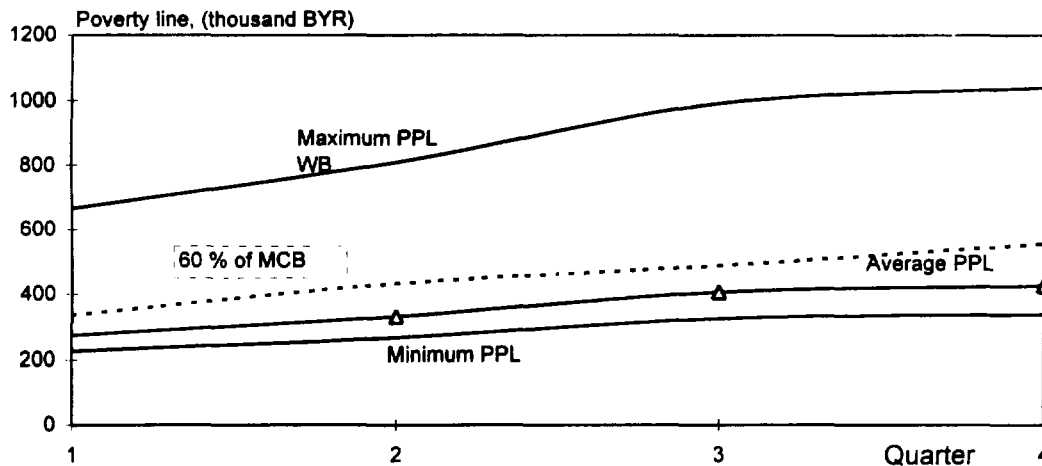
Box 2.1: Measuring Poverty in Belarus—A Brief Overview of the Proposed Methodology

The methodology used in this report to measure poverty in Belarus is described in Annex 1. In this box, the main features of the poverty standard(s) that are proposed are discussed and compared with the official "Minimum Consumer Budget" methodology in Belarus.

- Minimum Consumer Budget (MCB)**—provides a definition of minimum desirable levels of consumption for four family types: young families with one child, families with two children, families of four, and pensioners' families. Fourteen other individual situations exist. These are characterized by gender, active and nonactive status, age (for children only), and schooling. The MCB basket is based on 38 food items and hundreds of other nonfood items grouped under the following five categories: (a) clothing and footwear; (b) home amenities; (c) sanitary, hygiene, and medical products; (d) housing; and (e) communications and services. MCB composition has been criticized because, e.g., the consumption of daily meat products and animal fats is larger than internationally recommended calorie norms; economies of scale are improperly treated; consumer baskets bear little relation to actual product availability or actual patterns of consumption; obvious luxuries such as alcohol, tobacco, silk shirts, and personal income taxes are included; and the real value of baskets change over time. Moreover, MCBs have proved to be too high to be credible or fiscally sustainable minimum income standards. These criticisms have led to a recalculation of MCBs. While lower, new MCB levels have proved to be still too high, currently 60 percent of the per capita value of a four-person MCB is used by Belarussian authorities as a poverty line for all individuals
- Proposed Poverty Line (PPL)**—is based on a methodology that is very similar to the MCB's. It includes seven item categories: (a) food; (b) clothing, footwear, and underwear; (c) durable households goods; (d) medicines, sanitary and hygiene; (e) shelter and utilities; (f) cultural, educational, and recreation; and (g) services, transport, and communication. PPL's and MCB's specific composition and items weights are quite different. Unlike the latter, the PPL meets the following four requirements: (a) conformity to Food and Agriculture Organization (FAO)/World Health Organization (WHO)/United Nations University (UNU) recommendations for minimum nutritional intakes; (b) actual rather than prescribed consumer choice; (c) tailoring to family size and needs; and (d) reflection of market prices, with costs minimized and poverty lines adjusted to take territorial price differentials into account.

The figure below shows trends and differences in the MCB based poverty lines used by the Government of Belarus for all individuals and the World Bank's maximum, average, and minimum poverty lines during the four quarters of 1995.

Comparison of poverty lines: MCB and PPL



Report 1990, Table 2.1, p. 29.) Different availability and access to public goods and social services suggest, however, that data for Belarus and from the World Development Report are not strictly comparable.

A. Changes in Inequality and Poverty in a Highly Unstable Environment

2.4 Many factors indicate that incomes in Belarus are highly unstable, with most households moving up and down the income curve. Probability values, such as those contained in Table 2.1 are not uncommon in Western countries. However, in Western countries changes in poverty and non-poverty status are characterized as those that occur over the long term—ten years or more.⁴ In Belarus, the high mobility rates that are observed happen in an extremely short period—three months. *This remarkable mobility suggests a high turnover among the poor, and emphasizes the importance of categorizing the poor according to number, duration, and recurrence of poverty spells. The severity of poverty depends on these factors.* Together with access to land plots, the number, duration, and recurrence of spells are key to cost-effective policies for targeting programs for the most needy, since these characteristics help to define and differentiate between permanent and temporary poverty. In this kind of situation, waiting periods before people become eligible for income support programs are an excellent way of focusing scarce social assistance resources on the longer-term poor who need the help most. This approach also reduces the risk that easy access to benefits will reduce incentives to find new jobs.

Incidence of Poverty and Recent Trends

2.5 *Overall Incidence of Poverty.* Income data for the first quarter of 1995 of the *New Household Survey* (NHS) show widespread poverty incidence. Measured as a percentage of individuals below the income threshold that is described in Annex 1, the incidence of poverty grew very sharply between 1993 and 1994, reaching about 36 percent in the first quarter of 1995, and then falling back to significantly lower levels in the other quarters, according to a pattern that is also found for 1994. On a yearly basis, poverty incidence was about 22 percent in both 1994 and 1995 (Table 2.2).⁵ This reflects largely the cumulative effect of the output decline described in Chapter I. If poverty incidence is measured in terms of cash income rather than total household resources, the poverty rate reached 51 percent in 1995 (70 percent in the first quarter of 1995).⁶ The dramatic growth in poverty in Belarus reflects largely the severe drop in output and real incomes in recent years.

Table 2.2: Changes in Poverty,^a 1991-1995

Year	Poverty incidence (head count) ^b	Poverty gap ^c	Poverty severity ^d
1991	0.2	0.1	
1992	5.0	1.4	
1993	5.1	3.0	
1994	22.4	7.0	5.1
1995 ^e	22.5		
Q1	35.7	12.7	4.0
Q2	24.2
Q3	28.1
Q4	28.7

a. Based on total resources.

b. Number of poor as a proportion of the population. Data for 1991-

c. 1994 are based on the Family Budget Survey. That for 1995 is

d. Based on the New Household Survey. Note that poverty rates tend to be higher in the winter than in the summer, mainly because of seasonal differences in income in kind from garden plots. Also, because of the relatively short duration of most poverty spells, annual poverty rates are lower than quarterly poverty rates.

e. The transfer that would bring the income of the poor exactly up to

Source: Staff estimates from Q1 1995 microdata.

2.6 *Trends in Poverty Since 1991.* Comparisons between poverty statistics based on 1991–94 *Family Budget Survey* and the 1995 *New Household Survey* require great care, given differences in methodology

4 According to U.S. statistics for the period 1975–1993, out of 100 households in the middle quintile, 28.3 percent remained in the same quintile, 21 percent migrated to the bottom quintile, and 10.2 percent migrated to the top quintile. See M. Cox and R. Alm, "By Our Own Bootstraps," Federal Reserve of Dallas, 1996.

5 The decline in poverty in the summer and fall reflects in large measure increased in-kind income from household plots.

6 See Annex 2 for a definition of total resources and cash income.

and definitions.⁷ Nevertheless, a clear trend is discernible from the data: a sharp rise in poverty that mirrors the drop in output and a deepening of poverty. Despite the sharp increase in the poverty headcount, however, those who are poor are still close to the poverty line. As shown in Table 2.2 under the "Poverty Gap" column, the income transfer needed to bring people above the poverty line represents a relatively small percentage of the poverty line. Poverty in Belarus today is quite "shallow," which means that small variations in average income levels can have a large impact on the poverty headcount index. Two other points also stand out from analysis of the data.

- *In-kind income* is a key component of households' well-being. In many instances, in-kind income (which averages between one fifth and one third of total household income during the winter and summer months, respectively) determines whether a household suffers or escapes poverty. Its importance declines with income. As noted above, its inclusion causes poverty incidence to fall from 70 to 36 percent (in the first quarter of 1995).
- *Interfamily transfers and savings* play an important role, and for the poor are quite substantial in relation to household needs. The importance of both sources tends to fluctuate throughout the year. Interfamily transfers vary between 8 and 16 percent of "needs-adjusted income" (i.e., the total amount of interfamily transfers divided by the value of each household's poverty basket), and are highest during the summer months. Moreover, they are more important for higher than lower-income households. Savings are generally negative for the poor, but play an important role for non-poor households; they permit families to even out income shortfalls, especially in the winter months. On average, savings are negative or negligible from October to January. Savings are highest in the summer months, showing substantial correlation with income from plots of land.⁸

B. Poverty Patterns

The 1995-Q1 Static Poverty Profile⁹

2.7 Certain household characteristics are closely correlated with poverty and can help identify at-risk groups. These include the following:

Table 2.3: Poverty by Household Type, 1995-Q1 (percent)

	Poverty rate ^a	Composition ^b
<i>Type of Family</i>	35.7	100.0
Single	30.4	5.5
Single parent	53.6	3.3
Married couple	12.5	4.3
Married with child	34.8	10.1
Married with 2 children	40.9	18.2
Married with 3 children	56.4	5.8
Married, adults and children	43.5	30.4
Adults only	30.1	18.4
Adults with children	59.2	3.9
<i>Household Size</i>	35.7	100.0
1	30.4	5.5
2	18.9	9.0
3	32.6	20.8
4 more	42.9	64.7

a The poverty rate is the percentage ratio between all people in a group who are poor and the total number of people belonging to that group.

b Composition is the percentage ratio between the number of poor people with given characteristics and the total number of poor, multiplied by 100.

Source: Staff estimates from Q1 1995 NHS Data

7 This implies that the exact magnitude of the poverty trend is difficult to assess because of too many heterogeneities in the two data sources that are used.

8 See Kakwani, N., Minimum Consumption Basket and Poverty in Belarus, mimeo, 1994.

9 At the time this report was prepared, only 1995 first quarter (Q1) data were available. The static poverty profile refers therefore to the first quarter of 1995. Another reason to use 1995-Q1 data for the poverty profile is that poverty in Q1 is highest. The dynamic analysis of poverty that follows provides a good description as to how the profile changes when a yearly perspective is considered.

Family Size and Composition. A direct correlation exists between household size and poverty incidence. Poverty is lowest among two-person households and highest among larger households with children. Poverty among large households is higher in rural than in urban areas. The number of children in a family is perhaps the most notable determinant of poverty. Two out of five households with two children are poor, as are almost three out of five households with three or more children. Single parents with children face a risk of poverty exceeding 50 percent (Table 2.3).

Regional Poverty. Location affects opportunities and household well-being. In Belarus, urban households have higher cash incomes than rural households.¹⁰ They also have access to better social facilities. Rural households, however, have greater access to arable land and can thus count on more in-kind income than urban residents. Consequently, poverty incidence, based on total resources and with poverty lines corrected for rural-urban price differentials, is lower in rural than in urban areas (30 percent versus 39 percent). The incidence of poverty by oblast, as reported in the first quarter of 1995 based on aggregate (cash plus non-cash) income was highest in Brest and lowest in Minsk. Oblasts with poverty rates close to the national average include Vitebsk, Mogilev, and Grodno.

Poverty by Gender. Gender differences are generally insignificant; poverty incidence is about 35 percent for both males and females (see Table 2.4). However, there are more poor females than males, reflecting the demographic structure of Belarus (aggravated by the heavy loss of young males during World War II). Moreover, gender inequalities inherited from the Soviet system have a bearing on this pattern. The Soviet system resulted not only in the relative concentration of women in certain lower-paying sectors and at pay levels about three quarters those of men, but also in their limited participation in management and economic decisionmaking, and their greater dependence on social transfers. These features make women particularly vulnerable to poverty (see Annex 4). Most often, women's greater risk of poverty is moderated by income pooling at the household level. When income pooling is not possible, e.g., as is the case with single mothers and elderly widowers, the risk of poverty increases dramatically, to 50 percent or more.

Poverty by Age. Poverty hits children more than any other group. The younger the child, the higher is the risk of poverty.¹¹ For children less than 15 years old, the poverty rate is 45 percent. Poverty incidence decreases with age, however, and persons aged 56 or more are almost half as likely as children to be poor, but the risk of poverty increases again after age 65 (Table 2.4).

Table 2.4: Poverty by Geographic Location, Gender, and Age, 1995-Q1 (percent)

	Poverty rate ^a	Composition ^b
<i>Location of residence</i>	35.7	100.0
Urban	38.9	69.2
Rural	30.1	30.8
<i>Gender</i>	35.7	100.0
Male	35.4	45.9
Female	35.9	54.1
<i>Age</i>	35.7	100.0
0-15	44.6	28.4
16-25	38.0	15.7
26-40	39.2	24.4
41-55	31.3	16.2
56+	23.1	15.3

a. Poverty rate is the percentage of all people in the group who fall below the poverty line.

b. Composition is the percentage of all households with at least one person in the work force (employed or not) who falls into each group. Retired persons are excluded.

Source: Staff estimates from Q1 1995 NHS microdata.

¹⁰ See Annex 3 for some measurement problems and a more detailed discussion of rural-urban living standard issues.

¹¹ The relatively high risk of poverty for children does not reflect their individual income, which is generally zero or close to it, but rather the fact that families with children, especially large numbers of children, tend to be poorer than those with few or no children.

Poverty and Work. As one moves from households with no active members to households with active members, one observes an increase and then a fall in the incidence of poverty (Table 2.5). Nonactive people (most often elderly) face a low risk of poverty. The risk then increases for one-income households (42 percent), and falls as the number of earners increases to 35 percent for two-earner households, and 29 percent for three-earner households. Nonetheless, the presence of at least two income earners often determines whether or not a household is in poverty. In examining these issues, one must look beyond sheer numbers and consider factors such as education level and the challenge of balancing child care with work, which partly explains the higher incidence of poverty among four-income households. Access to cultivable land also weakens the relationship between the number of earners in a family and the incidence of poverty. The presence of at least two earners remains important, but for all family sizes, possession of a garden improves chances of escaping poverty. The same holds true for pensioners, although the pension by itself is not high enough to avoid poverty. Accumulating retirement, labor, and plot income—as it indeed happens for many elderly people—significantly reduces the risk of poverty.

Education and Poverty. Education clearly affects prospects for well-being. Adults with only compulsory education or specialized basic education experience an average rate of poverty (Table 2.5). Those with undergraduate or graduate education fare better. For each group, the poverty rate is about 14 and 16 percentage points lower than for individuals with basic education, respectively. Statistics on adults who have incomplete secondary education are distorted by a larger than proportionate percentage of pensioners, who in general fare better than many workers.

Socioeconomic Status and Poverty. Poverty incidence by socioeconomic status varies from 13 percent for military personnel to over 50 percent for the unemployed. Pensioners and white-collar workers face a common risk of poverty (26 percent), suggesting that retirement does not necessarily result in declining living standards. Poverty is high among households with nonactive persons. The self-employed face an average risk of poverty, indicating that a transformation strategy that encourages private sector development of new small-scale enterprises would create new jobs where people could on average earn more than in blue collar jobs, and where some might be able to earn as much as or even more than white-collar workers.

Table 2.5: Poverty by Number of Workers, Education, and Socioeconomic Status, 1995-Q1 (percent)

	Poverty rate ^a	Composition ^b
<i>Number of workers^c</i>	35.7	100.0
0	30.3	12.6
1	42.1	27.8
2	35.3	47.9
3	29.6	8.0
4	37.8	3.7
<i>Type of education^c</i>	35.7	100.0
Incomplete secondary	32.0	31.7
Basic secondary	37.1	24.0
Specialized secondary	35.9	35.4
Undergraduate	22.2	8.7
Postgraduate	21.7	0.2
<i>Socioeconomic status^c</i>	35.7	100.0
Blue-collar	41.6	40.4
White-collar	26.1	17.6
Collective farmer	30.0	7.1
Self-employed	34.5	0.6
Military	12.9	0.3
Pensioner	26.1	21.2
Student	38.7	0.8
Disabled	45.7	1.4
Unemployed	52.1	4.9
Housewife	48.3	4.4
Other	43.1	1.3

a. The poverty rate is the percentage ratio between all people in the group who are poor and the total number of people belonging to that group.

b. Composition is the percentage ratio between the number of poor people with given characteristics and the total number of poor.

c. Excluding children.

Source: Staff estimates from Q1 1995 NHS microdata.

Dynamic Aspects of Poverty: An Analysis over the Course of 1994

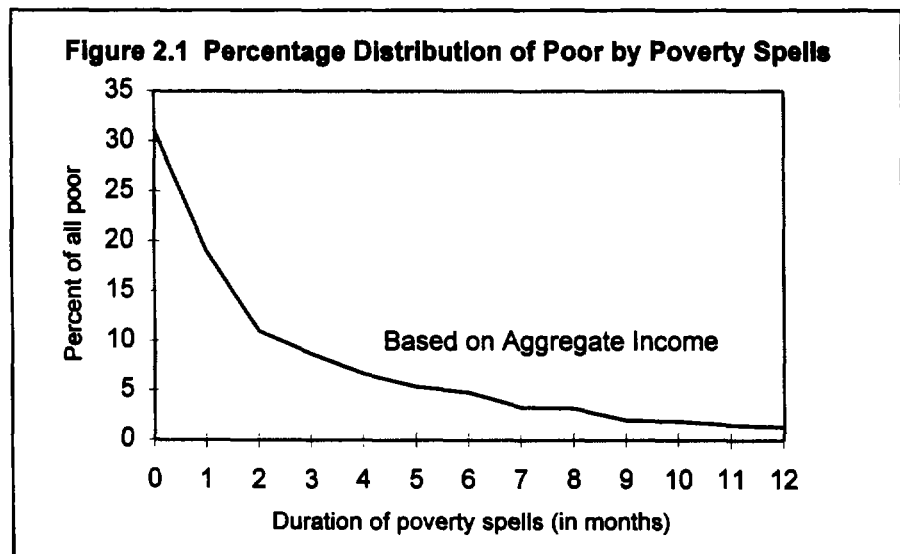
2.8 Static poverty profiles rely on poverty head counts or other statistics that are calculated using income at a particular point in time to classify households as poor or non-poor. The Belarus 1995 poverty profile outlined in the previous sections, for example, is based on a snapshot taken in the first quarter of 1995. When incomes fluctuate dramatically during the year, as they presently do in Belarus, static poverty profiles have severe limitations as policymaking tools. In the specific circumstances of Belarus, poor households face spells of poverty that vary widely in severity and duration over the course of the year. Moreover, poverty can be a one-time experience for some households, while for others it can be recurrent. It can last for a few weeks or months, or for years. Good policy formation therefore requires information on the frequency, duration, and intensity of poverty, not just its presence at any one point in time, and this requires a dynamic analysis of poverty. The present report, for example, using information available from the 1994 monthly panel surveys of the family budget survey (FBS) and from information regarding households' total resources, examines the following aspects:

- *Frequency of Poverty Spells*—the distribution of the population in terms of number of poverty spells per year;
- *Average Duration of Poverty Spells*—the average length of poverty spells and their relation to family circumstances;
- *Severity of Poverty*—poverty status in terms of the depth and duration of poverty episodes; and
- *Transitional Probability In and Out of Poverty*—the probability for the poor to become non-poor and for the non-poor to fall into poverty.

