

# **Social reform in socialist economies**

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# Social reform in transition countries

- What reforms “paths” have state-socialist economies taken?
- What is the relationship between social-policy reform and other reform components in centrally-planned economies (esp., enterprise reform and labor-market changes)?
- What were the social consequences of the transition?
- What are the implications for Cuba?

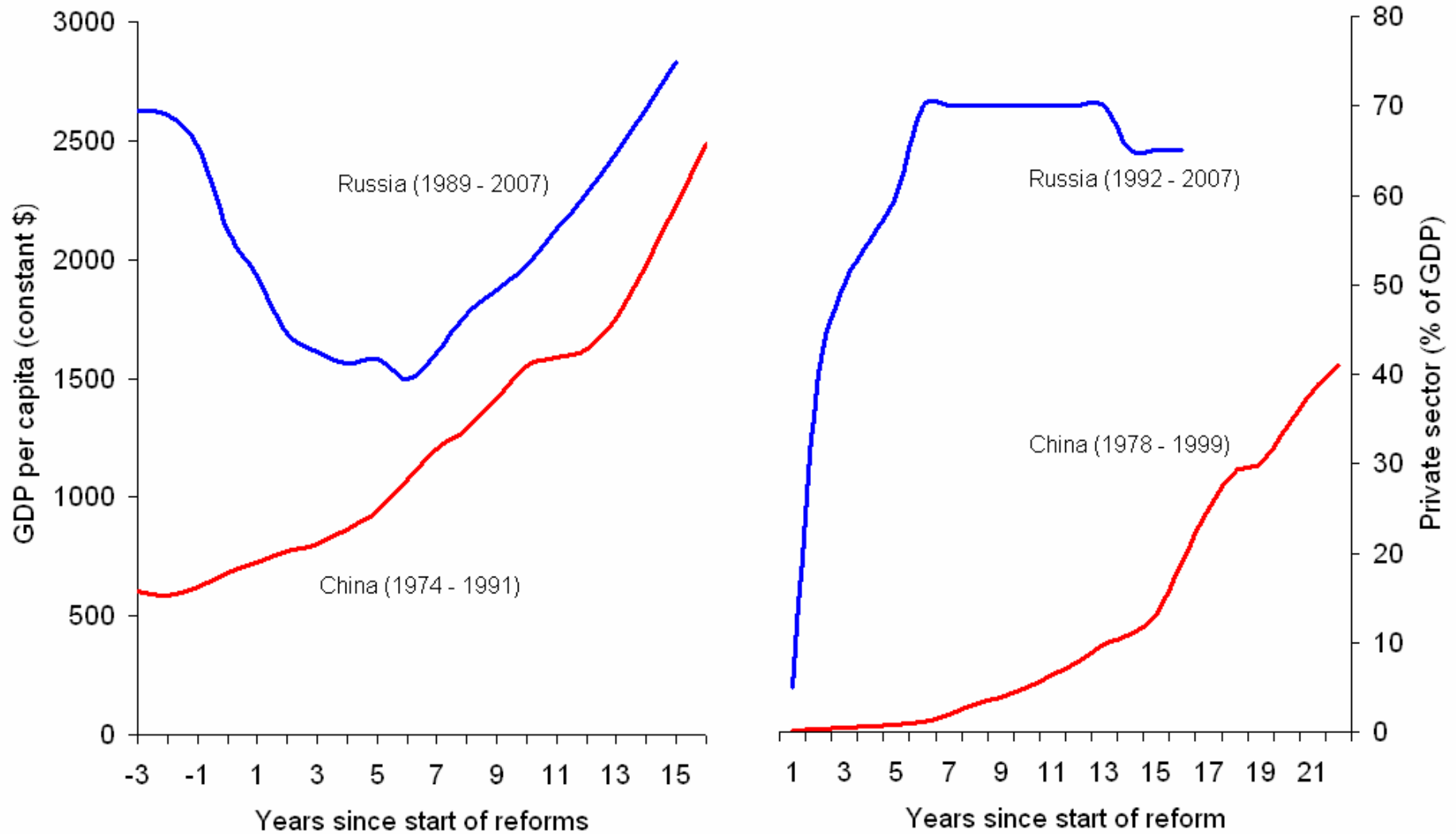
# The conventional wisdom

- Reform differences in centrally-planned economies defined mainly by speed of
  - Liberalization (prices, trade, currency convertibility)
  - Structural reform (state enterprises, financial sector, labor markets)
- **EE/CIS** → adopted the “big bang”
- **China** → designed an “institutions-first” approach

*Standing in marked contrast with [Russian] failures has been the enormous success of China, which created its own path of transition. . . It succeeded not only in growing rapidly, but in creating a vibrant, non-State-owned collective enterprise sector.*

– J. Stiglitz (1999)

