THE SOCIAL IMPACT OF INFORMAL ECONOMIES IN EASTERN EUROPE (TRANSITION AND DEVELOPMENT) pdf

1: Transition economy - Wikipedia

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This may be the greatest social cost of the central planning pension legacy. Most countries envision leaving the pensions already granted to current pensioners as is with some form of purchasing power guarantee, either partial or full , as the politics of taking away a benefit already granted are almost insurmountable. In demographically mature countries, old-age security systems should achieve the following goals: Prevent poverty in old age. Assist with income smoothing by supporting savings and insuring against the risk of long life. Equitably support economic growth and development. While the systems of the post-communist states have been effective in preventing old-age poverty during the transition, they have done so at a cost, as discussed above, and thus have not contributed to the third goal above. The high and growing number of the aging relative to workers means that this cost will only continue to rise. By relying on pay-as-you-go funding, these systems have also not encouraged savings. Based on an analysis of pension systems around the world, the World Bank recommends a combination of pay-as-you-go and funded pension systems. Pillar 1â€"a mandatory pay-as-you-go public pension system designed to provide an income floor for all elderly persons Pillar 2â€"a mandatory funded and privately managed pension systemâ€"one whose current reserves are equal to or greater than the present value of all future pension payment liabilities, based on personal accounts the Latin American approach or occupational plans the OECD approach Pillar 3â€"a voluntary system also funded and privately managed , with strong government regulation, to provide for additional savings and insurance. For a critique of these recommendations, see Beattie and McGillivray James offers a response. Page Share Cite Suggested Citation: Transforming Post-Communist Political Economies. The National Academies Press. The post-communist states need to place greater reliance on prefunding of pension obligations with private management of reserves to 1 smooth out contribution rates as the "baby boomers" retire, and 2 deepen capital markets, and thus enhance growth, through the development of a contractual savings industry. The main difficulty in applying these recommendations in transition economies is that prefinancing in a mature pay-as-you-go system implies that the members of one generation must bear an additional burdenâ€"saving for their own retirement while simultaneously paying for that of their parents. In the typical post-communist system, governments can reduce future entitlements by the following means: Raising the effective retirement age eliminating early retirement and raising the normal retirement age Changing the formula to lower the average benefit Reducing indexation provisions to, for example, the lower of wage or price increases Prefunding can be achieved in the public system only by building up a reserve fund. The World Bank recommends that these reserves be allocated to individual accounts the Latin American approach , as this reduces the "taxation" element of the public pension system, thereby reducing labor market distortions. It also improves the management of the reserves. Funding can also begin through the development of optional, privately managed programs private pension systems. Few governments in Eastern Europe have tackled this entire agenda. All of the Baltic countries, Albania, Georgia, and the Czech Republic have tackled major parts of it, with some success. Of these, only Latvia and Georgia have adopted radical pension reforms. While Lithuania, the Czech Republic, and Estonia have been able to avoid the kinds of pension cost explosions faced by Poland, Bulgaria, and Slovenia, even the former three countries are experiencing steady growth in expenditures, as they have simply not reformed entitlements sufficiently. Estonia was able to implement a steady increase in retirement age, but left in place all the exemptions from the Soviet period, even adding a few. Lithuania and the Czech Republic courageously eliminated almost all early retirement, but chose generous formulas as they attempted to return to the status quo ex ante. Lithuania and Estonia have also 4 Strictly speaking, the savings of the working generation is not a "burden" since the money saved will come back to them later. Saving represents postponed consumption, however, which has a cost. Were the members of this generation able to obtain from future generations the equivalent on a per capita basis to what they are transferring, they would be better off than under a reformed approach that includes more funding and less reliance on current transfers. However, this is an unrealistic scenario. Hungary and the Czech Republic were the pioneers in starting private pension systems, demonstrating that transition capital markets can respond to a supply of long-term funds. In the Czech Republic, where subsidies are offered as an alternative to tax concessions, roughly 20 percent of the labor force is now participating in these programs. Russia and the Baltic countries hope to follow their lead shortly. In other countries, the strategy has been to muddle through, hoping that a resumption of economic growthâ€”including growth in real wages and improved tax systemsâ€”will solve the problem. Why has reform proven so difficult? First, the claims of current pensioners have not been resolved. Their pensions were originally based on some kind of earnings-related formula and barely replaced their monetary income. The policy response during hyperinflation e. Most pensioners are not happy with this, and oppose pension reforms even though pensions are untouched. While the macroeconomics of fiscal stability and growth suggest that future entitlement payments should be reduced and savings by the current working generation increased, the political agenda is often quite different. Second, the weaknesses of the system are poorly understood by most of the voters. Pay-as-you-go systems are inherently nontransparent, which is why reform is so difficult. Until a crisis occurs, most pensioners imagine that their contributions have been placed somewhere safe, that their entitlement is actuarially fair, and therefore that they are entitled to their benefits. After years of central planning, most of the active and retired populations are used to thinking of income as an obligation of the state and are unaware of the issues identified above. And of course, those groups entitled to special early retirement provisions want to keep them. In short, there is not yet a constituency for reform. The active population has not focused on the cost of this system to them, as the contributions are paid by their firms. Even among policymakers, the depth of the problems is poorly understood. The extent to which the post-communist systems are at variance with both Western European systems and the systems of countries at their income level is not well known. And even in the high-income welfare states, public pay-as-you-go systems are facing pension financing crises. Innovation and risk taking will be needed to move forward on this ambitious agenda of reform. Over the last year, a handful of countries have been developing major reforms that involve prefunding through a mandatory second pillar. In Hungary and Croatia, the governments have decided in principle to create a mandatory second pillar, despite the painful reductions this will Page Share Cite Suggested Citation: Similar proposals are also circulating in Poland and the Czech Republic. In , the Latvian government became the first in Eastern Europe to enact a radical reform of the system, including a commitment to developing the second tier for the purposes of prefinancing. Latvia achieved this goal by adopting a whole new approach to the benefit formula. The remainder of this chapter discusses that reform and draws from it lessons for further reforms. An initial reform of the Soviet system was undertaken in But the reformed system left in place most of the Soviet eligibility conditions retirement at age 55 for women and age 60 for men, with earlier retirement permitted for certain occupations and categories of people. The benefit formula provided a flat guarantee of 30 percent of the national average wage, with an increase of 0. By July , the average old-age pension was 33 lats, or 50 percent of the average net wage pensions are not taxable. This formula implied full wage indexing for pensions, although in practice this indexing did not take place when revenues were inadequate. In January , the government submitted to Parliament a new pension reform concept, calling for the introduction of a three-tier system. The first tier would be a modified pay-as-you-go system, with stronger links to contributions and a minimum pension to protect the lifetime poor. The second tier would be a mandatory, funded system of privately managed savings accounts. Participation would be limited to new entrants and the younger members of the current labor force. The third tier would be voluntary, privately managed pensions, organized primarily but not exclusively through employers. The new concept was accepted by Parliament, and work began immediately on the first stage of the reformâ€”new legislation for the first tier. This legislation was submitted to Parliament in July and approved in November as part of the package of welfare system reforms. The new system took effect in

