



*ECA Poverty Team's Quarterly Newsletter with highlights from recent activities and analytical work on poverty/gender issues in the ECA countries.*

## Addressing the Economic and Social Challenge of Informality in Hungary

Throughout ECA, informality is a concern for policymakers because of its potentially negative consequences for poverty as well as for social protection, competitiveness and for the fiscal position of governments. Upon the request of the Hungarian Government, a team comprising government officials, local and internal experts and Bank staff conducted a study to look at the issues around informality and make recommendations for addressing it.

The study concluded that the informal economy accounts for between 15-25 percent of the total economy in Hungary, with about 20 percent of the labor force engaged in undeclared work. Low-wage, low-skill workers are overrepresented in the informal sector, but the researchers found that the sector also includes better educated workers. This suggests that the phenomenon of informality includes not just those who cannot find work in the formal sector, but also those workers who have chosen to operate informally. In Hungary, the major disincentive to formal work is the tax system. On the one hand, a high tax wedge for low-wage labor prices many low-productivity workers out of the formal labor market. On the other hand, the high overall burden and distortions in the tax system create incentives for employers, employees, and the self-employed to operate in the "gray" economy.

The report concludes that a successful strategy to bring more workers into the formal economy will require both "carrots" and "sticks". The most important measures will involve reforms to lighten the tax burden, especially on low-wage labor. This can be done even while retaining fiscal neutrality by shifts in the structure of taxation and removal of various "traps" and distortions that occur through the interplay of taxes and benefits. At the same, better enforcement and sanctions in both the tax system and labor market regulation will reduce informality. **For further information contact Gordon Betcherman.**

## Revised Internationally-Comparable Poverty Estimates for ECA Countries

The World Bank has recently overhauled its methodology for global poverty estimation, concluding that while extreme poverty in the world is more pervasive than earlier thought, there is robust evidence of continually declining poverty since the early 1980s. Revised country-level poverty estimates are now available on the World Bank's website through PovcalNet, whereby users can derive country-level, regional, or global poverty estimates using the distribution of income/consumption in the countries concerned and different reference poverty lines.

### What are the Main Changes in Methodology Employed?

The new poverty estimates use results of the 2005 International Comparison Program (ICP) on purchasing power parities (PPP), whereby PPPs were estimated for 146 participating countries using data from price surveys from each country. All ECA countries were covered in the 2005 ICP, except Turkmenistan and Uzbekistan (where PPP imputations were used instead). The 2005 ICP is a clear improvement over 1993 PPP round: (i) a much larger number of countries participated in the surveys, (ii) price surveys in all participating countries were implemented on a more scientific basis, and (iii) more strict standards were employed in defining internationally comparable qualities of goods identified in the price surveys. A recent evaluation of the 1993 round concluded that it may have systematically under-estimated the cost-of-living in poorer countries.

The World Bank now recommends a new international poverty line of \$PPP 1.25 per person per day in 2005 prices, the mean poverty line of the world's poorest 15 countries (as opposed to \$PPP 1.08 per day in 1993 prices recommended earlier). However, a poverty line of \$PPP 2.50 per person per day in 2005 prices is likely more relevant for ECA countries, reflecting the higher cost-of-living associated with living in a colder climate. Similarly, a higher poverty/vulnerability line of \$PPP 5.0 is more relevant for middle-income countries (i.e. updating the earlier ECA practice, as reported in 2005 regional study "Growth, Poverty, and Inequality in Eastern Europe and the Former Soviet Union", of using \$PPP 2.15 and \$PPP 4.30 respectively).

## Main Findings of Particular Relevance for ECA Countries:

The updated ECA poverty estimates using the 2005 \$PPP 2.50 poverty line are slightly higher than in our earlier regional ECA analysis, but continue to show considerable progress in the ECA region between 1999 and 2005.

The updated ECA sub-regional profile is similar to that indicated by our earlier analysis, with the notable exception of low-income CIS countries (which are poorer than earlier thought):

- Higher poverty levels: Tajikistan, Kyrgyz Republic, Kazakhstan, Armenia, Azerbaijan, and Ukraine (because of higher cost-of-living than we thought earlier).
- Lower poverty levels: Serbia and Montenegro (because of lower cost-of-living than we thought earlier).

However, poverty trends based on the revised estimates for all ECA sub-regions (including low-income CIS countries) are very similar to those indicated by our earlier regional analysis.

One reason poverty estimates for most ECA countries do not change much compared to before is that the earlier ECA regional analysis was based on 2000 PPP estimates (i.e., on more recent PPP estimates than the 1993 PPP estimates used globally).

A final caveat worth bearing in mind is that while the above exercise is useful for international benchmarking, it is not a substitute for the national-level poverty analysis (e.g., from country Poverty Reduction Strategy Papers, World Bank-sponsored poverty and living standards assessments) used for domestic policy purposes. For more details, see <http://iResearch.worldbank.org/PovcalNet>. **For further information on ECA countries, contact Salman Zaidi and Victor Sulla.**

## Poverty Falls Sharply in Bulgaria

Incidence of poverty in Bulgaria has been cut by half between 2003 and 2007, according to a joint study by the Bulgarian Ministry of Labor and Social Policy and the World Bank. The study examined trends in living conditions, the distribution of wealth among different geographic and social economic groups, and the role of economic growth on poverty outcomes, as well as identified who the poor are and where they live.

The report--fittingly called "Bulgaria: Living Conditions before and after EU Accession"--points out that household consumption has increased by over 20 percent between 2003 and 2007 and resulted in poverty reduction from about 20 percent in 2003 to only 10.2 percent in 2007. The improvements are attributable to a series of structural reforms, macroeconomic stability and ensuing robust and

sustained growth, which has continued to lift the living standard of most households since 1998. The decline in the unemployment rate and a low share of the working poor due to real wage increases have also contributed in clamping down the incidence of poverty. However, despite the considerable improvement in living conditions nationwide, the study highlights that there are still severe pockets of poverty among distinct and identifiable groups including the unemployed, ethnic minority groups (such as the Roma), children in large families, and the elderly with weak family support structure. In particular, the study highlights the challenges for Bulgaria towards achieving a more inclusive and equitable society. **For further information contact Lire Ersado.**

## Are Low-Educated Women in Macedonia facing a Monopsonistic Labor Market?

A recent study on "Analyzing the reasons for economic inactivity among women in Macedonia", which is part of a broader Labor Market Assessment conducted by ECSHD (and funded under the Gender Action Plan), finds that female labor force participation rates in Macedonia (at 49 percent) are one of the lowest in the ECA region.

Low labor force participation for women is mainly explained by very low participation rates among women with low levels of education. While there are cultural values affecting this choice, especially among women from Albanian origin; low market wages, high reservation wages, and harsh employment conditions seem to be important exclusion determinants influencing uneducated women to stay at home. Indeed, large wage gaps exist between unskilled men and women that are not necessarily explained by labor segmentation (whereby women enter sectors offering lower-pay) but which seem to occur due to discrimination (whereby men in similar sectors doing similar jobs earn higher wages than their female counterparts). Also, low labor mobility, especially among low skilled workers, strengthens the sense of fragmentation of labor markets.

Such factors are generally prevalent in labor markets where firms have monopsonistic power. Indeed, in some regions of Macedonia, a large share of working women in Macedonia is employed by a few large textile companies. The implications of this is that firms may be paying women workers below their marginal product of labor, which causes supply of female labor to be below that in a competitive setting. **For further information contact Diego Angel Urdinola.**

**For future issues, please send your submission to [jwiltshire@worldbank.org](mailto:jwiltshire@worldbank.org).**