# Russia and China

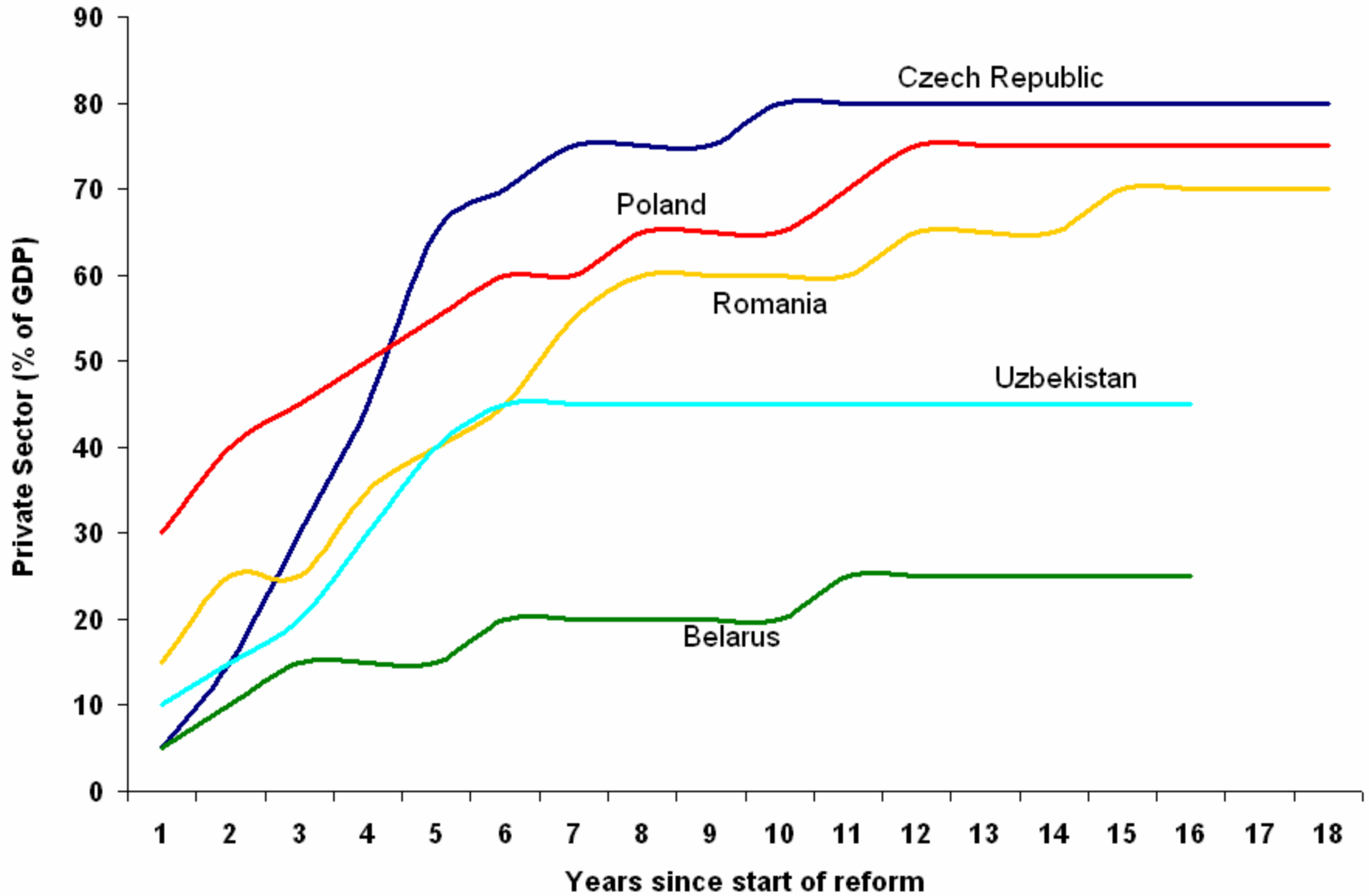


Source: EBRD, China Statistical Yearbook

# Reality was more complex

- **In EE/CIS**
  - Sharp debates between advocates of “big bang” and gradualism
  - Many compromises, even for the staunchest “big-bangers” (Balcerowicz, Klaus, Gaidar)
  - Many countries experimented with gradualism only to see their economy deteriorate (Bulgaria, Ukraine, Slovakia, even the USSR under Gorbachev); 15 years on, the “gradual” reformers have fared the worse (Belarus, Uzbekistan, Turkmenistan)
  - All were “gradual” in some areas (legal, labor markets, social insurance)
- **In China**
  - Post-Mao era saw clashes between reformers and hard-liners
  - Eventual reform path—lifting restrictions on investment, management reforms to public enterprises (without ownership change), etc.—was a result of protracted conflicts between 1976 and 1980
- **To what extent can reformers in socialist countries freely choose their reform path? (not much . . . )**

# Private sector growth



Source: EBRD

# State-socialist “social policy”

- “Social assets” in the hands of enterprises
  - Housing, utilities, health clinics, childcare facilities, schools, vacation resorts, etc.
  - Tied firmly to state-sector employment
- Mid to high levels of non-wage benefits
  - E.g., pensions ~55-60% of state-sector wages in EE; ~40% in the USSR
- In China→ “iron rice bowl”
  - pensions, healthcare, education established for urban employees of SOEs (*danwei* or “work units”)
  - rural population covered by cooperative schemes
- Low inequality (in EE/CIS, average Gini = 22 in 1990; in China, rural Gini = 17, urban Gini = 24 in 1980)

# Two routes in the East Bloc

## East & Central Europe

- Higher non-wage benefits (an implicit “wage floor”) meant that firms were forced to shed labor
- Movement to service sector from industry for skilled workers; more unemployment among unskilled
- Higher unemployment, higher wages

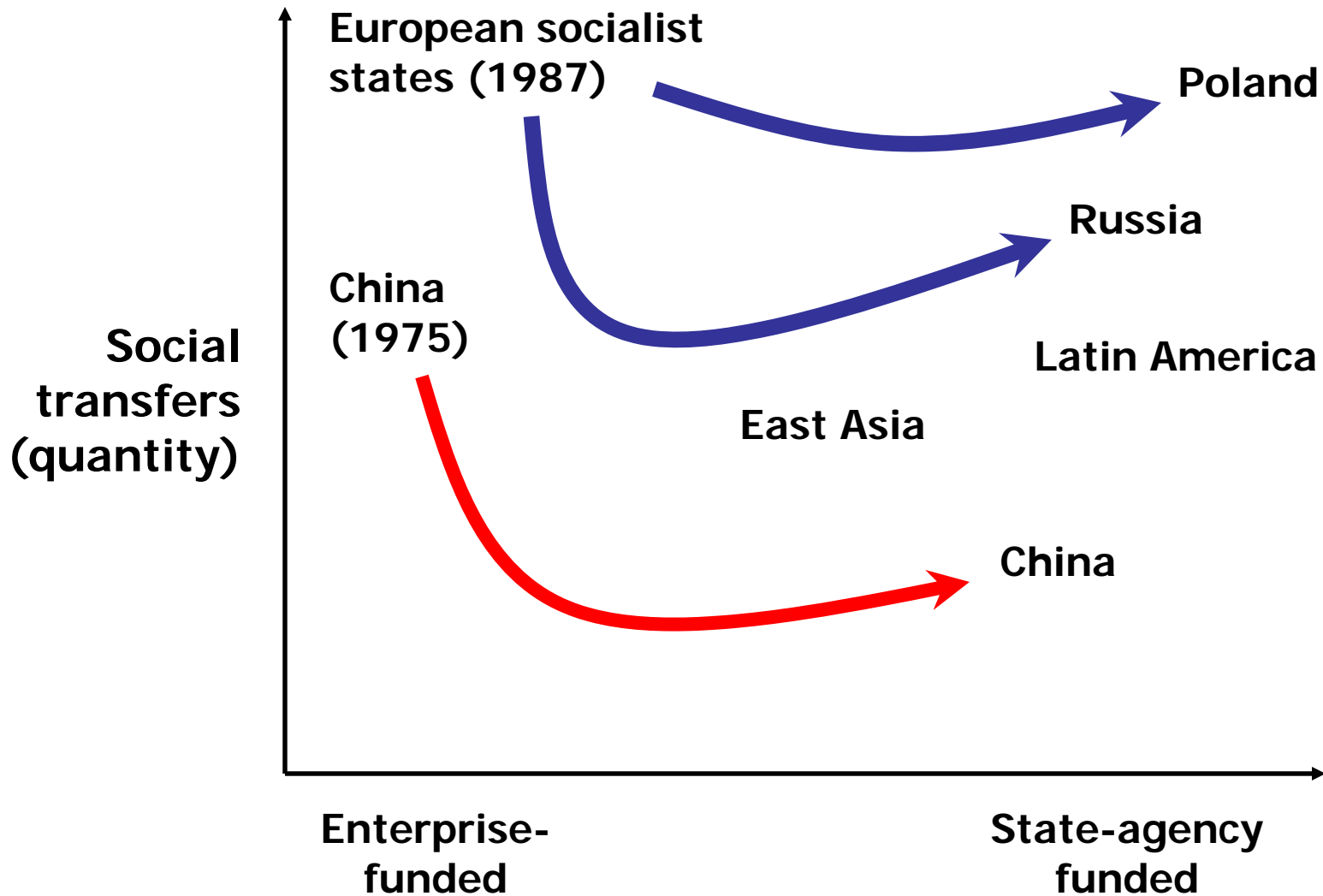
## Former USSR (CIS)