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January The new public pension system has two main elements: Provision is made for introduction of the second tier. Beginning in , contributors will have the option of assigning a portion of their contributions to privately managed individual savings accounts. This will result in a partial funding of the system, reducing the debt for future generations. It is designed to mimic the contribution-based pension that would be offered in the private sector by an efficient insurance company. The system starts by giving an account to everyone paying the social tax. As contributions earmarked for the pension system are paid, the account is credited as if it were a savings account. The "capital" in the account earns a rate of return just as a savings account would. This rate of return is equal to the growth of the sum of wages on which contributions are collected the contribution wage base. For example, if a person has 10, lats in his or her account at retirement and is expected to live 10 more years, the pension will be lats per year or 83 lats per month. The pension will be indexed, adjusting for price changes. However, each contributor gets an annual statement showing the capital in his or her account. A table of average life expectancy at retirement called the G-value is also published every year by the government. Since life expectancy changes very slowly, and the amount of capital in the account is known, those nearing retirement can roughly estimate their future pensions as they did under the old system. In the new system, there is no mandatory retirement age and no "full pension. However, the system provides strong incentives to work longer. Longer working years will shorten the number of payments, allowing each to be higher, and increase the initial capital. As a result, assuming a constant wage, the pension will double when an individual works until age 70 instead of The new system also includes a minimum guaranteed pension for all those who reach the age of This minimum is set at the level of the social pension, a social assistance pension for those adults who were disabled at birth. The social assistance pension is also available to those who reach the age of 65 but do not have 10 years of service. The nominal level of the social pension is set by government. It is currently 25 lats 60 percent of the average pension and 20 percent of the average wage. Once the second tier is in place, the minimum will include both first- and second-tier funds, providing a floor under the total pension. Transitory provisions in the new law gradually enforce the minimum retirement age of Some politically sensitive exceptions remain, including a provision for early retirement at 55 for women and a few occupations e.