2.9 *Frequency of Poverty Spells.* The data suggest considerable mobility in and out of poverty (an aspect already discussed above). The differences in frequency of poverty among various groups and areas are significant.¹² Hardest hit by recurrent poverty are the following:

- larger households with children;
- children, especially between ages 0 and 6;
- families with only one worker; and
- collective farmers and female pensioners in rural areas.

2.10 *Average Duration of Poverty.* Figure 2.1 maps the distribution of poverty in terms of duration over the course of 1994. Thirty-one percent of the population is never in poverty during the year. Less than 2 percent of the population is poor during the entire 12 months. For the remaining 68 percent of households, poverty is a temporary experience that lasts less than a year.



12 N. Kakwani, op cit., pp. 69-86.

2.11 On a cash income basis, the average person is likely to be poor for 4.7 months. When measured against total resources, this duration drops to 2.7 months. Lengths of poverty bouts are likely to be longer in rural than in urban areas (3 months against 2.5), longer for pensioners and collective farmers (3.2 and 3.1 months, respectively) than for blue-collar and white-collar workers (2.5 months), and longer for larger families with children (over 5 months) than for single persons or families without children (less than 2 months). (See Figure 2.2.) Spells are also longer in the age group 0 to 17 years, and in families with only one worker.

2.12 *Severity of Poverty.* A taxonomy of the severity of poverty in terms of income and the number and duration of spells helps to identify more accurately "the poor" and to distinguish among them those whose needs are greatest and should be the prior focus of any social safety net programs. Four categories of income status are established for this analysis: (a) *permanent poor* (in poverty more than nine months in one year); (b) *semi-permanent poor* (five-month to eight-month poverty spells); (c) *temporary poor* (one-month to four-month poverty spells); and (d) *not in poverty*.

Figure 2.2 Average Number of Spells by Residence and Household Size

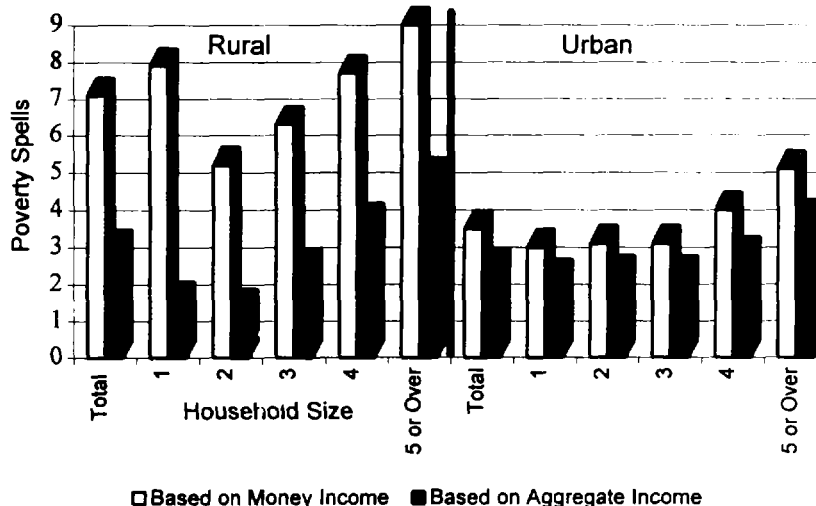
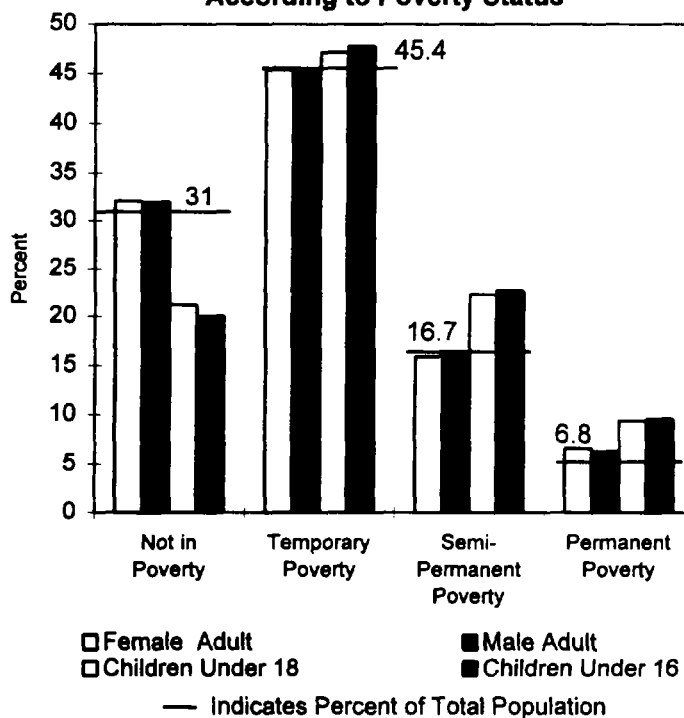
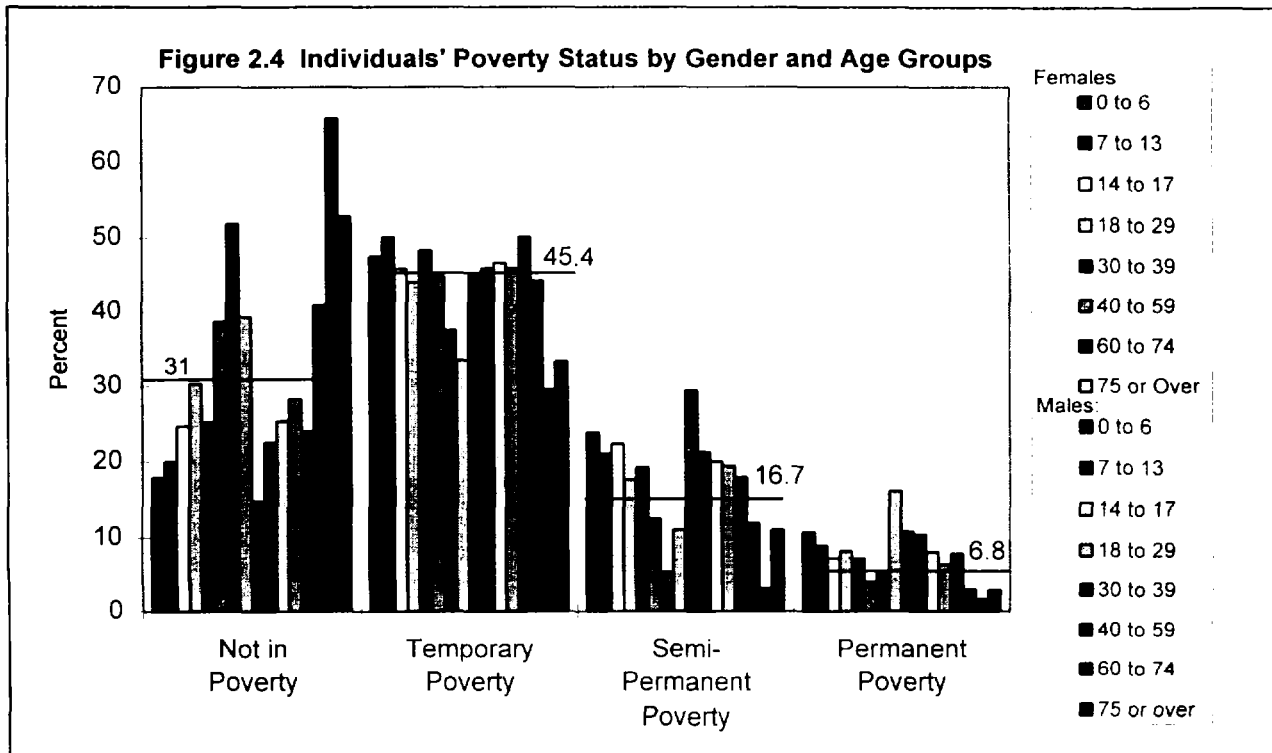


Figure 2.3 Distribution of Individuals According to Poverty Status





2.13 Most individuals (see Figures 2.3 and 2.4) can be divided into two groups: three quarters suffering temporary poverty or none at all, and one quarter suffering semipermanent poverty or permanent poverty. The incidence of poverty for adult males and females is about the same. Women aged 75 and over (most men do not reach this age) are particularly exposed to economic hardship (see Figure 2.4). The elderly in general are more likely to escape poverty than are other age groups.

2.14 Children run a particularly high risk of poverty. The incidence of permanent poverty increases with the number of children in a family and is highest for larger households; more than 50 percent in rural areas and about 40 percent in urban areas are permanently poor. Single-parent households and couples with three or more children have the highest probability of poverty, and the presence of additional adults in the family reduces the risk of poverty.

2.15 Finally, of those who are already poor, poor blue-collar and white-collar worker households have the lowest probability of being permanently poor (only 13.1 percent), while poor households of collective farmers and pensioners have the highest (42 percent and 57 percent, respectively).

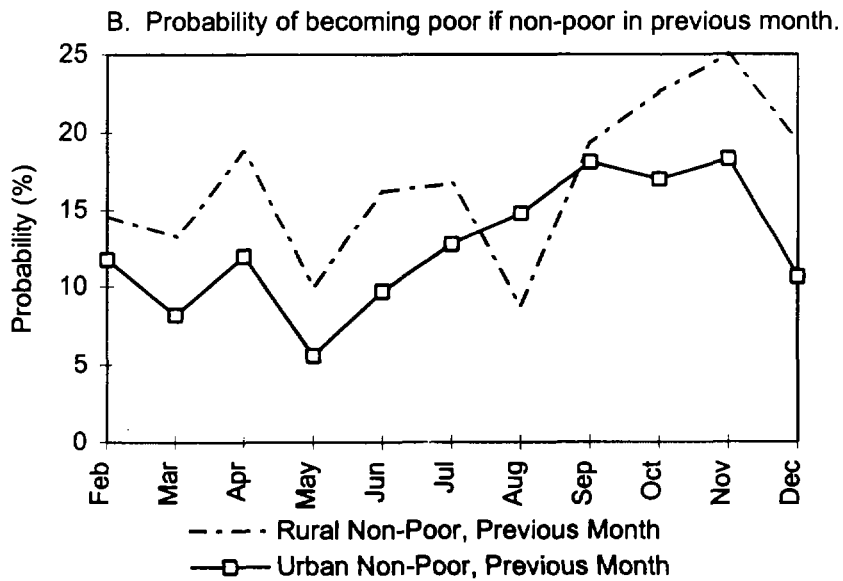
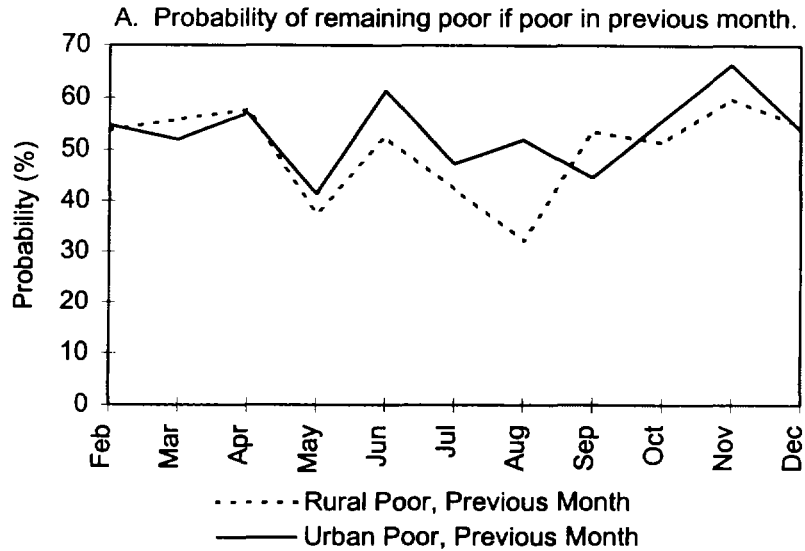
2.16 *Transitional Probabilities.* (See Figure 2.5.) Individuals have different probabilities of escaping poverty. Moreover, probabilities show important seasonal variations. For instance, the probability that an individual who is poor in January will remain poor in February is 53.7 percent if he lives in a rural area, and 54.7 percent if he lives in an urban area. However, the probability that an individual who is non-poor in January will become poor in February is 14.6 percent if he lives in a rural area, and 11.7 percent if he lives in an urban area. For both rural and urban households, the status of being poor or not poor is likely to persist rather than change.

2.17 The dynamic profile presented here clearly indicates that policies to assist the poor that do not take duration of spells into account carry the risk that (a) the different needs and circumstances of the transient and chronically poor are disregarded, with both obtaining access to the same relief; and (b) too

many households will be eligible for social assistance, which has serious implications for social assistance costs and equity. Careful consideration should be given by the policymakers to issues such as the following:

- Who should be eligible for social assistance? Everybody experiencing poverty? Or only the long-term or chronic poor?
- How long should a poor person have to rely on savings and transfers from relatives and friends before becoming eligible for social assistance?
- How long should benefits be paid and how frequently should cases be reviewed?
- Should benefits be tailored to the severity of poverty? If so, how large will the difference have to be between short- and long-term benefits, and how can the effects of work disincentives be avoided?

Figure 2.5 Probability of Poverty According to Previous Month's Poverty Status, Rural vs. Urban



As it will be seen in Chapter IV, the answer to these questions is not independent from the fiscal constraints faced by the Government—the tighter the fiscal constraints, the harder the task faced by policymakers. In Belarus, the scarcity of fiscal resources makes it urgent for policymakers to distinguish clearly between the short-term poor and the longer-term poor.

C. Risk Factors for Poverty

2.18 Analyzing the risk factors for poverty is a complex task. One approach is to analyze the variables that characterize the poor and correlate them with poverty. This method is followed in Table 2.6, which shows how certain socioeconomic characteristics affect the odds of poverty for a hypothetical person (single man, aged 30 to 40 years, with basic secondary education, working at a state enterprise, and living in an urban area in Minsk oblast). Two factors appear to be particularly important:

- With more children, the odds of poverty increase, especially for single mothers and widows.
- With more education and workers in a household, the odds of poverty decrease.

2.19 Another approach is to look at earning capacity¹³ and income sufficiency. The latter is the approach followed in Table 2.7, based on a comparison of *need-adjusted income components*, which is the per capita value received by a household from a given source, divided by that household's per adult equivalent poverty threshold. For instance, a ratio of 20 for family benefits indicates that these benefits meet 20 percent of the household's needs. This approach suggests the following:

- The main cause of poverty is limited earning capacity. Wage income for the permanently poor represents between 40 and 60 percent of "minimum requirements." For the temporary poor and non-poor, this ratio is close to or above 100 percent.
- In-kind income is of much greater importance to the non-poor (57 percent of "minimum requirements") than the semipermanent (24 percent) and permanent poor (7 percent).

2.20 Moreover, consideration of need-adjusted income components indicates that agricultural income is more important to the temporary poor or the non-poor than the poor, and that the non-poor have greater access to other

Table 2.6: Characteristics Affecting the Probability of Poverty, 1995-Q1

This table shows deviations from the probability of being poor for an hypothetical individual aged 30 to 40 years, with basic secondary education, working in a state enterprise and living in an urban area in the Minsk Oblast. This individual's probability is 42.5% .

PROBABILITY OF POVERTY IS HIGHER IF:		% Higher
Living in:	Brest Oblast	8.0
	Vitebsk Oblast	3.2
	Gomel Oblast	1.1
	Grodno Oblast	2.4
	Mogilev Oblast	2.0
Single with:	1 child	16.8
	2 children	14.4
	3 children	50.0
Married with:	1 child	11.1
	2 children	18.0
	3 children	32.1
	Has no children in household	4.3
	In a household with adults and children	20.7
	Female	2.4
Working in:	State farm	8.0
	Collective farm	6.6
PROBABILITY OF POVERTY IS LOWER IF:		% Lower
Living In:	Rural Area	19.5
	Minsk City	0.8
Married couple		13.3
2 workers in household		11.3
3 workers in household		16.8
Age is:	Less than 30	4.2
	40 to 50	4.5
	60 or Over	4.6
Attained:	Specialized secondary education	5.6
	Undergraduate education	18.5
	Postgraduate education	17.6
Working for:	Budgetary organizations	2.9
	Joint stock companies	18.8
	Private individuals	8.5

13 The concept of "earning capacity" is used as an indicator of the capacity of a household to earn enough labor income to satisfy its basic requirements as defined by the family-specific poverty lines proposed in this report. A ratio of 1 between labor income and the family-specific poverty line indicates that a household can earn wage income to satisfy its basic needs. A ratio lower than 1 indicates that earnings are insufficient to satisfy basic needs.

income sources than the poor, including social protection benefits, which are generally distributed to favor the non-poor twice as much (see Chapter III for more details). This result comes directly from the fact that in the FSU, old people are supported by universal pensions that are topped up to a common minimum for all, irrespective of contributions paid and individual resources.

Table 2.7: Needs-Adjusted Income Components^a by Poverty Status (percent of household income)

	Non-Poor	Temporary Poor	Semi-Poor	Permanent Poor
Wage and salary	158.4	110.4	76.1	50.0
Social protection benefits	26.4	14.7	11.5	12.6
Agriculture income	5.0	9.2	5.6	3.1
Property income	1.2	0.8	0.4	0.0
Other income	12.4	10.8	8.1	9.2
Total taxes	16.0	9.8	5.7	3.6
Net income	182.8	131.9	96.0	68.8
In-kind income	57.1	39.8	24.2	7.1
Aggregate net income	237.3	171.2	119.8	73.4

a Per capita value received by a household from a given source divided by that household's per capita poverty threshold, multiplied by 100.

Source: Staff Estimates from FBS Data

2.21 This analysis of the risk factors for poverty, showing the close ties between individual labor market performance and living conditions, as well as the unsatisfactory performance of social programs, raises two important questions:

- What can be done to improve the earnings of the poor in the labor market?
- How can social programs be redesigned to achieve better social protection for the destitute?

The first question requires an analysis of the distribution of earnings and of the factors characterizing low-wage earners. The second requires an analysis of the distributive impact of social programs.

