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Inequality and Transformation of Social Structures in Transitional Economies

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UNU World Institute for
Development Economics Research
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FOREWORD

Social consequences of the economic transformation from centrally planned to market economies have attracted considerable attention by policymakers, international organizations, including donor institutions, media and serious academic research. Many scholars have contributed to the analysis of social changes in the countries in transition. Considerable knowledge has been accumulated on social costs of the transition, winners and losers of the reforms, poverty, its incidence determinants and composition. Yet much more remains to be analysed and understood. Apart from poverty and the poor more knowledge is needed about new economic and political elites, the nature of emerging capitalism as well as the prospects for a middle class in transitional societies. These issues are even more complex due to a wide diversity of developments in different countries. In sum there is an enormous field for new original research which prompted UNU/WIDER to undertake a new project on Income Distribution and Social Structures during the Transition directed by Dr Vladimir Mikhalev. The overall objective of this project is to raise the study of social stratification under transition to a qualitatively new level and contribute innovative theoretical insights to the understanding of these societies. This paper by Dr Mikhalev outlines the major concept of this study, gives an overview of research findings and policy conclusions. In particular it considers (i) determinants of social change (i.e. factors of social mobility, causes of inequality and poverty); (ii) the emerging patterns of social stratification; (iii) diverging individual country developments.

Among his findings Dr Mikhalev concludes that economic recession, inflation and privatization have increased inequality and caused changes in social ranks and status so as new social classes have replaced old status groups. A new elite and a middle class have emerged alongside the socially deprived. These processes considerably differ between the faster advancing reformers in Central Europe and the CIS countries of the Former Soviet Union: Central Europe shows much less social stratification than the FSU. Social polarization holds back economic prosperity, causes social tension and hinders human development. Based on this analysis of trends and causes of social stratification Dr Mikhalev formulates economic and social policy approaches conducive to poverty alleviation, social integration and social cohesion. He emphasizes the importance of policies promoting social mobility, entrepreneurship, employment and skills as a major way of improving living standards of the working population. Such policies must be supported by effective safety nets for children, the elderly and other socially vulnerable groups.

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ABSTRACT

The transition to a market economy in Eastern Europe and the Former Soviet Union (FSU) has been associated with greater inequality and social stratification. Living standards have fallen for the majority of people, unemployment and poverty are high, the distribution of assets and earnings has changed radically, and social benefits have fallen. The social distance between the 'winners' and 'losers' of the reforms has widened dramatically. This paper prepared within the UNU/WIDER project on 'Income Distribution and Social Structure during the Transition' analyses trends in social stratification and their causes with the aim of drawing social policy conclusions.

Social structures have been deeply affected by macroeconomic and social-sector reforms. Privatization shifted assets towards the wealthy while changes in labour markets have led to the rise in earnings inequality. In the pretransitional socialist societies which were stratified into 'status groups' where social capital rather than economic capital—and social networks rather than market power—determined a person's status. With the transition, people's prospects in life are being increasingly determined by their possession of assets, goods and income opportunities. This study considers emerging social classes and groups—a new elite—the product of rising capitalism, and the new commercial, managerial, and professional middle classes. The large majority of the population, however, consists of blue-collar workers, farmers, and state-sector employees bearing the social costs of the transition. The bottom of the social hierarchy has enlarged due to a considerable number of socially deprived and marginalized people who fell into long-term poverty.

The slowly reforming economies of the FSU have particularly high inequality and social polarization. Central Europe's transition countries have shown smaller increases in income inequality. Many professional workers there, especially the young have successfully entered the market economy. In contrast, an extremely wealthy and powerful economic elite has emerged in Russia and some other FSU countries amidst impoverishment and deprivation of a large part of the population.

Social polarization has large economic costs. Thus, a more active social policy—promoting better livelihoods and more investment in human capital—could have large economic returns. But there is also a need for more effective public transfers and income redistribution policies to alleviate and reduce poverty. Social cohesion cannot be ignored.

I INTRODUCTION

Transformation of social structures in countries of Central and Eastern Europe and the Former Soviet Union undergoing transition from state socialism to market economies requires understanding of determinants of the change, evolving patterns of social stratification, and formulation of relevant policy approaches conducive to sustainable social development and social cohesion. This paper has been prepared for the project on 'Income Distribution and Social Structure during the Transition' being implemented within the research programme of UNU/WIDER during 1998-9. Its purpose is to summarize available evidence on a number of these issues, set out a research agenda and present preliminary findings and hypothesis.

The transition to a market economy has entailed a move from largely egalitarian social structures to greater inequality and social stratification. The high economic and social costs of the reforms, radical shifts in distribution of assets, increases in earnings inequality, changes of welfare regimes (in many cases associated with decline in major social benefits) resulted in the reranking of relative income positions and social status of many social and professional groups. One of the most important outcomes of the transition has been increasing social distance between the 'winners' and 'losers' of the reforms (Haggard and Kaufman 1995; Hellman 1998).

The extent of economic and welfare crisis experienced by most countries in transition has been far higher than could be initially anticipated. The collapse of the centrally planned economic system combined with major systemic change resulted in massive economic decline and a fall in living standards. The elimination of price controls followed by high inflation, the liberalization of wages, the appearance of unemployment together with privatization of state properties put at a disadvantaged position a wide group of the society (Nelson 1997). The decline in production, which affected particularly the public sector and non-competitive large-scale industries was exacerbated by lack of progress in establishing the necessary institutional environment for the development of the private sector economy (North 1997; Polishchuk 1997). The outcome has been massive informalization of the economy where the informal sector is absorbing an increasing proportion of the economically active population.

The heretofore unknown rise in income inequality in some countries has introduced sharp contrasts between expanding poverty, and concentrating wealth in the hands of only a few. Over 1989 and 1993-5, the number of the poor in 18 countries of the region rose twelvefold from nearly 14 million, or about four per cent of the population, to 168 million, or approximately 45 per cent (UNDP 1998: 15). Unemployment rose with a few exceptions to 11-14 per cent (Commander and Tolstopiatenko 1997). More social hardships have been inflicted on the population of Russia and other countries of the Former Soviet Union (FSU) by the deep crisis that shook local economies in the second half of 1998. Living standards have plunged further after just first signs of their stabilization. The deterioration of welfare manifested itself in an unprecedented mortality crisis with additional deaths reaching 3 million over the 1989-95 period alone (Cornia and Paniccià 2000). At the same time the newly prosperous elites have managed to consolidate considerable economic and political power.

With important similarities in social consequences of the transition, the intensity, timing and causes of this change in individual countries have been far from uniform. The Central European countries have experienced smaller increases of income disparity, lower poverty rates, and possibly less radical shifts in social structure as compared to the Former Soviet Union and South Eastern Europe. In a historically very short period the countries of the FSU have acquired strongly unequal patterns of income distribution similar to those of high-inequality economies of Latin America (Milanovic 1998; Cornia 1996 and 1999). Consequently, the emerging social structure is characterized by extreme polarization between a tiny newly prosperous elite and the mass of impoverished population. Such a pattern of social stratification hinders consolidation of the middle class and hence social cohesion.

In this paper I analyse new determinants of social stratification emergent with the transition and the impact of different reform strategies on inequality and increasing inter-country divergence in social structures. This analysis is followed by discussion of major social classes and groups of transitional societies: the new elite (new capitalists ranging from profitseekers to rentseekers, bureaucrats, managers); the middle class (professionals, managers and small entrepreneurs); the working class; the poor and socially deprived. The paper concludes by an overview of policy priorities conducive to greater equality, social integration and social cohesion.

II SOCIAL STRUCTURES PRIOR TO THE TRANSITION

The essential characteristics of the economic organization and redistributive system, which defined social structures in socialist countries before the transition, included:

- state ownership of the means of production
- full employment
- labour wages earned at state enterprises as a principal source of income
- income levelling policy which did not encourage accumulation of individual wealth
- pervasive system of public transfers providing everybody with basic social services and benefits.

Under such conditions social structures were characterized by very limited private property ownership, high labour force participation rate (including women) with employment predominantly at state sector enterprises, egalitarian structure of income distribution with low levels of inequality. The control of the economy by the state essentially diminished the importance of the ownership of the means of production as the basic definitional distinction of social classes (Słomczyński and Shabad 1997: 160). The class structure of societies under state socialism did not strictly correspond to the division of economic power. The widely shared understanding by Marxist and most other social scientists is that major classes existing in socialist societies are working class, peasants and white-collar workers (intelligentsia) (Connor 1979: 89-90).

Szelenyi and Kostello (1998) characterize the socialist economies prior to transition as redistributively integrated. The average level of cash incomes was generally low and barely above subsistence minimum but basic food and consumer goods were heavily subsidized and essential social services including education, health care and housing were distributed free of charge. Even with the existence of unofficial ways of supplementing income inequalities in countries of Eastern Europe and in the Soviet Union were much narrower than in the *western* capitalist world (Davis and Scase 1985; Lane 1978).

Using Max Weber's approach, social stratification in the pretransition societies may be considered as stratification into 'status groups' rather than into classes (Weber 1978: 305). Market mechanisms there were suppressed, so that they could not develop to the extent allowing real class divisions to emerge. Relationships based on reciprocity played more important role than that of the market. Social divisions in these societies nevertheless existed but they were based on social networks and political power determining allocation and redistribution of resources according to a rigid system of ranks and status. Status positions were associated not with market power but with being part of a group, to which access was restricted by social networks. Thus status in pretransitional societies was determined by possession of 'social capital' rather than economic capital.

Social inequalities in pretransitional socialist societies became more evident and complex in the course of modernization as a result of which they were increasingly becoming mixed economies incorporating more elements of market-based relationships, even if prevailing in the expanding shadow rather than official economy. Status determinants increasingly incorporated economic, political and social components. However due to non-market natures of the economies political components acquired a disproportional significance, in some socialist countries to a greater extent than in others. In Eastern European countries these components were more balanced while in the Soviet Union according to Tatiana Zaslavskaya all these factors were reduced to a political component (Zaslavskaya 1997). Social status there totally depended on one's place in power hierarchy from the top level of the party *nomenclatura* to ever lower levels of bureaucracy with ordinary citizens at the very bottom of social ranking. Political power was the source of privileges of the soviet *nomenclatura*, which formed a clear status group, rather than class, with its distinct virtues, privileges, obligations, functions, and lifestyle marking its position in society (Piirainen 1997: 23).

A distinctive important part of *nomenclatura* consisted of managers of state enterprises, who although not being owners of the means of production, exercised essential control over their utilization. Middle level managers were lower in the hierarchy. Unlike top managers they had no control over the use of means of production but instead exercised direct supervision over labour (Słomczyński and Shabad 1997: 163). *Nomenclatura* positions were achieved according to rules, norms and policies which made these social groups increasingly closed with channels of upward mobility for the most part restricted. The higher groups in the social hierarchy had a tendency of becoming castes (Starikov 1996). *Nomenclatura* status led to honour and prestige with necessary attributes of lifestyle and elite consumption supported by various perks.

Within the overwhelming majority of ordinary, not particularly well-off, citizens who did not belong to *nomenclatura* social distinctions were determined not so much by income or asset ownership but rather by level of education and qualification of labour. Professionals and intellectuals generally enjoyed a higher social status and occupied more prestigious positions although their income was not necessarily higher than that of the working class. On the other hand, the official communist ideology attributed high importance to manual labour workers who represented a social base of the communist party and were regarded as politically more reliable than intellectuals. Part of higher-skilled labour elite enjoyed a privileged social status.

Peasantry in the former socialist societies had more distinctive class characteristics. In the Soviet collectivized system farmers occupied a clearly inferior position being discriminated against industrial workers in the wage remuneration and cash transfer benefits. Even more marked distinctions of peasantry as a social class existed in countries, which had preserved private land ownership (e.g., in Poland).

More social divisions emerged in the last decade of communist rule when private activities on a limited scale were allowed and shadow economic activities expanded on an ever increasing scale. Players in the second economy began to earn higher incomes changing considerably their lifestyles, including access to better housing and availability of cars and other consumer goods which used to be regarded as luxury by the majority of the society

(Szelenyi and Kostello 1998: 316). Such processes intensified in the 1980s, particularly in Central Europe and by the late 1980s in the Soviet Union. Young engineers, part of the *nomenclatura* offspring, who opted to move into self-employment, took new business opportunities and engaged in the process of early capital accumulation in both semi-official and shadow economies. Thus prior to the beginning of radical market-oriented reforms former socialist societies were already acquiring important elements of market economies and with them certain features of a class society.

Poverty and exclusion in the prereform period was limited to certain vulnerable categories of the population. These included single-parent families or large families with more than three children or with other dependants (for instance, a disabled family member) as well as mainly young families where one of the parents was temporarily not working (often on maternity leave). One income in a family was often inadequate due to low wage levels and the official income levelling policy. Social benefits, including maternity and childcare allowances, disability pensions and certain forms of assistance provided to single-parent and large families, were barely sufficient to raise living standards up to the level of subsistence (Braithwaite 1997). Pensioners on a low pension living alone were another high-risk category as such pensions were unable to provide for a minimal level of subsistence.

