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.*

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

- European socialist states (1987)
- Poland
- Russia
- Latin America
- East Asia
- China (1975)
- China

Social transfers (quantity)

Enterprise-funded vs. State-agency funded
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
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

<table>
<thead>
<tr>
<th>Author(s)</th>
<th>Sample</th>
<th>Explanation</th>
<th>Effect</th>
</tr>
</thead>
<tbody>
<tr>
<td>Garret (2001)</td>
<td>mixed</td>
<td>trade integration</td>
<td>negative</td>
</tr>
<tr>
<td>Garret, Mitchell (2001)</td>
<td>OECD</td>
<td>level of trade</td>
<td>weakly negative</td>
</tr>
<tr>
<td>Kaufman, Segura-Ubiergio (2001)</td>
<td>Latin America</td>
<td>change in trade openness</td>
<td>negative</td>
</tr>
<tr>
<td>Takahashi (2004)</td>
<td>Latin America</td>
<td>trade openness</td>
<td>negative</td>
</tr>
<tr>
<td>Rudra (2002)</td>
<td>mixed</td>
<td>globalization x labor “power”</td>
<td>negative</td>
</tr>
<tr>
<td>Swank (2002)</td>
<td>OECD</td>
<td>globalization</td>
<td>no effect</td>
</tr>
<tr>
<td>Rodrik (1997)</td>
<td>mixed</td>
<td>trade x instability (exposure to risk)</td>
<td>positive</td>
</tr>
<tr>
<td>Adsera, Boix (2002)</td>
<td>mixed</td>
<td>trade x democracy</td>
<td>positive</td>
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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

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<th><strong>China</strong></th>
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<tr>
<td><strong>The Transition trajectory</strong></td>
<td>Dramatic increases in absolute poverty rates (from 2 to 21% between 1988 and 1998); initial deterioration in several standard-of-living indicators</td>
<td>Urban poverty significantly reduced; poverty in rural areas down but resistant to state interventions</td>
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<td><strong>Programmatic changes</strong></td>
<td>For CIS, end of transfers from Moscow prevented cushioning social impact of transition; for EE/CE social transfers remained relatively high</td>
<td>Private sector employees excluded from new social protection schemes, and state did not force new private enterprises to commit to work-based social contributions</td>
</tr>
<tr>
<td><strong>Poverty profiles</strong></td>
<td>Shrinking labor demand, consequently a large number of “working poor”; changes in relative prices; declining revenues</td>
<td>In urban areas, larger groups of unemployed; in rural areas, marginalized poor farmers and migrants’ families</td>
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</table>
Source: Ravallion and Chen (2004)
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)