2: Chapter Trade and economic reform in transition economies[]

Presenting research on the importance of informal economies, especially in Bulgaria, Hungary, Romania and Russia, the editors give a short introduction for each country and a common compilation of.

Soviet-type economic planning The economic malaise affecting the Comecon countries â€" low growth rates and diminishing returns on investment â€" led many domestic and Western economists to advocate market-based solutions and a sequenced programme of economic reform. It was recognized that micro-economic reform and macro-economic stabilization had to be combined carefully. Price liberalization without prior remedial measures to eliminate macro-economic imbalances, including an escalating fiscal deficit, a growing money supply due to a high level of borrowing by state-owned enterprises, and the accumulated savings of households " monetary overhang " could result in macro-economic destabilization instead of micro-economic efficiency. Unless entrepreneurs enjoyed secure property rights and farmers owned their farms the process of Schumpeterian " creative destruction " would limit the reallocation of resources and prevent profitable enterprises from expanding to absorb the workers displaced from the liquidation of non-viable enterprises. A hardening of the budget constraints at state-owned enterprises would halt the drain on the state budget from subsidization but would require additional expenditure to counteract the resulting unemployment and drop in aggregate household spending. Monetary overhang meant that price liberalization might convert "repressed inflation" into open inflation, increase the price level still further and generate a price spiral. The transition to a market economy would require state intervention alongside market liberalization, privatization and deregulation. Rationing of essential consumer goods, trade quotas and tariffs and an active monetary policy to ensure that there was sufficient liquidity to maintain commerce might be needed. The strategy was strongly influenced by IMF and World Bank analyses of successful and unsuccessful stabilization programmes which had been adopted in Latin America in the s. The strategy incorporated a number of interdependent measures including macro-economic stabilization; the liberalization of wholesale and retail prices; the removal of constraints to the development of private enterprises and the privatization of state-owned enterprises; the elimination of subsidies and the imposition of hard budget constraints; and the creation of an export-oriented economy that was open to foreign trade and investment. The creation of a social safety net targeted at the individual to compensate for the removal of job security and the removal of price controls on staple goods was also part of the strategy. Policy-makers were persuaded that political credibility took precedence over a sequenced reform plan and to introduce macro-economic stabilization measures ahead of structural measures that would by their nature take longer to implement. The "credibility" of the transition process was enhanced by the adoption of the Washington Consensus favoured by the IMF and the World Bank. Western advisers and domestic experts working with the national governments and the IMF introduced stabilization programmes aiming to achieve external and internal balance, which became known as shock therapy. It was argued that "one cannot jump over a chasm in two leaps". They favoured free trade and exchange rate convertibility rather than trade protection and capital controls, which might have checked capital flight. They tended to support privatization without prior industrial restructuring; an exception was to be found in Eastern Germany where the Treuhand Trust Agency prepared state-owned enterprises for the market at considerable cost to the government. It had been expected that the introduction of current account convertibility and foreign trade liberalization would force a currency devaluation that would support export-led growth. Consumers reacted by reducing their purchases and by substituting better quality imported goods in place of domestically produced goods. Falling sales led to the collapse of many domestic enterprises, with personnel lay-offs or reduced hours of work and pay. This further reduced effective demand. As imports grew and exporters failed to respond to opportunities in world markets due to the poor quality of their products and lack of resources for investment, the trade deficit expanded, putting downward pressure on the exchange rate. Many wholesalers and retailers marked prices according to their dollar values and the falling exchange rate fed inflation. The central banks in several countries raised interest rates and tightened credit conditions, depriving state agencies and enterprises of working capital. These in turn found it impossible to pay wages on time, dampening effective demand further. Economic output declined much more than expected. The decline in output lasted until for all transition economies. By , economic output had declined across all transition economies by 41 percent compared to its level. The Central and Eastern European economies began growing again around , with Poland, which had begun its transition programme earliest emerging from recession in The Baltic States came out of recession in and the rest of the former Soviet Union around Inflation remained above 20 percent a year except in the Czech Republic and Hungary until the mids. Across all transition economies the peak annual inflation rate was percent percent in the CIS. Labour force surveys undertaken by the International Labour Organization showed significantly higher rates of joblessness and there was considerable internal migration. Local-manufactured higher quality consumer goods became available and won market share back from imports. Stabilization of the exchange rate was made more difficult by large-scale capital flight, with domestic agents sending part of their earning abroad to destinations where they believed their capital was more secure. Some economists have argued that the growth performance of the transition economies stemmed from the low level of development, decades of trade isolation and distortions in the socialist planned economies. They have emphasized that the transition strategies adopted reflected the need to resolve the economic crisis besetting the socialist planned economies and the overriding objective was the transformation to capitalist market economies rather than the fostering of economic growth and welfare. Although the foundations had been laid for a functioning market economy through sustained liberalization, comprehensive privatization, openness to international trade and investment, and the establishment of democratic political systems there remained institutional challenges. Liberalized markets were not necessarily competitive and political freedom had not prevented powerful private interests from exercising undue influence. Growth in the transition economies had been driven by trade integration into the world economy with "impressive" export performance, and by "rapid capital inflows and a credit boom". But such growth had proved volatile and the EBRD considered that governments in the transition economies should foster the development of domestic capital markets and improve the business environment, including financial institutions, real estate markets and the energy, transport and communications infrastructure. The EBRD expressed concerns about regulatory independence and enforcement, price setting, and the market power of incumbent infrastructure operators. Poverty re-emerged with between 20 and 50 percent of people living below the national poverty line in the transition economies. The UN Development Programme calculated that overall poverty in Eastern Europe and the CIS increased from 4 percent of the population in to 32 percent by , or from 14 million people to million. In other words, it took nearly 20 years to restore the level of output that had existed prior to the transition. The slowdown hit government revenues and widened fiscal deficits but almost all transition economies had experienced a partial recovery and had maintained low and stable inflation since Some nations have been experimenting with market reform for several decades, while others are relatively recent adopters e. In some cases reforms have been accompanied with political upheaval, such as the overthrow of a dictator Romania , the collapse of a government the Soviet Union , a declaration of independence Croatia , or integration with another country East Germany. In other cases economic reforms have been adopted by incumbent governments with little interest in political change China , Laos , Vietnam. Some countries, such as Vietnam, have experienced macro-economic upheavals over different periods of transition, even transition turmoil. Mr Tanzi stated that these spending programs must be financed from public revenues generatedâ€”through taxationâ€”without imposing excessive burdens on the private sector. These outcomes had not yet been achieved by and progress in establishing well-functioning market economies had stalled since the s. Price liberalization, small-scale privatization and the opening-up of trade and foreign exchange markets were mostly complete by the end of the s. However economic reform had slowed in areas such governance, enterprise restructuring and competition policy, which remained substantially below the standard of other developed market economies. The highest inequality of opportunity was found in the