Another disadvantaged social group comprised wage earners in poorly-paid occupations, including employees in the retail trade, primary education, some branches of light industry as well as lower skilled medical staff and cultural (for instance, library and social club) workers. Finally, there has always been a small marginalized group of homeless people and those released from the penitentiary system with the highest risk of poverty due to significant disadvantages for them in finding jobs, getting housing and residence permit.

III DETERMINANTS OF SOCIAL STRATIFICATION IN TRANSITIONAL SOCIETIES

Generally speaking, the process of transition has substantially changed the importance of major determinants of social stratification. Transition to the market brings about distinctive social classes (as opposed to status groups) defined by economic interests in pursuit of possession of assets, goods and opportunities for income as major determinants of life chances. According to Weber, in modern societies inequalities generated by the markets translate into uneven distribution of life chances and thus produce a major source of social stratification. The significance of income, type of employment and property ownership as a determinant of a social status has greatly increased while the role of state provided welfare and as well as of numerous perks available to formerly privileged groups has drastically diminished or ceased to exist. With transition to the market the life chances of working people have become more dependent on the quality of education, level of skills, and professional experience. In general, economic factors became predominant while distribution of income and assets received primary importance among economic determinants of social stratification. Distributional patterns were in turn determined by many factors, in the first place by those pertaining to overall economic conditions and policies. Purely economic factors are deeply interrelated with institutional, political, ethnic and cultural.

In reality, the societies in transition demonstrate a complex combination of different processes of social stratification with a mixture of interrelated old and new status and class groups. Post-communist economies continue to be mixed systems where markets coexist with redistributive mechanisms and reciprocity based relationships (Szelenyi and Kostello 1998: 307). While new market-based factors of social stratification gain in significance over redistribution, other determinants of the old social structure, in the first place social networks, continue to play an important role. Moreover essential assets (social capital) which defined social ranking prior to transition can be converted into new assets—economic capital crucial for occupying a higher status/class position in the newly evolving social structure (Piirainen 1997: 42-43). The extensive net of relationship, which used to be a vital asset guaranteeing high life chances in the old societies does not lose its importance with the transition to the market. Although in a market-based society money and private property directly determine life chances, the social capital gained under the old system may be indispensable for the acquisition of economic capital and wealth in the post-transitional society.

Undergoing a transformation with transition to the market these social networks demonstrate strong sustainability and largely influence the processes of social mobility, particularly the formation (or transformation) of local elites. Private networks have also a direct impact on income structures through widespread private transfers. The share of such private transfers (from extended family and local community networks, migrant remittances and Diaspora) has risen steadily, particularly in those countries, such as those of the Caucasus and Central Asia, where the wage economy and social transfers have collapsed. Extended family and clan relationships are deep-rooted in social structures of the FSU (particularly in the Caucasus and Central Asia) and Southeastern Europe (SEE). In some countries social networks are interrelated with the ethnicity factor. Ethnicity has a strong influence on social stratification in many countries of Eastern Europe and the FSU, particularly on the formation of new elites as well as on determinants and composition of poverty.

Political and economic liberalization is removing rigidities in social structure. The emergence of multiparty systems and freedom of personal choice of type of activity, place of work, and place of residence, as well as lifestyle, greatly increased social mobility. These processes have been enhanced by the opening of the society to the outside world, increasing integration of local economies into the world economy. International factors came to influence social stratification. At the upper end, elites are benefiting from their role as mediating between the domestic and international economies. They are also socialized into the global economic perspective, as they may personally move their assets and their families abroad. The internationalization of elites contributes to the domestic social division. At the other end of the scale there is a considerable migration of the labour force. Armenians moving into Russia and Ukrainian workers taking jobs in the Czech Republic are not the only examples. Remittances make up an important part of the income in poorer countries, while a new ethnic worker underclass is emerging in the more developed post-socialist economies. All of this is reinforcing the informal sector.

The expanding freedom has also had its big costs in a weakening of the rule of law and social order. The institutional vacuum caused by the disintegration of the communist party has lead to a decline in the capacity of the state to implement consistent economic and social policies. The old administrative system could not be immediately replaced. Law-abiding societal standards and institutions need a much longer time to be built and mature, which may require a generational change. The collapse of the state is reflected by informalization of the economy, the inability of government to deliver basic public goods, to set up and enforce an appropriate regulatory framework. It manifests itself in the accumulation of wage, tax and trade arrears, demonetization of the economy. Underdevelopment of civil society causes the spread of rent-seeking opportunities and practices. In its extreme form rent-seeking leads to outright corruption, while weak legal system and poor law enforcement give rise to organized crime and mafia. All these processes have a strong impact on the position of various social classes and groups.

As suggested by Słomczyński and Shabad (1997: 171) 'for some period of time the class structure of post-communist societies will be a hybrid one, shaped both by the legacy of the past political-economic order and by the requisites and opportunities afforded by emergent capitalism'. There are as yet no clear social boundaries between classes and status groups, as well as no internal unity and understanding of common interests within them. Mobility between the groups is high. The emerging classes and social groups are themselves fragmented to the point of internal polarization (Starikov 1996). Although the process of transition was a peaceful one, in a number of countries it had a revolutionary nature leading to disintegration of the very fabric of the society. Thus social ties remain very unstable and the process of reintegration may take decades.

The collapse of the centrally planned economic system, macroeconomic stabilization and structural reforms aimed at transition to a market economic system caused a fall in output and living standards. In most cases transformational recession proved to be much deeper and longer, and decline in welfare more profound than anticipated. The overall decline in real incomes has affected the welfare of wide groups of the population. Simultaneously the emergence of powerful forces of the market caused a profound shift towards more unequal income distribution. The considerable differentiation in earnings opportunities affected both wages and other sources of incomes originating from newly emerging forms of economic activity: profits, rent, interest earnings, and dividends.

TABLE 1
CHANGES IN INEQUALITY DURING THE TRANSITION

	Gini coefficients of income per capita (annual)	
Country	1987-8	1996-7
Balkans and Poland	*23*	*33*
Bulgaria	22	36
Poland	25	34
Romania	23	30
Central Europe	*21*	*25*
Czech Republic	20	28
Hungary	24	25
Slovakia	19	24
Slovenia	22*	24
Baltics	*25*	*33*
Estonia	27	34
Latvia	25	32
Lithuania	24	32
Slavic Republic and Moldova	*25*	*35*
Belarus	24	25
Moldova	26	46
Russia	26	38
Ukraine	25	31
Central Asia	*31*	*35*
Kazakhstan	29	33**
Kyrgyz Republic	31	35**
Turkmenistan	32	36
All transition	*25*	*32*

Note: The income concept per capita household income.
Regional averages are unweighted.

* 1989
** 1993

Source: UNU/WIDER World Income Inequality Database.

Research by Milanovic (1998: 40-46) has revealed an increase in inequality measured by the Gini coefficient of income distribution on average from 24 to 33 in all countries in transition since the initiation of market oriented reforms (Table 1). This change is particularly striking because it occurred in an unprecedented short period of time—only six years. It implies a radical transition from prereform egalitarian distributional structures to levels of inequality prevailing in OECD countries or even, in the case of the FSU, to patterns of high inequality in Latin America (Cornia 1996: 18).

Income inequality has become a major factor of social stratification. The extent, speed and direction of changes in distributional patterns themselves were largely determined by reform strategies (big-bang or gradualist) or chosen 'target models' of market economy (ranging from 'liberal Anglo-Saxon model' to social-democratic welfare state or 'middle-income developing country model'). However the impact of the speed and direction of reforms was significantly influenced by different initial socioeconomic conditions in transitional economies.

IV MACROECONOMIC AND SOCIAL SECTOR REFORMS: THE IMPACT ON INCOME DISTRIBUTION

Distributional consequences of the economic transformation are largely determined by concrete economic and social policies followed by the governments of post-communist countries. Economic reforms aimed at transition to the market include such essential components as elimination of price controls, efforts to stop inflation, the process of transferring property from the state to private individuals, liberalization of labour markets, exchange rate and foreign trade regimes. All this has direct implications for economic growth, employment, and opportunities to earn income and patterns of its distribution. The above policies have been the primary focus of the governments implementing reforms. Other policy components called safety nets—support for the unemployed, pensions for the elderly, and programmes for the relief of poverty—received much less attention (Kapstein and Mandelbaum 1997) because of financial constrains, or sometimes out of neglect. Unlike macroeconomic policies affecting production, policies in the social sector are redistributive. If rigorously pursued they would have an equalizing effect on distribution of income and wealth. However due to the weakness of social polices their impact on income distribution and social structure have generally been a very passive one—they failed to contain rapid increases in inequality.

4.1 Macroeconomic policies

Macroeconomic policies involved fiscal and monetary austerity, simultaneous trade and price liberalization, the removal of subsidies, the unification and devaluation of the exchange rate, and an increase in interest rates. Even in the case of successful stabilization, these measures exacerbated the recession, initiated by the collapse of the socialist economic system, caused a fall in the labour share and worsened income distribution (Cornia and Popov, forthcoming). The removal of subsidies had a negative impact on the distribution of welfare penalizing to a greater extent socially disadvantaged groups and thus exacerbating inequality.

Price liberalization followed by high inflation has unequal effect on different groups. The cost of inflation is much higher for the lower-income part of the population represented by such social groups as budgetary sector employees, farmers, workers in hardest-hit industries like textiles, machine-building, defence-oriented production, and the unemployed (Granville *et al*. 1996). Unlike wealthier groups they have less means available to protect themselves against inflation, such as asset ownership and hard currency savings. Thus inflation is generally accompanied by considerable adverse shift in income distribution.

Tax reforms may have long-term distributional consequences. Unlike that of the socialist countries (characterized by modest progressiveness), the tax system of market economies is generally characterized by medium-to-high progressiveness. The move to a western-type tax system would therefore lead, if properly implemented, to a fall in the dispersion of the net per capita household income. This effect is likely to emerge gradually with the implementation of these changes—which normally take years to reach a steady state.

4.2 Privatization

Privatization leads directly to redistribution of assets and hence sources of income and determinants of social status. While privatization can follow different paths (reprivatization, insiders privatization, voucher distribution, public auctions, sale to foreign companies, removal of barriers to entry, etc.), in all cases it can be expected to increase the share of private profits in total income. Since access to new property ownership, and hence capital incomes, is limited to a minority of the population privatization may lead to an increase in inequality and social polarization.

The faster the privatization of the economy, the more rapid the increase in the share of highly concentrated capital income and in overall inequality. In principle, the dispersion of private profits is most pronounced in the case of re-privatization, the least is that of voucher privatization and auctions, and somewhere in the middle is that of workers' privatization. The share of capital incomes (dividends, interests, rents, financial rents and capital gains) may often be underestimated due to the massive under-reporting of these sources of income. In some countries (e.g., in SEE or Uzbekistan) it has not increased substantially due to the slow pace of privatization and retarded development of the financial sector. Distributional consequences of privatization are more likely to have longer term rather than short-term consequences.

The number of capital asset owners has risen sharply with 'small privatization', the informalization of the economy, and the removal of barriers to entry. While measurement presents a serious problem, some evidence suggests that the share of income from profits, self-employment and 'other incomes' has risen steadily, particularly in those countries where the wage economy and public transfers have collapsed. In Russia, the share of entrepreneurial and property incomes in total personal monetary income increased from 11.2 to 45.5 per cent during 1990-6 (Goscomstat 1997: 73). It is likely that an increase in their share entails a rise in overall inequality.

A general trend appears to be a sharp rise in concentration in larger properties and capital incomes and a more moderate one in self-employment income. The shift in property concentration would likely be larger in the FSU, where the regulatory role of the state (to ensure, for instance, market competition) is less developed. So, despite a relatively modest increase in the share of property and self-employment incomes, their contribution to the overall increase in inequality seems to have been substantial in view of the rapid increase in the skewdness of their distribution.

The formation of large private properties in Russia came about as a result of massive redistribution of natural resources and productive assets through the privatization of state property, to which most ordinary people had never had real access. Managers of former state-owned enterprises have acquired a substantial part of shares of their privatized companies. Resorting to numerous means of control, managers act as *de facto* owners of enterprises. Although shares of privatized assets were distributed to the population through privatization vouchers, particularly to workers in cases of insider privatization, the value of property per individual is negligible to provide a meaningful source of income or ownership control. The evolving ownership patterns are characterized by widespread disregard of rights of minority shareholders in a situation of underdevelopment of corporate governance and poor enforcement of corporate laws (Blasi *et al*. 1997). At the second stage of Russian privatization called 'loans for shares' powerful financial tycoons and magnates of the oil and gas sector obtained most lucrative assets at, as widely believed, unfairly low cost. Thus capital incomes have concentrated heavily in the hands of the newly prosperous elite. This has created considerable moral hazard since it eroded the whole idea of people's capitalism and undermined public trust in the new economic and social system.