2.22 The results of the empirical analysis of the determinants of earnings and low pay are contained in Annex 5. This analysis shows unequivocally that the prosperity and living standards of the majority of the working population depend upon a well-performing economy in which productivity gains sustain real wage growth and expand employment opportunities. Low pay for most is but the consequence of a malfunctioning economy, low investment in higher education or training, and gender inequalities. Low family income is the consequence of a combination of low pay and scarce job opportunities. This confirms the results of the simulations reported in Chapter I, showing the positive effects that employment and/or real wage growth could have on poverty. Chapter III will focus on the reform policies needed to spur efficient growth and generate employment opportunities and higher real wages. The answer to the question "How can social programs be redesigned to achieve better social protection for the destitute?" is provided in Chapter IV.

CHAPTER III

ATTAINING SUSTAINABLE AND EQUITABLE GROWTH

A. Belarus Since Independence: Costs of Maintaining a Decaying and Obsolete System

3.1 Five factors stand out in the recent history of Belarus. First, the breakup of the FSU has had profound effects on the Belarussian economy and society, and the country's links with the rest of the FSU have weakened. Second, an end to centralized and extensive price control was followed by a general price shock, the result, in large measure, of sharply higher energy prices and inflationary monetary policies. Third, there is a lack of free market institutions, such as financial markets and wholesalers. Fourth, there is continued resistance to reforms. Finally, investment in productive physical capital is inhibited by political instability, uncertainty, and distortionary price policies.

3.2 Independence brought Belarussians personal freedom and democracy; it has not, however, brought "Western living standards." This is hardly surprising, since these standards are not automatically achieved even in market economies. Instead, Western living standards result from a combination of rules and institutions permitting a mobility of factors and goods on a "level playing field" that is conducive to their efficient use. Despite more than four years of independence, Belarus still has not progressed sufficiently in its market reforms to meet these conditions. *As long as its institutional and economic structures remain like those of the old centrally planned, command system, Western living standards can only remain an elusive goal.*

3.3 Without market-driven, high-quality investments, Belarus stands no chance of resuming rapid growth. Every rubel redirected from investment to social programs or public consumption must be carefully evaluated according to the following criteria:

- Will foregone investment negatively affect growth and employment, thereby increasing demands for social support?
- Will diverted funds create new opportunities and empower poor individuals with knowledge and skills that will help them become self-sufficient?
- Do alternatives to public aid exist (e.g., family, community ties, charities)?

3.4 This approach may seem harsh, but the benefits of social spending will be lost if the problems of increasing poverty and dwindling purchasing power are not addressed in market-oriented ways compatible with the resumption of growth. Give-away social justice, based on social programs that ignore incentives, runs the risk of creating a situation where, eventually, only poverty can be redistributed. Harsh policy choices must be faced. To ignore or postpone them does not help, and in the long term is not possible. The sooner they are faced, the better.

B. Preconditions for Success

3.5 In Belarus, as in any other country, there are only two ways to improve individual and household living standards: by generating more *market income* based on economic growth, or by increasing *transfer income*—income that is taxed away from some individuals and given to others, or voluntary transfers such as interfamily gifts. Market income increases most people's well-being by generating additional national wealth and raising the average living standard. Transfers can do neither when incomes are falling; they only

increase taxpayers' average tax rates. Governments sometimes print money to finance more transfers, but this merely creates an "inflation tax" that erodes the welfare of everyone and will probably reduce output.

C. Prospects for Economic Growth

3.6 Before the breakup of the Soviet Union, Belarus enjoyed a trade surplus, a budget surplus, and one of the highest standards of living in the FSU. After the breakup, demand for Belarussian exports dropped sharply. GDP has declined sharply since independence, led by the industrial sector in which output has fallen by as much as 80 percent in some areas. Hyperinflation and drops in output have had multiple initial causes. Their protraction, however, had only one major cause: futile attempts to maintain past economic structures and living standards. One root problem has been printing money to finance wage and social spending increases, which have not been supported by increased productivity. As a result, Belarus suffered hyperinflation between late 1993 and early 1995: inflation averaged nearly 3,000 percent per year. When the authorities began to understand that monetary expansion is the leading cause of inflation, they reduced monthly monetary expansion from nearly 30 percent to single-digit figures in 1995. The fiscal deficit fell from 8 percent of GDP in 1993 to 1.7 percent in 1994. With tighter monetary and fiscal policies, monthly inflation declined from 30–40 percent per month in early 1995 to less than 3 percent in July 1995.

3.7 Government efforts to cut the deficit by imposing firm controls on revenue and spending are yet another positive step toward macroeconomic stability. However, insufficient commitment to sound macroeconomic policy and structural reform—as indicated by the sudden June 1995 increase in money supply—continues to raise doubt about the credibility of the Government's programs. Recent efforts to support agriculture, pay wage arrears, expand industrial production, and finance housing construction through substantial expansions of credit from the banking system provide more recent examples of the reason for this concern. Prospects for stabilization remain guarded and depend on the continuing commitment to stabilization.

D. Reforms Are Key to Economic Growth

3.8 The process of resolving macroeconomic problems is not the same as that for creating microeconomic and institutional change.¹ Without fundamental restructuring of institutions and the economy, and substantial progress toward the development of the private sector, output growth will continue to lag. Good private and public investments that are subject to transparent rules of business conduct, buttressed by a policy environment that fosters efficiency and profit maximization, are key to the resumption of growth. This is a huge, long-term task, and its outcomes depend on the correct sequencing of reforms and the speed of change in the following areas:

3.9 *Reforms that Affect the Institutional Environment.* Laws and institutions in Belarus continue to be heavily influenced by its Soviet past. They must be overhauled to promote a general environment supportive of economic growth, characterized by the following:

1 On the importance of microeconomic and institutional change, see OECD, *Economic Outlook*, 5, December 1992, which argues that "Tight monetary and fiscal policy are clearly necessary...but tight macroeconomic policies by themselves are unlikely to lead to thorough-going economic stabilization and may in the end become politically unsustainable if they are not adequately supported by structural reform" (p. 129).

- *Clear, general “rules of the game,”* achieved through revision of existing laws, new laws, and regulations that minimize transaction costs and are compatible with European Union (EU) norms.
- *A competitive environment,* supported by legislation that minimizes entry barriers, provides legal foundations for current and new enterprise structures, and impedes monopolistic behaviors.
- *A reduced role for the Government* that drastically cuts the costs of regulation and governmental involvement in production. Instead, involvement in the social sector, especially in the field of antipoverty income support policies, must be strengthened.

3.10 *Reforms that Develop Key Components of the Market Economy.* The institutional reforms listed above are important, but without additional supportive actions (including technical assistance, transfer of knowledge, and training) they are unlikely to have an impact on market structures and functioning. For instance, laws can be bent, and enforcement may be ineffective if policing is not set in place. This applies, in particular, to the following:

- *A broad-based incentive structure,* founded on meaningful prices for factors, goods, and services. This requires minimal governmental involvement in determining wages and prices, the removal of administrative controls and quotas, and hard budget constraints. Moreover, the development of behaviors incompatible with the market, such as oligopolistic behavior by large enterprises, will need to be monitored and constrained.
- *Development of an efficient financial system* to assist enterprises in raising needed funds for restructuring and expansion. Access to funds is the most common obstacle for many existing or new entrepreneurs. The transformation process cannot occur if funds needed to finance new investments are unavailable. The public and financial organizations must be willing to participate, which in turn rests on marketplace developments that breed confidence, such as the availability of reliable information (e.g., disclosure of information and registrars).
- *Promotion of new enterprises,* especially small and medium-size firms, that can employ displaced workers and start new productive activities with modest amounts of investment per worker. Because of the novelty of existing problems and challenges for potential entrepreneurs in a post-Soviet economy, support for the development of new enterprises is important, provided that the need for diversity is understood and that the support is flexible enough to adapt quickly to changing demands.

3.11 The list of priority actions compiled above is not exhaustive. Nevertheless, success in these areas is more urgent and vital than in others, creating the core conditions upon which the process of economic transformation and restructuring is founded. Eventually, sound sectoral policies must be implemented to create sustained growth, as well as the higher GDP per capita that growth would bring.

E. Economic Growth is Key to Reducing Poverty

3.1 Growth is the first pillar of high living standards, since it can provide cost-efficient redistribution and thereby increase the well-being of the population. Figure 1.1 has shown the importance of growth for poverty reduction, even in the presence of increasing inequality. Generalized increases in pensions or family benefits can help, but are by no means that powerful. Simulations show that raising pensions and family benefits have only a limited effect on poverty even when increases are large (see Figure 1.2). Moreover, raising pensions or family benefits is costly and requires significant increases in taxation that, especially in the case of pensions, may prove to be unbearable. Targeting of benefits can lessen the resource constraint by controlling total costs and by increasing cost-effectiveness. (This is clearly shown by the simulations presented in Chapter IV.)

3.2 To conclude, economic prospects and living standards in Belarus are highly dependent on national policy choices that mobilize the country to invest in the institutional environment and in the development of basic components of the market economy. These choices are the subject of the next section, which discusses the main features of a social policy agenda for equitable and sustainable growth.

F. Social Sector Reform Is Vital to the Success of Economic Transformation

3.3 Social programs are vital to the development of a sound market economy. They can assist in the following ways:

- building political consensus around needed reforms;
- reducing uncertainty and risk associated with labor market flexibility; and
- building human capital through health and education.

3.4 Moreover, social programs are needed to protect the most vulnerable groups and to ensure that the benefits of growth are fairly distributed between economic “winners” and “losers.” Presently, Belarus does not have a well articulated and cost-effective system of antipoverty policies that protects the poor, including families with children. With poverty affecting so many families, this gap in the Belarussian social protection system constitutes a major drawback for the country.

3.5 Social policy can have undesired effects and limitations, the first of which is their cost and the tax required to cover this cost. As seen above, resources to finance social programs mostly come from taxation, and the size of the tax base is determined by the country’s total output. Relevant questions for social policy in Belarus include the following:

- Is the tax level excessive and likely to distort incentives and penalize economic activity?
- Can tax revenues be improved through better compliance enforcement, thus spreading the tax burden more evenly while holding down the total average rate of taxation?
- Is cash income redistribution the most efficient way to fight poverty? If so, are there dangers of encouraging dependence?

High Tax Levels

3.6 With a direct and indirect tax burden of about 30 percent of GDP (of which about one third is from direct taxation and about two thirds are from indirect taxation), the level of taxes in Belarus is similar to those found in many Western countries. Yet if allowance is made for differences in GDP per capita, the Belarussian burden of taxation is relatively high. At just over 11 percent of GDP, taxes levied on labor to finance social insurance are also high, given the country's per capita income. Moreover, the payroll tax rate is beyond that needed to finance current levels of social insurance benefits. Mostly this happened for reasons of expediency. Payroll taxes are relatively easy to collect in a country where most people work for wages in Government-owned enterprises and offices. Two undesired effects are likely, however. First, the use of labor can be discouraged relative to the use of capital, thus hurting the competitiveness of enterprises in a country where labor is less scarce than capital. Second, with increasing privatization, tax evasion and avoidance are encouraged. For instance, in Belarus, wages in the private sector are reported to be split into two components: an official wage bill that is taxed, and an unofficial wage bill that is not subject to taxation.

3.7 Further studies are needed to define the optimal solution to the taxation problem in Belarus, but it seems clear that the solution will involve broadening the tax base and lower, more even rates, many fewer exemptions, and better enforcement.

Distorted Incentives to Work and Save

3.8 Incentives to work and save are distorted when income differentials between work and idleness erode. Relatively generous pension benefits that create a high replacement ratio reduce the incentives to save for retirement or other contingencies in life, negatively affecting the national savings and investment rate. In Belarus, the high replacement ratio at retirement and the greater protection granted to retired workers is doing just that. In addition, narrow wage differentials and narrow differentials between families of workers and families living on social benefits are also affecting incentives to work. Staying on the payroll of a doomed state-owned enterprise for as long as possible is often as attractive as moving to a new job. Long-term dependence on social benefits also can be as attractive as working.

3.9 These are common problems in social welfare programs throughout the world, but they are particularly acute in Belarus due to the low opportunity costs of living on welfare. The drawback is that these distortions eventually increase demands upon public funds, and by distorting incentives they impede the functioning of the market mechanism. In redesigning the social systems of Belarus, these aspects will need to be carefully weighed (see Annex 6 for a brief overview of the main problems and negative economic effects associated with the social programs in Belarus).

Untargeted Transfers Are Costly and Inefficient

3.10 Cash redistribution, the country's preferred form of income distribution, can be costly and inefficient. In Belarus it is both. Costs are high since cash redistribution is mostly universal. Redistribution is inefficient because policies are badly designed and do not meet their objectives. Spillovers are a costly problem with programs. For example, disability pensions are often granted to individuals whose earning capacities have not been significantly affected by the disability, and special pensions are given to certain occupational groups on a categorical basis without due concern for need or the possibility of alternative employment opportunities. Today social pensions are paid to as many non-poor as poor elderly persons. Reducing such inefficiencies through better targeting will reduce fiscal pressures, improve economic

stability and growth, and allow the Government to provide better support for the truly poor who really need the help.

CHAPTER IV

SOCIAL POLICY FOR SUSTAINABLE AND EQUITABLE GROWTH

A. The Impact of Existing Social Programs and Services

Background

4.1 In the former command system, employment guarantees, social protection programs, and a far-reaching system of social services and public goods redistributed national income and wealth. As with everything else, income distribution was centrally determined. By planners' fiat, everybody was alleged to receive according to his merits—or at least enough to meet his minimum needs.

Since independence, this system has faced severe and increasing problems. Some guarantees have lost credibility, as witnessed by growing unemployment and the risk of mass layoffs hovering over many workers. Similarly, the guaranteed standard of living, manifested in the “minimum consumer basket,” is no longer a certainty, nor is it affordable—although expectations for high levels of social support remain high. Overall, the demands of an increasing number of low-income people are being overlooked because of ineffectively targeted programs. Belarus has continued to adhere to universalist programs and has only reluctantly discovered targeted programs. Few people have completely escaped the negative consequences of the economic decline experienced since independence. Nevertheless, the increasing and sizable group of poor people has suffered more than any other group. Developing cost-effective social policies—together with restoring conditions conducive to economic growth—is an essential component of the twin challenge of growth and equity that calls for an urgent answer.

Table 4.1: Individuals Who Could Not Access Health Services Because of Cost, by Type of Service, 1995 (percent of total population)

<i>Unable to:</i>	
Obtain medicine	66.3
Obtain medical equipment	90.5
Visit a doctor	13.9
Visit a dentist	39.5

Source: New Household Survey.

Human Development Trends Since Independence

4.2 Since 1990, many areas of human development in Belarus have worsened.¹ In addition to the decline in real income, health conditions have deteriorated, and more people have encountered problems in accessing health facilities (as indicated by answers to health questions in the 1995 NHS). Standard performance indicators for education show no significant change. Appearances are deceiving, however, since the quantitative indicators mask qualitative shortcomings and growing inequalities of access and quality of service. The education system has increasingly failed to provide badly needed skills and training.

4.3 The current social protection system of Belarus was not built to favor the poor, since there was no sizable group of poor under the Soviet system, and as seen above, the system is now unable to provide

¹ On human development issues, see also UNICEF, “Children and Women in Belarus,” Minsk, 1995.

such protection to the poor. Moreover, there is no evidence to show that current welfare programs are cost-effective. The Government spends large amounts of money on social protection, yet only limited resources are specifically channeled to alleviate poverty. Only a fraction of social support is targeted to the poor, and the cost-effectiveness of the whole system of social protection is low and in jeopardy.

4.4 *Health.* Male life expectancy has fallen to levels prevalent before the 1950s, and general mortality has increased. Infants and women stand out among those groups that are suffering most. More people have met with problems in accessing health services.² The state-run health care system has found itself ill-equipped to deal with resource constraints and rampant disease. Private medical practice has been slow to develop. The parts that have developed or have been privatized are priced out of reach of low-income individuals.

4.5 The health care system appears powerless to battle negative developments. Inequalities in delivery and access are widening. While in theory the entire population continues to be covered for a full range of public health services, in practice the system is skewed toward those who are employed. Children, the unemployed, and pensioners do not receive adequate care, especially preventive care. Differences also exist across geographic regions. Better-off groups can purchase medical services and receive up-to-date therapies from the private sector on a fee basis, or from enterprises. As portrayed in Table 4.1, a large number of individuals encounter problems of accessing health care services and medical treatment. Very often, the limiting factor is lack of money, leading to an observable positive correlation between families' income and health status. The deterioration of health services is affecting the poor in two ways. First, the private health care sector is clearly underdeveloped. Services are mostly limited to ambulatory care, which implies that it does not constitute a serious competitive alternative to the public sector, especially in poor and rural areas. Second, even when private health care services and prescriptions are available, they are often too expensive for low-income citizens. Existing trends, then, call into question the claim that the state has remained an equal provider of health services.

4.6 *Education.* Belarus developed an important scientific potential during the Soviet era. However, the public education system has lagged in training students for the new challenges of a free market. The mismatch between educational supply and demand for specific skills has grown. The insufficient investment and depletion of the country's human capital resulting from this mismatch of training with needs could lead to even further declines in outputs and living standards in the coming years. Without reforms that enhance education quality and efficiency, Belarussian educational achievements are in jeopardy. So are the country's prospects for growth.

4.7 Education and experience play key roles as determinants of pay. Evidence from the household surveys indicates that undergraduate and graduate degrees in particular boost earning capacity. For many women, good education opens opportunities that otherwise would not exist. Maintaining a good education system is particularly important to prevent increasing poverty and inequity among low- and middle-income groups that cannot access the private education and training sector because of the relatively high fees that are charged (US\$150-\$250 per semester).

4.8 *Social Protection.* Belarus has a comprehensive system of social insurance (see Table 4.2). However, current social programs are unsustainable in their current form. Worse yet, there is no evidence to show that the current system of welfare benefits is particularly cost-effective. Social policy in Belarus

2 This conclusion is supported by NHS data. See also the UNICEF publication quoted in the previous footnote.

has yet to place emphasis on assisting poor individuals and their families. Moreover, poverty was never a policy concern, and this has hindered the development of targeted social assistance programs. The absence of a clear pattern of vertical redistribution appears in the data, confirming that redistribution of wealth was not a goal of the social protection system in the FSU.

4.9 On the whole, social programs support the non-poor more than the poor, except for the child allowance (see Table 4.3). Pensions form an important part of the social programs in Belarus, and pensions are

a type of insurance—based directly or indirectly on lifetime contributions of workers—designed more to *prevent* than to support those already poor. As such, it is reasonable that pensions and various other parts of the social safety net in Belarus benefit the relatively large group of non-poor more than they benefit the relatively smaller group of poor people. Nevertheless, the empirical evidence suggests a significant scope for the transfer of public resources from richer to poorer people. The data also suggest that failures occur in the actual administration of benefits, possibly due to limited experience with means testing programs. For instance, a considerable leakage of funds for poverty relief is observed in the case of the social pension—about 60 percent of non-poor elderly receive family benefits, and a significant share of poor families (about 37 percent) are not paid family benefits even though they qualify.