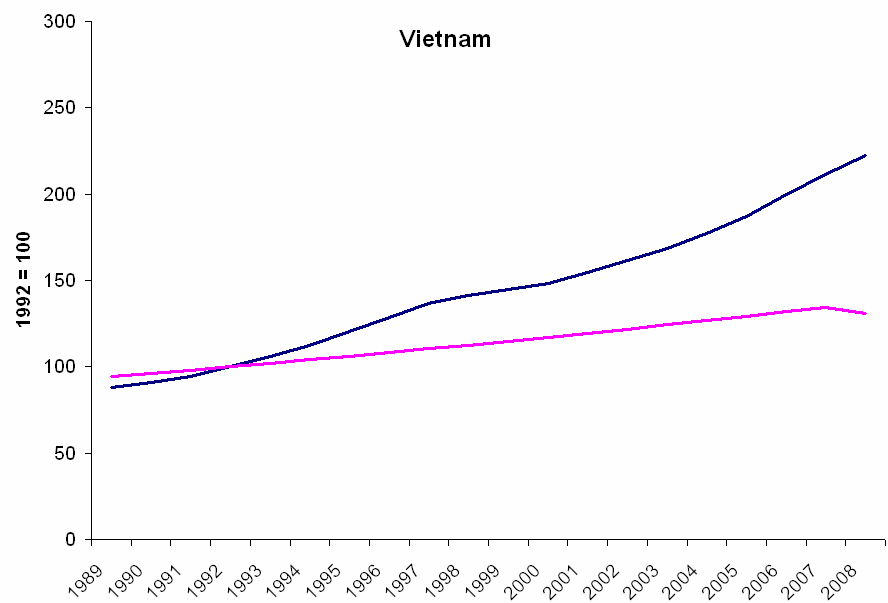
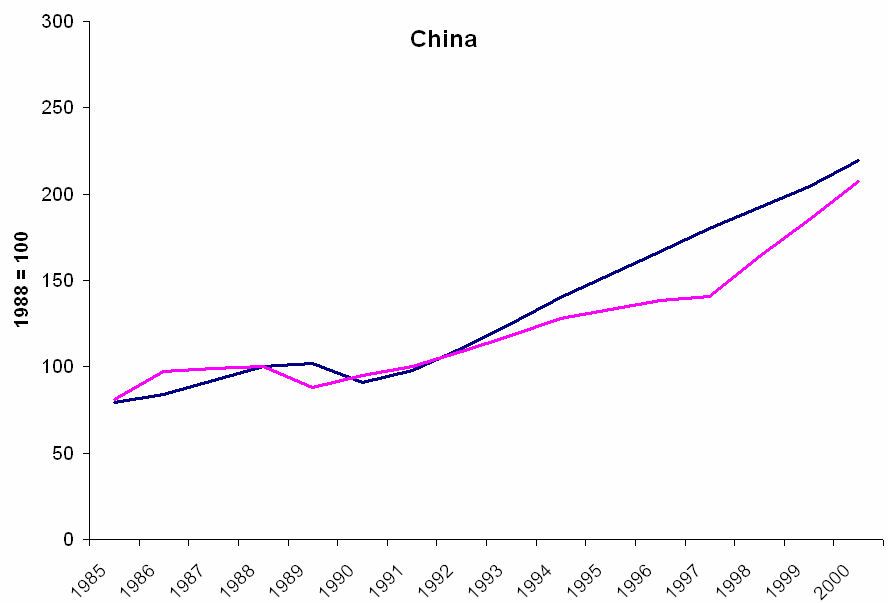
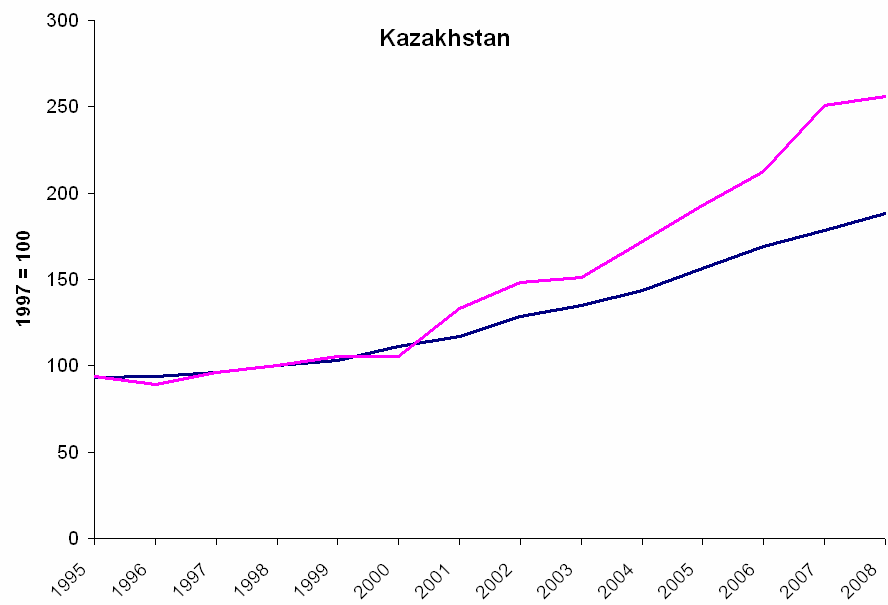
- Lower amount of non-wage benefits
- Some countries adjusted in wages downward
- Others stopped paying portions of wages (widespread arrears problem)
- Larger groups of “working poor”
- Lower unemployment, lower wages

# China's path

- **Erosion of benefits tied to farms after 1978; expansion of urban non-enterprise-based safety nets**
  - “Household responsibility” system (allowing farmers to leave collectives, fiscal decentralization)
  - Spread of town-village enterprises (TVEs)
- **Labor reallocation**
  - from collective farms to TVEs and to a growing urban private sector
  - In cities social protection disconnected from “work units”
- **Social policy changes**
  - Collapse of rural cooperative healthcare, since households no longer contributed to these schemes; loss of public housing, social security, healthcare, etc. to farmers
  - Privatization of urban housing
  - Shifting of investment in rural schools towards “beacon schools”
  - Private businesses exempted from “new” social protection programs