Self-employment as a main form of economic activity has extended on the contrary to a much larger proportion of the population but in most cases this development has not been associated with an increase of income and social status. The class of self-employed is however not homogeneous. Only a fraction of it constitutes 'nascent' small entrepreneurs. The larger part of self-employed in transitional economies expanding parallel to informalization of the economy does not represent growing small businesses and emerging middle class but rather widespread subsistence economies, which are becoming a form of survival for a large section of local populations. Thus transition to self-employment may be more frequently associated with a decline in a relative income position and social status.

4.3 Change in the labour market

Change in the labour market model has led to increase in wages differentials, and in the appearance of unemployment and underemployment. The abandonment of income levelling policy via centralized wage regulation leads to greater earnings differentiation reflecting labour productivity and returns to human capital. Earnings differentiation by skills, sector and occupation appears to be a major source of inequality. The increase was the greatest in Bulgaria and the FSU, where earnings dispersion almost doubled and is now much greater than in western economies. In the FSU and SEE wage differentiation and its generally depressed level has been the most important source of the increase in inequality. In contrast, in Central Europe (except Poland) the rise in earnings dispersion was more contained.

Wage deregulation has had an overall disequalizing effect of an increase in wage dispersion across industries (controlling for the skill intensity of each sector). In many cases this increase in inter-industrial wage dispersion is explained by the monopolistic behaviour of strategic sectors (mining, energy and utilities) able to extort wage and price increases due to their political strength and influence (Mikhalev and Bjorksten 1995). Greater productivity differentials, following price liberalization and productivity gains due to restructuring, appear to have yet a minor influence on wage levels.

Overall earnings dispersion might have been influenced by the weak policy towards minimum wages. Indeed, the countries experiencing the largest increases in wage dispersion are generally the same in which the minimum wage has fallen the most relative to the average. This trend was enhanced by weakness of trade unions and collective bargaining, which does not ensure the protection of labour and counterbalance the increase of wages inequality. Labour legislation is largely ignored, particularly in the private sector where workers often have no contract guarantees with regard to pay level, working hours, and job tenure, let alone benefits like sick pay, medical insurance or paid leave (see Dmitriev and Maleva 1997). Another factor contributing to earnings inequality by sector and type of employment is the inability of the state to sustain social sector wages, growing self-employment and informalization of the economy.

Due to the above factors compounded by unemployment (following the recession of 1989-92/3 and industrial restructuring) the share of wages and salaries as a source of income has declined everywhere (Table 2). Prior to transition wages formed about 70 per cent of personal incomes in the FSU, close to 60 per cent in Bulgaria and Hungary, over 50 per cent in Poland. By 1996 the wage share in income fell to about 60 per cent in Ukraine, below 50 per cent in Bulgaria and Hungary, 45 per cent in Poland, 40 per cent in Russia (Milanovic 1998: 50-3, 196-208). In extreme case—such as Armenia and Georgia—the wage share dropped below 20 per cent. The concentration of wealth in the FSU has also occurred as a result of an alienation of part of the population's consumption fund by depressing their wage levels as well as by monopolization of consumer prices. Hence, the capitalization of the national wealth in the FSU has also removed that part of it which used to be at the disposal of the working population. In Central Europe the wage economy appears to have lost much less ground.

TABLE 2
STRUCTURE OF INCOME (%)

Source of income	Russia		Ukraine		Poland		Latvia	
	1990	1996	1990	1995	1989	1996	1990	1996
Labour income (wages and salaries)	74.1	40.5	67.5	42.6	57.3	45.4	72.6	50.0
Social transfers	14.7	14.0	13.2	8.9	22.0	32.1	11.2	27.1
Private and informal sector income (including self-employed and in-kind)	11.2	43.0	19.2	48.0	20.7	22.4	16.7	22.9

Source: Calculated from Milanovic (1998: 196-214).

Social stratification within the working class is determined by segmentation of labour markets by type of skills and sector of economic activity. A smaller fraction of most competitive workers enjoys considerable advantages in higher pay levels and job security (Gimpelson and Lippoldt 1996). Partially this can be explained by short supply of skilled workers needed for jobs entailing 'new skills', leading to over-remuneration of a privileged segment of the labour force. Better position and stability in the job market is ensured not least by personal networks which may have an even greater influence in the new private than in the public sector.

The rise in unemployment is directly related to a loss of income and social status of the part of the population affected in a situation where unemployment insurance did not offer sufficient compensation. Moreover, the suppressed form of unemployment, which prevails in the region of the FSU and takes the form of short-time working, unpaid leave and mounting wage arrears, contributes to greater social inequality. Such hidden forms of underemployment redistribute losses from stronger (more competitive) to weaker (less competitive) workers and thus lead to further segmentation of the working class (Gimpelson 1998).

The collapse of wage economy, growing job insecurity and decreasing formal employment opportunities force people to resort to activity in the shadow economy. The increasing part of the working population living outside the official economy is left out of the boundaries of any legal norms and safety nets. The formation of such a dual economy, which has a potential to evolve into a pattern characteristic of economic structures of Third World countries, creates a serious impediment to the development of socially integrated society.

4.4 Changes in social security regime

Transition towards a market economy is compatible with the development of a social security system capable of providing effective protection to low-income and vulnerable groups and mitigating inequality via social transfers. However, as widely expected, it proved difficult to combine measures of financial stabilization and structural reforms with the development of new welfare institutions. While the demand for income transfers and safety nets has grown tremendously, the availability of fiscal resources, as well as the administrative capacity of their efficient distribution, was sharply decreasing. Severe budget constraints and a high rate of inflation determined the priorities of monetary stabilization over social protection, and therefore did not allow sufficient resources to be allocated to restore adequate levels of welfare.

The share of public transfers (on account of pensions, unemployment benefits, family allowances and social assistance) does not follow a universal pattern. Over the short-to-medium-term, it increased or remained at a fairly high level in most countries in transition including the FSU[1]. However in real terms social expenditures in the FSU countries have substantially declined due to the fall in GDP and high inflation while in CE it was maintained at relatively high levels in real terms as well. It is disputable, however, if the CE pattern can be sustained over the long-term. These differences are not the result of endogenous factors (e.g. differential population structures) but reflect policy choices, or the inability-unwillingness to collect the taxes needed to finance adequate levels of transfers in a market economy.

Thus, reforms of welfare systems may have a complex effect on social stratification. In the first place, realignment of social transfers to those countries with similar levels of income per capita would likely cause an increase in inequality. Second, the introduction of new transfers—such as unemployment compensation and social assistance—which are generally well targeted on the poor—are likely to alleviate inequality and poverty.

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[1] Dmitriev compared the proportion of social expenditures in GDP in transitional economies with countries of the OECD and with developing economies. In 1993 Hungary spent on social programmes 22.5 per cent of GDP, Poland 21 per cent, Czech Republic—14.9 per cent, Russia—17.9 per cent, Bulgaria—12.9 per cent. This proportion is lower than in OECD countries (27.1 per cent) but higher than in Latin American countries (10 per cent), which have comparable levels of per capita GDP with Russia or Bulgaria (Dmitriev 1997: 22-4).

However this effect may be limited by the low level of protection provided due to tight budget constraints. Third, the inability and/or unwillingness of the state to index pensions depress the share of pensioners in total income and thus worsen their relative position. The erosion of the social security regime has initiated the emergence of a social class of poor pensioners. Furthermore, shifts in pension regimes towards fully funded systems or systems characterized by greater emphasis on the contributory story of the insured are expected to increase social inequality among pensioners in the longer run. This latter effect of pension reforms however cannot be evident during the first years of the transition.

V REFORM STRATEGIES AND DIVERGING COUNTRY TRENDS IN INEQUALITY

While the above determinants of social stratification can be observed in all countries in transition the actual effects by country have been very diverse. Major differences lie between the situation in Poland, Hungary, Czech Republic, Slovakia and Slovenia on the one hand, and countries of the FSU and SEE on the other. Generally speaking the social situation in East-Central Europe has been much better than in the rest of the former socialist world undergoing transition. Market reforms in the FSU have been far more difficult because of much heavier legacies of centrally planned economy to a greater extent burdened by massive inefficiencies and distortions compounded by pervasive militarization of production. Contrary to Central European states, which managed to implement consistent fiscal and monetary reforms that brought quick stabilization and economic recovery, Russia and other republics of the FSU (with the exception of the Baltics) demonstrated failures in macroeconomic stabilization and major structural reforms (Cornia and Popov, forthcoming). The social costs of lack of stabilization, prolonged inflation and recession there have been very high. The hardships of the majority of citizens and extraordinary social inequality have been made worse by very poor tax collection, pervasive corruption and rent-seeking.

Available evidence allows suggesting the following major causes of diverging country patterns of inequality and social mobility. First, inequality has risen faster in the FSU because of the sharper recession experienced in comparison with CE. In the FSU, the fall in the wage share has been compounded by the huge wage arrears accumulated by most companies. Second, earnings inequality in the FSU rose much faster than in CE. In addition, adverse policy factors (the abandonment of effective minimum wage regulation; the more than proportional decline of social sector wages; the inability to contain wage increases in the monopolistic-rent sector) in the FSU seem to have greatly contributed to income inequality and decline of social status of several professional and occupational groups. Third, social transfers in the FSU were traditionally lower, have fallen faster, and are less efficiently targeted. The decline of social welfare there can be explained by weakening of the state capacity to implement consistent social policies. In Central Europe, social transfers have not fallen as dramatically and helped to contain the surge of inequality over the short-term. The long-term effect of this policy is, however, questionable because of the long-term inter-generational distributive problems it may cause. In addition, even over the short-term transfer policy may have been less than ideal. While family allowances, unemployment compensation and social assistance appear to have been increasingly better targeted, pension reform has contributed to a shift towards greater inequality. Finally, in some of these countries, the surge in inequality might have been exacerbated by the approach followed in the privatization of state assets and by a greater informalization of the economy.

Two broad patterns seem to be emerging from the analysis of available evidence.

5.1 Central Europe (CE): a comparatively moderate increase in inequality

In the CE economies the Gini coefficient of net per capita household income rose on average by 4 percentage points, an amount surprisingly similar to the 'average difference' between the market and socialist economies of Europe during the pretransition period. At present, the CE economies (with the exception of Poland) have Gini coefficients similar to those of the UK and Canada and higher than those of the Nordic countries and Germany. For these economies one could hypothesize a 'physiological adaptation of inequality' to levels typical of a western market economy. However, this 'spontaneous adaptation' hypothesis does not seem to be borne out by the evidence, as in CE the sources of inequality are substantially different from those of the developed market economies.

The social structures of Central European countries in transition did not experience polarization to an extreme extent. While reranking of social status of various groups is certainly taking place the gap between the elite and the rest of the society looks less profound while the group of severely deprived people is far less massive than in the FSU. These countries have made real progress in the formation of a middle class of small entrepreneurs. A substantial part of professionals and intellectuals, especially the younger of them, have found their successful way in the market economy.

Significant differences however exist between Central European countries as well as the comparison between the Czech Republic and Poland shows. Poland and Czech Republic are both radical and most consistent reformers which had inherited more mobile economies less burdened with the military sector and over-industrialization, and more developed social sectors. They both experienced a modest recession and rather quick recovery. The distributional consequences of the transition however happened to be quite different. The Czech Republic demonstrated persistence of wages economy, low earnings inequality, voucher privatization, and strong and targeted transfer system. In Poland privatization was delayed, wage economy experienced a decline while social transfer system, albeit quite large, had significant distortions. Consequently, Poland has much higher levels of earnings and income inequality as well as the incidence of poverty. Social reranking in Poland also looks more significant than in the Czech Republic. It appears that the Czech Republic has preserved much more of the old social structure than Poland where the formation of the new capitalist and middle class is among the most intensive in countries in transition.

5.2 A rapid surge in inequality in the FSU and SEE

In most of the FSU and SEE, the Gini coefficient of the distribution of net per capita household income rose by about 10 percentage points—i.e. 2-2.5 times faster than in CE. Income inequality in these countries is now substantially greater than in most OECD countries and is gradually moving in the direction of that of the high-inequality countries of Latin America, even if the sources of inequality seem to be quite different. Even these data may give only a partial idea of the distributional earthquake underway in the region. In view of the growing under-reporting of income affecting official surveys, it is likely that income disparity over the past decade has risen even faster. Smaller surveys (with fairly accurate reporting of incomes) seem to indicate that a tiny class of 'new rich' now controls an exorbitant share of total income. In Russia, the income gap between the more affluent

10 per cent of the population and the 10 per cent poorest increased from four times at the start of the reforms to 13.3 times in April 1998 (Goscomstat 1998: 213). The former receive 33 per cent of all incomes, and the latter, a meagre 2.4 per cent.