Balkans and Central Asia. In terms of legal regulations and access to education and health services, inequality of opportunity related to gender was low in Europe and Central Asia but medium to high in respect of labour practices, employment and entrepreneurship and in access to finance. In Central Asia women also experienced significant lack of access to health services, as was the case in Arab countries. These gains had been driven by sustained growth in productivity as obsolete capital stock was scrapped and production shifted to take advantage of the opening-up of foreign trade, price liberalization and foreign direct investment. The report acknowledged that the academic literature was divided on whether economic development fostered democracy but argued that there was nonetheless strong empirical support for the hypothesis. It suggested that countries with high inequality were less inclined to support a limited and accountable state. Those countries with large natural resource endowments, for example oil and gas producers like Russia and Kazakhstan, had less accountable governments and faced less electoral pressure to tackle powerful vested interests because the government could rely on resource rents and did not have to tax the population heavily. Countries with a strong institutional environment â€” that is, effective rule of law, secure property rights and uncorrupted public administration and corporate governance â€” were better placed to attract investment and undertake restructuring and regulatory change. Open-up trade and finance, which made reform more resilient to popular pressure "market aversion" and meant that countries could access the EU single market either as member states or through association agreements such as those being negotiated with Ukraine, Moldova and Georgia ; Encourage transparent and accountable government, with media and civil society scrutiny, and political competition at elections; Invest in human capital, especially by improving the quality of tertiary education. There are countries outside of Europe, emerging from a socialist-type command economy towards a market-based economy e. Moreover, in a wider sense the definition of transition economy refers to all countries which attempt to change their basic constitutional elements towards market-style fundamentals. Their origin could be also in a post-colonial situation, in a heavily regulated Asian-style economy , in a Latin American post-dictatorship or even in a somehow economically underdeveloped country in Africa.