# Social policy reform paths





Source: EIU, EBRD

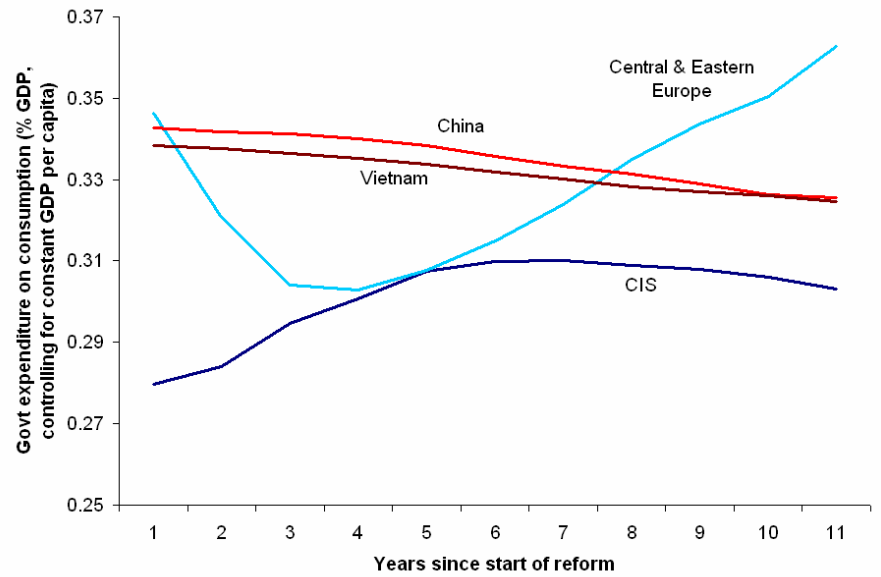
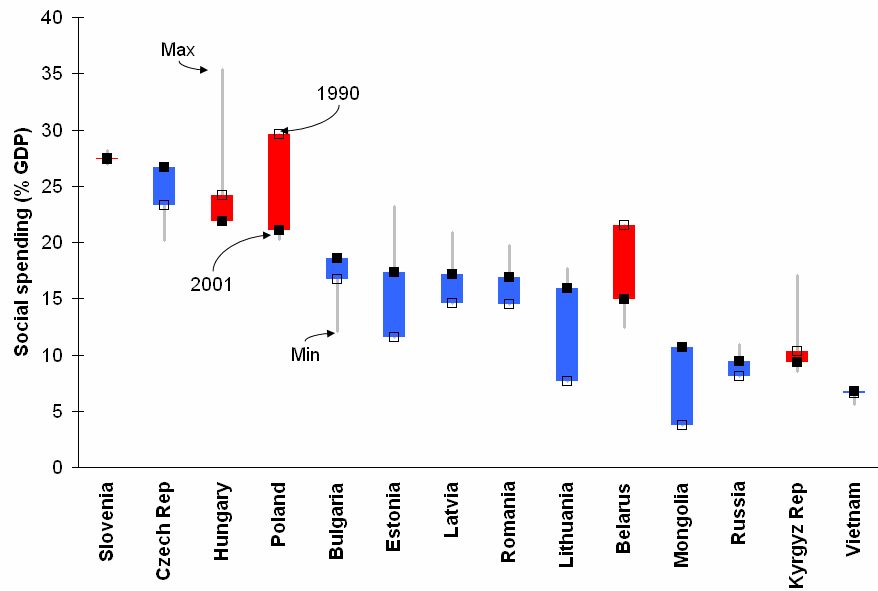
# Social consequences of the transitions

## EE/CIS

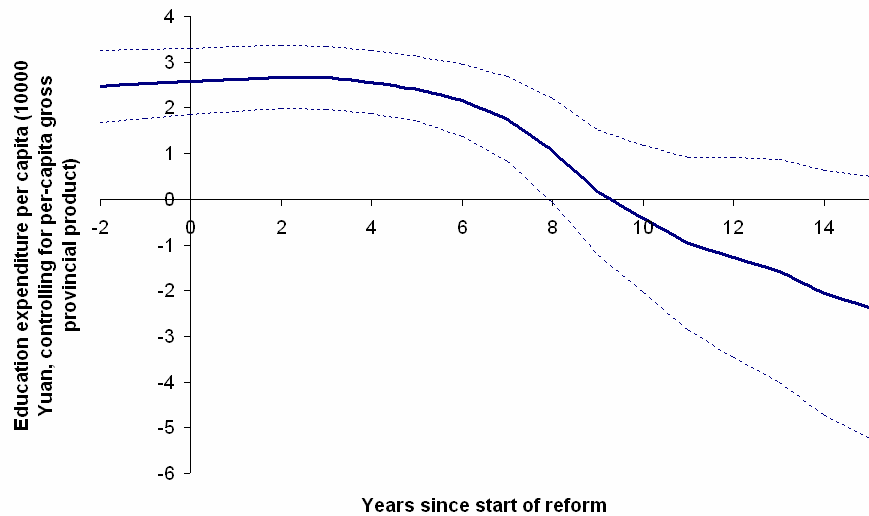
- Rising poverty across and within countries between 1989 and 1998
- Recovery since 1999 benefitting middle classes (with large inter-country variation)
- Ageing populations
- Limited targeting of antipoverty programs

## China

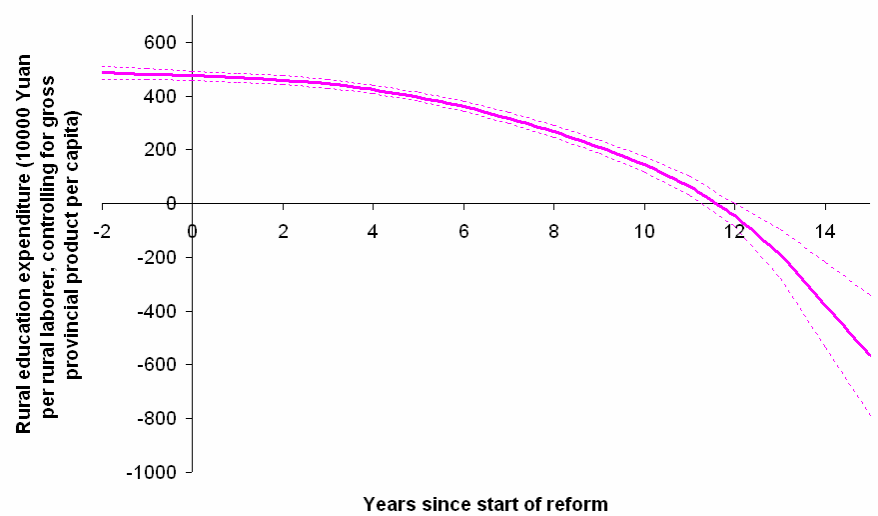
- Tensions
  - Widening urban-rural inequality gap
  - Stagnant rural poverty
  - Rural unrest
- 2005: “Harmonious Society” programs launched
- Targeted minimum living-standards guarantee (*dibao*) expanded



Education (Within-province, China)



Rural Education (Within-province, China)



