

PART III

PUBLIC ACTION TO REDUCE POVERTY

Widespread poverty in Europe and Central Asia need not be a permanent phenomenon—even as it runs the risk of becoming one. As evidenced by the experience of many other countries, social and economic policies can go a long way to create opportunities, reduce poverty, and bring about a more egalitarian society. But in order for these policies to work, institutions must work well and must work in the interests of all parts of society, including the poor. Politicians captured by national elites or private interests have little incentive to act on behalf of the public good, and they are unlikely to implement the policies that will deliver better poverty outcomes. Indeed, it is hard to envision captured governments in much of the Commonwealth of Independent States (CIS) undertaking the actions needed to fight poverty and reduce inequality, when many of those actions (such as fostering the deconcentration of economic power through new entry and competition) may collide with their own private interests. If they are to attack poverty at all, governments throughout the region must first function effectively and be accountable and responsive to their broad electorates. Transition societies need to have mechanisms to ensure that different groups can express their preferences and demands in the political and social arena and that their voice is heard. With these fundamental elements in place, governments—and societies more broadly—will be better placed to design and implement a poverty strategy responsive to the needs of their citizenry.

Tackling state capture and building inclusive institutions are necessary elements of any effective antipoverty strategy in the transition economies. In all countries, even among the advanced reformers, there is scope to

build more inclusive institutions and create better mechanisms for voice. But the problem is particularly acute in the CIS, where efforts to restart growth and make progress on the poverty agenda hinge on building accountable and responsible governments. Captured states, however, are unlikely to “correct” themselves. The pressure must come from nonstate institutions and actors—from the development of civil society and of inclusive institutions at the national and community levels. Chapter 5 addresses the issue of state capture and outlines a multiprong strategy to fight it. This strategy encompasses measures to increase the costs of state capture to bureaucrats and politicians (stronger checks and balances, more political competition, stronger oversight mechanisms and civil society); it also includes measures, such as more economic competition and further deregulation, to reduce the benefits to firms and individuals from engaging in capture activities. The chapter also emphasizes the importance of building civil society and inclusive community-based institutions—both as a means to pressure governments to change and as instruments to compensate for the limitations and failures of state institutions.

Institutional change alone, without progress on the economic policy front, will not be sufficient to reduce poverty and inequality. Better-functioning and more inclusive institutions will facilitate the implementation of policies aimed at the broader public good, but even the best-intentioned governments will need a well-thought-out and coherent strategy to deliver improvements in living standards.

Broad-based growth that translates into new jobs and higher incomes is a critical element of this strategy. Some countries are on the road to growth, but prospects are more uncertain in others. And all countries, even the advanced reformers, face the challenge of ensuring that growth translates into new jobs and employment. Chapter 6 lays out the main elements of a policy package that can underpin sustained growth and help translate growth into jobs. Some elements of this package (such as reforms to reduce widespread economic rents and foster competition) will be good for growth but will, in addition, facilitate institutional change and reduce inequality. Other reforms (such as efforts to fight discrimination) will help to ensure that the benefits of growth are widely distributed. Many of the transition countries still have highly distorted economies. Indeed, in many instances there are no explicit tradeoffs between growth and equity objectives; on the contrary, they tend to reinforce each other. In other instances there may be tradeoffs, and policy choices must be navigated with care. For example, in some of the countries in Central and South Eastern Europe and the Baltics (CSB), the need to carry out fiscal

adjustment must be addressed without compromising the demonstrated effectiveness of the social safety net.

A second element in a strategy to fight poverty is building the capabilities of the poor, to allow them to take advantage of new employment and income-generating opportunities. The achievements of the education and health systems during the socialist era are undeniable. Countries are faced now with the challenge of reforming their systems to provide today's students with the skills they need to adapt to the changing demands of market-based economies. They are also faced with the challenge of providing their rapidly aging populations with high-quality health care that both households and the government can afford. The health and education systems have absorbed the large decline in financing that came with transition in ways that compromise quality and equity. Public sector salaries and expenditures on inputs (such as heat, textbooks, and drugs) have been downsized, but personnel and facilities have not. In this environment corruption has flourished as households have needed to make side payments to public sector employees to obtain services. Much of the burden of furnishing basic educational and health supplies has been *de facto* shifted to households. Serious illness is dreaded by poor households, since for many of them the costs of getting treatment are prohibitive. Chapter 7, on education, and Chapter 8, on health, suggest that poor communities and poor families are often the hardest hit by inadequate public spending and the rise in under-the-table payments. Chapters 7 and 8 review the important systemic reforms that are needed in each sector to ensure that the poor have the capabilities to participate as full members of society.

The transition has magnified the risks faced by households. Much of the security of the past was provided by guaranteed employment. This guarantee is gone. Largely because of the enormous fiscal contraction, programs that were intended to provide security and help people cope with economic shocks have had difficulty meeting their objectives. Free access to comprehensive health care has virtually disappeared in most countries. Under increasing stress, pension systems in some countries no longer provide a secure future for the elderly. Chapter 9 discusses how governments have tried to address the needs of the growing number of poor through expansion of social assistance programs, utility price compensation schemes, unemployment benefits, and pension reform. While many programs have provided some degree of support to families at risk, the sheer magnitude of the challenge has overwhelmed many countries' limited fiscal and administrative resources. Reform of pension programs is well under way across the region; still unresolved, however, are the inher-

ent difficulties of identifying the poor and providing them with meaningful levels of social assistance while preserving work incentives.

Governments can play an active role in reducing inequality and enhancing the mobility of those at the bottom. While responding to societal preferences, better distributional outcomes have been shown to have an important positive impact on growth, on social cohesion, and on the functioning of democracy. Governments may want to influence inequality simply because they believe in social justice and in maximizing social welfare. Chapter 10 examines a set of policy options to affect the distribution of income. Some of these are policies that are needed to restore growth, but they also will have positive distributional effects. Others focus more directly on raising the income of those at the very bottom, essentially through two channels. The first is through measures to increase their earnings potential and remove barriers to their employment. The second is by rebuilding the capacity of governments to deliver basic services and carry out an effective fiscal policy, so that societies can achieve their distributional objectives.