Social structure of Russia and some other countries in the FSU is characterized by the emergence of extremely wealthy and powerful economic elite, with the impoverishment and deprivation of broad strata of the population. Extremely skewed income and asset distribution impedes the formation of the middle class, and generally the losers of the transition largely outnumber a small heterogeneous group of winners. Corruption and crime largely influencing the processes of social stratification acquired far larger scale compared to Central Europe.

Within this vast region itself significant divergence of emergent social structures by country can be observed. The two largest countries Russia and Ukraine are characterized by similar initial conditions having the longest history of central planning and economies distorted by large-scale inefficient heavy industries with a big share of military-industrial complex. The reform paths and emerging economic and social structures nevertheless look rather different. Russia has demonstrated a shock therapy approach, large recession, collapse of wage economy, insider privatization, and a high extent of informalization of the economy. Ukraine attempted to implement a gradual reform strategy and had even larger inflationary recession, significant informalization of the economy, delayed privatization. Both countries at the same time experienced the highest level of earnings and income inequality and have weak social transfer systems. Poverty rates in both countries are quite high, the number of losers is massive, while the might and wealth of powerful elites largely determine the economic and political scene. Corruption and crime have reached exorbitant proportions. With this important similarity Russia appears to have had a much greater reranking in income positions and social hierarchy than Ukraine. It may be also suggested that the change within the elite has been more significant in Russia than in the Ukraine where the old class of managers and bureaucrats has managed to safeguard more influence and social status.

SEE, in the first place Romania and Bulgaria, is characterized by a slower progress of economic reforms and high levels of social inequality and poverty. Local economies have experienced a considerable recession and medium-to-high informalization. Privatization and liberalization until recently have been quite limited, earnings inequality is high while social transfer system proved rather weak. Despite growing inequality social mobility and reranking is yet more limited compared to other countries in Eastern Europe. Delayed privatization did not allow significant capitalist class to evolve. Much slower is the formation of small-scale enterpreneurship. While income levels of the working class, farmers and intelligentsia have declined due to economic recession, stratification of their social status (apart from earnings differentiation) have not yet taken place on a significant scale. These processes, however, are likely to intensify after more radical reform policies have been initiated.

The region of Central Asia has considerable specificity as well as diversity, which can be seen by comparing Uzbekistan and Kyrgyzstan. These two newly independent countries have a common heritage as former Soviet republics with similar social and economic structures. They were characterized by higher proportions of rural populations; largely distorted economies dominated by narrowly specialized collectivized farming; substantial portion of defence industries and high dependence on financial transfers from the metropolitan centre. Reform strategies however have been quite different. Kyrgyzstan introduced rather radical liberalization similar to the Russian case. Transformational recession there as well as the collapse of wages was very deep while the system of social protection proved far inadequate. Consequently, Kyrgyzstan has had pervasive informalization of the economy and very high levels of income inequality and poverty. On the contrary, Uzbekistan following a gradualist reform strategy has had modest recession limited informalization, moderate earnings inequality, no privatization, and strong social protection system. Social stratification in Kyrgyzstan has gone considerably further than in Uzbekistan. Kyrgyzstan has seen the formation of a noticeable group of businessman, mainly in the commercial and banking sector. A considerable part of the Kyrgyz population has moved into subsistence self-employment, ranging from shuttle-traders to farmers who received their plots of land for individual use but are for the most part unable to set up productive crop cultivation or cattle breeding. Similar changes in Uzbekistan are much more limited due to slow transition. Corruption and crime are widespread in both countries but Kyrgyzstan may be more exposed to those phenomena due to a weaker government. Drug trafficking is a particularly serious social problem, especially in Kyrgyzstan. Clan relationship and community networks have crucial influence on social structures in both Central Asian countries.

VI SOCIAL RERANKING AND EMERGING SOCIAL CLASSES

For purposes of the analysis of changes in social structure social actors can be grouped according to descriptive typological characteristics into politicians, bureaucrats, managers, entrepreneurs, professionals, blue-collar workers, farmers and peasants. These distinguishable groups differ by such features as levels of skill and education, employment in the private or the public sector, or in informal economic activities (in particular, subsistence self-employment). They can be further ranked and ascribed to broader social status and class groups using such determinants as income, asset ownership (including land), education, political influence, lifestyle, consumption, and social prestige of the job. The above indicators can also serve to measure economic and social distance between groups.[2] In many cases a higher level of income and consumption corresponds to higher education and social prestige. However, in the specific situation of transitional societies a high educational level and socially prestigious job (e.g. professor, researcher, or artist) may still indicate a higher social status despite low-income (declined in the course of transition) and restrained consumption.

Redistribution of income and assets and the rise in inequality in transitional societies has lead to greater social polarization which is understood here as widening distance between groups, in particular between upper and lower levels of social structure. Apart from an increase in 'economic distance' between groups of households the economic transition is also associated with considerable reranking among socioeconomic groups, sharp changes in social hierarchies. Such social reranking can be viewed as mobility from one group to another or up or down in the hierarchy. These changes have been rather rapid and the process of social stratification has not yet stabilized. Statistics and social surveys available do not allow a clear definition of newly emergent social groups. The widespread concept of winners and losers in the course of the transition may be used although its analytical limitations should be recognized.

In addition to the loss of income they may have experienced, many of the people enjoying high social status and political power during the former regime appear to have been relegated at the bottom of the social ladder. Loss of social status has been common among the former 'labour elite', i.e. the middle-aged, semi-skilled workers employed in heavy industry, part of the intellectual class, and managers of state companies. A considerable part of this wide group, especially members of the *nomenclatura*, enterprise managers and younger professionals, seems, however, to have adjusted to the new situation and retained considerable social status. Social disorientation is acute for most of the elderly who see the vanishing of the values, norms and their lifetime savings. Loss of political power is, obviously most acute among the older generation of party cadres and bureaucrats. The

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[2] Tatyana Zaslavskaya used ten status variables to identify the position of various groups in the social structure: educational level; self-assessment of skills; basic occupation; principal kind of activity; economic branch in which the person is employed; sector of the economy (according to type of property); size of the enterprise (firm) in terms of number of employed; professional and occupational group (determined by the nature of the work performed and the respondent's self-assessment); and the level of real income (Zaslavskaya 1997).

position of civil servants is also weakened by lack of funds and widespread mistrust in anything that is socialist, social or even public.

The intensity of social reranking, mobility and the width of social distance between upper and lower classes in comparison with the situation prior to transition significantly differs by archetypal transitional countries as diverse as Poland, Russia or those in Central Asia. A broad pattern of social stratification apparent in transitional societies includes:

(1) the new elite (it is especially important to investigate who are the new capitalists and what is the nature of emerging capitalism);

(2) the middle class (despite widespread perception that there is no middle class in post-communist societies, there is evidence of a rapidly growing new commercial, managerial, and professional middle class);

(3) the most numerous base stratum—'the people' including the bulk of the working class (blue-collar workers), farmers and peasants, the mass intelligentsia employed in the state budgetary sector;

(4) socially deprived and marginalized groups.

Attempts to assess quantitative proportions of social classes in a transitional society face serious methodological and data problems. For this purpose information from various sociological surveys and income statistics is usually used. Income levels and household asset holding generally serve as prime criteria for ranking by social class or status. This information may be supported by self-evaluation of respondents obtained in opinion polls. Such survey by the Moscow Institute of Socio-Political Research in 1994 estimated about 6 per cent of Russians as belonging to the rich or the upper class, and 29 per cent to the middle class (Khlop'ev 1996: 99-100). The majority of the remaining 65 per cent of the population would represent the base stratum of the society. Part of this majority has been affected by poverty and belongs to severely deprived social groups.

Poverty measurement in transitional society present specific problems, which do not allow attaining any accurate numbers. For the analysis of social stratification further difficulty lies in the fact that poverty for many people affected has transitional short-term character. In the Russian case official estimates of the poverty rate fluctuated within 25-33 per cent of the population. For the analysis of social structures the incidence of long-term poverty is a more reliable indicator of the proportion of the population qualified as severely deprived or marginalized. A new research by Ovcharova and colleagues based on multiple criteria revealed 8.3 per cent of Russian households in a representative sample affected by long-term poverty in 1996 (Ovcharova *et al*. 1998).

In sum not only the social structure has undergone serious changes in a historically very short period of time as a result of social reranking and emergence of new entrepreneurial capitalist classes. The process of upward and downward social mobility has greatly intensified with new opportunities open to winners—also with many of losers whose ranks may be adjoined by part those who initially did well in the new market economy. Deep polarization based on income inequality has become a salient feature of social stratification marking divisions not only between social classes but within each group, including the base stratum, due segmentation of labour, the spread of unemployment, self-employment and informalization of the economy. While the process of transition proceeds the social structure remains unstable and variable with intense changes of numerical sizes of the groups and strata from year to year.

6.1 The upper class: the new economic and political elite

One of the fundamental questions pertaining to elite formation in transitional societies regards the linkage between the old elite—*nomenclatura* and the emergent new capitalist class. Surveys show that the old elite (*nomenclatura*) has in general adjusted quite well to the transition in most of the countries. Political and social capital that the elite had possessed in the form of administrative control, management of state assets, access to information, various privileges and networks proved to be convertible into economic power ensuring new positions in the upper class of the society. However new findings also show that political capital alone in most cases was not sufficient to secure elite positions in the post-transitional society. Those members of the old elite who commanded higher levels of human (or cultural) capital did better in the transition than those possessing only political capital (Szelenyi and Glass 1999).

In the process of social change elite formation appears to have distinct differences between Russia and, similarly, many other CIS countries, on the one hand, and Central Europe and SEE on the other. The political capitalism thesis, i.e. the concept claiming that the new capitalist elite in transitional societies is largely formed by the old members of communist *nomenclatura*, proves valid for Russia and the CIS countries but does not hold for east Central Europe (Szelenyi and Glass 1999).

Evidence from such countries as Poland, Hungary and Bulgaria shows considerable changes in the composition of local elites, particularly among the members of political class. Many of the old party bureaucrats had to retire, others moved to minor jobs. The general trend in this region has been a downward mobility of the high level party political cadres. However the technocratic managerial fraction of the communist elite in Central Europe did much better during the transition. Another general trend characteristic of Central Europe is a much stronger continuity of economic elites than of pure political elites. Managers of the former state enterprises have for the most part succeeded in retaining their positions. They formed the core of the new elite in these countries and occupied command positions in the peculiar 'managerial capitalism' of east Central Europe (Szelenyi and Kostello 1998: 319).

An interesting study by Słomczyński and Shabad confirmed such trends in the upper class formation in Poland (Słomczyński and Shabad 1997). According to their findings former state socialist managers in general have made quite a successful career in the new system. However, far from all high positions in new social hierarchy have been occupied by former top *nomenclatura* bureaucrats and managers. Particularly advantageous were middle level managers who showed high propensity toward entrepreneurship. Thirty four per cent of capital asset owners and 58 per cent of top and middle level managers in 1993 belonged to managerial stratum in 1988. Sixteen per cent of owners and 13 per cent of higher managers come from professionals who had no managerial positions in 1988 (Table 3). On the other hand about 40 per cent of former managers were no longer working in 1993. Nevertheless managerial position in a former state enterprise proved to be a convertible asset in a market economy.

TABLE 3
JOB MOBILITY OF MANAGERS, EXPERTS, AND OFFICE WORKERS BETWEEN 1988 AND 1993 IN POLAND

	Class position in 1988				
	Top managers	Middle managers	Lower managers	Experts	Office workers
Social class in 1993	Percentage distribution				
Top managers	17.9	5.8	.7	5.5	.7
Middle managers	5.1	29.0	5.5	7.3	3.0
Lower managers	5.1	14.5	22.1	7.3	7.1
Experts	2.6	2.9	.7	45.5	3.4
Office workers	7.7	4.3	12.4	9.1	50.7
Service workers	2.6	2.9	7.6	.0	1.9
Manual workers	.0	2.8	10.4	.0	2.9
Farmers	2.6	1.4	3.4	.0	1.5
Owners and self- employed	15.4	18.8	7.5	16.4	7.1
Not working in 1993(a)	41.0	17.4	29.7	9.1	21.6
N	*39*	*69*	*145*	*55*	*268*

Source: Słomczyński and Shabad (1997: 174).
Note: (a) Includes retired and unemployed.

With a considerable degree of continuity in elite formation in Central Europe studies on these countries also reveal a substantial inflow into the upper classes. The inflow of new members is most significant in the political elite, but within the economic elite too about one quarter are newly recruited professionals, among which are many young people. Therefore cultural capital measured by the level of education and skills proved to be no less an important factor of upward mobility than political capital. In the fast reforming Central European countries individuals with cultural capital who did not belong to any elite group before the transition received equal or even better chances to move to upper class positions than those who were members of the communist elite (Szelenyi and Glass 1999).

Contrary to Central Europe, Russia and much of the FSU demonstrate a strong reproduction of both political and economic elites. In Russia as Krishtanovskaya (1996) puts it, 'the party and state *nomenclatura's* authority over the economy was exchanged for property. The state privatized itself. Whereas formerly property was at the disposal of, but not at the possession of *nomenclatura*, it now became legally defined property'.