# Globalization and social spending

- No effect on social spending in advanced industrialized countries
- Restrains social spending and transfers in middle- and lower-income countries
  - Downward pressure on labor costs and payroll taxes (and social security contributions)
  - Reduces income from excise taxes
  - Severs link between labor and left-wing political parties
- OR: creates new vulnerabilities leading to expansion of safety nets
  - Market volatility due to trade/financial integration
  - Falling real wages/higher unemployment puts pressure on governments to act

# Determinants of social spending

<b>Author(s)</b>	<b>Sample</b>	<b>Explanation</b>	<b>Effect</b>
Garret (2001)	mixed	trade integration	<b>negative</b>
Garret, Mitchell (2001)	OECD	level of trade	<b>weakly negative</b>
Kaufman, Segura-Ubierno (2001)	Latin America	change in trade openness	<b>negative</b>
Avelino, et al (2002)	Latin America	trade openness	<b>negative</b>
Takahashi (2004)	Latin America	trade openness	<b>negative</b>
Rudra (2002)	mixed	globalization x labor "power"	<b>negative</b>
Swank (2002)	OECD	globalization	<b>no effect</b>
Avelino, et al (2002)	Latin America	financial openness	<b>positive</b>
Rodrik (1997)	mixed	trade x instability (exposure to risk)	<b>positive</b>
Adsera, Boix (2002)	mixed	trade x democracy	<b>positive</b>

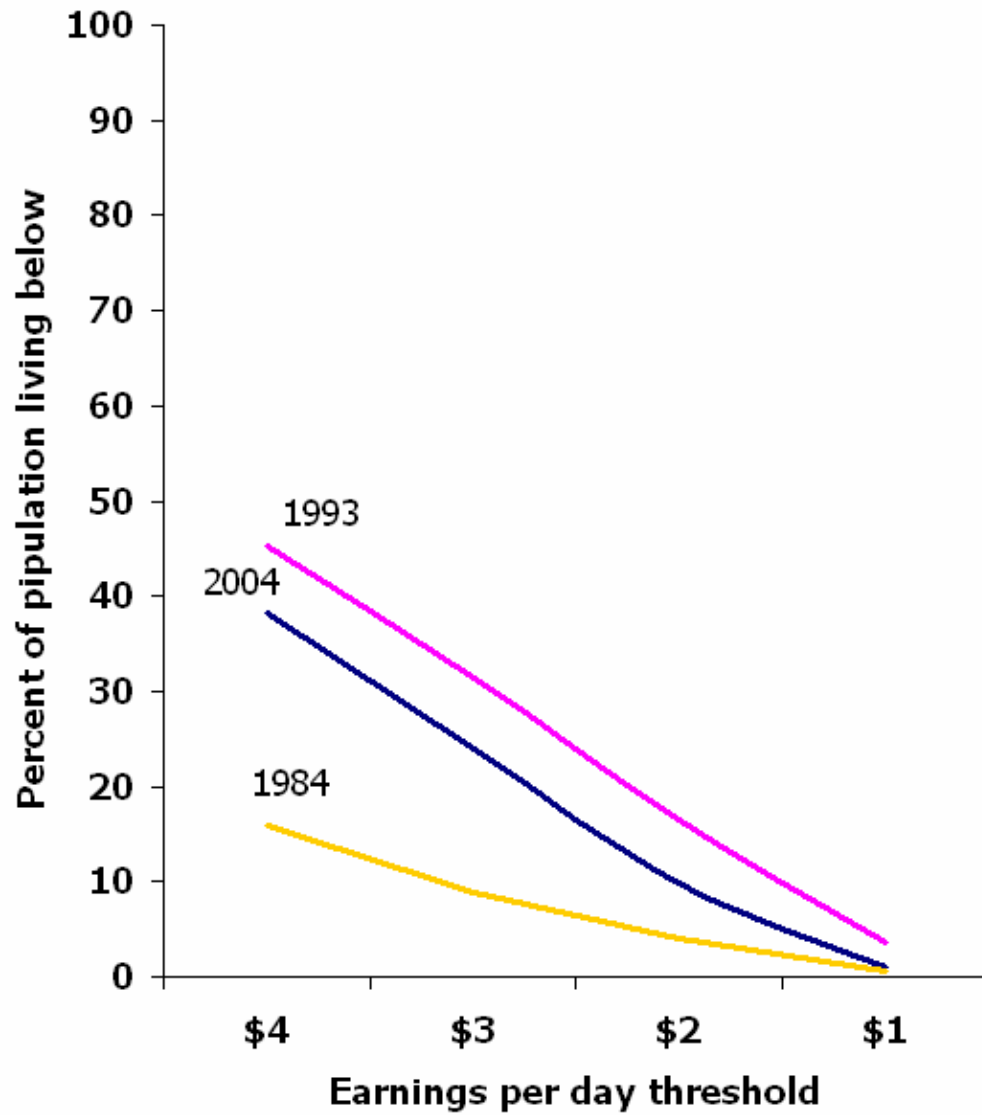
# Alternative explanations

- **Distribution of political franchise**
  - Lindert (2004) traces rise of social transfers to extension of the franchise in OECD countries & L. America
  - Stasavage (2003) finds that democratization shifted resources to primary education in African states
  - Zhang et al. (2004) find that Chinese villages holding elections since the early 1990s provide greater access to social services
- **Demographic shifts**
  - Age dependency ratio associated with greater social transfers (mainly due to public pension expenditures)
- **Labor-market institutions**
  - Degree of unionization (Esping-Andersen, 1996)
  - “Corporatist” institutions (Hicks and Swank, 1992)
- **Public opinion**
  - Attitudes towards the poor or unemployed influence support for transfers (Graham 2002)