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3: The Social Impact of Informal Economies in Eastern Europe: 1st Edition (Hardback) - Routledge

'The post-communist transition in Eastern Europe is generating a variable and changing range of new forms of informal and underground economy. This book is one of the first attempts to explore the phenomenon and a very useful tool for understanding the present transition in eastern European societies.

Some Lessons from the World Bank Enterprise Survey The aim of this paper is to evaluate the variable impacts of the informal economy on businesses and employment relations in South East Europe. The finding is not only that a large informal sector reduces wage levels but also that there are significant spatial variations in the adverse impacts of the informal economy across this European region. Small, rural and domestic businesses producing for the home market and the transport, construction, garment and wholesale sectors are most likely to be adversely affected by the informal economy. The paper concludes by calling for similar research in other global regions and for a more targeted approach towards tackling the informal economy. Size, Causes and Consequences of the Underground Economy: Investment Climate Around the World: Bank competition and access to finance: Journal of Money Credit and Banking 36 3: Informal farm work in North Western Bulgaria and eastern Serbia. Tax policy in emerging countries. Environment and Planning C 26 1: The forms of capital. Corruption and the shadow economy: Like oil and vinegar, like water and fire? John Hopkins University Press, Centre for the Study of Democracy. Levelling the playing field in Bulgaria: The informal economy in Bulgaria: Undeclared work in the Republic of Cyprus http: Cross J and Morales A eds Street entrepreneurs: The underground economy and its macroeconomic consequences. Journal of Policy Reform 8 2: Informal economy, tax evasion and poverty in a democratic setting: Mediterranean Quarterly 18 2: The Mystery of Capital: Johannes Kepler University of Linz. How do institutions affect corruption and the shadow economy? The shadow economy in transition countries: World Development 30 7: Communication of the Commission on Undeclared Work. Stepping up the fight against informal employment. European Industrial Relations Observatory. Informal Economic Activities and Deprived Neighbourhoods. Department of Communities and Local Government. Dodging the grabbing hand: The determinants of unofficial activity in 69 countries. Journal of Public Economics 76 3 , Propositions on trade unions and informal employment in time of globalisation. Informal employment in Romania. University of Minnesota Press. An empirical examination of corporate tax noncompliance. Cambridge University Press, Tax toleration and tax compliance: How government affects the propensity of firms to enter the unofficial economy. American Journal of Political Science 54 1: The impact of governance on wellbeing. Social Science Indicators Hudson, R. Informal employment in Slovenia. Decent work and the informal economy. Women and men in the informal economy: Why do firms hide? Journal of Public Economics 76 3: Corporate income tax compliance: A time series analysis. Atlantic Economic Journal 25 1: Poverty and informal economy participation: Economics of Transition 13 1: Hidden economy - an unknown quantity? A comparative analysis of hidden economies in transition countries, Economics of Transition 8 1: Survival ethnic entrepreneurs in Greece: Sociological Research On-Line, http: Informal Economic Activity in Belfast. Informal payments in public hospitals in Greece. Health Policy 87 1: Albanian immigrants in Athens: Journal of Law and Society 32 4: Aspects of the informal economy in a transforming country: International Journal of Urban and Regional Research 26 2: Determinants of business tax compliance. Measuring the non-observed economy. Economic Survey of Greece Purchasing and performing informal employment in Sweden: The informal economy and its paradoxes. Princeton University Press, Netherlands Geographical Studies no. Informal employment in an enlarged Union: The role of the underground economy in irregular migration to Italy: Journal of Ethnic Migration Studies 24 2: Migrants in irregular employment in the Mediterranean countries of the European Union. International Migration Papers no. The corporate tax gap: Evidence on tax compliance by small corporations. Tax Compliance and Enforcement. University of Michigan Press, Corruption in the post-Soviet workplace: Service employment regimes and the new inequality. Mingione E ed Urban Poverty and the Underclass.

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