According to findings by Zaslavskaya, 60 per cent of the new elite in Russia has emerged from the younger segment of the old elite who occupied top *nomenclatura* position or was at the second level in the hierarchy (Zaslavskaya 1997). The leaders of the Komsomol (the Young Communist League) were among the first to use newly opened business opportunities. They engaged actively in privatization of the state property from the very start.[3] These former members of the *nomenclatura* have formed the core of the new elite. This core is surrounded by a larger stratum of upwardly mobile new entrepreneurs who in most cases are, to a varying degrees, nourished by '*nomenclatura* capital' (Piirainen 1997: 167).

On the other hand the non-*nomenclatura* road to the top has become open to other subelite groups. According to Krishtanovskaya (1996), half of all party leaders in Russia, 59 per cent of the new businessmen, one third of the deputies, and one fourth of the presidential team and the members of the government had not previously been part of the *nomenclatura*. Early entrepreneurs of the late 1980s have also formed an important part of the business elite. These are professionals, engineers, civil servants who at that time quit jobs in the state sector and opted for self-employment in the informal economy or opened newly allowed co-operatives and small private businesses. Roughly 30 per cent of the 'new Russians' are representatives of legalized capital accumulated in the shadow economy (Zaslavskaya 1997).

New capitalists in Russia command positions of a powerful oligarchy headed by financial tycoons or magnates of the oil and energy sector. Some of them managed to gain enormous wealth and political influence through trading, in some cases speculative, rather then productive activities. Managers of the privatized big enterprises who acquired substantial ownership share of privatized assets are in many cases in effective control over their companies. They have formed an important part of the new class of capitalists.

Top managers are normally cadre personnel of large enterprises. Their upward mobility typically began from low-level duties to deputy manager or middle manager, and eventually to the position of a director general. Directors in Russia, unlike chief executive officers in a western company, became owners of extensive industrial capital almost overnight. They have been engaged in shady commercial activity since the beginning of political changes (leasing properties, trading products at low prices for bribes, etc.). While workers at their firms are on forced leave and go unpaid for months, the management buys property abroad and indulges itself to conspicuous consumption notorious of the 'new Russians'. Managers' earnings exceed wages of their employees by forty to sixty times. To consolidate their positions the Russian directors actively cultivate their ties with political establishment and financial oligarchy (Kukolev 1997: 8).

Bureaucrats of various levels form another important part of the new elite. Most frequently they come from a younger generation of older clans of party *nomenclatura* of the socialist

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[3] Krishtanovskaya has done an interesting analysis of the leading role of functionaries of the Komsomol (the Young Communist League) in privatization of the Soviet state and party property, which ended up in appropriation of state-owned assets by *nomenclatura*. This younger wing of *nomenclatura* engaged in the so-called 'komsomol economy' in the late 1980s became a most prominent part of the Russian business elite of the 1990s (Krishtanovskaya 1996).

times. Those of them who managed to adjust succeeded in securing political or administrative control and used it to accumulate considerable material wealth and social status. In spite of democratization of the system of government, the size and power of bureaucratic stratum does not necessarily reduce. Frequently in a number of countries quite the opposite can be observed. The number of bureaucrats per 100 thousands residents in post-Soviet Russia is fifty per cent greater than it was in the former Soviet Union (Bilenkin 1996). Bureaucrats are deeply interconnected with the new business elite forming a social class base for state bureaucratic capitalism. This is particularly characteristic of regional level elites in Russia. Subnational Russian elites form increasingly monolithic integrated groups of the political administrative and business directorate. They have consolidated their position by 'colonizing the new democratically elected regional soviets/assemblies' (Hughes 1997).

The economic power of new capitalists: financial tycoons, managerial and bureaucratic elite has been strengthened by their increasing influence over the political process. Political interests of business elites are driven by rent-seeking. Opportunities for extracting rents abound in all transitional economies due to incomplete reforms but especially in those countries where reforms have slowed down at an intermediate partial stage. Market distortions in a partially liberalized economy generate rents at a high social cost to the majority of the population (Hellman 1998). Liberalized prices coexisting with barriers to market entry and prevalence of monopolies create monopolistic profits in the domestic market. Liberalization of foreign trade with continued price controls for natural resource inputs allowed state enterprise managers to get rents by selling their subsidized products in foreign markets at real world prices. Subsidized state credits can be used by firm managers in short-term money markets at high interest rates. Considerable rents are created by imperfections of exchange rate regimes in a situation of high inflation. Bankers of newly formed commercial banks have profited greatly on the instability of exchange rates through currency speculation. For that reason they had a stake in perpetuating high inflation and opposed financial stabilization (Dmitriev *et al*. 1996). Rents are also extracted through pervasive trade, tax and wage arrears.

The elites that have benefited from market distortions have an economic and political interest in sustaining the flow of rents going to them no matter at what social cost. They therefore become a major impediment to the progress of reforms having a stake in preservation of the economic system in this partially reformed distorted state (Hellman 1998). In its extreme, rent-seeking is taking openly illegal criminal forms especially in such an increasingly criminalized economy as Russian.

Pervasive corruption as a salient ill-starred feature of the bureaucratic crony capitalism in some of the transitional societies determines a complex combination of economic and political power. The weakness of the state and poor enforcement of law allows corrupt and criminal elements to penetrate the economic and political elite, so that mafia-type groups tend to form an essential component of the privileged classes. Corruption and criminal economy are having a deep and long-term effect on mobility, class composition and social inequality (Słomczyński and Shabad 1997: 171). Research carried out in the Moscow region in the winter 1993-4 has revealed that 30 per cent of the starting capital in the private sector was of criminal origin while 51 per cent of sales operations had similar ties

(Staroverov 1996). Criminal money has also quite likely been involved in privatization and thus established deep-rooted links between the criminal world and much of the private sector. Crime is also becoming increasingly internationalized. Widespread migration with weak controls and lack of international co-operation in this area allows criminals from Russia, the Caucasus, Central Asia and other regions to expand their activities within the region and worldwide. Thus criminalization of transitional societies produces deep distortions in their upper classes and social structures in general.

6.2 The middle class: professionals, managers and small entrepreneurs

The prospects of the middle class—sometimes the question of its very existence in transitional societies—provoke ardent discussions among scholars of post-communist transition. The controversy of this polemics is intensifed by coexistence of a widespread pessimistic perception of the position of middle classes, on the one hand, with the understanding of a particular role attributed to the middle class as a guarantor of democracy and an integrating core of the society, on the other. Meanwhile the whole notion of middle class in such discussion is rather uncertain. Basing on ideas of major theorists in this field, such as Giddens (1973) and Goldthorpe (1982), three key criteria seem to serve best in identifying the middle class: ownership of the means of production, control over labour in process of production, and possession of education and technical qualification. According to this principle entrepreneurs, managers and professionals belong to the middle class. Following Goldthorpe's approach Lengyel and Robert ascribe managers and professionals to service class. Thus the middle class can be viewed as consisting of two key components: the entrepreneurial class and the service class (Lengyel and Robert 1999).

The countries undergoing transition from state socialism to a market economic system have many important pre-conditions for growth of the middle class. In the decades under the state planning system (even earlier in the 1920s and 1930s in Central Europe) these countries had undergone modernization and urbanization along with important changes in economic and employment structures, particularly the increased prominence of the service sector. Most important of all had been the very significant progress in education and generally high level of qualification of the labour force. These trends gained momentum during the transition in the 1990s. The service sector of the economy continued to expand and property ownership was legalized giving rise to a class of asset owners. The ranks of the nascent middle classes were joined by entrepreneurs and self-employed. The increased role of cultural capital, the upward mobility of professionals also contributed to this trend. Thus in terms of employment there has been a relative growth of the middle class against the entire population (Lengyel and Robert 1999). Such trend however is far from straightforward. High inequality, impediments to development of small businesses, low earnings of many professionals, especially those employed in the budgetary sector, hinder consolidation of the middles class in transitional economies. Thus the process of formation of middle classes is controversial and again considerably different between Central Europe and the FSU.

An important characteristic of the middle classes 'in the making' (Lengyel and Robert 1999) is their broad diversity. The middle classes in transitional societies appear to be more disparate and fractionated than their counterparts in western society and also less homogenous than both the upper and the lower classes. The groups belonging to the middle of the social structure: medium-level managers, small- and medium-sized entrepreneurs, highly skilled professionals, have been divided by the transition between winners and losers of the reforms. The position of these social groups is generally more favourable in the more advanced reformers of Central Europe than in much of the FSU and SEE. Faced with a drastic fall in their salaries and complete or partial loss of employment many representatives of the old middle class, professionals and intellectuals, have been left to survive by taking odd jobs or resorting to whatever means of self-subsistence were available.

It is believed that small and medium businessmen are the main reserve for the expansion of the middle class. Numerous reports provide evidence of growing entrepreneurial activity. However, high incomes are derived from currency deals, trade and mediation, commercial loans, etc., but not from real production. Most of the above incomes go to the top rather than to the middle of the income ladder. The emerging group of small businessmen has virtually no entrepreneurial incomes. Some reasons for that are obvious, and the largest of them is the inadequate support given to small businesses by the bodies of state authority. Instead of creating a favourable regime for them, they are weighed down by a heavy bureaucratic and tax burden, which forces them to evade the control of state agencies, poisons their psychology and turns the potential middle class from law-abiding citizens into their direct opposite (Tartanov 1998). Rent-seeking has influenced middle class formation in a similar way as it forged the new elite. A wide range of market instruments is used, including the artificial rise of prices, machinations with the quality of commodities, 'failure' to repay credits, racketeering, direct deceit, embezzlement, and unjustified business risks which take the most daring ones on to the criminal highway.

Yet a number of scholars maintain that new middle classes are emerging in transitional societies including not only the most advanced of them in Central Europe but also Russia and the FSU. Balzer (1998) characterizes the Russian middle class as hybrid of the old survivors and newcomers. Some of the old professionals have managed to sustain their positions, particularly those in the administration and those who succeeded in converting their social assets: connections and marketable skills. Furthermore, members of the new professions meeting the needs of the market economy have joined the ranks of the middle class. Among socio-professional groups of winners of the reforms figure an emerging 'productive bourgeoisie' of small entrepreneurs, the well-educated, workers with skills needed to make the market economy work (bookkeepers, computer experts, lawyers, linguists, managers, etc.), employees of western corporations, and part of the self-employed. There is also a large growing commercial class, although Starikov objects that the majority of it (numbering as much as 10-15 per cent of the Russian population) comprises traders and shopkeepers who are not a 'possessing' middle class but serve the upper class of owners, top enterprise managers and bureaucrats (Starikov 1996). Even in such an advanced reformer as Hungary the new class of owners remains relatively small. Counting such property as a means of production, shares, money and land 18 per cent of the population in Hungary can be classified as a class of proprietors (Lengyel 1998).

Due to the problems mentioned above—lack of governmental support, excessive taxation, harassment by corruption, threats by criminals—the middle class in post-communist societies is much smaller than in developed market economies. However, it would also be wrong to try to identify middle class in transitional societies according to criteria typical of the middle classes in Europe and America. In a western society the middle stratum encompasses from 60 to 80 per cent of the population with high status, steady incomes, substantial property and highly skilled occupations. Clearly middle class formation in post-communist societies has a lot of specificity. Based on extensive surveys relying on self-referential assessments and income data Zaslavskaya (1997) estimated that the middle class constitutes about one fourth of Russian society. Yet about 15 per cent of representatives of this middle class, included in this category by criteria of education or type of occupation, were living in poverty.

Although the intelligentsia is in a better position than the blue-collar workers in terms of marketable skills, these skills cannot ensure a higher status within the present occupation in the budgetary sector. This has provided a powerful incentive for intellectuals to leave their profession for the commercial sector, or even emigrate. Russia has witnessed a mass exodus from science. The number of research workers decreased by one third in 1991-3 alone, and every tenth scientist leaving this sphere went abroad (Starikov 1996). Those who stay in their profession normally have to take a second or a third job wherever available, often rarely related to their actual qualification. However employees in mass intellectual professions like teachers and doctors are in the worst position since they are the lowest paid and, due to a heavy workload (as well as to lack of second jobs available), are unable to earn anything additional on the side.

Despite the unstable and uneven situation concerning incomes of the middle classes there is other evidence that more members are joining their ranks. The prosperity of the middle strata of the population has strengthened with privatization of housing which gave households possession of an essential asset of considerable value. A survey in four Central European cities: Budapest, Warsaw, Krakow and Prague has found out that entrepreneurs and higher educated white-collar workers have been most active in housing privatization between 1989 and 1995. At the same time lower white-collar and manual workers (belonging to the base rather than the middle stratum) were most likely to continue living in the state sector housing. For example, in Warsaw the percentages of members of occupational groups living in self-owned housing clearly demonstrated class inequalities: 79 per cent of entrepreneurs and 70 per cent of upper white-collar workers owned the apartments they occupied, while for lower white-collar and manual workers similar percentages were respectively 60 and 35 (Duke and Grime 1997). The process of housing privatization has advanced farther than capital cities. In the Siberian city of Novosibirsk in 1992-6 30 per cent of the state and municipal apartment stock became private property of the population. Moreover, 6-7 per cent of households in that city proved to be wealthy enough to purchase an apartment in the emerging housing market (Tapilina 1998).