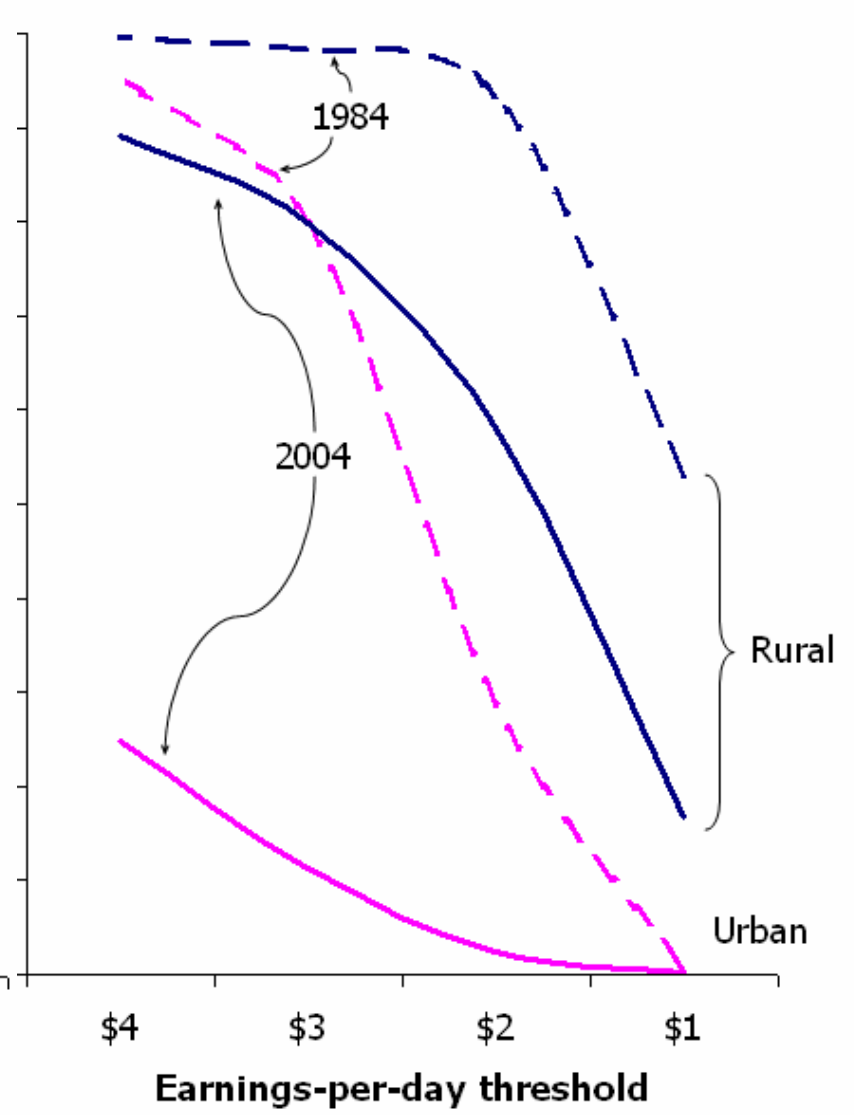
# Poverty and the transition

	<b>Eastern Europe/CIS</b>	<b>China</b>
The Transition trajectory	Dramatic increases in absolute poverty rates (from 2 to 21% between 1988 and 1998); initial deterioration in several standard-of-living indicators	Urban poverty significantly reduced; poverty in rural areas down but resistant to state interventions
Programmatic changes	For CIS, end of transfers from Moscow prevented cushioning social impact of transition; for EE/CE social transfers remained relatively high	Private sector employees excluded from new social protection schemes, and state did not force new private enterprises to commit to work-based social contributions
Poverty profiles	Shrinking labor demand, consequently a large number of “working poor”; changes in relative prices; declining revenues	In urban areas, larger groups of unemployed; in rural areas, marginalized poor farmers and migrants’ families

## EE/CIS

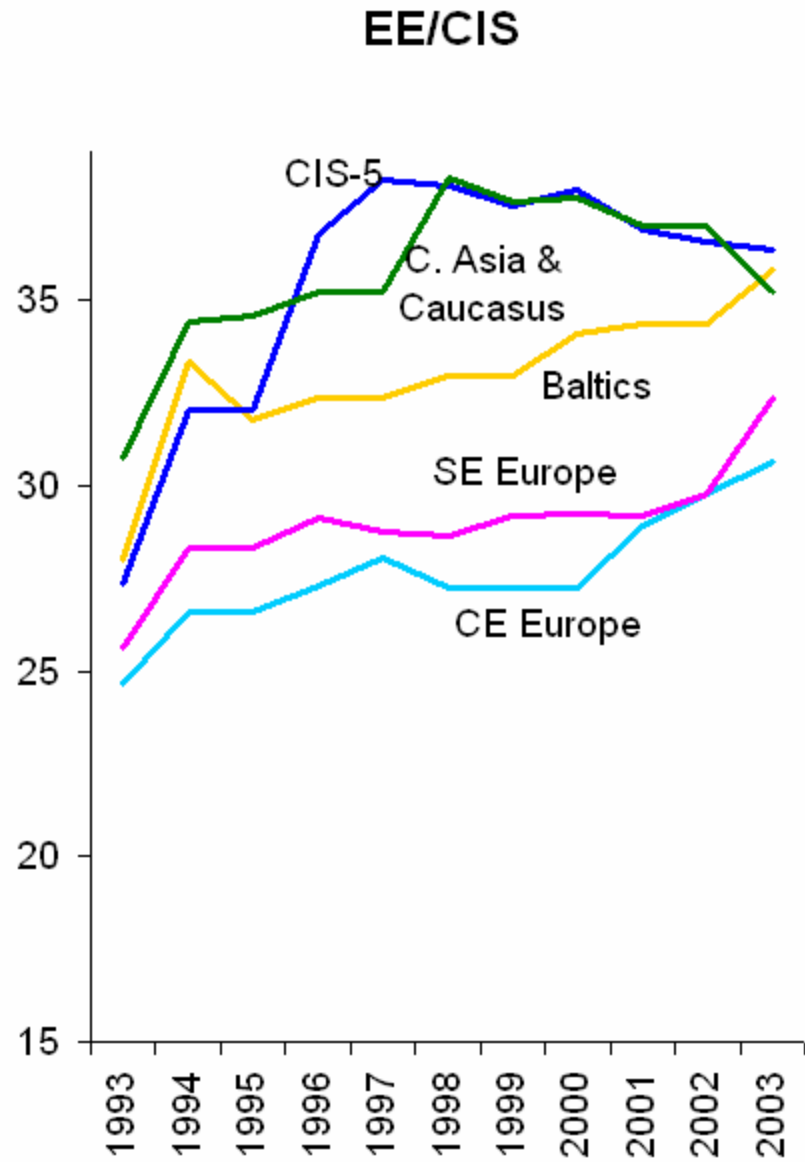
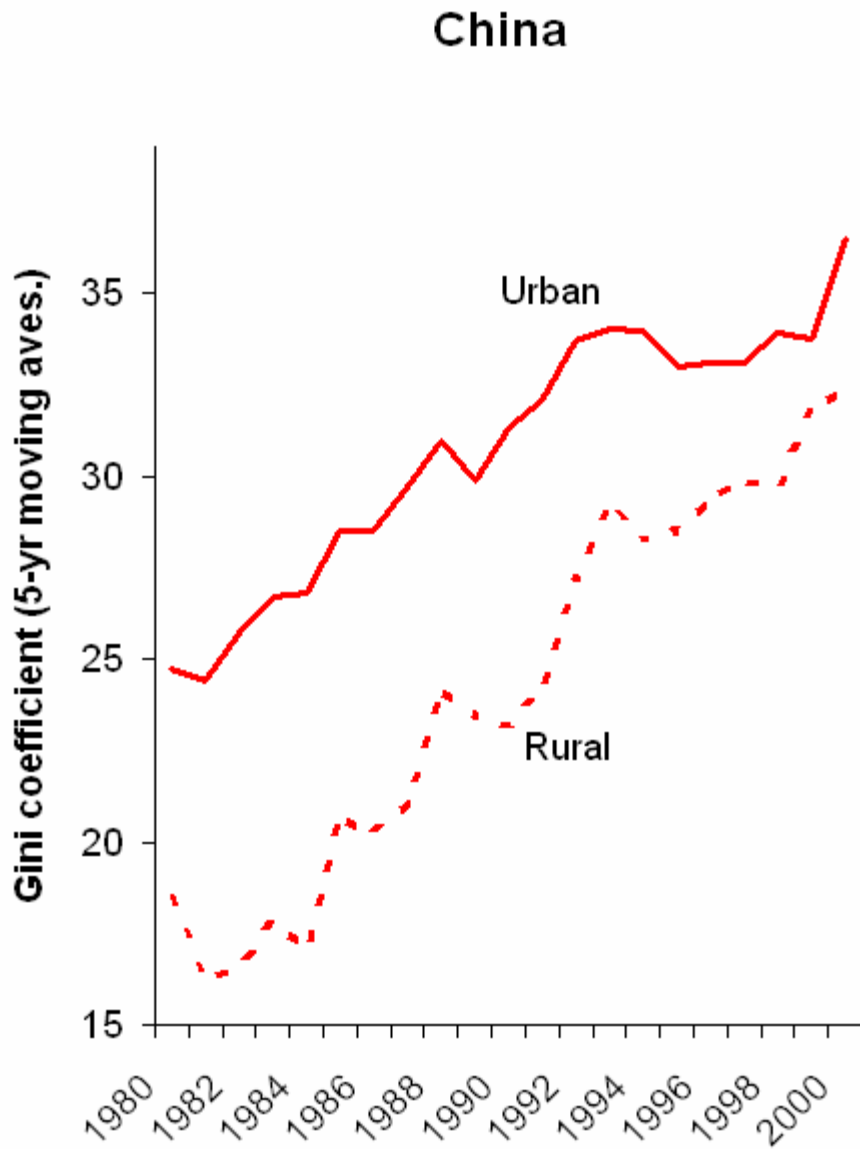