4.10 *Social Services.* Demographic, fiscal, and other pressures from the country's social and economic transformation are putting the social services delivery system under considerable strain, reducing the overall quality of services and jeopardizing their effectiveness and sustainability. Meanwhile, social services are further strapped for resources, partly because the Government has assumed many responsibilities traditionally carried out by state-owned enterprises. Social services are vital for frail, poverty-stricken groups. The challenge for the Government is to preserve and improve the existing system by reorienting it toward a needs-based service system, and by exploring alternative methods of financing and delivery.

4.11 As it happens, two consequences can be expected. First, there will be an increased reliance on user fees, which will fall most heavily on the poor. This is suggested by, for instance, the higher incidence

Table 4.2: The Social Safety Net in Belarus

<i>Social insurance</i>	<i>Cash benefits</i>		<i>Benefits in kind</i>
		<i>Social assistance</i>	
Old age and military pensions	Family allowance ^a		Nurseries
Unemployment benefits	Single parent payment		Kindergarten
Disability benefits	One-off birth payment		School meals and milk
Survivors' pensions	Noncontributory (social) pensions		Children's holidays
Sick pay	Pension supplements		Boarding schools
Loss of support of primary wage earner	Privileges/consumer compensation		Residential and foster care
Maternity benefit	One-time refugee benefit		Special needs education for children
	Careers of disabled in nonpaid work		Orphanages and homes for infants
	Funeral allowances		
	Other allowances		
	Other cash transfers		Other in-kind benefits
	Maternity leave		Health care
	Parental leave		Education
	Sick child leave		Other social services
			Housing subsidies
			Transport subsidies

a. Child allowance benefit.

of child care costs in low-income groups. In early 1995, the incidence was more than five times higher for the bottom decile than for the top decile. Second, lessened access to free or affordable child care can have direct implications for women's participation in the labor force, especially among single-parent families. The notion of part-time work is also new, and attempting to balance child care and paid employment can become a major concern, especially for those families most in need of earned wages. For many poor people, lack of access to affordable social services can be the determining factor between self support and social welfare.

The Social Policy Challenge

4.12 A clear conclusion emerges from the above. Social policy in Belarus has not yet been focused on assisting poor individuals and families. Poverty was never a policy concern under the Soviet system, and this has hindered the development of targeted social assistance programs. In the conditions that have developed since independence, universal programs are too costly to be sustainable and will almost certainly fail to protect the poor.

4.13 The challenge is to reinvent social policy in Belarus. A new integrated system of universal and targeted programs must be designed to prevent poverty and assist those who become poor. This key concern should be placed at the top of the policy agenda.

4.14 As seen in Chapter I, the future of social programs hinges critically on restoring economic growth. The level of resources available for pensions, social services, health, and education is intimately tied to changes in output. Conversely, economic growth reduces the need for welfare and other social protection programs. Social policy, like economic growth, requires macroeconomic policies that bring stability and structural reforms, and that enable resources to flow efficiently to activities promoting sustainable growth in employment and income.

4.15 Social policy is a necessary condition for growth. Adequate social programs assist in generating a social consensus, which is a fundamental element of successful reform. Moreover, good social policy helps markets function better by providing income security and reducing risk. Finally, income redistribution smoothes the path of adjustment, especially for society's most vulnerable groups. Good social policy supports and complements growth, assuring that the fruits of development are more equitably

Table 4.3: Needs-Adjusted^a Government Benefits and Taxes by Poverty Status (percentages)

<i>Program</i>	<i>Benefits as percentage of minimum baskets^b</i>
<i>Poor</i>	
Pensions	9.1
Other social insurance benefits	0.8
Children allowance	2.7
Unemployment benefits	0.0
Student grants	0.4
Other benefits	0.7
Total benefits	13.7
Income taxes	4.0
Other taxes, fees and fines	0.2
Total taxes	4.1
Net Government benefits	9.6
<i>Non-poor</i>	
Pensions	13.7
Other social insurance	3.9
Children allowance	0.9
Unemployment benefits	0.0
Student grants	0.8
Other benefits	1.0
Total benefits	20.8
Income taxes	14.1
Other taxes, fees and fines	0.2
Total taxes	14.4
Net Government benefits	6.4

a. For a definition, see Section E of this chapter.

b. Annual averages. Totals may not add due to rounding.

Source: Staff estimates based on 1994 Family Budget Survey (FBS) data.

distributed throughout society. To this end, Belarus needs to move from its existing programs toward an infrastructure of more selective programs, tailored to the needs of specific regions and segments of the population. Absolute poverty must be prevented where possible, and where poverty occurs, assistance should be provided in ways that do not encourage dependency.

B. Cornerstones for the New System

4.16 The main principles for social policy reform are the following:

- *Ample opportunities for wage income sufficiency*—as opposed to public income support—should be available for all able-bodied people. Education, health, and a well-functioning labor market in a growing economy are key ingredients for obtaining this objective.
- *Self-reliance should be the keystone of the new system.* All active-age citizens should fend for themselves and earn a wage or other income. Risk protection (i.e., sickness, disability, retirement, survivors, and unemployment) should be in the form of flexible social programs tied to income and tailored to the differing needs and preferences of the population. Child support programs should also be work related.
- *Concern for the special needs* of frail individuals should be expressed through a flexible system of in-kind and cash provisions tailored to handicaps that affect functional ability. This requires an integrated system of social services and special cash supplements, provided by local communities and non-governmental organizations.
- *A system of social assistance should be in place* that complements the above set of programs with targeted initiatives addressing the varied needs of families and individuals who cannot fend for themselves, either because they are unable to work or because they have fallen through the other social safety nets. Means-tested social assistance at the local level is required to fulfill this need.

4.17 The conditions for social policy reform are the following:

- *Fiscal sustainability.* Spending should be contained at levels consistent with the available resources to avoid jeopardizing macroeconomic stability.
- *Neutrality.* Programs should provide incentives and services consistent with the efficient operation of the market economy.
- *Support of human capital formation and savings.* This is key for productivity growth.
- *Cost-effectiveness.* This requires clearly defined objectives (e.g., poverty reduction), good targeting, and administrative efficiency.

4.18 This set of principles and conditions emerges from the analysis in this report. The main cause of poverty—as seen from the poverty profile described in Chapter II—is limited earning capacity resulting from economic decline. In these circumstances, more redistribution can only be ineffective (and costly) as a device for improving the living conditions of the poor in the longer term (see Figure 1.2). Pensioners fare reasonably well in Belarus and have one of the lowest poverty rates. Moreover, less than 10 percent of all poor individuals are people of pensionable age (females aged 55 or more, or males aged 60 or more). The rest of the poor, about 90 percent, live in families with working members. Poverty generally results from one or more of the following factors: low pay, nonpayment of earned wages, open or hidden unemployment, and withdrawal from the labor force because of a lack of jobs. As shown by Figure 1.1 and the simulations plotted in Figure 1.3, poverty caused by such factors is highly sensitive to growth.

and the simulations plotted in Figure 1.3, poverty caused by such factors is highly sensitive to growth. Output and real income growth would reduce poverty by bringing more income or jobs; it would also increase the tax yield, which in turn could be used to finance higher social benefits. Belarussian antipoverty strategy must therefore involve a careful mix of general and targeted policies that indirectly or directly improve the living standards of the poor. The following sections contain suggestions for a social policy agenda for sustainable and equitable growth.

C. Policies that Foster Human Capital Development

Health

4.19 The health of many Belarussian citizens, especially the poor, is in jeopardy. Nevertheless, better outcomes would be possible, even with the available resources, with a vigorous commitment to efficiency in the delivery of health care services. Appropriate policy action would improve existing standards of quality and effectiveness. The population at large would profit, but the poor would profit the most, given the following:

- They are the first victims of the falling performance of the public health care system.
- They have less access to and cannot afford private over public health care services.

4.20 Understanding and identifying the challenges ahead is a first, necessary step for health reform. This involves assessing the following issues:

- The organization of health priorities around basic preventive health care and a basic package of clinical services along the lines recommended in the Bank's *1993 World Development Report*.³
- The implications, especially for lower-income groups, of new methods of reimbursing institutional health care providers (e.g., by patient day, patient treated, diagnosis, global budget, and other patient classification systems) and of paying individual providers (e.g., capitation, fee-for-service, or salary).
- The economic burden of disease and the prevention of avoidable deaths, especially those due to tobacco, alcohol, traffic accidents, violence, and inadequate nutrition.
- The revision of medical training curricula, requiring the integration of public health and family medicine in graduate and post-graduate training, and the organization of a problem-oriented teaching curriculum focused on the integration of modern epidemiology, public health, clinical care, and health care administration.
- The quality of health information systems and the adoption of good methods for health outcomes assessment, service utilization, patient records, management of hospital accounting and finances, and management information systems.
- The cost-effectiveness and priority of treatment for victims of Chernobyl to avoid unnecessary reliance upon programs that foster welfare dependency and that fail to address their psychological as well as physical ailments.

3 World Bank, "Investing in Health," *1993 World Development Report*, Washington, D.C.

4.21 These features all lend urgency to the reorientation of the health care model in Belarus. Reforms are needed for the following:

- *To change the priorities of the health care system*, which currently gives low priority to health promotion, is clinical-oriented and hospital-based, has an excessive number of hospital beds and other facilities, has too many doctors and too few nurses, is overly specialized, and gives an excessive role to the state.
- *To enhance human resources*, which at present lack several of the modern health functions, such as nursing care specialists, general practitioners, and family doctors that are needed to ensure access for all citizens to a core of basic health services.

4.22 Given the present level of resources, improved allocation is possible through the following actions:

- Separating health care financing and provision.
- Decentralizing health care administration and financing.
- Making way for methods based on population needs for the geographical allocation of central funds (i.e., capitation, with corrections for age, sex, and risk group).
- Introducing managed competition based on the principle, “money follows the patient, not the service.”
- Improving incentives for better individual and institutional performance.
- Introducing cost recovery for drugs prescribed in ambulatory care, dental care, elective surgery and direct access to tertiary care without proper referral, and for other types of non-essential services.
- Establishing a well-balanced and diversified public-private mix of services, fostered by practices such as contracting-out or opting-out.

4.23 Improved health care financing and resource allocation methods would provide new opportunities to overcome resource constraints and to preserve access to good health care services. In various instances, health care services that are lacking might even be introduced and improved. For Belarus, improving efficiency is not an option, but rather a necessity to overcome transitional difficulties that are adding health problems to a population that is already struggling to make ends meet. All citizens would benefit, but the poor, who have access only to state health facilities, would benefit the most.

Education

4.24 The close relationships between economic performance and schooling, life expectancy, and other human capital measures make education vital to improving living standards and alleviating poverty. Incomplete secondary or lower education hurts pay and reduces the ability of working families to earn enough to avoid poverty. As noted in Chapter II, the poverty rate in Belarus for those with only a basic secondary school education and no specialized training is 14 to 16 percentage points higher than those with at least an undergraduate education. Workers with lower levels of education are at a particular disadvantage during the current transitional period. They are slower to respond to opportunities that open up; they are more fearful and face greater difficulties than more educated workers in making the shift from those jobs that are disappearing to those that are developing. Less educated workers are overrepresented among the low paid and the poor. In early 1995, about a third among the poor had

incomplete secondary education, while less than 10 percent of the poor had undergraduate or post-graduate education.

4.25 The educational system is facing serious challenges and needs to be changed to respond effectively to the demands of a market-based economy while, at the same time, helping to reduce poverty. In addition to measures that improve efficiency (e.g., increasing student-faculty ratios, streamlining staff use and improving incentive systems for teachers), areas that require structural improvements include the following:

- *Targeted support to students from low-income families.* Scholarships and food subsidies should no longer be universal, but should be reduced and targeted to the poor.
- *Addition of a twelfth grade.* This change would bring Belarus into line with most of the rest of the world. Greater emphasis on newly created gymnasia and lyceums is also desirable to permit more diversification at the higher grades, and to take advantage of unit costs that are significantly lower than those for specialized secondary education.
- *Vocational education reform.* The considerable efforts made toward reforming vocational education are in the right direction. International experience should continue to be tapped to help develop a coherent and integrated vocational education system.
- *Higher education.* Present expenditures on higher education are adequate. Nonetheless, a slow decrease in the share of public spending as GDP increases total spending capacity, and a reallocation of funds in favor of basic and general secondary education are desirable. This would be justified by the declining and changing school age population. Increasing the number of private institutions and placing greater reliance on cost recovery through fees could help to offset reduced allocations. The curriculum should be modified to include more social sciences and to concentrate on subjects that are relevant to the market economy. Merging research institutes into universities would lead to increased relevance of both teaching and research, and to increased efficiency.
- *Curriculum redevelopment and new textbooks.* Action is required at all levels if the new skills required by the market economy are to become available.

Labor Market Reform

4.26 Job losses are a necessary cost of structural adjustment. They are a sign of vitality and of progress toward sustainable growth, and they cannot be avoided. While some jobs are destroyed, others must be created by investing in human and physical capital. The Government can play a key role by expediting structural reforms in areas where job expansion is jeopardized, and by removing obstacles that hinder the flow of resources into efficient activities. A variety of regulations and labor market rigidities presently discourage economic activity. These policy-induced problems hinder employment creation and real wage growth and therefore contribute to poverty.

4.27 Needed labor market reforms include the following:

- *Implementation of new laws and regulations,* including a new labor code that facilitates labor mobility. Other legislative action is required on the activities of small and medium-size enterprises, as part of efforts to reduce regulatory obstacles to economic activity and labor mobility.

- *Containment of spending on passive labor programs* through tightened eligibility (i.e. benefits should be paid only to those who have a six- or twelve-month employment record period or who have been out of work for at least two to three months. This avoids giving scarce resources to those who suffer only transitory rather than more permanent poverty. Costs could also be contained by reshaping the term-structure of benefits, i.e., introducing flat-rate payment for long and recurrent spells of unemployment.
- *Trimming the present myriad of labor market policies* to concentrate scarce resources on cost-effective active programs that facilitate labor relocation and encourage the acquisition of new skills. Programs should be coordinated with enterprise restructuring and development. They could include training vouchers, privately assisted training, employment services and information centers for small and medium-size businesses, job schemes for former military personnel, free enterprise zones and incubators, and financial assistance to small enterprises. These activities should be examined carefully before major expenditures are incurred to ensure that they are cost-effective and consistent with broader efforts of private sector development and financial sector reform. Moreover, limited resources should not be unduly dispersed by attempting to finance too many programs.
- *Lowering of payroll taxation and other legislated costs* (hiring and firing) that increase labor costs and affect the ability of Belarussian firms to compete in international markets.
- *Removal of gender inequalities* inherited from the Soviet system that discriminate against women and negatively affect their pay.

D. Policies that Foster and Protect Lifetime Savings

Social Security

4.28 Pensions play a key role in preventing poverty, as witnessed by a poverty rate for pensioners that is significantly below the mean. The pension system in its current form, however, is unsustainable and urgently needs reform. Otherwise, the financial pressures generated by long-term demographic trends could undermine the ability to maintain universal coverage and wage-related pensions. Recommended actions include the following:

- *Distinguishing between savings and income redistribution.* Drawing a clear distinction between lifetime savings and income redistribution would permit the separation of social *insurance* functions, which relate to lifetime savings, from social *assistance* functions, which redistribute income. This would help shelter the social security system from political demands for income distribution to the poor, distributions that violate the principle that social insurance should be essentially self-supporting on the basis of contributions paid during a working life. Redistributive transfers should be means-tested, universal minimum benefits that are granted to all.
- *Ensuring fiscal sustainability.*⁴ Pension reform must remove the most severe threat to sustainability—the expected further increase in the support ratio (the ratio of those on pensions to those working and paying pension contributions). Under very optimistic assumptions, this ratio will increase to 60–70 percent by the end of the decade. To reduce this ratio and, at the same time, preserve the coverage of all of those employed, it is necessary to tighten eligibility

4 For a detailed review of sustainability issues, see the World Bank's "Fiscal Policy Study," 1995.

to those working and paying pension contributions). Under very optimistic assumptions, this ratio will increase to 60–70 percent by the end of the decade. To reduce this ratio and, at the same time, preserve the coverage of all of those employed, it is necessary to tighten eligibility criteria for old age and disability pensions. This can be accomplished by the following actions:

- Increasing the retirement age or introducing flexible retirement provisions (i.e., benefits that are actuarially increased if retirement is postponed, and vice versa).
- Curtailing early retirement.
- Tightening disability criteria and switching from costly long-term cash provisions to rehabilitation.
- Introducing a system of categorized means-tested benefits targeted to raise pension benefits to minimum levels. These measures would provide lower benefits for those groups that are likely to have alternative sources of income or employment, while preserving adequate total incomes for the majority of pensioners.

4.29 Moreover, pension reform must reduce replacement ratios—the ratio of pension to working life income—to a level consistent with the prevailing support ratio. Pension levels and costs should be set so that they do not require exceedingly burdensome taxation of the active population and enterprises, and they should provide incentives to work and save. This, in turn, requires (a) that pension benefits be determined not according to the highest wages received, but rather on the basis of individual lifetime earnings and contribution records; and (b) the development of adequate social security information records.

4.30 *Efficient administration.* Pension reform should be accompanied by the following:

- Reorganization of the social security administration to strengthen the independence of the fund and to avoid the use of social security funds as easy money to cover unproductive public expenditures.
- The establishment of a regulatory environment that fosters the development of private pension programs.

4.31 *Modernization.* Effective reform requires a modernized administration that can provide high-quality service and process information on all enterprises and workers. This is essential for efficient financial management, to fight abuse and noncompliance, to provide a quick information basis for antipoverty policies, and to provide information needed to enforce tax compliance. Above all, it is necessary to move toward work- or contribution-related benefits.

4.32 *Savings and private pensions.* The existing pension system in Belarus has never served as an instrument to generate savings that might add to the productive capacity of the country. Reform of the pension system based on the above principles would allow a fundamental change with positive implications for income and employment growth. First, the independence of the social security programs would protect workers' social security savings from confiscation by the Treasury. Second, reduced replacement ratios would open the way to increasing lifetime savings through private pensions (e.g., occupational pensions) and other forms of financial instruments. The experience of other countries indicates that private programs can successfully complement public pension programs and can contribute to mobilizing resources for domestic financial markets. In addition, there are already some indications in Belarus of the demand for private pension programs.

Housing Ownership

4.33 Privatization of housing will require reduced public subsidies and higher cost recovery rates. Privatization may reduce the quality of housing and increase its cost, putting a special burden on the poor, who already suffer from relatively low housing standards in many cases. Middle- and upper-income people can be expected to devote resources to buying and improving their homes, but the poor are less likely to do so. They do not have accumulated savings that they can use to buy their apartments, nor do they have access to credit. Moreover, they face relatively greater housing costs (which in early 1995 were equal to 7.2 and 3.1 percent of total income for the bottom and top quintiles, respectively), and are hard pressed to pay for basic maintenance, let alone renovation. In addition, while higher-income families can make energy conservation investments to reduce utilities bills, the poor cannot. Access of low-income households to home ownership should be facilitated through financial assistance programs and special housing projects targeted to low-income families. Ad hoc supplements to basic income support benefits should be granted to cover recurrent spending on housing, as well as spending for maintenance and even small improvements. A system of *block grants to oblasts*, determined by the regional poverty rate, could assist the poor with basic housing and energy conservation measures.