Another significant wealth and lifestyle characteristic of the middle class is automobile ownership, which has been expanding quite rapidly in most countries in transition. According to a survey in Novosibirsk Oblast in 1994 a car was available to one quarter of households. Half of all the cars have been purchased after 1991. By occupation 72 per cent of car owners were employed in the market sector of the economy, in particular in small firms and joint ventures, joint-stock companies, banks, stock markets, individual private businesses and co-operatives (Tapilina 1998).

The quantity of assets possessed by this class is, however, essentially smaller than that of the elite. By consumption patterns and lifestyle they find themselves in the middle position between the new rich and the base stratum—'the people' (Piirainen 1997: 167). A new survey by the Institute of Social and Economic Problems of the Population categorized 20 per cent of Russian households in 1996 as belonging to middle income level with monthly incomes ranging within US$100-1,000 per capita. This proportion corresponds to another finding of the same survey: the share of the Russian population having monetary income above their current expenditures enabling them to make savings is also about 20 per cent (Diskin and Rimashevskaya *et al*. 1997). Thus various indicators of the size of the middle class in the largest post-communist economy in transition fall within the same range. They confirm assessments of the share of the Russian population belonging to the middle class within one-fifth to one-quarter of the population.

6.3 The base stratum

Unlike western industrial societies where the majority is represented by the urban middle class, in transitional economies where the elite is very small and the middle class is not so numerous two-thirds of the population rather belongs to a lower class. Russian sociologist Zaslavskaya suggested regarding the majority of the Russian population as a 'base stratum'. These are most of the workers engaged in wage labour, mainly in the state sector and privatized industrial enterprises. By occupational status they are quite diverse comprising lower level medical staff (nurses), supporting staff in research and education, low-ranking employees in administration, the bulk of the blue-collar workers, peasants, and the majority of pensioners. Their income level is not much different, and is just about the level of moderate sufficiency. It is mostly equal or only slightly above official subsistence minima. In many cases, however, it may be lower than the official level of subsistence. Thus, a considerable part of the base stratum of the population in countries with higher poverty levels (especially in the FSU and SEE) falls into poverty.

A substantial majority of these groups have experienced deterioration in their social status, so may be considered as losers of the reform. The loss of social status occurred because these people have been deprived of their former social guarantees, once the egalitarian redistributive system ceased to exist, while they had no social capital to be converted or marketed under the new conditions. This is particularly true of the unskilled and semi-skilled proletariat who has been dispossessed of 'its "hegemonic status", however false and illusory it may have been' (Starikov 1996).

The bulk of the working class has suffered a substantial decline in real incomes and faced the threat of mass unemployment due to industrial decline and impending reorganization of the economy with ensuing closures of many unprofitable enterprises. The frustration and disillusionment of the working class has been made worse by the perversion of insider privatization which failed to give workers more control over production and make the administration more accountable to employees. Once the management amassed the controlling power over privatized firms, the workers became even more powerless than before.

The majority of the base stratum has limited strategies available for coping with hardships of the transition. Since they rarely possess valuable social networks and/or marketable skills they typically resort to more passive non-competitive forms of behaviour. The most widespread strategy is to keep employment at the enterprise even facing short time working, forced leave and wage arrears while seeking activities in informal economy. This includes in some cases unofficial commercial activity (shuttle and street trading) but even more often traditional forms of self-subsistence such as household food production on individual country plots.

Peasantry represents another big disadvantaged social group in all countries in transition. The cuts in subsidies to the agricultural sector combined with the strongly negative effect of price liberalization on inefficient farming led most farmers to particularly difficult financial straits. Price increases for energy, agricultural machinery and industrial inputs considerably raised the cost of agricultural products and undermined their competitiveness. The terms of trade changed dramatically in favour of urban residents. Agricultural producers faced demand constraints and intense competition from imports on the product markets. The incomes of farmers and farm employees fell more sharply in comparison with industrial workers. Economic hardships do not allow outdated machinery and farm equipment to be replaced. For all these reasons many regions experienced a profound decline in farm production. Some regions have considerable hidden unemployment in agriculture, resulting in a loss of wage income for the affected farm workers. Rural areas are also disadvantaged in possibilities for alternative employment and hence sources for additional incomes. Thus opportunities for the rural population to improve their well-being are extremely limited. In addition, there is a widespread collapse of infrastructure and social services in rural areas, which has always been far inferior to those of the cities. Rural poverty, however, is less acute in fertile regions, which are used for intensive farming, allowing household food production to provide adequate food products for rural families. Such self-subsistence virtually does not produce any cash income, so the livelihood of households in such regions may consist entirely of consumption of the harvest collected from private plots.

The agricultural sector has been more prepared for market reforms in Central European countries, Slovenia and the Baltics than in much of the FSU and SEE. Where rural residents have managed to establish themselves as individual farmers oriented to the market they have secured better material well being and higher social status. Agricultural reform in Russia and the FSU, however, proved much more difficult. The large-scale grain production there is still dominated by the collective sector, which, although having been reformed into joint-stock companies, remains quasi-market, and centralized. It is still based on fixed prices and depends on massive subsidies. The economic interests of the collective farmers are concentrated rather in their small private plots, which they use mainly for subsistence of their families and urban relatives. Purely private farms that have been allowed and emerged in limited numbers are not competitive to large collective farms. They prove unviable under existing circumstances due to underdevelopment of markets for commodities, land, services and labour. Moreover, the severe 'class competition' with collective farms unfolds not in favour of individual farmers. In Russia the latter are faced with hostility by rural communities due to deep-rooted collectivist traditions of communal land ownership of many past centuries (Starikov 1996). Psychological unreadiness of the rural population for market-oriented entrepreneurship combined with the dilapidated state of rural infrastructure does not present favourable prospects for rapid reforms and development in the farming sector and, thus, improvement in the social status of peasantry in quite a number of countries in transition.

Pensioners form a very important and numerous part of the local populace falling mainly into the base stratum of the social structure. They constitute about 40 per cent of the electorate and thus politically vocal and influential group. In Russia they number 36 million or 19 per cent of the population. Retirement pensions—which took the largest share of expenditure on social transfers—were in general better adjusted to inflation compared to other social benefits. This meant that any expansion of poverty among pensioners has not been further than for the population at large. Nevertheless the value of pensions in real terms has decreased resulting in substantial fall in living standards. In general, pensioners clearly consider themselves as losers, although they are at no higher risk of poverty than the population of working age. In some cases (e.g., Poland, Hungary and the Czech Republic) the pensioners seem to have done relatively well (Kramer 1997). The elderly have also been actively involved in housing privatization.

There are, however, wide variations in the positions of different groups of pensioners. Pensioners who are still employed (about 20 per cent of their total number in Russia) run virtually no risk of poverty. This risk is also significantly lower for the elderly who live in larger households together with their children. The situation is more difficult for households comprised purely of pensioners; however, two pensioners living together are less likely to be poor. Pensioners living alone are at the highest risk, and this increases further with age. There is also a gender difference among the elderly. For elderly females the poverty rate is nearly twice as high as that of males (44 per cent against 22.5 per cent by RLMS data on Russia) (World Bank 1995: 21), the latter representing less than a third of all the pensioners due to the considerably lower male life expectancy in Russia.

6.4 The poor: socially deprived and marginalized groups

Virtually no country in transition has escaped an increase in poverty, but in some of them it has been particularly dramatic. By the mid 1990s nationally determined poverty rates ranged from lower levels of 8, 14, and 16 per cent in Estonia, Hungary and Poland respectively to as high as 25 to 62 for the republics of the FSU (UNDP 1998: 12).

Poverty measurement itself presents a serious theoretical and political problem. Countries in transition generally utilize the absolute concept of poverty. Official poverty lines and estimates of the percentage of the population below it are based on income levels equal to official subsistence minimum. The calculation of that minimum is based on the cost of goods forming the minimal consumer basket. This cost of subsistence is regularly adjusted to inflation. These minima are often criticized as too low, particularly in Russia. Indeed the subsistence minimum contrasts sharply with people's perception of an adequate income, which is obvious from surveys of public opinion. The results of such surveys are heavily influenced by the specific situation where the average income has fallen sharply against a rapidly growing income disparity and the emergence of wealthy groups of the population. In their individual perception of a sufficient income, people naturally refer to standards typical of their previous rather than their current circumstances (McAuley 1994: 31) as well as to the living standards of the newly prosperous elites. A poverty rate for Russia based on individual perception of how much income is needed to provide for a minimum subsistence would be as high as 50-80 per cent of the population.

A number of socially vulnerable groups found themselves particularly disadvantaged under the new economic situation. This cluster of losers includes single parent families and households with many children or other dependants, single elderly pensioners, people with disabilities. These categories are disadvantaged in the labour market and critically dependent on social transfers. The decline of such transfers including family allowances, old age and disability pensions seriously affected the welfare of such households. They have formed the so-called group of the 'old poor' (meaning that the same group was affected by poverty in the prereform times). Similar social categories are found among the poor in other societies. Families with children are a majority among the poor while children are the largest demographic group affected by poverty.

The economic difficulties of the transition put additional stress on the family resulting in breakdown of family ties. The growth in the divorce rate has led to an increase in the number of poor children living in single parent families. The universal trend of growth of divorces, decline in the marriage rate and the rise in the number of children born out of wedlock (including higher incidence of teenage mothers), takes more acute forms and causes much greater hardship in countries under transition. A sole supporter is severely disadvantaged in the private sector labour market due to harsh time constraints imposed by childcare. Wages in the state sector jobs, if available, are too low to provide for a family. With lack of support from family members or relatives, opportunities to earn extra income in the informal sector for a single mother are also extremely limited.

Apart from socially vulnerable individuals or households low-income adults of working age and their families form a considerable group of 'losers' of the reforms. They fall into a large category of the 'new poor' including the 'working poor': low-paid job insecure workers, and the unemployed (Mikhalev 1997). The working poor are more frequently found in sectors with lowest paid jobs, in the first place in the state budgetary sector (education, culture and health care services), and other disadvantaged sectors, e.g. light industry or agriculture. By professional status low-qualified industrial blue-collar workers would be more likely to be poor. However, poverty has widely affected qualified workers and white-collar employees, e.g. engineers as well, particularly in heavy industry.

Since the poor in most of the countries in transition receive inadequate income support, they have to rely mainly on private safety nets, informal economic activities and traditional means of self-support, such as household food production. Private safety nets of relatives, friends and communities act as a most important means of poverty relief. Although such transfers do not go exclusively to lower income families they benefit such vulnerable groups as new households, elderly pensioners, female-headed households with many children, the disabled and those affected by unemployment (Cox *et al*. 1997). While in Russia intra-family transfers are much more important than assistance based on other than family ties, in Central Asia wider community networks are no less important as well. Although transfer behaviour tended to persist during the difficult reform years despite high inflation, the decline in incomes and the rise in inequality, its pattern is undergoing changes. In the prereform years younger families typically received transfers from their better-off parents. Nowadays it has become more common for elderly pensioners to get support from their children, including especially those engaged in new private businesses. In the latter case particularly, the recipients of such transfers are much less likely to represent a low-income or vulnerable group.

The hardships of the transition have increased the number of such specific categories of the poor as homeless, vagrants, and persons released from the penitentiary system. This group has been augmented by inflow of migrants (both internal and external) and refugees. Displacement of people is caused by economic reasons as well as by such factors as of disintegration of the Soviet Union, ethnic conflicts and civil wars. Migrants together with certain local ethnic minorities (e.g. gypsies) form specifically deprived marginalized groups.

Unlike in the Third World countries, the majority of the poor in transitional economies do not yet represent a clear underclass. By income level they are not so distant from average as for instance in Latin America. The poor still possess substantially high educational levels, reasonable dwellings and household assets and enjoy access to major social services, including schooling for children and health care. All of this does not differentiate them too much from the rest of the population (Milanovic 1998: 132). The decline in their income is still recent and looks as though it is a transitory shock. They could easily restore normal life, provided they can earn adequate income. However, for many in this group, ability to adjust to the new conditions, chances of retraining, starting new activities are generally limited. The growing incidence of long-lasting unemployment, transition of part of the unemployed to inactivity (documented by declining labour force participation rates), leads to deskilling and, hence, to loss of human capital with a high potential of social degradation. When poverty status persists over the long-term the poor are likely to acquire characteristics of an underclass which will make their way out of poverty still more difficult. The signs of such emerging underclass are already apparent, particularly in the countries of the FSU affected by mass poverty. In the Russian case long-term poverty has extended to at least 8 per cent of the population, which is a rough indication of the proportion of the severely deprived and marginalized group.