## CHINA



Source: Ravallion and Chen (2004)

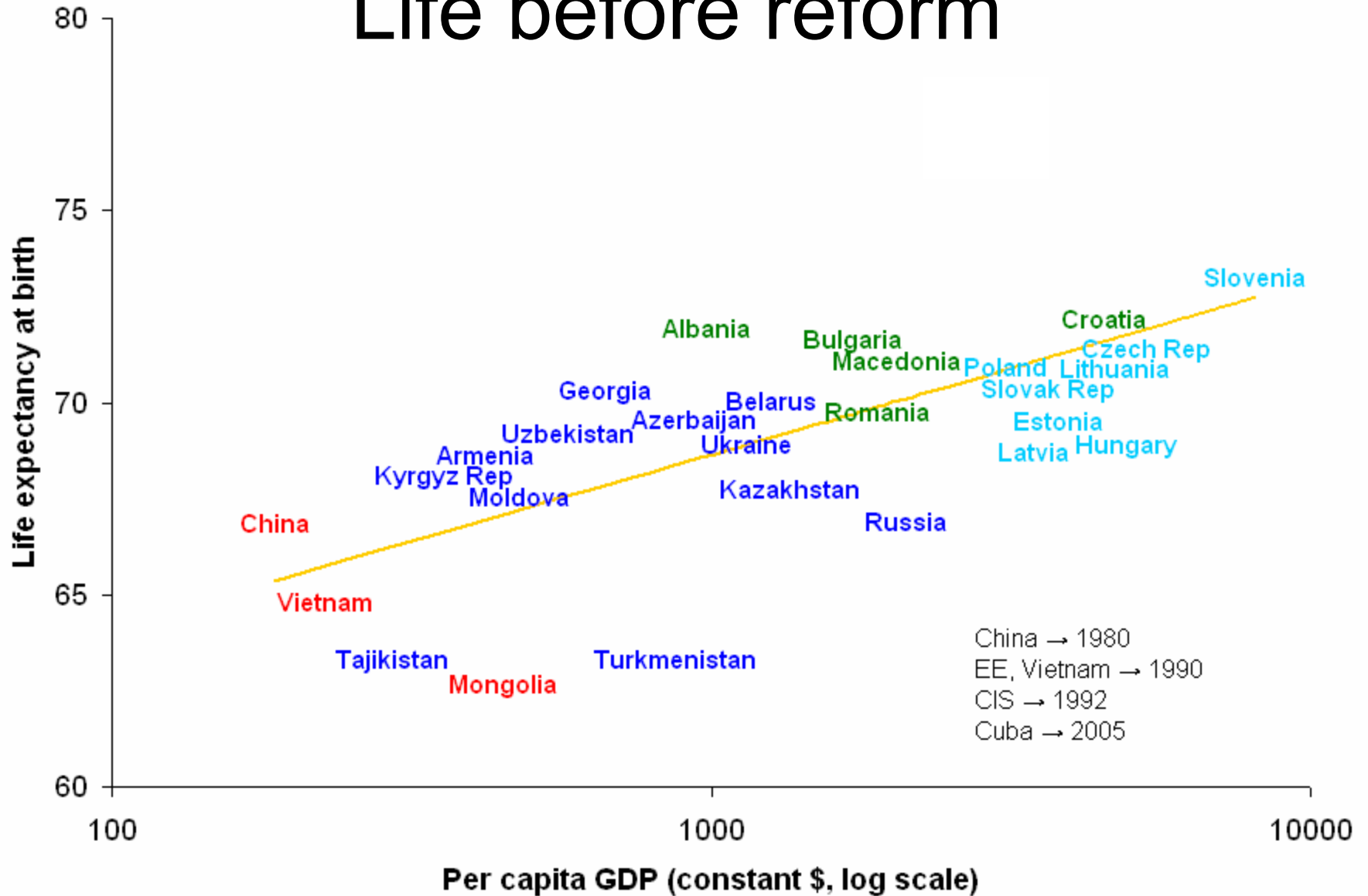
# Inequality

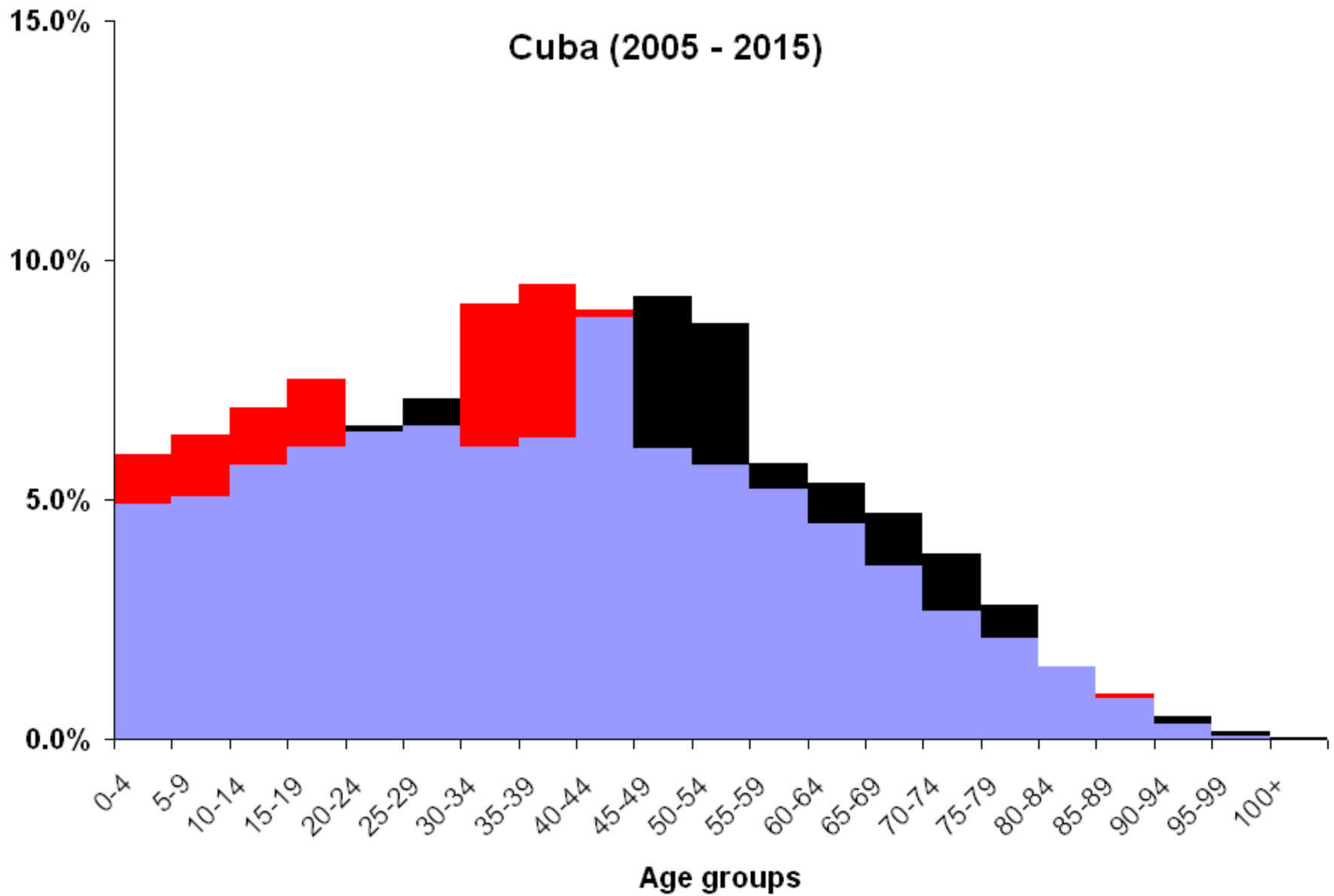


# Implications for Cuba?

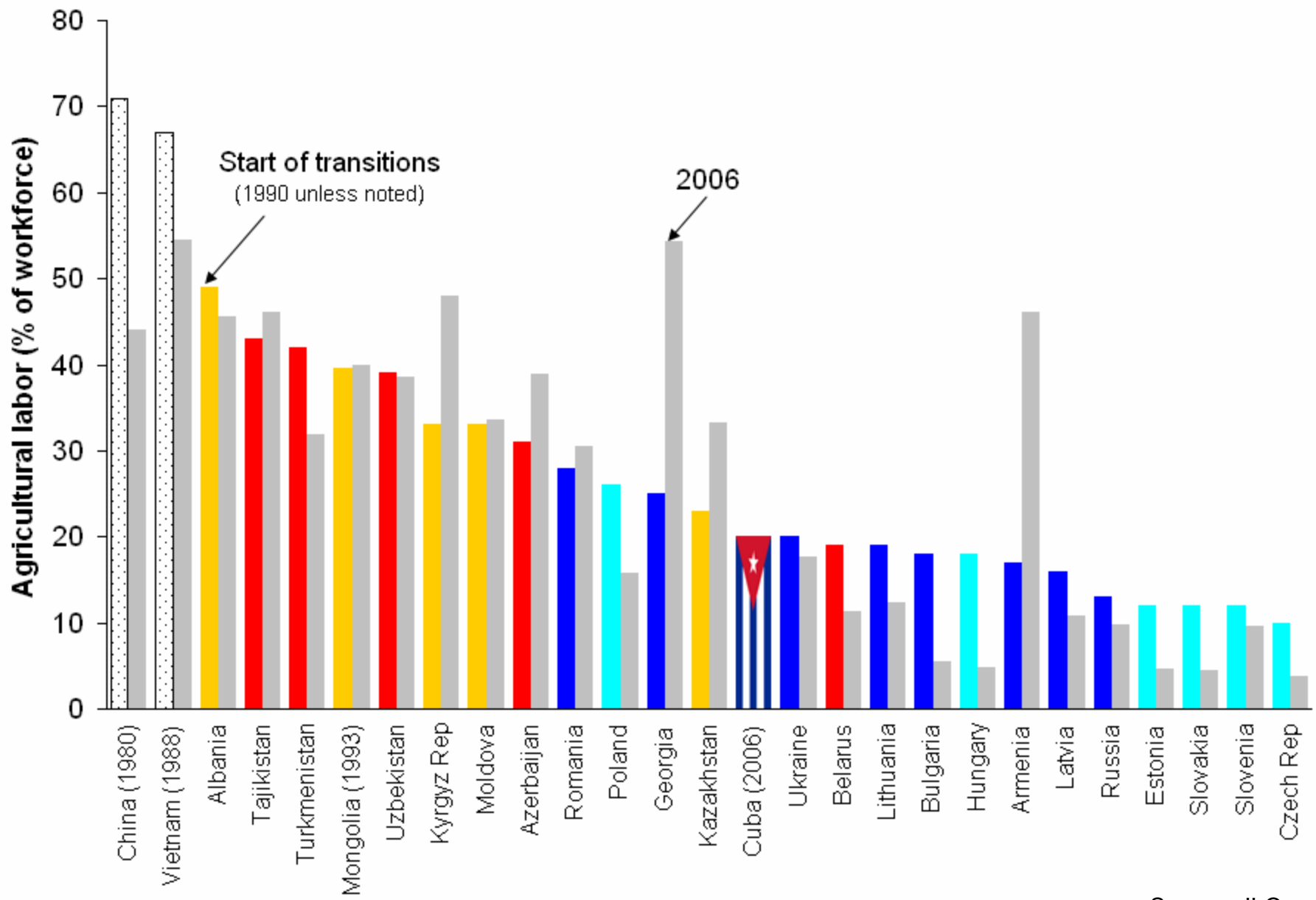
- How can European and Asian post-socialist reform experiences inform the Cuban case?
- Demographic patterns → more similar to middle-income Central European countries than to China or Vietnam
- Composition of GDP → resembles poorer Eastern European countries (Lithuania, Belarus, Ukraine)
- External sector (trade, investment, remittances)

# Life before reform





Source: UN Population Division



Source: ILO