E. Policies that Improve Income Sufficiency

4.34 Emergency programs and policy actions in the fields of social assistance, social services, and support for marginalized areas are needed to control and reduce the incidence of poverty.

Social Assistance

4.35 Targeted income support in Belarus is limited. Attempts to develop such support have either failed or have been characterized by unsatisfactory targeting and low cost-effectiveness. Growing poverty and falling resources make the development of targeted programs a priority.

4.36 The menu of available strategies for reducing poverty includes both *income support strategies* (Credit Income Tax, Negative Income Tax, Earned Income Tax or Earnings Supplement, Basic Income Guarantee), and programs that are more directly focused on *labor markets* (wage rate subsidies, employer-based marginal employment subsidies). All have merits and disadvantages.⁵ Major hindrances in developing modern income support programs such as the above, include the following:

- Lack of experience with means-tested programs.
- Shortage of skills and equipment needed for accurate means-testing.
- The nonexistence of an adequate system for gathering reliable information on individual and family *income or earnings*, especially that from *non-wage* sources.
- Weak enforcement capacity.

4.37 With no reliable knowledge of a person's earnings, income, or work status, the implementation of a comprehensive system of means-tested income support runs the risk of widespread fraud and errors, and

⁵ For a detailed discussion, see R. Haveman and B. Wolfe, "Towards a Social Policy Reform Strategy for Belarus: A Primer on Alternative Strategies to Reduce Poverty and Maintain Employment," mimeo, Washington, 1994.

consequent high cost. Such an approach would also engender unfairness, because of the greater opportunity of access implicitly offered to the self-employed and workers in the informal economy. On the other hand, the development of social programs at the local level is also open to abuse, or it can be so stigmatizing that very few people avail themselves of help.

4.38 Given the existing conditions, a balance should be struck between these two extreme approaches, taking into account the size and characteristics of the poor population. The poor fall into three broad categories: households with children with at least one active member; pensioners; and a small, residual and rather heterogeneous group that does not fall into either. Means-tested programs can then be developed for the following categories of probable poor:

- *Active workers with many children.* Envisaged are family benefits in the form of means-tested payments conditional on the payment of social security contributions.⁶ Benefits would be a function of the gap between the poverty line and earnings, and based on family size. If this program were kept simple, the low wage supplement could continue to be dispensed through enterprises at minimal cost.
- *Pensioners living alone or as couples,* who could receive pension supplements that would be granted to take into account special needs for housing, mobility, dependents, etc. A simplified means test could be envisaged. Local offices of the Ministry of Social Protection could easily administer the test and authorize benefits payments.
- *Other groups.* Means tests for other groups would have to be comprehensive, detailed, and pervasive. It would also be important to maintain a close relationship between the applicant and the administration. For this purpose, given again the small number of cases, local regional offices need to be given the responsibility and authority to exercise discretion. In all cases and for all categories, potential beneficiaries should be required to validate their own eligibility according to clear, well-publicized rules, should face significant penalties for fraudulent applications, and should be obligated to recertify their eligibility on a quarterly basis, except in the case of extreme physical hardship, such as immobilizing physical handicaps.

4.39 This system would immediately address the needs of poor families with children, pensioners, and—later on—the remaining groups. The population receiving social protection would comprise 200,000–250,000 pensioners out of 2.5 million. Enterprises would deal with about 0.9–1 million workers with children, while the 172 local raion offices would work with about 30,000–40,000 persons (50–100 each on average). Depending on program design, the income reference period, benefit levels, and phase-in and phase-out rates, the total costs of the proposed system of social assistance could range between 2.0 and 2.9 percent of total household income (see Box 4.1 for more details and simulations of possible schemes). Given the sensitivity of poverty to the length of the income reference period over which eligibility can be assessed, this variable will be a key determinant of total cost.

6 Conditionality upon payment of social security contributions is necessary to encourage full wage reporting and work in the formal sector. To avoid “poverty traps” and work disincentive effects, appropriate design will have to ensure benefit phase-out or withdrawal rates lower than 50 percent.

Box 4.1: Antipoverty Means-Tested Programs: Fiscal Cost and Effectiveness

The cost of eliminating poverty in Belarus is equal to about 13 percent of total household income, which is about 1.5 and 2.5 times present levels of spending on social insurance or social assistance programs, respectively. Given available resources and the stringency of the budget constraint, Belarus cannot afford to redistribute this large amount. The economy and the active population would not be able to bear the high cost, and growth would be jeopardized. A much more modest policy target must then be set to maintain fiscal costs within bearable levels.

Overall fiscal cost: The burden of the proposed means-tested programs shall not exceed 2.0–2.9 percent of total household income. Of this, 0.5–1.0 percentage points can be covered through spending savings resulting from improved target effectiveness, as a result of a reduction in the leakages that presently characterize the administration of family benefits and social pensions. Another 1.4–1.9 percentage points can come from existing targeted programs that can be discontinued and substituted with the new programs.

Cost of the three programs: The Income Supplement for active workers with children is estimated to cost about 1.5–2.2 percent of total household income. The Pension Supplement for the elderly is estimated to cost about 0.3–0.5 percent, while the cost of locally administered programs can be estimated at around 0.2–0.3 percent.

Benefit design: Benefits must be designed to maximize target effectiveness (i.e., the impact on poverty) and minimize leakages (i.e., payments to the non-poor) and disincentives (i.e., implicit marginal tax rates). The benefits that are proposed for low-income families with children and for pensioners are designed to meet the above criteria. Administration is simple (which implies very low administrative costs), and possibilities for fraud and abuse are limited. Benefits for families with children and for pensioners are determined as a multiple of earnings or pension. Locally granted income support is discretionary.

Simulations: Given objectives and basic scheme features, various models and models variants can be chosen. Simulations help in choosing the model that can best secure cost-effectiveness, given the fiscal target.

For Belarus, a model that combines a lump sum ($Y_1 = A_i$) and a proportional income supplement (Y_2)—paid at a rate a of a worker's pay (W)—has been found to perform best. The variable part of the benefit reaches a maximum when pay equals $W = Wk$ (at kink point). After the kink point, both the lump sum and the variable benefit are taxed at a rate t . Eventually, the tax paid equals the value of the benefit received, and the net benefit becomes nil (break-even point). The following is a mathematical description of the model:

Before the kink point:

$$Y_1 = A_i$$

$$Y_2 = (1 + a)W$$

Beyond the kink point:

$$Y_1 = A_i$$

$$Y_2 = (a + i) Wk + (1 - t)W$$

$$Y_{wi} = A_i + (a + t)Wk + (1 - t)W$$

At break-even point:

$$Y_{tax} = 0 \text{ and no supplement is paid}$$

The cost and the impact of the scheme are a function of a —the phase-in rate⁷; t —the phase-out rate⁸; A_i —the amount of the lump sum payment; and Wk —the kink point wage. The simulated impact and performance of various combinations of possible values of the above parameters are shown in Annex 9.

Social Services

4.40 Social services are an important instrument of in-kind redistribution that avoids overreliance on cash benefits. Objectives of reform should include the following:

- Adapting the current system to the needs of a market economy.
- Improving targeting and the quality of services.
- Ensuring uniform standards of service throughout Belarus.
- Modernizing and reorganizing the administration.
- Making available computer links between social services and social security offices.

7 That ratio between a benefit and total prebenefit income, or the benefit-payment ratio.

8 That is, the benefit withdrawal rate or the rate at which the value of the supplement is reduced as pretax income increases.

4.41 Recommended actions would include the following:

- Improving the targeting of services and in-kind benefits to needy groups. Orienting the system toward a needs-based service system.
- Improving the range and quality of services and benefits provided. Encouraging the introduction of flexible and innovative community services. Strengthening quality assurance mechanisms and developing monitoring and inspection initiatives.
- Permitting an expanded role for the private and voluntary charitable sectors.
- Training social workers and social security staff, especially by integrating current theoretical courses with practical experience and developing an independent professional association.
- Exploring alternative methods of financing services (e.g., introducing flexible new services for those who can afford to pay, considering new financing schemes for old age homes and shelters).
- Striking an appropriate balance between residential and community care.
- Encouraging the formal rehabilitation of disabled adults and children, with the aim of reintegrating disabled people into the community. Building up professional training in prosthetics, and ensuring internal consistency within broader policy reforms (e.g., re-evaluation of disability assessment methods, reconsidering targeted disability pensions).

Support for Marginalized Areas

4.42 Regional inequalities, such as those affecting localities in the Grodno and Gomel oblasts and in other areas formerly occupied by military bases, already affect the standard of living in these areas. Economic decline serves to widen these inequalities even more, especially in single-enterprise towns where closure may result in the collapse of the local economy. This would have destructive effects upon localities and lead to pockets of severe and chronic poverty. It is therefore important that policies be designed to do the following:

- *Re-education and training.* Local populations, especially those in relatively isolated rural areas, are not accustomed to thinking in terms of marketing strategies. Although rural areas may have potential attractions—natural resources, historical structures, and local skills in crafts, for instance—local residents do not necessarily know how to exploit existing opportunities. Before any financial investment decisions can be taken, residents should learn to identify potential business opportunities and to develop, package, and market the goods or services effectively.
- *Protection and development of an attractive and hospitable local environment (e.g., for tourism).* Possible measures might include a housing development plan, incorporating current efforts to privatize, save energy, and modernize existing housing. The central idea would be that if housing redevelopment and marketing strategies were combined, local residents would have vested interests in becoming involved with both. As part of the efforts to privatize and renovate housing, funding should be aimed at the creation of cooperatives. These would be composed of local residents who would have the dual responsibility of identifying local housing needs and undertaking cosmetic renovations.
- *Bring people to jobs,* through schemes that support labor mobility. These would include elements of the two programs mentioned above, as well as improved housing.
- *Housing.* Housing scarcity was a major reason for the Soviet-era *propiska* system, which restricted labor mobility by direct police-enforced controls. The ability of people to move to

jobs can be enhanced by housing development programs that stimulate private construction of new housing units by the public provision of serviced land that is available for private ownership.

F. The Balance Between Short-Term and Long-Term Needs and Policy Objectives

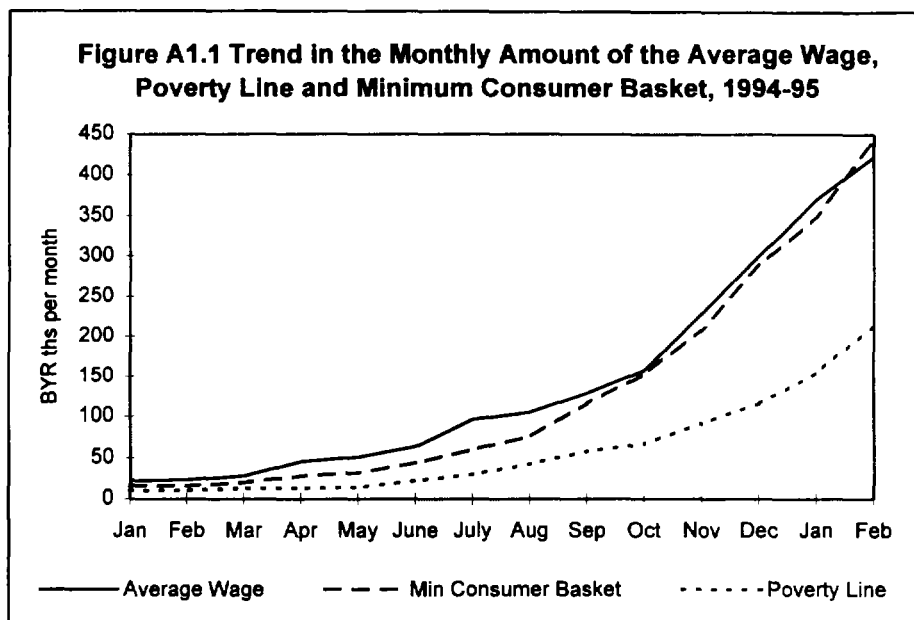
4.43 Social policy reform demands easy access to information, administrative capacity, and means. This cannot happen abruptly. Reform has to be planned within a realistic and manageable period, distinguishing between short-term and medium-term tasks. The tasks could be planned to begin and end in an integrated manner. Tasks should overlap, which would ensure continual reform activity. Moreover, urgency may demand the implementation of temporary programs for problems that are urgent and particularly acute during the early stages of the transition. It is important that these short-term solutions should not jeopardize the implementation of longer-term reform plans but, where possible, should pave the way for them.

ANNEX 1 BELARUS POVERTY LINE

A. The Definition of Poverty

1.1 Belarus has no official poverty line, nor is any existing definition of a minimum income standard or benefit useful for the measurement of poverty. For policymakers in the command system, poverty was an alien notion. The state guaranteed individuals' employment, income, housing, and other necessities, while the attention of the policymaker was focused on

general distributive issues and income differentials. The minimum consumer basket, the minimum wage, and the so-called employee's unified "tariff scale" were key in these decisions. Only the elderly and the disabled had access to social assistance—and then only to cover specific handicaps, not as a remedy for income shortfalls. In varying degrees, past ideas have continued to influence the wage and benefit determination process. However, neither the minimum consumer basket (Figure A1.1) nor the minimum wage have facilitated definitions of minimum or poverty incomes: the first has proven unsustainably high, and the second too low¹ to provide a meaningful reference.



1.2 Like all other FSU republics, Belarus faces the urgent challenge of developing policies to protect groups that lag behind or whose incomes erode more quickly under the pressures of inflation and falling output. This requires a credible and sustainable poverty line that can be used to demarcate real poverty in Belarus, so that those with highest priority needs may claim a fair share of resources.

1.3 The poverty line can be defined by using a variety of approaches. *In the face of falling real incomes and tight fiscal constraints, the protection of absolute minimum living standards—not relative standards—is paramount.* In this regard, a realistic definition of a minimum basket becomes key. Box A1.1 outlines an approach to the measurement of poverty in which the minimum baskets underlying the poverty lines meet four requirements:

- Conformity to FAO/WHO/UNU recommendations for minimum nutritional intake.
- Inclusion of both food and nonfood items and of choice.
- Tailoring to family size and needs.
- Reflection of market prices, with costs minimized and adjusted for regional differences.

¹ For instance, in February 1995 the official minimum consumer basket was equal to BYR 429,433 and the minimum wage equal to BYR 30,000 per month. Average pay was equal to BYR 387,733. Even attempts to define a poverty line by taking a proportion of the minimum consumer basket (e.g., 50 percent) proved to be problematic due to the peculiar features of the minimum consumer basket.

BOX A1.1: BELARUS POVERTY LINES

Details about the methodology used to estimate the poverty lines for Belarus are contained in a separate study (N. Kakwani, *Minimum Consumption Baskets and Poverty in Belarus*, mimeo, 1995). The methodology is based on a fundamental distinction between separable goods and services and joint consumption goods. The consumption of the former can be attributed to individuals. Joint consumption, such as in the case of most durable goods, housing and utilities, cultural, transport, communications and some services, implies sharing by two or more individuals. Because of sharing, economies of scales occur, depending on household size and composition. Economies of scales can also be observed for separable consumption items. All food, clothing, footwear, sanitary, hygiene, and medicines are considered as separable.

The process of determination of poverty lines followed in this consists of the following steps:

- Food requirements are estimated using available information on the nutritional needs (norms) of individuals distinguishing according to age, gender, residence, and intensity of labor activity. Subsequently, the composition of the food basket satisfying minimum requirements is determined on the basis of food consumption patterns of low-income rural households. Differences in the cost of rural and urban households are observed, depending partly on price differentials and partly on quantities or the composition of the basket. Given the nutrients' content, the rural basket appears more cost-effective and is chosen to determine the physical composition of the food basket meeting minimum requirements norms. Finally, this basket is priced using urban and rural prices, respectively.
- Nonfood items are estimated with reference to six categories: (a) clothing, footwear, and underwear; (b) durable household goods; (c) medicines, and sanitary and hygienic goods; (d) shelter and utility; (e) cultural and educational activities and recreation; (f) services, transport, and communications. Estimates are based on an extremely detailed list of items, taking into account their expected life, possible joint consumption, and differences in requirement by age and sex. Finally, the composition of the nonfood budget is determined by taking into account the actual consumption pattern of the bottom 50 percent of the population. This basket is costed by taking into account rural and urban price differentials.

On the basis of the above information, poverty lines are determined for each household, depending on its size, composition, age of members, and residence. The average value of the poverty lines used to compute the poverty profile are shown below:

Monthly Average Poverty Line*
by different types of families and different categories of families for targeting

FAMILY TYPE	Pensioner and others			Families with at least one worker			Other family types		
	Number of families	Average per family poverty line, ** in thousands of rubels	Average per capita poverty line, *** in thousands of rubels	Number of families	Average per family poverty line, ** in thousands of rubels	Average per capita poverty line, *** in thousands of rubels	Number of families	Average per family poverty line, ** in thousands of rubels	Average per capita poverty line, *** in thousands of rubels
Single	151579	319	319	37190	333	333	7921	333	333
Single parent	1564	582	291	42198	670	280	4404	970	270
Married couple	38375	551	275	38353	575	287	777	591	296
Married couple with 1 child	5261	822	274	111954	829	276	4642	832	277
Married couple with 2 children	2607	1080	270	160864	1059	265	1251	1044	261
Married couple with 3 children	-	-	-	37456	-	-	1226	-	-
Married couple, adults and children	6332	1292	263	215162	1318	270	1893	1470	277
Adults only	29490	686	279	176189	928	284	3561	796	294
Adults and children	5782	997	272	34552	951	276	618	861	287
Total	240991	463	303	853918	1004	276	26293	773	295

* The monthly average poverty line is equal to the sum of each month, inflation adjusted quarterly poverty line divided by 3.