An overview of changes in social structures in transition reveals considerable reranking and redistribution of life chances for many social groups. The market has opened new opportunities, created new social classes and groups and intensified upward and downward social mobility. The most important outcome however has been an unprecedented rise in inequality and social polarization. Apart from economic decline the rise in inequality of income distribution has been a major factor of the expansion of poverty with all its negative consequences for human development. This apparent social dislocation bears dangerous prospects of loss of self-identity by part of the society, decline in solidarity and potential for rising social conflict. The processes of social stratification in transitional societies thus present serious challenges for policy, which is needed to promote social integration and social cohesion.

VII POLICY CONCLUSIONS: PRIORITIES FOR SOCIAL INTEGRATION AND SOCIAL COHESION

The evidence on social inequality and class formation reveals the need for polices which are capable of influencing the processes of social change. Such policies should pursue the goals of social integration and social cohesion. The gap between the rich and the poor, the economic and political power of the elite amidst massive deprivation of the impoverished population create a potential for social tension that may lead to disruptive outcomes. Furthermore, high inequality and poverty undermine human capital and thus erode the very base of sustainable development.

The priorities of poverty eradication, human development, and social integration, which essentially present the ultimate goal of market oriented reforms, underscore both distributional and efficiency objectives. The issues pertaining to the formation of the social structure lie in the political economy of income distribution and welfare systems. Policy implications stemming from the observed trends in social stratification entail trade-offs between inevitable inequality and social integration, broad-based growth, and poverty alleviation.

The task of policy in view of the evidence on inequality and its causes is viewed not so much as to curb the wealth of the elite, redistribute it to the poor and create a social safety net for the losers in the transition. The focus is rather on those policy choices, which encourage social mobility and investments in human capital. Consolidation of the middle class is considered as important objective as eradication of poverty. Therefore the primary attention of this study is on active policy measures promoting economically gainful employment, human capital, labour productivity and personal responsibility of citizens for their well being. These policies are believed to lead to widespread entrepreneurship, competition, co-operation, and development.

The role of the social safety net is understood as to provide support to the most needy citizens and vulnerable groups disadvantaged in the labour market. Discussion of safety nets in this study does not aim to give an overall assessment of welfare systems in transitional economies but rather to identify their proper role in social protection within the context of priorities of reducing inequality and poverty, and promoting social cohesion. While welfare may largely address the poverty of the weak and play a redistributive role, active employment policies, i.e., job creation, training, and SME support, target the working (or unemployed) poor. The goals of consolidating the middle class in turn highlight policy priorities in education, promotion of enterpreneurship, wages for professionals and public servants.

7.1 Promoting economic growth, stability and opportunities as a way to reduce inequality and poverty

While sustainable economic growth is a key to improvement of social welfare at large it may not automatically bring about more equitable distributional effects or improvements of the conditions of the poorest members of the society. Pro-poor orientation of economic growth requires consistent integrationist policies aimed at providing equal opportunities to all, spreading entrepreneurship, ensuring social mobility based on merit, preventing corruption and unlawful enrichment.

The analysis of social structures of the societies in transition has shown that policies conducive to social integration and social cohesion should address both the poor and the middle classes. Hence such policies cannot be reduced to distribution of poverty relief for the poorest. Promoting a solid productive middle class as the integrative core of the society requires a complex set of proactive socioeconomic measures aimed at creating opportunities for employment and business, developing human capital and marketable skills. The priority of proactive social policy is equally relevant to poverty alleviation. Given the structure of poverty the majority of the poor in transitional economies are normal households with working age able-bodied heads who are either working poor or unemployed. It appears that the greatest effect of poverty reduction can be achieved by effective employment and labour market policies rather than by expansion of safety nets. The main objective of such proactive policy agenda is to promote social mobility based on human capital, enterprise and creativity by citizens directed towards improvement of their well being.

7.1.1 Creating employment opportunities

The rise in inequality has largely been a result of increasingly unequal employment and earning opportunities, constraints on labour mobility, the spread of long-term unemployment. Therefore creation of employment opportunities figures as a key to major improvements in the social situation, in particular to growth of real incomes, their more equitable distribution and thus, to alleviation of social tension caused by frustration of a large section of the society seeing no prospects for the future.

Although employment opportunities are above all determined by economic growth there is a considerable scope for proactive employment policies promoting quality, competitiveness and mobility of labour. A set of required active policy measures includes specific employment programmes, training for the unemployed, support of small business, farmers, and individual economic activities.

Employment services were set up in all countries in transition, but everywhere this was a new institution with virtually no relevant prereform experience to draw on. Initially such services were more oriented to income support for the jobless through unemployment benefits. Assistance in job-seeking and job-matching was largely ineffective. Still less developed were active prolabour market services supporting job creation, self-employment and training. Employment services were burdened with bureaucracy, which further diminished their efficiency.

In most of the countries funds for labour market policies were concentrated in specially created national employment funds which became independent of ministries. Active employment policies were launched and budgetary allocations for active policies increased from initially negligible levels. In the Kyrgyz Republic, for instance, the relative expenditure of the Employment Fund on proactive labour market measures increased markedly from 4.2 per cent in 1993 to 29 per cent in 1997 (MLSP 1998: 34). Nevertheless the proportion of active policy measures everywhere is less than spending on pure safety nets for the unemployed. Moreover, the percentage of the unemployed participating in active policy programmes has been declining in some countries. In such countries known by strong social policy as the Czech Republic and Slovakia the number of clients of employment services benefiting from active programmes rather than unemployment benefits decreased from 38 per cent in 1991 to 12 per cent in 1996 and from 51 to 21 per cent respectively (Potucek and Radicova 1977).

The heavy reliance of employment services on unemployment benefits did little to reduce poverty, mitigate inequality and increase labour mobility. An overall assessment by Guy Standing (1997) based on the analysis of the situation in the whole region concluded that unemployment benefits were arbitrary, unfair and inefficient. They are too low and at the same time hard to obtain. Almost everywhere such benefits are below the subsistence income or poverty line, while in Russia, Ukraine or Kyrgyzstan they are equivalent to the minimum wage which is several times below subsistence minima. They put workers into unemployment and poverty traps as benefit recipients are unable to take low paid jobs legally for fear of losing entitlement. They do not offer a solution to income insecurity but rather intensify it (Standing 1977). Moreover, reforms in this area driven mainly by financial constraints were for the most part reduced to limiting benefits, thereby exacerbating insecurity and diminishing the role of income support for the unemployed as a safety net.

Employment policy objectives of promoting labour mobility, marketable skills, job creation and job-matching require a specific set of programmes and measures. One of the most urgent of them is strengthening job placement services of employment centres, i.e. in depth counselling, job finding incentives and job search assistance. Among others this requires:

- increased responsibility by employment centres in identifying vacancies;
- provision of independent access by the unemployed to databases of vacancies combined with counselling for those who experience severe difficulties in finding jobs;
- dissemination of information on job vacancies in mass media;
- promotion of job sharing between employees;
- encouragement of part-time working;
- creation of short-time or seasonal jobs, organization of public works.

Measures to promote employment for the youth are in particular need. These may include such tools as job fare or 'job vouchers'. The latter provides employers with incentives to hire young people for new jobs by way of direct wage subsidy or through some cuts in the social contributions their company is obliged to pay.

The experience of many countries, however, indicates that job placement services need to be combined with additional proactive programmes for the unemployed, such as: (i) recurrent training and retraining (ii) promoting small businesses (including self-employment); (iii) supporting employment promotion companies; and (iv) creating new jobs for the unemployed.

Among these diverse programmes and policies, training for the unemployed has possibly the highest priority since this is an important way of investing in labour skills and mobility. Therefore, if properly designed, such programmes may have the biggest and longest lasting effect. The experience thus far has not been very successful for various reasons, most importantly for lack of resources, poor programme design due to lack of experience resulting in mismatch between training offered and labour market demand, and bureaucratic hurdles. As a result job placement rates of trainees are generally low. This is particularly true for labour market training open to all unemployed and not targeted to specific labour market needs. Given particularly budgetary constraints recurrent training and retraining programmes would be more successful if they are well targeted, both to individual and to local labour market needs, and supported by occupational counselling and guidance services. Furthermore, desirable social effect of such programmes would be higher (even though the number of people placed in jobs may not be so high) if they focus on the most disadvantaged groups. Training should be offered in the first place to those unemployed who face particular difficulties in finding jobs, and among them—to those with long spells of unemployment. Such priorities would meet specific objectives of reducing inequality and poverty through promoting social mobility.

Equally important are job-creating activities. For obvious economic and financial reasons directly subsidized jobs may have only a limited scope but may be particularly effective for specifically vulnerable groups in the labour market such as young job seekers or disabled workers. Among job creation programmes greater attention should be paid to self-employment schemes and to socially useful public works. Such programmes should be designed and implemented in close collaboration with local governments, interested employers and initiatives by local communities. Public works can be organized by special employment promotion companies in situations of mass layoffs from closing enterprises. Participation in public works programmes gives the unemployed a short-term job and a small but stable income. As a result it helps to alleviate poverty and to overcome difficulties of unemployment. Innovative ways out of unemployment may be found in community building partnerships implementing area development projects, co-operatives, community businesses, home based family enterprises. Such initiatives are an important incentive to social mobility helping the unemployed to find their way from social dependency to economic independence.

7.1.2 Wages

The structure and determinants of poverty as concluded by McAuley and country case studies reveals that the majority of the poor are working and their poverty is caused by inadequate earnings. Therefore promoting employment may not be sufficient to reduce poverty unless wage levels guarantee incomes above the poverty line. Thus wage policy is another essential component of a strategy directed towards social integration. At the same time correction of distortions in the wage structure is a major way to reduce inequality since the latter has been primarily driven by earnings disparity (Cornia 1999).

In transitional economies employment cannot yet guarantee adequate remuneration covering the cost of essential goods and services. These economies are facing a fundamental structural problem of real wage readjustments. Under socialism wages were low because such essential social services and benefits as healthcare, education, childcare and housing were provided free of charge or at very low cost. During the transition real wages have drastically declined and with the exception of Central Europe have not recovered their prereform level. To ensure that employment guarantees an income above poverty, labour costs have to be adjusted upwards if many previously available social services and housing are to be purchased under market conditions.

Another significant issue pertaining to wages and living standards lies in changes in labour force participation. Declining employment of women signifies transition from two-income families, typical of the prereform times, to one-income families, widespread in many developed market economies. Thus the wage of a sole breadwinner in the family has to increase in order to afford a decent living standard for his/her household.

Approaches to regulation of the wage spread and wage settlements include regulatory policies to stimulate market competition, ensure returns to human capital and correct interindustrial wage differentials not justified by productivity. The pivotal task is to abolish unreasonable differentiation of wages and salaries and in the first place its declined level in the budget sector, including those employed in the government administration, public health, education, science and culture. In the countries of the CIS and SEE skilled specialists employed in the budgetary sector, and among them teachers and doctors, who normally belong to the middle class, turned out to be among the lowest income groups. Wage increase in the budget sector seems to be one of the urgent tasks on poverty alleviation. It also meets the objective of consolidating the middle class.

The correction of wage distortions should be initiated by the increase of minimum wages. The minimum wage has long ceased to play a real regulating role in the labour market. It also lost a function of income security guaranteed by the state. Instead it has been used as a benchmark for scaling various social benefits. The link between the statutory minimum wage and social benefits effectively blocks reform of both the wage system and social transfers since any decision to increase the minimum wage entails adjustment of social benefits as well, and the latter proves impossible due to budget constraints. Delinking social benefits from the minimum wage would allow increasing minimum wages gradually to national subsistence minima.

With regard to employment and wage policies there is considerable scope for a greater role played by 'labour institutions', i.e. union representation in wage negotiations, and regulation of minimum wages and pay levels in the social and monopolistic-rent sectors. This trend may be sustained in those countries aiming to be associated with the European Union which will require them to introduce policies similar to those followed in the union.

Such prospect is less certain for other transitional economies. If labour institutions there continue to be eroded, it would perpetuate long-term open unemployment and the spread of part-time insecure jobs, greater earnings dispersions, and the massive numbers of working poor.

7.1.3 SME support

The sector of small businesses and self-employment has a great potential to contribute to the growth of employment, social mobility and thus to reduction of inequality and poverty. Simultaneously development of small- and medium-scale entrepreneurship is a major way of generating and consolidating the middle class. Mass development of private small business and entrepreneurship provides powerful incentives for economic and labour activity of the population, citizens' responsibility for their own welfare, i.e. increasing socioeconomic independence and reducing dependence on state social support. The SME sector can strengthen the social insurance system and social protection through payments of insurance contributions and taxes into the budget and public insurance funds. It will facilitate the integration of informal sector activities into the formal economy, which means an increase in the number of tax and contribution payers. All this would bring large positive effects conducive to social integration and social cohesion.[4]

The environment favourable to SME development on the whole depends on overall macroeconomic situation, investment climate, market-friendly legislation and law enforcement (UNDP 1998: 171). Apart from these strategic priorities a set of micro level support measures for SME is highly needed, in the first place in the area of training in business management and provision of credit lines. These policy priorities can be summarized as follows.

