



Safety Nets in Transition Economies

Economic Performance and Poverty

Transition economies are commonly understood to be countries that have moved or are moving from a primarily state-planned to a market-based economic system with private ownership of assets and market-supporting institutions. These countries include those of the former Soviet Union, those of Eastern and Central Europe closely allied with the Soviet Union and those in Asia and Africa recently undergoing market transformations of various degrees, such as China, Mongolia and Vietnam.

While transition countries in the former Soviet Union differ from others in Asia and Africa and from one another in many respects—i.e., culture, economic structure, extent of the informal sector, and pre-transition starting points—they were similarly affected by the dismantling of the state-owned enterprise systems. These changes were exacerbated by the collapse of historic trading relationships and fiscal shocks to state budgets.

The combined effects of these shocks have been dramatic. Poverty and unemployment increased, wages dropped, and newly created private firms struggled to become competitive. By 1998, 5.1 per cent of the population lived on less than \$1 a day (compared to 1.5 per cent in 1990), with substantially higher rates and increased inequality in the lower-income and conflict-ridden countries.

The resulting vulnerable groups were not always able to rely on heavily state-subsidized support services. Increasing urbanization further stressed and weakened family and community-based coping mechanisms, particularly in Asia. In Africa, conflict and severe deteriorations in the terms-of-trade have complicated transitions in very-low-income countries.

The Role and Effectiveness of Safety Net Programs

Three basic policy responses emerged to fight poverty and reduce vulnerability.

Middle-income, faster-reforming countries with high spending and the lowest poverty rates in the region. In these countries, social spending—mostly cash transfers (child benefits and public pension program)—accounted for about 15-20 per cent of GDP and represented an important source of income for the vast majority of households. In contrast, the means-tested social assistance system, introduced in the early years of the transition, remained a very small fraction of total social expenditures.

Few countries made use of scholarships or fee waivers, relying instead on broad-coverage health insurance programs and universal free primary and secondary education. The subsidized provision of privately consumed goods was limited.

The resources allocated to pensions helped to maintain social cohesion—a necessary condition for the reforms which brought growth—but at the same time discouraged labor supply, lowering employment and economic growth and raising dependency ratios.

The spending on health and education guaranteed access to social services, and lowered the risk of high medical payments causing poverty. Most of the spending was progressive but untargeted and therefore had high leakages.

There is no doubt that the package of high social insurance spending combined with child allowances and small social assistance programs prevented poverty.

Middle-income, slower-reforming countries, with poverty rates significantly higher than in the first group. These countries allocated a similar ten per cent of GDP on health and education, but relatively more than the middle-income, faster-growing countries did on subsidies to households for private goods—housing, utilities, etc. They also maintained a broad range of non-targeted benefits for categorical groups (i.e., war veterans) costing three to five per cent of the GDP. These countries

did not spend very much on child allowances, only ten per cent of GDP on pensions, and little if anything on means-tested programs.

These complex systems favored those in the urban, state-owned sectors, leaving the rural poor behind. Many of the benefits were not progressive. They were nationally mandated but locally financed and administered, and poor areas were not able to support them.

Spending patterns in these countries can be faulted both for the overall social-protection-expenditure mix—too much spending on insurance programs that did not benefit the poor and encouraged withdrawal from the labor force—and for poor targeting. While targeting was considered administratively feasible, with the exception of child allowances it has been politically unpopular.

Low-income, slow-reforming countries, with high poverty rates. In these countries with greater needs and less means, social expenditures were the lowest (in relative and absolute terms). Because of the collapse of the fiscal systems, spending for education and health was at most three per cent of GDP.

Many of these countries also maintained, on paper, the same range of social assistance benefits and privileges as their higher-income neighbors from the former Soviet Union but few of the legal obligations were honored, given the low funding. The long administration time for very small benefits limited participation. Utility subsidies (in the form of tariff reductions or arrears forgiveness), when provided, were concentrated on and favored urban households in the capital cities.

Poor households were not protected against the high cost of health care expenditures and the higher probability of falling into poverty. Selling assets, labor migration, and relying on informal safety net transfers from family, clan and community members became the dominant coping mechanisms for the poor.

Successful targeting systems to allocate foreign aid have been used only in a few countries (Armenia, Kosovo and Albania).

Lessons and Recommendations

Several lessons can be learned from the experiences of transition economies. First, in slower-growing, middle-income countries, where most of the poor are not marginalized or excluded, and most earners in the household have skills and are capable of work, poverty is often transient. In these situations public resources should be redirected to investments that support growth and away from expensive and complex 'compensation' or 'privilege' systems.

Second, it may be better to develop strategies based on existing institutions and laws, even if these are second or third best. Institutions imported from other cultures need to be adapted, and this takes time. Meanwhile, governments should consider trying to move resources out of social insurance programs into overall social service delivery and investment programs.

Lastly, when social programs in middle- and low-income countries are deemed necessary, reforms may be needed to reduce wasteful or untargeted programs. This can be achieved by doing the following:

- Tighten eligibility, make wider use of targeted subsidies for social services and school feeding programs, and eliminate those subsidies that cannot be targeted properly.
- Rely more on means testing methods to achieve better targeting, taking into account that this is more difficult to achieve in lower income countries with weak administrative capacities.
- Ensure adequate financing for safety net programs. Local financing favors richer areas: national financing leads to better results.
- Monitor program outcomes and evaluate the impacts on families (and especially children at risk) of program modifications and new approaches.

Several countries in the central and eastern European and central Asian regions improved the coverage and targeting of their programs and, by providing adequate financing, have shown that it is possible to alleviate poverty at a relatively low cost.

The World Bank Social Safety Nets Primer series is intended to provide a practical resource for those engaged in the design and implementation of safety net programs around the world. Readers will find information on good practices for a variety of types of interventions, country contexts, themes and target groups, as well as current thinking on the role of social safety nets in the broader development agenda.



World Bank, Human Development Network
Social Protection, Social Safety Nets
<http://www.worldbank.org/safetynets>

WORLD BANK INSTITUTE
Promoting knowledge and learning for a better world



Printed on 100% post-consumer recycled paper