** Overall average per family poverty line is 797 thousand rubels.

*** Overall average per capita poverty line is 282 thousand rubels.

Figure A1.2 Price Changes by Main Expenditure Categories, January 1994 - February 1995

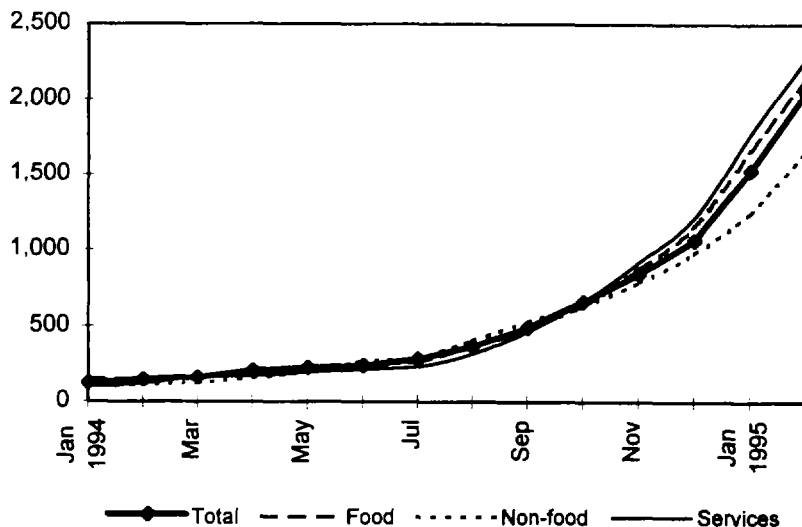
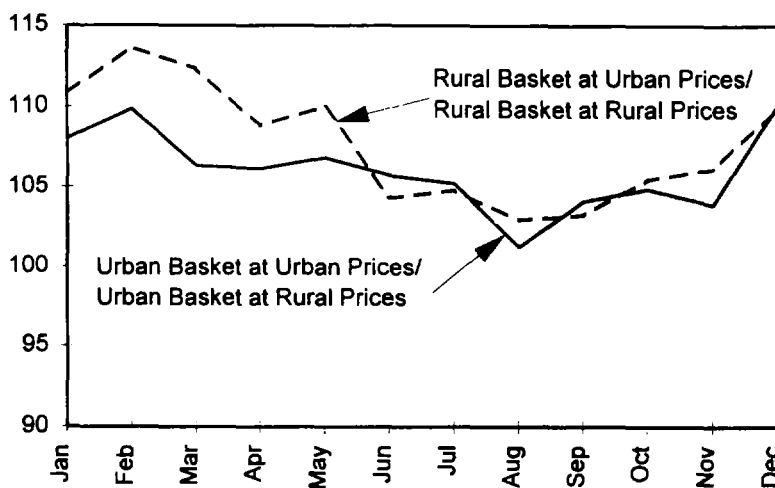


Figure A1.3 Changes in Urban-Rural Price Differentials in 1994 (Spatial Quality Indices)



1.4 Box A1.1 provides further details, while Figure A1.1 shows that the (average) poverty line used in this report is substantially below the official minimum consumer basket and average national wage. Nonetheless, the ratio between the poverty basket and average per capita income is well within the range found for most Western countries (i.e., around 50 percent of average earnings).

1.5 The suggested definition of poverty described in Box A1.1 makes allowances for differences in needs and for economies of scale, which are possible in larger households. Regional adjustments for price change and differentials are also considered in this definition.

1.6 *Adjustment for Regional Price Differences.* The cost of a basket of goods varies by region. For example, in December 1994 two identical individuals buying a minimal basket would have required BYR 49,079 in a rural area or BYR 195,394 in an urban area. These differences are too large to ignore, and require poverty lines that take urban-rural price differentials into account.

1.7 *Adjustment for Price Changes.* Rates of price change also differ across regions. The impact of inflation varies, depending on the composition of a particular basket. Fast inflation and geographic differentials necessitate that (a) minimum baskets are adjusted in a timely manner to account for price changes, and (b) indexation procedures are timely and fair. This requires that indexation mechanisms be based not on overall inflation, but on the actual change in cost of living, given the baskets' composition. Figures A1.2 and A1.3 show price changes for different expenditure categories and for rural and urban

basket values evaluated at rural or urban prices. They indicate that an indexation mechanism based on the general price index can fail to protect the real value of the urban basket. At the same time, it can overcompensate residents in rural areas, where nonfood items have a lower weight and prices change more slowly. For instance, in 1994 poor families in urban areas would have required twice as much as rural families to be fully compensated for price changes.

B. Sensitivity of Poverty Counts to the Level of the Poverty Line that Is Chosen

1.8 Although absolute poverty measures are grounded on predefined, “objective” criteria based on judgments that concern minimum quantitative consumption of goods and services, policymakers may not want or indeed may be unable to ensure enough income redistribution to close the full poverty gap. Fiscal cost can be one consideration. Another can be, as in Belarus, the existence of widespread underreporting or the sheer difficulty of evaluating certain income sources (e.g., the cash value of in-kind income). In the circumstances, a less ambitious objective than closing the poverty gap for all may be chosen. What this choice may mean in terms of costs and results is a function of the shape of the income curve. In Belarus, taking 1995-Q1 data, it can be estimated that the percentage change in the incidence of poverty for a 1 percent change (either up or down) in the level of the poverty line (i.e., the elasticity of poverty to the level of the poverty line) tends to be somewhat less than unity, about 0.8. This value is not constant along the income curve, but tends to assume different values. Estimates of the change in poverty incidence for given changes in the value of the poverty line are shown in Table A1.1.

Table A1.1: Impact of Changes in the Value of Poverty Line (PA) upon Poverty Counts (PC)

<i>Percentage increase/ decrease in PL value</i>	<i>Percentage point increase in PC, if PL is raised by stated percentages</i>	<i>Percentage point decrease in PC, if PL is reduced by stated percentages</i>
1	+0.80	-0.75
5	+3.90	-4.00
10	+7.80	-8.70
15	+11.40	-12.11
20	+15.00	-16.3
30	+22.00	-22.30

Source: Staff estimates.

ANNEX 2

INCOME CONCEPT AND OTHER METHODOLOGICAL ISSUES

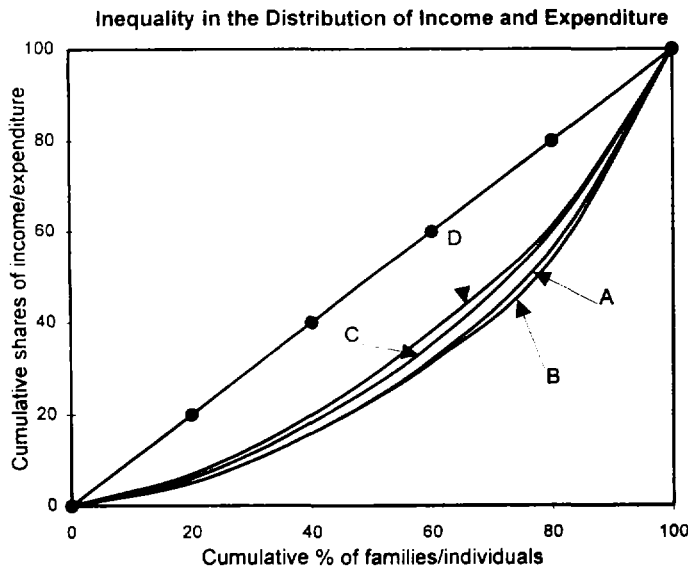
2.1 Income or consumption can be used to assess poverty. The latter is preferred in economic analysis of well-being and its distribution. The former is (with or without recourse to the use of other indicators) used by offices of the social protection administration whenever faced with the problem of determining eligibility and access to means-tested programs.

Box A2.1: Unit of Measurement: Income or Expenditure

Both income and expenditure data are used to measure well-being and assess poverty. Due to income fluctuations, current consumption (including consumption from own production) is often regarded to reflect households' ability to buffer their standard of living through saving and borrowing, better than current income. However, this not always is true; under some circumstances, consumption can turn out to be a less satisfactory measure of households' typical standard of living. (On this issue, see World Bank, "Poverty," *World Development Report 1990*, Washington, DC; P. Johnson and S. Webb, "UK Poverty Statistics: A Comparative Study," Institute for Fiscal Studies, London 1991; and P. Roberti, "Some Methodological Considerations on the Measurement of Poverty in Italy," *Rivista di Politica Economica*, May 1989, pp. 129-50.) In practice, however, the choice between income and expenditure must be judged on specific survey features, not theoretical reasons.

Belarus has two data sources. The Family Budgets Survey (FBS) and the New Household Survey (NHS). In the FBS basically no difference exists between income or expenditure data, since the survey is based on the following definitions:

- Total resources (TR) = total cash income + in-kind income + transfers from other households + dissaving.
- Total Outlays (TO) = total consumption + in-kind consumption + transfers to other households + saving, with TR=TO for all households.



The ratios between the highest and lowest income percentile are:
A=8.2, B=8.1, C=5.8, and D=4.8.

No such precise balance is available for NHS data. Moreover, collection of NHS expenditure data has started only in January 1995. Because of the inclusion of in-kind and cash income, one can expect, by and large, that use of income or expenditure would lead to similar results. This conclusion is supported by the four Lorenz Curves in the figure to the left. The curves are based on four definitions of total resources, as shown in the key below.

- A= Household total cash income
- B= Household total cash expenditure
- C= Household cash and in-kind expenditure
- D= Per capita cash and in-kind income

The data in Table A2.2 suggest, however, that this conclusion needs to be qualified. Conclusions do not just depend upon the choice of income or expenditure, but rather on their actual definitions, i.e., on how comprehensive they are and the items that are eventually included under the two definitions.

2.2 The focus of this report is on policy, not well-being. This requires the use of income as an indicator of households' standard of living.

A. Income Concept

2.3 The notion of income can take various meanings. Cash income is an obvious one. However, unlike in most Western industrial countries, where cash income tends to be the major and often sole determinant of household living standard, there are two or three additional income sources that are important in Belarus. The first is *income from informal and hidden activities*. The second is *in-kind income*, most often from private land plots, but also from the employer and the state. The third is the *command over goods and services, obtained through a network of relatives, friends, and other contacts*. In Belarus, these sources are undoubtedly important, but are difficult to evaluate, especially the third. For example, which prices should one use to evaluate in-kind income, especially considering that such income is a crucial, some say the most crucial, determinant of household well-being, particularly at the lower income levels? Also, inflation affects different income sources differently (i.e., in-kind income is a store of value while the purchasing power of cash income is eroded).

2.4 This analysis in this report is based on the following two concepts of income:

- *Total cash income*, including income from wages and salaries, fringe benefits and other cash or in-kind benefits from enterprises, self-employment income, interest and property income, agricultural income, transfers, and lump sum income.
- *Total resources*, which include the above items, as well as in-kind household income from various sources, but primarily from garden plot yields.

2.5 Table A2.1 provides an overview of the importance of different income sources in 1995 distinguishing between (a) labor or wage-related income, (b) enterprise and capital income, (c) in-kind income, (d) social

protection benefits, (e) alimony, and (f) other incomes. Other items are also important and considered in this analysis, notably, borrowing and access to saving. These sources help in smoothing income fluctuations and in reducing the impact of possible income shortfalls upon households living standards, though they are not regular income components.

2.6 No quantitative estimate is available on informal activities in addition to those surveyed in the NHS. (See Table A2.1, items "Other jobs" and "Occasional jobs.") It can be expected that they are much

Table A2.1: Importance of Different Sources of Income, 1995

<i>Source of income</i>	<i>Percentage of total income</i>	<i>Average amount per receiving household</i>
a. Wage and wage-related income:	40.74	363,165
• Main job * Cash pay	37.8	634,181
• * In-kind pay	0.13	59,031
• * Fringe benefits	0.28	70,916
• Other jobs * Cash pay	0.28	261,710
• * Fringe benefits	0.00	66,328
• Occasional jobs	2.26	218,268
• Severance pay	0.04	62,699
b. Mixed and capital income	4.10	546,639
• Entrepreneurial income	3.70	586,111
• Dividends and rent	0.40	183,571
c. In-kind income	35.30	376,940
d. Social protection benefits:	16.86	276,232
• Pensions	14.30	313,505
• Unemployment benefits	0.10	61,081
• Family benefits and subsidies	1.90	66,643
• Stipends	0.56	73,985
e. Alimony	0.30	106,702
f. Other income (including aid from relatives)	2.70	148,390

Source: Staff estimates from NHS

more important than is suggested by the data in Table A2.1. Unofficial estimates, put the size of informal activities to about 30 percent of GDP.

2.7 The influence that different income-expenditure concepts can have upon poverty counts can be gauged from Table A2.2. Depending on the resource concept that is used, poverty in Belarus can rise to nearly 70 percent (on a cash income basis) or fall to as low as 13 percent (on a “maximum between income or consumption” basis). Expenditure includes all cash outgoes, e.g., plot expenditure for forage, farm machinery, food for animals, investment, and savings also leads to lower poverty incidence than using only cash income to define expenditures. However, important double counting may occur in this instance (e.g., purchase of foreign currency at the beginning of the month and sale of foreign currency to pay for clothing are counted twice). Moreover, seasonal factors can influence results. For instance the difference between the income and expenditure poverty counts is very small in Q2, but is substantial in Q1.

B. Influence of the Income Reference Period on Poverty Counts

2.8 When, as in Belarus, incomes fluctuate significantly during the year, the choice of the reference period that is used to assess poverty can prove to be extremely important. It can significantly affect the conclusions that are drawn from the analysis, and it is crucial for the success and sustainability of antipoverty programs. Poverty estimates for Belarus change notably as the reference period is extended from three to six, nine, and twelve months. The

Table A2.2: Poverty Incidence in Belarus with Different Income Concepts (percent)

<i>Income concept</i>	<i>Poverty rate 1995-Q1</i>	<i>Poverty rate 1995-Q2</i>
Net cash income	69.5	44.0
Total resources (net cash income plus in-kind income)	35.7	24.3
Cash expenditure ¹	46.0	41.2
All cash expenditure ¹ plus in-kind income	22.3	23.4
Maximum between cash income or all cash expenditure ¹ plus in-kind income	17.5	13.3

Note: In addition to total consumption, the following are included: plot expenditure, forage; farm machinery, etc.; food for animals; purchase of securities; purchase of foreign currency; purchase of real estate; and aid from relatives.

Source: Staff estimates.

choice of reference period is therefore a key factor to consider when designing a social assistance program. The number of individuals and families eligible for income support can be extremely different—varying from up to 35 percent, when income is assessed over a three month period, and dropping to 22 percent when income is assessed over a twelve-month period. The cost of poverty alleviation programs therefore depends heavily on the choice of income reference period.

C. Possible Incidence of Income Underevaluation on Poverty Counts

2.9 In Belarus, where many new activities are developing and individuals get involved in informal, often occasional activities, assessing household or individual income for access to income support programs is bound to prove very difficult—the more so, the more widespread and diffused are informal activities.

2.10 Table A2.3 shows the possible impact of income underestimation on 1995-Q1, total resource-based poverty counts. As can be seen, differences can be significant. This suggests that authorities in Belarus must be prepared to deal with possible income underreporting by applicants to means-tested programs.

Table A2.3. Impact of Underreporting of Income on Poverty Counts (PC)

<i>Underreporting (percent)</i>	<i>PC with underreporting confined to the self-employed, sale of agricultural products and in-kind income (percent of all families)</i>	<i>PC with generalized underreporting (percent of all families)</i>
Baseline PC	35.7	35.7
10	34.8	28.0
20	33.9	22.1
30	32.9	17.7

Source: Staff estimates.

D. Statistical Sources, Methodological Considerations, and Possible Pitfalls

2.11 Various statistical sources are available to depict changes in living standards and poverty; each has its strengths and drawbacks. For instance, concepts may diverge from internationally used definitions, or may be subject to various uncertainties owing to differences in data collection and sampling methods. Moreover, the statistical reliability of the data is often dubious, given the lack of appropriate assessment of data quality. The analysis in this report is mainly based on two data sources: the *Family Budgets Survey* (FBS) for the years until 1994, and the 1995 *New Household Survey* (NHS). Information on main NHS characteristics and on the definitions used is contained in relevant official publications.¹ A comparison of NHS data with FBS and other sources is contained in the forthcoming NHS annual publication.²

2.12 One should note that the pitfalls of FSU data pitfalls have formed the subject of many analyses and are not covered here. It is also worth noting that long-term comparisons of output and incomes are especially subject to uncertainties due to unrealistic prices and measurement practices followed in the FSU. Moreover, the production decline in certain sectors (such as the military) has probably had little or no impact on living standards. Similarly, quantity-based and value-based data may fail to depict important qualitative changes, possibly hiding excess supply or low-quality goods, or goods that are no longer in production. Informal activities and the growing involvement of the population in household garden plots are particularly subject to uncertainty.

2.13 Additional problems in comparing the past and the present arise because of nonlinear and unpredictable structural changes and the great degree of instability which has accompanied socioeconomic change. These specific features of the transition imply that snapshots and use of summary descriptive measures may be misleading, or may indeed lead to distorted perceptions of change. For example, net employment figures based on measuring stocks rather than on hiring, separation, and inter- and intrasectoral moves fall short of showing changing balances between existing old and new activities. Conclusions based on net employment changes may be biased to the extent that attention is focused on the destruction of command system structures rather than on the development of new market structures. Similarly, income distribution and poverty snapshots can hide aspects of seasonal mobility and duration that are important for policy design.

1 See Ministry of Statistics and Analysis, "Income and Expenditure of the Population of the Republic of Belarus," quarterly data, Minsk 1995.

2 See, *ibid.*, "Annual Results," forthcoming 1996.

2.14 In market economies, these aspects are less important because living conditions do not change abruptly for the majority of individuals. In FSU countries, however, living conditions have been destabilized by a host of factors including Government decisions (e.g., discretionary benefit indexation). Living conditions are also affected by the ability of households to gain access to a household garden or other in-kind sources of income, or to support from relatives and friends.³ Insecurity and instability in living conditions are important considerations for balancing different degrees of hardship with benefit eligibility.

3 On this aspect, see R. Rose, *Who Needs Social Protection in Eastern Europe?* Center for the Study of Public Policy, Glasgow, 1994.

ANNEX 3 RURAL-URBAN DIFFERENTIALS

3.1 One third of the Belarussian population live in the city of Minsk and in the other five oblast capitals; one third are in small urban towns; and one third reside in rural settlements, which number about 25,000 and have, on average, 130 inhabitants. The size of the rural population remains comparatively high, reflecting the role the countryside had in Soviet times and the high degree of subsidization of agricultural activities. However, there has been a slow, continuous decline in the number of rural inhabitants since the 1970s as young people have left rural districts. In the 1950s and 1960s about 60 percent of children born in rural areas grew up and remained there. Recent figures show that only about a quarter do so now. At the same time, because of the falling birth rate, the proportion of children under 16 has declined from 31 percent to 20 percent. Consequently, the rural population and the rural labor force are aging. Since 1970, the proportion of people over 60 has risen from 17 percent to 29 percent. More than one tenth of the working population in rural areas consists of pensioners (as opposed to 5 percent in urban areas), and there are villages where the proportion of pensioners is as high as two thirds. Half of all rural households include at least one elderly person. Concurrently, the proportion of workers aged 30–44 years has dropped, as has the share of households with children. Another feature that characterizes demographic change in rural areas is the feminization of the rural population. In particular, this applies to the age group 60 years or over, and is partly explained by the higher male death rate.