- It is necessary to develop services providing consultation, information and training for all kinds of businesses (including help in developing business plans among others). Training in business in educational institutions, in various specific courses should meet the new market economy requirements, develop entrepreneurial culture and high quality standards of products and services.

- Legislation stimulating entrepreneurial activity is extremely important. Clear, accurate and simplified registration and licensing procedures are required in order to speed up the development of the SME sector, including stable regulation of ownership rights, simplified taxation rules and effective contract enforcement.

- Small businesses cannot start off and survive without access to credit resources. Apart from developing the financial sector at large special credit programmes targeted to SME are necessary. For mircobusinesses and self-employed individuals special micro credit schemes prove most effective. The purpose of such programmes is to provide credit and financial services to SMEs, which have no access to commercial credit due to inability

[4] An extensive analysis of policies promoting the SME sector development in transitional economies was done within the UNU/WIDER project on Transition from Below: the Role of the New Private Sector, directed by Robert J. McIntyre (McIntyre 1999).

to meet many banking requirements, such as deposits, and well developed business plans.

- Setting up business incubators will help newly created businesses with access to premises and public utilities (heating, electricity, communications), administrative assistance; consulting support and business expertise, including assistance in setting up businesses (which are most vulnerable at the very initial stage).

7.1.4 Agricultural policies and support for rural population

Country case studies revealed that rural residents have been disproportionately affected by hardships of the transition. They represent a considerable group (in SEE, Caucasus and Central Asia—the largest group) among the poor. Therefore policies oriented to social integration and social cohesion must have a critical objective elimination of rural poverty and support of rural livelihoods. Agricultural reforms have not been successful so far in creating a private sector-led farming system. While large state and collective farms have been either dismantled or virtually collapsed individual farmers proved for the most part unviable without effective support by the state under dire economic conditions. Subsistence farming as a most common and only available option for large sections of rural populations does not offer a way out of poverty and cannot generate a steady growth of rural economies. Revitalization of rural communities as an essential condition of social integration at large requires consistent government policies in support of the agricultural sector, farmers and rural economy as a whole.

The following major policy directions aimed at poverty alleviation in rural areas can be highlighted.

- Land reforms should be completed and property rights made clear, including regulations for purchases and sale of land. In areas where holdings are small and fragmented government intervention is required to bring about land consolidation (e.g. measures to encourage lease of peasants' small plots to stronger farmers capable of organizing larger scale and more efficient production).

- Non-agricultural employment should be promoted in rural areas in food processing industry, infrastructure, and services for farmers and rural residents.

- State assistance to farmers is needed in access to machinery and equipment, advanced technologies, consulting services.

- Agricultural marketing system needs to be restored and restructured to meet the needs of individual farmers, including wholesale markets and state marketing channels.

- More favourable conditions for agricultural producers should be created via improving the taxation system.

- Credit needs of farmers should be met by development of credit unions and microfinance schemes for farmers, including special insurance arrangements.

7.2 Promoting human capital and access to social assets

Creation of equal opportunities requires investments in human capital, especially for the poor. The highest priority is guaranteed access to essential assets and services such as housing, education and training, medical care, and to basic cultural goods and services. The development of an educational system, in particular, has a crucial role in providing equal opportunities as a key road to social integration.

The health of the citizens is an important asset and basis of welfare, and an overall access to health care services forms a necessary condition for poverty alleviation. A major task of the state is to guarantee access and a basic range of free health care and medical services in public health institutions through budgetary funding. Compulsory medical insurance systems introduced in many countries may serve as a base to widen the range of free medical services—for low-income citizens, in particular. High priority has to be dedicated to the development of mass preventive healthcare: immunization campaigns, sanitary and anti-epidemiological programmes embracing all low-income citizens and funded by public budgets. Maternity and childcare programmes too have a high priority for poverty alleviation.

Housing used to be a key social asset available to citizens under state socialism. Reforms in this sector currently under way have been limited to privatization of housing by residents and gradual elimination of rent and utility subsidies. The outcome has been that housing has virtually ceased to be a part of state provided welfare. Privatization and marketization in this sector has contributed to high income and asset inequality. At the same time housing markets remain underdeveloped. For the majority of the population access to rental accommodation is limited due to low-income inadequate to pay a market rent, while a system of mortgage loans, which would allow purchase of a house or an apartment for medium-income households, is practically non-existent. Such housing situations greatly impede geographical mobility of labour, thereby exacerbating unemployment. Housing policy meeting the new conditions of the market economy is therefore an essential part of a development strategy aimed at poverty alleviation and social mobility. Such policy presumes provision of affordable social housing for the poor and measures for the development of housing market, including widely available mortgage loans.

7.2.1 Education

Education has probably the greatest role to play in forming social structures as it provides a major investment in human capital. Studies have shown that both income levels and social status at large strongly correlate with the level of education. People with higher education and particularly with marketable skills have done their best in the course of the transition and formed the ranks of winners of the reforms. On the other hand workers with low levels of skill happen to be the most disadvantaged and thus are found largely among the losers. Education and skills appears to be key determinants of individual success in the new market economy. They are therefore the prime engines of social mobility.

Ensuring access to education and simultaneously reforming education in order to meet the needs of the market economy figure as strategic measures serving the goal of poverty eradication and social integration in the longer run. Education and training offer a way out of poverty and guarantee that the children of today's poor avoid poverty. At the same time education is an essential factor of consolidating the middle class as a class of professionals and entrepreneurs.

With regard to the above objectives the following key problems are to be addressed in the educational sector.

(1) The general erosion of the educational system due to the lack of budgetary funds has led to a decline in education and coverage with a real possibility of illiteracy to re-emerge. This threat is particularly acute in Central Asia and the Caucasus. Therefore more resources need to be mobilized to meet educational needs through redistribution of budgetary funds and by promoting the private sector in education.

Difficulties in acquiring clothes, shoes, textbooks and food are reasons for dropouts and declining school attendance by children from poor families. More children are compelled to quit school due to the widespread use of child labour, disruption of family ties, as well as increasing social and economic difficulties of many families.

In order to prevent dropping out the role of the school as a social protection institution has to be strengthened. Thus, access to primary and secondary education for poor children must be ensured by means of targeted social support addressing the causes of school dropouts and creating incentives for going to school. Furthermore, school meals should be provided and free uniforms and textbooks distributed, in order to prevent non-attendance of poor children. Schools, working in daily contact with children, have the most precise and extensive information on families, which need help. Thus, they are in the best position to identify children's real needs.

(2) Emerging inequalities in higher education deny access to training and skills for the poor and disadvantaged groups. Thus appropriate policies are needed to guarantee such access to the poor, rural residents, children of large families through specific targeted measures. Such access opportunities based on merit should be provided within the publicly funded educational system.

Young people, who completed nine years in a secondary school should receive a state guarantee of primary vocational or technical training. Young job seekers with incomplete secondary education and no vocational training have little opportunities in the labour market and thus run a high risk of unemployment and poverty. Therefore, the state has to guarantee equal start up conditions for young people entering an occupational career.

(3) Reforms in school curricula are needed to meet the requirements of human capital development and demand for skills in the market. Serious adjustments are necessary first of all in the too narrowly specialized vocational training. Vocational schools should introduce more demand-driven and shorter-cycle courses.

(4) While ensuring merit-based access to publicly provided higher education there is a need to offer more options to the better off part of the population for high quality education. This can be achieved by attracting private funds to expanding private sector educational services, which cater to the needs of the wealthier middle classes.

(5) Special care and necessary financial support must be provided to orphan children. This task requires implementation of special programmes for development of orphanages and boarding schools for orphans, as well as for social integration, vocational training and employment of these school graduates.

(6) It is also necessary to ensure access to preschool education for children of low-income families through adequate financial state support. Here too private services should be expanded in order to augment scarce public resources and offer more options for pre-primary school coverage, which is an important component of strategic investments in human capital of the future generation.

7.3 The social safety net

While policy priorities for social integration and social cohesion focus in the first place on proactive measures promoting social mobility and personal responsibility of citizens for their well-being, they should be combined with social assistance targeted to vulnerable groups. The welfare of large sections of the population depending on social transfers, in the first place, pensioners, the disabled, families with many children, has been affected by erosion of real value of most social benefits. While in Central Europe more vigorous attempts to increase or index some benefits helped to maintain living standards of these groups of the population, in the CIS countries most benefits were allowed to devaluate to extremely low levels (Nelson 1997). In Russia the average pension barely kept up with the official poverty line, unemployment benefits averaged about 15 per cent of the average wage and family allowances equaled to only 18 per cent of the subsistence minimum for a child. Obviously, people depending on those benefits cannot escape poverty without other forms of support.

The present system of social services and benefits, even in the countries where it is far from generous (like in Russia), is unsustainable and needs to be reformed in order to face the challenges of transition to the market. Since pension systems everywhere occupy the largest share of social transfers the need for reforms is the most urgent with pension systems. But pensions generally do not mean to be targeted to the poor and to be redistributive. Thus other types of social benefits are needed specifically for purposes of poverty alleviation.

Most transitional countries have no country-wide systems of social assistance especially for the poor. The design and implementation of programmes for poverty relief takes place at local levels and is regionally specific. Assistance is provided according to both income and categorical criteria. Usually recipients of poverty relief should not only have an income below the poverty line but also meet other criteria such as three or more children in the family, single-parent households, presence of disabled or elderly family members, etc. In all such cases social assistance is still offered temporarily and is most often provided in kind (e.g. hot meals or food vouchers, medicines, help in looking after children, payment for kindergartens, help to repair a house). The amount of support depends on the availability of funds in local social security budgets and on the judgement of a local social worker. Such assistance does not aim to cover the difference between the poverty line and actual income (Milanovic 1998: 116).

One possible approach to alleviating poverty is to move toward the West European model and introduce a benefit to all those whose incomes fall below the poverty line (and who have less than a certain level of assets). The amount of such a benefit would mean to cover the entire gap between the poverty line and actual income. No country in Eastern Europe has such a system, although the Czech system is apparently closest to it (Milanovic 1998: 115).

Given the scarcity of budgetary funds several countries attempted to introduce stronger targeting of social assistance. Experience in operating targeted social assistance programmes, e.g. in Kyrgyzstan shows that: firstly, introduction of income testing without prior experience and administrative framework is costly and organizationally difficult. Countries affected by mass poverty are unable to carry out such programmes without financial and technical assistance. Secondly, it is impossible to monitor full households' incomes due to widespread informal activities and forms of support. Attempts to refine means testing to make it more sophisticated greatly increase the cost of administering the benefit programme. Therefore reliance of self-targeting is preferable but it must be nevertheless supported by reasonable procedures of verification of the household welfare situation. Thirdly, social security budgets are unable to provide adequate funding to fully fill the poverty gap. Targeted poverty relief can only alleviate most acute poverty but it is unlikely to bring about significant reduction of the proportion of the poor.

Targeted social assistance may be effective only when the number of claimants is relatively low. The key economic variables including the minimum wage, the minimum pension, minimum unemployment benefit, maternity and childcare benefits are to be set up at adequate levels, so that most of their recipients cannot be candidates for social assistance. A lot here also depends on the wage reform, first of all in the budgetary sector. If such potentially active families no longer need social assistance the number of benefit recipients would be considerably reduced. Then assistance would be targeted to those really vulnerable among low-income families, in which, for instance one parent is unfit for work. In that case benefits might considerably increase and will indeed insure protection. In other words, strengthening of targeting of social assistance mostly depends on effectiveness of proactive social policy measures.

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Sustainable development, social integration and social cohesion to a very great extent depend on the success in the fight against poverty. Many of the policy priorities for poverty alleviation have been outlined and discussed in this study. These priorities figure in policy programmes and documents of national governments and international organizations, such as UNDP, UNICEF, ILO, and the World Bank. Somewhat less attention has been accorded to policies supporting the middle class. Meanwhile formation of a new broad middle class is closely interrelated with mass poverty alleviation and, therefore social integration and social cohesion. Such a middle class type forms an essential core of the society closely related to education, science, culture and thereby generating socioeconomic progress for the country as a whole. Wherever the government policy is aimed at dovetailing the capital onto production, entrepreneurship is oriented to the production of material values. Hence there is a greater need of knowledgeable staff, high-qualification workers, researchers and people of the arts. That is to say, the dormant potential of the 'middle class' is put to use. Where this social group is broad enough they would serve as guarantor of social welfare and the impossibility of another redistribution of property, they provide a major source of budgetary revenues and vote for efficient reforms thus ensuring the continuity of the transition.

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