A. Falling Living Standards

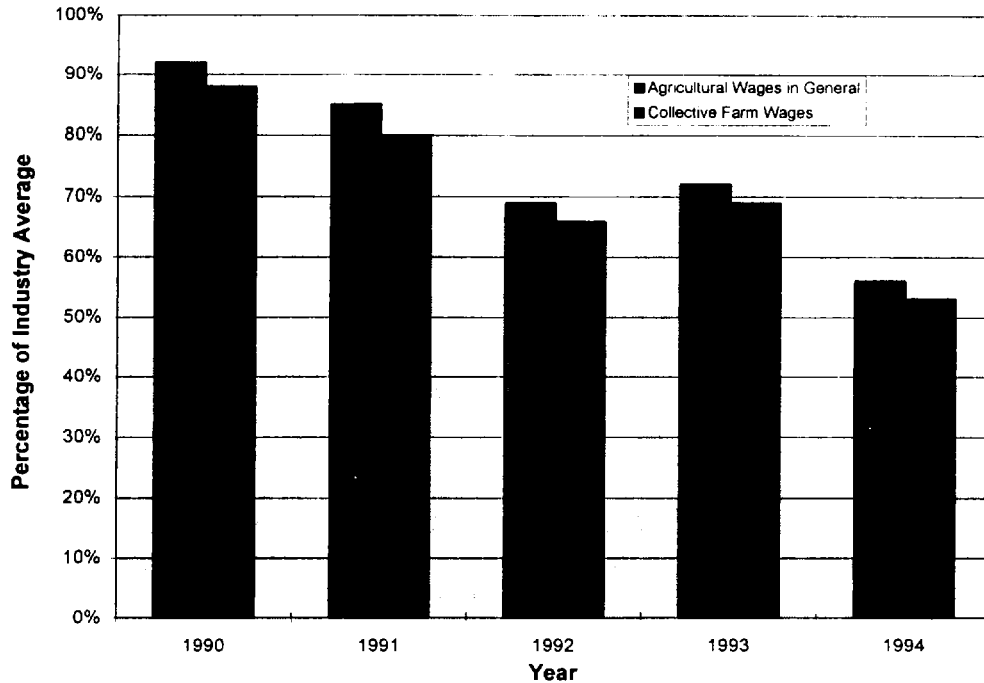
3.2 Living conditions have always been lower in rural areas, due to a lack of communal services and amenities. For instance, in rural areas, only one third of households has running water; another third gets water from its own wells, while the rest use public pumps or wells. Almost all rural households use gas, but only one third has central heating. Less than one quarter has a bath or shower, and only 15 percent have hot water. In contrast, in urban areas, about four fifths of households have central heating, hot running water, and a bath or shower. In rural areas, only about one in four households has a telephone—half the rate of urban areas. The number of households living close to public transportation, i.e., needing less than five minutes to reach a bus stop, is only 17 percent, as opposed to 36 percent in urban areas. Meanwhile, 13 percent of rural households (the same as in urban areas) need over half an hour to reach a bus stop. Many aspects of social services and general infrastructure suffer from similar disadvantages.

B. Widening Rural-Urban Wage Differentials

3.3 In spite of lower-quality social and communal services, wage differentials between agriculture and the other sectors of the economy were small until the disintegration of the USSR. They fell significantly during the 1970s, bottoming out in the second half of the next decade. In 1990, average earnings in agriculture were equal to about 98 percent of the national average and 92 percent of the average wage in industry. Starting in 1990, agricultural wages have lagged behind and fallen even more than other sectors of the economy, though the Government has continued to control production and distribution decisions. In 1994, collective farm's pay was equal to 58 percent of the national average (benefits and material aid included) and equal to 48 percent of the average industrial wage. In January–February 1995, corresponding figures were 42 percent and 31 percent, respectively. The living standard of the rural population has therefore suffered a triple blow: first, real cash income

losses; second, relative cash income losses; and third, cuts in rural “social capital.” Increased private plot activity and greater reliance on family and village ties have often compensated for these losses. However, continuing large cash income differentials would threaten economic and social life in small rural communities and towns over the long term.

Figure A3.1 Agricultural Average Wage as a Percentage of Industry Average Wage



C. Importance of Private Plots

3.4 While wages and more generally cash income have fallen, families have increasingly relied on the cultivation of private plots and the raising of animals for their personal use. Practically all rural households (97 percent) cultivate at least one such plot and raise livestock for sustenance. Almost half of rural households have an additional plot. In urban areas, about half the households have one plot, usually at a rural second home or *dacha*. City dwellers usually grow vegetables, potatoes, fruit, and berries on their plots, but they do not typically raise animals. However, increased transport costs have penalized city dwellers and may make plot production uneconomical.

3.5 Private plots represent about 15 percent of arable land in Belarus. Their importance has increased considerably in the 1990s. Currently, plot production accounts for four fifths of potatoes and three fourths of all vegetables in the republic. This is up from one half and one third, respectively, in the 1980s. Rural households own about 70 percent of pigs and poultry, and about half have a cow, while only 5 percent own sheep, goats, or rabbits. Private plots in rural areas are cultivated in symbiosis with large-scale farming. The state and collective farms provide various kinds of help, such as machinery, seeds, fertilizer, help in plowing and harvesting, and even fodder for animals. Moreover, the new land act, giving rural people a right to get one hectare of private land, has extended the scope of private plot cultivation. Collective and state farms, rather than individuals, have often take the lead in implementing this act, and it is not uncommon for private one-hectare fields to be kept in “common crop rotation.”

Under this agreement, individuals would receive one hectare's share of harvest (grain for animal fodder, for example) and not farm the land themselves. However, even in cases in which plots are separate from collective land, collective or state farms still have continued to support cultivation in many ways: lending of machines, fuel and equipment, seeds, pesticides, fertilizers, transportation, plowing, and harvesting.

3.6 Given the importance of different income sources, comparisons of rural and urban living standards must look at both cash and in-kind income. In rural areas, almost 50 percent of total resources come from private plots. For urban households, this share falls to about 7 percent.

3.7 The share of income spent on food has risen for both household types, and indeed most other household types. This increase reflects falling real incomes and indicates a clear decline in living standards for the great majority of the population. For collective farm households, it also underscores an increasing degree of dependence on private plots to satisfy food needs and escape poverty. Self-sufficiency has become a passport to survival for employees on state and collective farms, forest workers, and rural pensioners.

D. Coping Mechanisms

3.8 Along with reliance on plots, rural residents can count, as do urban households, on the socioeconomic structures associated with state and collective farms, foraging activities (berry picking, mushroom gathering, hunting, and fishing), and skills (repair, construction, handicrafts). Complex networks of personal relationships are also vital to the handling of difficult situations. These permit the exchange of information, material, and labor within rural areas, and foodstuffs and consumer goods between rural and urban areas. All the above allow families to overcome day-to-day constraints due to cash shortages.

E. Increased Incidence of Poverty

3.9 Access to plots and coping mechanisms have permitted most rural households to compensate somewhat for losses in real cash income but, as in the rest of the country, poverty in rural areas has nonetheless increased. The definition of income one uses heavily affects estimates of poverty. In terms of cash income, poverty is higher in rural than in urban areas. However, if aggregate income (or total expenditure) is the measure, as it should be, the data suggest that the incidence of poverty is lower in rural areas than in urban areas, mainly because of access to in-kind incomes. Most affected by poverty are the following:

- pensioners unable to cultivate their private plots;
- low-paid agricultural workers employed by poor collective or state farms; and
- single persons supporting several children or other dependents.

3.10 Calculations such as these are surrounded by uncertainty. First, private plot production may be underreported. Second, even when quantities produced are properly reported, their monetary value is not easy to estimate for the following reasons: (a) price differentials exist between various markets; (b) goods traded by barter do not have clear prices; and (c) the value of in-kind production changes over time with inflation. The net value to households of goods from private plots is less than their market value because of the cost of inputs, such as fertilizers and transport. In this report, the prices used are

those prevailing at the time of consumption, as recorded in the expenditure section of *the New Household Survey*.

F. The Outlook for Rural-Urban Inequalities

3.11 Developments in living standards in the years ahead hinge on the Government's progress in the area of macroeconomic stabilization, and general and sector economic reforms that foster productivity improvements in agriculture. In view of the country's past reform record, great uncertainties hover over the future of agriculture in the years ahead. Without economic growth, even present levels of support to agriculture will become increasingly difficult to maintain. Moreover, deteriorating conditions will compound difficulties, rendering reform politically and economically more difficult. The effects of a further substantial deepening of the economic crises upon the standard of living of agricultural workers are not difficult to predict. More and more families will become cash poor and have to rely on in-kind income from private farming. With deteriorating economic structures, support to agriculture from the other sectors will decline, causing important losses in state and collective farm employment. Social services will also suffer or be discontinued. More and more people will have to work for themselves and their families, worrying about self-sufficiency and basic needs. If this were to happen, agriculture would turn back in time, metamorphosing from the existing, monolithic command structure into many small, local markets where families buy or barter goods only to satisfy daily needs. So far, rural households have mostly felt the effects of real wage losses. However, other losses have begun to manifest themselves at the collective level. Cuts have affected social services, housing, transportation, and other communal services run by local authorities or enterprises. Because of developments affecting rural households' "social capital," further deterioration in relative rural living standards can be expected.

3.12 Escaping poverty in rural Belarus is sometime dependent upon access to voluntary or paid support to assist, for instance, in specific tasks related to plot cultivation. This is certainly the case of elderly pensioners. Children, meanwhile, may lose the possibility of attending kindergarten or school because of distance and lack of transport. Similarly, other groups may be unable to function unless assisted by social workers. Divestiture of social services runs two risks. First, services may simply be discontinued. Second, they may be reorganized without tailoring them to the needs of different communities. In redefining the scope and need for social services, it is important that local administrations consider new methods of provision that are flexible and adaptable to serve small and remote communities. They must, above all, permit the maintenance of basic services to rural communities according to a sliding fee schedule.

3.13 The aging of the agricultural population and the exodus of young laborers from the countryside creates a one-sided social and age structure. This may easily ignite a downward spiral that will eventually bring an end to traditional village life in certain areas. Small and isolated communities are particularly at risk, and can easily become unattractive for young people. The continuation of basic social services for rural seniors is a challenge that calls for special efforts, and for innovative ways of organizing the production and delivery of social services. In the local context, new kinds of cross-sector cooperation are needed to develop innovative approaches to service delivery, e.g., multifunctional and mobile services. Although programs to support the elderly in rural areas will require substantial fiscal resources, it will usually be less expensive—and certainly more humane—to help them complete their lives in their traditional homes rather than seeking to relocate them to urban areas where many desirable social services are more easily available.

Table A3.1: Comparison of Urban and Rural Private Agricultural Plots
(percent of total household 1994)

	<i>First Plot</i>		<i>Second Plot</i>	
	<i>Urban</i>	<i>Rural</i>	<i>Urban</i>	<i>Rural</i>
Owns private land plot	49	97		
One land plot	43	56		
Two land plots or more	6	42		
Type of the plot				
Cottage	17	81	3	36
Dacha	28	15	2	5
Other	5	1	1	1
Use of the plot				
For recreation	0.3	0	-	-
Grow food, not for sale	46	94	5	0
Grow for family and for sale	1	3	0	39
Started developing	2	0.4	0	2
Ownership of the plot				
Owned	8	2	0.3	0.8
Rented	31	74	3	36
Used temporarily	9	20	2	5
Other	2	0.3	0.4	0.1
Owns farming machinery	2	11		
Tractor	0.4	2		
Horses, inc. hired	0.3	5		
Cart or sledge	0.2	5		
Poultry, cattle or bees	14	82		
Poultry	11	71		
Cows	1	50		
Young cattle	0.2	6		
Pigs	9	70		
Sheep	0.2	5		
Goats	0.4	3		
Rabbits	1	5		
Bees	0.4	3		

Source: Ministry of Statistics and Analysis, Republic of Belarus, 1995.

Table A3.2: Comparison of Urban and Rural Housing Conditions (percent of all households, 1994)

	Urban	Rural
Type of housing		
Separate apartment	76	19
Separate house	14	74
Communal apartment	1	1
Part of a house	3	4
Dormitory	5	1
Ownership of living quarters		
Owns self	43	79
Local government	32	1
Cooperative	5	0
Enterprise	11	17
Private	3	2
Conveniences		
Central heating	88	34
Gas	89	95
Telephone	56	27
Sewerage	82	26
Bath or shower	81	23
Garage	20	17
Water supply		
Hot water	78	15
Running water	87	33
Well in the yard	5	35
Public pump	6	15
Public well	2	17
Public transport access		
Less than 5 minutes to public transportation	36	17
Over 30 minutes to public transportation	1	13

Source: Ministry of Statistics and Analysis, Republic of Belarus, 1995.

ANNEX 4 GENDER AND POVERTY

A. Gender and the Labor Market

4.1 Gender differentials affecting poverty during the transition relate to labor market and social service issues on the one hand, and to household structure on the other. Changes in the labor market and in child care availability affect men and women differently. Certain types of households, principally those headed by single mothers and those with children, are at particular risk of poverty.¹ The chief conditions affecting poverty by gender in Belarus are the following:

- wage rate differentials;
- unemployment;
- child care services; and
- household structure.

4.2 *Wage Rate Differentials.* Women's lower overall pay makes them more vulnerable to poverty than men. As inflation erodes real income, lower wages put women at a higher risk of poverty. Not only are about 70 percent of female workers concentrated in lower-paying sectors, such as health, education, and culture, but they hold lower-paying occupations within those fields. Overall, women's pay is estimated at 78 percent of men's. Being female accounts for nearly 20 percent of the difference in hourly wages.

4.3 *Unemployment.* With near universal female participation in the labor market and the weaker position of women in the labor force, unemployment has affected women more severely than men in Belarus. Women constituted over three quarters of the unemployed in the early stages of the transition. The proportion of females in the labor force has since declined, but women still account for two thirds of the unemployed. Moreover, unemployed women are less likely to receive unemployment benefits than unemployed men; women constituted only 40 percent of those receiving benefits in January 1994. The unemployed are more likely to be poor, and 70 percent of the poor and unemployed are women. Antipoverty measures to reduce unemployment will therefore need to target women specifically.

4.4 *Child Care.* For households with small children, public, cooperative, or private child care arrangements are a prerequisite for full-time economic activity. In practice, however, child care availability affects women rather than men, because of the prevailing household division of labor. Since independence, a slight decline in public child care is evident. The number of preschool centers have declined by 7 percent, while the proportion of children in the age group attending preschool has declined from 68 to 55 percent. User charges are typically low, about 9 percent of total cost (with regional variations), but are they expected to increase as a larger share of the cost is transferred to parents. Households in poverty, for example single parent households, may experience greater strain because of increased expenditures on child care.

4.5 *Household Structure.* Women's greater risk of poverty is, in large part, moderated by household income pooling at the micro level. Well over half of all households in Belarus consist of married couples, with or without children. It is not women in this group, then, but the 51 percent of all households headed by single, widowed, and divorced women, that are at a higher risk of poverty because of their weaker position

1 Elderly women living alone risk poverty as pension levels fluctuate, but are not at present more vulnerable to poverty than other groups.

in the labor market. In the 1995 NHS first quarter survey, female-headed, single-parent households, with or without another adult present in the household, were most vulnerable to poverty, as discussed below. Single-person households headed by women are also more likely to be poor than those headed by men, 36 percent versus 27 percent, respectively, but both groups are less likely to be poor than other households, in particular, households with children.

B. Single-Parent Households

4.6 Households with children that are dependent on a single, low-income earner are at particular risk of poverty. Single parents are overwhelmingly women; 83 percent of households consisting of parent and child are headed by women. Those with a grandparent also in the household constitute another 10 percent according to the 1989 census. NHS 1995 survey data estimate that 99 percent of all single-parent households are headed by women; single-parent households with another adult member, for example, a grandparent or other relative, are 91 percent female headed. The risk of poverty is high for both groups. Fifty-five percent of single-parent households live in poverty, compared with 36 percent of all households. For single-parent households with another adult present, the poverty rate is even higher—67 percent. The principal risk factors affecting the poverty of single parents are (a) limited income and (b) fewer income sources. This is only partly compensated by child allowances.

4.7 *Income Sources.* Dependence on one adult worker makes single-parent households vulnerable to poverty on three counts:

- only one paycheck;
- smaller paychecks for women; and
- limited ability to engage in informal sector activities and subsistence food production.

4.8 Poverty protection for this group will need to address their lower income levels on all three counts. Family allowances can supplement one-earner incomes and limited informal sector income. Removing wage discrimination against women and providing training to increase their earning capacity can promote equity and efficiency in the labor market. At the same time, it will reduce poverty among single-parent households and the need for social transfers to such households.

4.9 *Child Allowances.* In the second half of 1993, nearly two thirds of all children received the means-tested child allowance. Single parents not receiving child support are entitled to an additional 50 percent, for a total family allowance of 150 percent of the minimum wage. For single parents, child allowances are a significant addition to family income—16.5 percent of their overall income, compared to 8 percent for married couples with one or two children.² While still not sufficient to lift many of these female-headed households out of poverty, the child allowance acts as an important buffer against destitution. Though not well targeted, child allowances provide badly needed support to poor, single-parent households. Better targeting of benefits or universal child allowances that are taxable can make them a more effective tool for fighting poverty.

2 For single-parent households with another adult present, it makes up 16.2 percent of income.

C. Women Pensioners

4.10 Pension regulations and pension levels have important gender implications. With the loss of a substantial share of the young men in Belarus, some 50 years ago during World War II, and with a ten-year difference in the life expectancy of men and women in Belarus, 65 percent of the population age 60 and over is female. For those over 70, the proportion of women increases to 72 percent. The age and gender gap is especially evident in rural areas. Together with a retirement age of 55 for women (compared with age 60 for men), this means that the large majority of pensioners are women, many of them living alone. Over a third of retirement pensions are paid to single-person households headed by women. The economic crisis, societal breakdown, and rapidly deteriorating health conditions now confront elderly women with a new set of challenges.

4.11 *Pensions and Poverty.* Pensioners as a group are less likely to be in poverty than other households. Indeed, the *poverty rate for those above age 55 is lower than for any other age group.* Pensions, being much larger than child allowances and generally being shared within smaller households, contribute about half the household income of recipient households. Pensioner households that lack land or labor to work in the formal or informal sector or in home production must depend largely on their pension income. With inflation and periodic increases in pension levels, they will move in and out of poverty. As of March 1995, the majority of single female pensioners (68 percent) are not poor, and most (86 percent) do not work in the formal sector. Nevertheless, work can be a buffer against poverty—working pensioners are less likely to be poor than non-workers.³

4.12 *Access to Land and Labor.* Access to land also protects this group of households against poverty; three quarters of female pensioners who have access to land are not poor, but only half of those without land are able to stay out of poverty. Those who are poor are twice as likely to be landless as the non-poor—37 percent versus 15 percent, respectively. However, the limited physical mobility of the elderly may reduce their ability to produce food. Indeed, age makes a difference to poverty in urban areas, where 48 percent of households with single females age 70 and above live in poverty, while in rural areas only 23 percent do.

3 A quarter of working pensioners are poor; among those who do not work, poverty affects a third.

ANNEX 5
DETERMINANTS OF EARNINGS AND LOW PAY

Earnings

5.1 While no time series analysis of the determinants of wages is possible, data from the NHS permit estimation of a standard type of wage function.¹ The estimates (see Table A5.1) show the following:

- Education and experience play key roles; undergraduate and graduate education particularly boost earning capacity.
- Wages vary by type of employer, with a negative effect of being employed in the state sectors, suggesting that the labor market may have started to differentiate between less and more productive work.
- Urban workers receive significantly higher wages than rural workers.
- Gender differences are important, which differentiates Belarus from other FSU countries for which similar analyses are available. Regression coefficients separately estimated for females and males show that residence in rural areas and employment in agriculture negatively affect men's pay more than women's (see Table A5.1, part b). However, females generally fare worse in the labor market than men, irrespective of enterprise type. Moreover, their working life earning profile is flatter and, thus, less responsive to experience than males'. This confirms an often-heard complaint about discriminating career patterns. Education appears to provide higher returns to women and to open opportunities for more rewarding work experience that otherwise would not exist.

Table A5.1: Determinants of Earnings in Belarus, 1995*

<i>a. Key factors</i>	<i>Coefficient</i>	<i>t-stat.</i>
Gender ^a	-.19	-255
Residence ^a	-.22	-209
No. of years of work ^b	.03	224
Squared no. of years worked ^b	-0.0	-211
Education		
Specialized secondary ^a	.13	160
Undergraduate	.54	502
Postgraduate	.58	108
Type of enterprise		
Budgetary ^a	-.02	-27
State farm	-.43	-221
Collective farm	-.56	-361
Joint stock co.	.15	76
Private individual	.22	65
Other	.06	28
Constant	7.87	3694
<hr/>		
<i>b. Regression results: earnings</i>	<i>Male</i>	<i>Female</i>
Residence	-.27	-.17
No. of years of work	.03	.02
Squared no. of years of work	-.00	-.00
Education		
Specialized secondary	.12	.16
Undergraduate	.43	.65
Postgraduate	.41	.72
Type of enterprise		
Budgetary	.09	-.08
State farm	-.48	-.32
Collective farm	-.63	-.38
Joint stock co.	.16	.14
Private individual	.27	.15
Other	.07	.03
Constant	7.75	7.42

a. Dummy variables = 1 if gender is male, residence is rural, and education and enterprise are stated types.

b. First and second derivatives for natural log of wage (w).

Note: Multiple regression = .460, Standard Error = .714, F= 77,941.1.

Source: Staff estimates based on NHS data.

¹ The Mincer type equations in Table A5.1 are estimated by regressing the log of hourly wages (*w*) on the number of years worked (a proxy for experience) and its square value, and dummies for gender, residence, type of education, and type of employer (see J. Mincer, *Schooling, Experience and Earnings*, Columbia University Press, New York, 1974). Dummy coefficients multiplied by 100 give expected percentage differences in *w*. The years worked coefficient (first derivative) gives the expected increase in *w* for each additional year of work. The squared years worked coefficient (second derivative) is negative, which confirms the hypothesis of decreasing returns to experience. Results are in line with Orazem and Vodopivec for Slovenia (see *Winners and Losers in Transition: Returns to Education, Experience and Gender in Slovenia*, mimeo, Washington, D.C., May 1994) and Milanovic for Poland (*Poverty in Poland*, World Bank, Washington, D.C., 1994), though coefficient differ.

Low Pay

5.2 Factors relating to low pay (defined as being less than or equal to half the median) are basic or lower education, location, and gender. This is suggested by Table A5.2, which estimates how certain characteristics affect the odds of low pay for a hypothetical low-paid worker.

Table A5.2: Characteristics Determining Low Pay

<i>Increased odds of low pay if:</i>	<i>Percent Increase</i>
Living in	
Brest oblast	3.0
Rural area	5.8
Female	4.3
Age (for each additional year)	0.4
Working in a	
State farm	15.1
Collective farm	23.4
<hr/>	
<i>Decreased odds of low pay if:</i>	<i>Percent Decrease</i>
Living in	
Urban area	4.1
Gomel oblast	2.3
Grodno oblast	5.0
Mogilev oblast	0.5
Vitebsk oblast	0.7
Work experience (for each additional year)	0.4
Attained	
Specialized secondary education	4.7
Undergraduate Education	17.3
Postgraduate Education	13.2
Working in	
Budgetary organization	3.3
Joint stock company	1.5
Private individual	1.4

Note: Hypothetical household: A single male with basic secondary education who works at a state enterprise and lives in Minsk oblast. Probability of low pay is 13%.

Source: Staff estimates based on NHS data. Only significant coefficients are shown.

ANNEX 6
PROBLEMS WITH THE EXISTING SOCIAL PROTECTION SYSTEM

A. Main Problems

6.1 The key problems with the current social protection system in Belarus can be summarized as follows:

- Benefits impose an excessive fiscal burden—public income support benefits are a high percentage of median income, relative to most other countries with income levels comparable to that of Belarus.
- The fiscal burden of benefits is high partly because of the low normal age of retirement—55 years for women and 60 years for men.
- Employees directly contribute only 1 percent of the financial support for the system.
- Financing is concentrated on a single instrument—the payroll tax—creating a major disincentive for hiring workers for any firm attempting to maximize profits.
- Virtually no actuarial considerations underlie the pension benefit structure, and the pension programs contain many features that undermine the social insurance basis of the programs.
- The system is very categorical in nature, and its administration is excessively bureaucratized and “state-centric.”
- Benefits in the primary programs are generally fixed sum or proportional to earnings; there is little attempt to condition benefits on income.
- There are no comprehensive programs to assist poor families and children. Only elderly persons without a pension and single-parent families obtain some form of income support.
- The entire system contains numerous horizontal inequities; for example, per capita benefits to the elderly are about twice those to children; per capita benefits vary substantially by size of family with small families favored.
- The lowest-income population receives a disproportionately small share of total benefits. (A primary cause for this is the substantial share of social benefits that are targeted on the elderly or the disabled, rather than on the poor.)
- Cumulative tax rates in the system (including the implicit tax of benefits that decline with rising income levels) can total more than 100 percent, creating a poverty trap.
- The benefit structure and the administration of the programs are not integrated.

B. Negative Economic Effects of Social Programs

6.2 The economic effects of the current set of policies in force in Belarus are distinctly negative in terms of employment and productivity. While providing income support to individuals and families not working, and above-productivity wages to some who are working, the net effect of the system is the following:

- To reduce the demand for labor (especially low-wage, low-skill labor), encourage the substitution of temporary employees for permanent workers and of capital equipment for labor, and encourage private sector activities to flourish outside the formal reported economy. These latter effects reduce the level of job training offered by (especially) the new private firms as part of the employment relationship, and limit the benefits from establishing long-term, employer-employee relationships in the newly formed private enterprises.

- To reduce the willingness to work and the incentive to seek jobs for those who are recipients of income support benefits such as unemployment and disability payments.
- To increase the costs of enterprises that are required to pay taxes to cover the costs of the benefits or higher-than-market wages; for an open economy such as that of Belarus, these costs reduce the foreign markets for the goods and services produced.
- To create rigidities in the labor market, keeping wage rates from equilibrating and labor demand from expanding to its true potential.
- To erode the incentive for diligence and efforts for current job holders, as the possibility of job loss is reduced by employment regulations, and the alternative available income support from public transfer programs is generous.

6.2 These negative economic effects reduce the rate of productivity improvements, inhibit employment, increase the unemployment of low-wage, low-experience, and low-skill workers, reduce the rate of economic growth, and create a low-income trap for many individuals and families who receive income support benefits. Proposals to reform social welfare policies so as to reduce poverty while stimulating employment and economic growth must be evaluated in this context.

ANNEX 7
CHECKLIST FOR THE DEVELOPMENT OF A MEANS-TESTED PROGRAM

7.1 Developing a means-tested benefit program requires policy identification, statistical analysis, and design of the necessary administrative procedures.

Initial Questions: In advance of defining the precise provisions of a benefit, some broad questions need to be addressed:

- Is the benefit to be comprehensive?
- In what circumstances will help be given?
- How is a means-tested benefit to relate to other benefits, housing subsidies, and privileges already in place?
- Should the means-tested benefit replace other forms of assistance in whole or in part?
- Will it cover different needs in different ways (cash or in-kind assistance)?
- How much can be afforded?
- How will the level at which benefits are paid be determined?
- How can benefits be tapered with rising income levels to prevent high marginal tax rates?
- Will benefits be available to all, or limited to nationals, or even to those who have paid taxes on income (as distinct from contributions for social insurance)?
- What information about means is available to support benefit calculation?
- What systems will be needed to prevent and control fraud?
- What conditions will be placed upon applicants?
- Will recipients be required to conform to certain patterns of behavior as a condition of continuing entitlement?
- How will other disincentives be minimized?
- Will a computerized system be used?
- Who will be responsible for developing the policy, writing procedures, and administering the benefits?

Project Planning: It is important, when developing a new policy, to ensure that all issues under discussion are considered properly by people best placed to give advice. No policy decisions should be made without ensuring that, at least, the following groups are consulted:

- other governmental units, who may be in some way affected by the benefit;
- finance experts, to assess monetary consequences;
- lawyers, to advise on legal problems;
- statisticians, to provide information about the numbers affected;
- computer programmers, to assess whether the change will be practicable;
- those who will implement the benefit, to consider whether it will be possible to deliver it and how much it will cost;
- fraud and security experts, to ensure that the benefit is secure against fraud, whether by staff or claimants; and
- training experts, to develop programs to educate staff.

7.2 Other groups might also need to be consulted. These might include, for example, representative groups, such as non-governmental organizations (NGOs), who will be able to comment on the impact of the benefit. All interested parties should be involved from the beginning and should be kept informed

of developments. They may not need to be involved at all stages, but the decision as to whether they need to be involved should be theirs.

Specific Issues: When developing a means test, some specific issues will need to be decided. These are policy decisions, but they will involve many other people and affect the way in which a benefit will be delivered. The key issues are the following:

- establishing the identity of the applicant;
- establishing the income (including benefits, savings and in-kind income) of the household in which the applicant lives;
- conditions of entitlement, such as proof of actively seeking work;
- medical evidence of incapacity for work;
- the checks to be performed at each stage;
- how payment will be made;
- periodicity of payment;
- security of the systems from fraud;
- penalties for misrepresentation;
- frequency of review; and
- internal checks on the quality of decisions, accuracy of payments, and the security of procedures against both internal and external fraud.

Post-implementation: After developing and implementing a new benefit, there should be a policy review at an early stage to assess whether the benefit is achieving its intended purpose. This review should examine evidence such as the following:

- the extent to which poverty is alleviated among the intended target population;
- whether benefit is being paid to those for whom it was not intended;
- whether the cost of the benefit is as predicted;
- the impact of the benefit upon people's behavior;
- the procedures, particularly with regard to effectiveness, security, and quality;
- the public perception of the benefit; and
- alternative proposals for targeting the benefit more effectively to tackle any other weaknesses revealed.

Overall Consideration: A means-tested social assistance benefit of last resort will involve a substantial investment in development and in administration if it is to be cost-effective.

ANNEX 8
CONDITIONS FOR GOOD SOCIAL POLICY:
EFFECTIVE MONITORING OF POVERTY AND SOCIAL WELFARE

8.1 An important element of the overall strategy of economic growth with equity should be the systematic effort by the government to monitor the evolution of poverty and the effectiveness of social policies in alleviating it. There should be three major components to this effort:

- The collection and use of survey data to produce and periodically update a basic *profile of poverty* in Belarus that includes social, demographic, and geographic dimensions.
- The ability to assess the *effectiveness of existing social programs* in alleviating poverty and, in particular, the degree to which they target the poor.
- The capability to simulate the *distributional impacts of proposed changes* to existing social programs and, in particular, their effect on the economic welfare of the poor.

8.2 Different levels of resources and types of technical expertise will be needed to implement these three components. The production and update of a poverty profile requires the ability to collect quality data through a household survey. Relatively limited analytical expertise is needed, and such expertise is already available in Belarus or can be mobilized fairly easily. On the other hand, analysis of the effectiveness of antipoverty programs requires more sophisticated techniques, which are currently unavailable in Belarus and need to be developed.

Producing and Updating a Basic Profile of Poverty

8.3 The major goal of a poverty profile is to illustrate how the incidence, depth, and severity of poverty varies across demographic groups and across different geographic areas. The most immediate use of a poverty profile should be to help policymakers identify areas and groups requiring immediate attention. A poverty profile is also a useful way to inform and orient public opinion—the public at large often has a distorted idea of the incidence of poverty and tends to cling to traditional views of economic and social vulnerability that do not take into account changing realities.

8.4 This section focuses on the data and analytical requirements necessary for sustaining in the future the kind of poverty profile presented in this report. The essential requirement is a household survey that provides information on the economic conditions of a representative sample of the population. The Government of Belarus has made substantial progress towards this goal by successfully implementing the *New Household Survey* (NHS). (See Box A8.1 for some facts about this survey.)

8.5 The progress in the design and implementation of the new Income and Expenditure Survey, however, should not conceal the many challenges to the Government of Belarus in developing, updating, and effectively using a poverty profile. On the data collection side, there are still several weaknesses. The ability of the survey to adequately represent the most vulnerable groups in society is still limited, either because of gaps in coverage or selective non-response. For example, the survey probably does not collect adequate data from the frail elderly due to the high burden imposed on respondents. Income is probably underreported in the survey, particularly income from informal entrepreneurial activities and from subsistence agriculture. The same applies to transfers of resources among households, which can have important equalizing effects on the distribution of income. If the poverty profile is to go beyond measuring material poverty, the survey instrument should be expanded to include other measures of well-being, such

as access to public services—particularly health services, quality of housing, fear of crime, and other psychological dimensions of well-being such as the perceived degree of economic security.

8.6 Other challenges lie on the data utilization side. Local capacity already exists within the Ministry of Statistics to collect the data and to provide first-cut descriptive analyses. However, other resources must be mobilized to evaluate the adequacy of the data for a poverty profile and to develop the profile itself. For these activities, other ministries and local universities can offer valuable expertise.

Box A8.1: Some Facts from the Belarussian *New Household Survey*

Households in the new survey were selected using probability sampling. The probability of selection of each household is known, and can be converted into sampling weights to obtain estimates valid for the entire population. The survey was designed to collect both expenditure and income information, including in-kind income, for an entire calendar year, using four successive quarterly interviews conducted of the same households. Data on food expenditures were recorded in diaries by the households for periods of two weeks at a time, once every quarter. In addition, a baseline interview collected detailed information on age, education, employment and health status of each household member, housing ownership and conditions, availability of land plots and cattle, and possession of household durable goods.

The design adopted for the NHS has many advantages for the development of an informative poverty profile. The availability of both income and expenditure information allows the implementation of alternative definitions of resources to determine poverty status. The panel nature of the survey allows an analysis of within-year changes in economic well-being and of the extent of movement into and out of poverty. It thus permits discrimination between short-term and long-term poverty. Data on assets can also be used as proxy of permanent income to distinguish between short- and long-term poverty. The data on free and purchased food, although not as appropriate as those collected by food use or food intake surveys, enables the development of measures of food security and food adequacy.

Monitoring the Effectiveness of Existing Social Programs

8.7 The effectiveness of existing antipoverty programs should be evaluated periodically and should become an integral part of an overall poverty monitoring system. This evaluation should involve a distributional incidence analysis of social expenditures that is able to answer the following types of questions: Which groups are receiving what benefits? By what percentage is the poverty gap reduced by each type of social program? To what extent is pre-transfer inequality reduced? How much leakage occurs in these programs? What is the take-up rate among the eligible population?

8.8 An informative and robust analysis of distributional incidence requires a higher level of analytical expertise than that needed by the poverty profile, and requires better data. For example, the quality of the income data becomes critical to conduct incidence analysis, whereas it might not be if expenditures are used as a measure of resources in counting the poor. Additional data sources, such as administrative data on program recipients, might be needed to integrate the information from the household survey, and to correct possible biases in the survey data due to underreporting of program participation or to higher non-response rates among program recipients.

8.9 Moreover, this type of analysis is likely to generate results that are more controversial and more politically sensitive than a simple poverty profile. For this reason and for the higher level of expertise required, the involvement of international organizations in these activities would be of crucial importance, at least the first time this analysis is conducted.

Simulation of the Distributional Impacts of Proposed Reforms

8.10 The third component of a system of poverty monitoring should be the development of a simulation capability to help policymakers in choosing between alternative policy packages. This would show the impact of proposed changes in social programs and tax legislation on the distribution of disposable income across different social groups. Although impacts can be calculated for the entire population, the issue that is of the greatest policy interest for most reforms is their impact on groups considered vulnerable or in need. This simulation capability can also be used to project the budget costs of changes in social sector legislation.

8.11 In its most advanced form, this type of analysis requires the development of formal tax-benefit models of the type widely used in Western countries. However, a simulation capability can also be implemented at a much lower level of sophistication by adding simple ad hoc simulation routines to the database generated from the household survey, and by using the same type of statistical software needed for the poverty profile and the incidence analysis. The real hurdles to developing this type of simulation capability are not the unavailability of data or software, but the lack of the necessary expertise and even of the awareness of simulation's potential uses for policy analysis. Building an appreciation among government officials for this type of policy tool is important. Once accomplished, the simulation capability should be permanently established, inside or outside the Government, so that it can be drawn upon every time a change in social legislation is contemplated.

BIBLIOGRAPHY

- Cox, M. and Alm, R. "By Our Own Bootstraps," *Federal Reserve of Dallas*, 1996
- Haveman, R. and Wolfe, B. "Towards a Social Policy Reform Strategy for Belarus: A Primer of Alternative Strategies to Reduce Poverty and Maintain Employment," mimeo, Washington, 1994.
- Johnson, P. and Webb, S. "UK Poverty Statistics: A Comparative Study," Institute for Fiscal Study, London, 1991.
- Kakwani, N. "Minimum Consumption Baskets and Poverty in Belarus," mimeo, World Bank, Washington, 1995.
- Mincer, J. "Schooling Experience and Earnings," University Press, Columbia, 1974.
- Ministry of Statistics and Analysis of the Republic of Belarus, Expenditures and Incomes of the population in the Republic of Belarus, Minsk, 1996. "Statistical Bulletin," Minsk, monthly publication, "National Accounts," Minsk, 1995.
- Roberti, P. et al., "Some Methodological Considerations on the Measurement of Poverty in Italy," *Rivista di Politica Economica*, May 1989, pp. 129-150.
- Rose, R. "Who Needs Social Protection in Eastern Europe," Center for the Study of Public Policy, Giasgov, 1994.
- UNDP, "Belarus Turning to People," National Human Development Report, Minsk, 1995.
- UNICEF, "Children and Women in Belarus," Minsk, 1995.
- World Bank, "Poverty," 1990 World Development Report, Washington, 1990.
- World Bank, "Investing in Health," 1993 World Development Report, Washington 1993.
- World Bank, "Fiscal Policy Study," mimeo, Washington, 1995.
- World Bank, "Belarus Agriculture and Food Review," Washington, 1994.
- World Bank, "Poverty in Poland," Washington, 1994.
- World Health Organization, "Women's Health Profile: Belarus Country Report," Vienna, 1994.
- Zaprudnik, J. "Belarus at a Crossroad in History," Westview, Boulder, 1993.

IMAGING

Report No: 15380 BY
Type: SR